CEFTA and The European Single Market: an appropriate preparatory exercise?

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CEFTA and The European Single Market: an appropriate preparatory exercise?

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Key words
CEFTA, EU Enlargement · Stabilisation and Association Agreements
Preferential Trade Agreements · Article XXIV GATT · Comparative Analysis
Free movement of persons · Free movement of capital.
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<th>Abbreviation</th>
<th>Full Form</th>
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<tbody>
<tr>
<td>BaH</td>
<td>Bosnia and Herzegovina</td>
</tr>
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<td>CAP</td>
<td>Common Agricultural Policy</td>
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<tr>
<td>CEE</td>
<td>Central and Eastern European</td>
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<td>CEFTA</td>
<td>Central European Free Trade Agreement</td>
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<td>CRTA</td>
<td>Committee on Regional Trade Agreements</td>
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<tr>
<td>CU</td>
<td>Customs Union</td>
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<tr>
<td>DG</td>
<td>Directorate General</td>
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<tr>
<td>ECJ</td>
<td>European Court of Justice</td>
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<td>EMU</td>
<td>Economic and Monetary Union</td>
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<tr>
<td>ENP</td>
<td>European Neighbourhood Policy</td>
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<tr>
<td>EU</td>
<td>European Union</td>
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<td>FDI</td>
<td>Foreign Direct Investment</td>
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<td>FTA</td>
<td>Free Trade Area</td>
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<tr>
<td>FYROM</td>
<td>The Former Yugoslav Republic of Macedonia</td>
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<td>GATS</td>
<td>General Agreement on Trade in Services</td>
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<td>GATT</td>
<td>General Agreement on Trade and Tariffs</td>
</tr>
<tr>
<td>LDC</td>
<td>Least Developed Countries</td>
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<td>MFN</td>
<td>Most Favoured Nation</td>
</tr>
<tr>
<td>NT</td>
<td>National Treatment</td>
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<tr>
<td>RTA</td>
<td>Regional Trade Agreements</td>
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<td>SAA</td>
<td>Stabilisation and Association Agreement</td>
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<tr>
<td>SAP</td>
<td>Stabilisation and Association Process</td>
</tr>
<tr>
<td>SEE</td>
<td>South Eastern European</td>
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<tr>
<td>SPS</td>
<td>Sanitary and Phytosanitary Standards</td>
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<td>UNSCR</td>
<td>United Nations Security Council Resolution</td>
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<td>WTO</td>
<td>World Trade Organisation</td>
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Abstract

This thesis analyses the Central European Free Trade Agreement (CEFTA) and its parties as regards their relationship with the EU. Taking into account that the CEFTA was designed to be a preparatory exercise for Western Balkan countries aspiring to EU membership, the central question to be answered is whether the CEFTA constitutes appropriate preparation for the EU Single Market.

Trade relations between the countries of the Western Balkans and the EU have to be scrutinised against the background of the WTO legal framework, the perspective of EU enlargement and the regional reality in South East Europe. In doing so, this thesis looks first at the EU-Balkan trade relations in general and gives a detailed account of the impact of the Stabilisation and Association Process (SAP) both for the Balkan countries individually as well as for the region as a whole.

Discussion then turns to the specific relationship between the CEFTA and the EU Single Market. In conducting a comparative analysis of the two similar but different trade integration projects, this thesis concludes that from a theoretical point of view, the CEFTA can be considered an appropriate preparation for the EU Single Market in all but two areas under analysis. The CEFTA substantively covers the majority of provisions of the EU Single Market acquis, despite being a Free Trade Area (FTA) and not a Customs Union (CU). However, the CEFTA fails to address free movement of persons and free movement of capital.

There is strong evidence in favour of considering labour mobility to be included in the scope of the CEFTA. The CEFTA brings about very favourable conditions especially for implementing skilled labour mobility, which would help the CEFTA area improve labour productivity, exploit economies of scale and foster economic growth. With regard to free movement of capital, the evidence is not as conclusive as to whether or not the benefits of liberalising the capital movements within the CEFTA would outweigh the costs of doing so. However, in assuming that the capital markets of the CEFTA countries are already liberalised to a large extent, it is estimated that introducing freedom of capital into the CEFTA would have a net beneficial effect on the region.

Finally, this thesis argues that the CEFTA parties should be ready to commit to the same level of trade liberalisation as they do in their Stabilisation and Association Agreements (SAAs), taking into account that both trade integration initiatives pursue the same goal: to prepare the countries for eventual EU membership. Recalling that the EU insists on a
positive track record on implementing the SAA as well as the full implementation of the CEFTA, it is not coherent for Western Balkan countries to refuse committing to certain issues in the framework of the CEFTA which are already binding on them under SAAs, despite the fact that the EU has reiterated on a number of occasions that the future of all countries of the Western Balkan lies with the EU.
**Introduction: The Natolin Best Master Thesis**

**Prof. Georges Mink**  
**Director of studies**  
**College of Europe (EIS programme, Natolin Campus)**  
**Directeur de Recherche au CNRS (France)**

The College of Europe (CoE) was the world’s first university institute of postgraduate studies and training specialised in European affairs. Its origins date back to the 1948 Hague Congress. Founded in Bruges (Belgium) in 1949 by leading European figures such as Salvador de Madariaga, Winston Churchill, Paul-Henri Spaak and Alcide de Gasperi, the idea was to establish an institute where university graduates from many different European countries could study and live together. The Natolin campus of the College of Europe in Natolin, Warsaw (Poland) was established in 1992 in response to the revolutions of 1989 and in anticipation of the European Union’s 2004 and 2007 enlargements. The College of Europe now operates as ‘one College - two campuses’.

The European Interdisciplinary Studies (EIS) programme at the Natolin campus invites students to view the process of European integration beyond disciplinary boundaries and offers them a well-rounded understanding of the European Union. Students are awarded a ‘Master of Arts in European Interdisciplinary Studies’. This programme takes into account the idea that European integration goes beyond the limits of one academic discipline and is designed to respond to the increasing need for experts who have a more comprehensive understanding of the European integration process and European affairs.

The EIS programme is open not only to graduates in Economics, Law or Political Science, but also to graduates of History, Communication Studies, Languages, Philosophy, or Philology who are interested in pursuing a career in European institutions or European affairs in general. This academic programme and its professional dimension prepare graduates to enter the international, European and national public sectors as well as non-governmental and private sectors. For many, it also serves as a stepping stone towards doctoral studies. Recognised for its academic excellence in European studies, the Natolin campus of the College of Europe has endeavoured to enhance its research activities. A programme aimed at producing high-quality research on EU internal and external policies in line with the specificities of the EIS academic programme was designed in 2010. This has been joined by the recent creation of two Chairs: the European Parliament Bronislaw Geremek European Civilisation Chair and the European Neighbourhood Policy Chair.
Beyond research and policy-oriented workshops and conferences, a new series of Publications has been created. The first issues were published in 2011, including a series on the EU and the neighbourhood as well as the inaugural “Natolin Best Master Thesis” publications. In order to get their Masters degree all students are required to write a Thesis within the framework of one of the course they follow during the academic year. The research theme chosen by the student or proposed by the Professor supervising the Thesis must be original and linked to European policies and affairs. An interdisciplinary approach is also encouraged. Masters theses are written either in French or in English, the two official languages of the College of Europe, often not the native language of the students. A scientific committee selects the Best Masters Theses among more than 100 produced on the campus every year. By publishing them, we are proud to disseminate some of the most interesting research produced by our students throughout the wider European studies academic community.
Preface of the Master Thesis Supervisor

DR. DAVID LUFF
PART-TIME PROFESSOR
COLLEGE OF EUROPE, NATOLIN CAMPUS, WARSAW

This thesis analyses the Central European Free Trade Agreement (CEFTA) and it assesses whether this agreement constitutes an appropriate tool for the preparation of the CEFTA countries’ accession to the European Union.

The CEFTA itself belongs to the new generation of free trade agreements which progressively create a regional trade integration area. Its purpose is to develop better economies of scale and an area of regional development and peace. At the same time, the European Union negotiated or is in the process of negotiating with each CEFTA country separately a Stabilization and Association Agreement (SAA), whose full implementation is a condition for accession to the EU. This may create among the CEFTA countries a race for the swift negotiation and implementation of the SAA, thus possibly undermining regional coherence and integration. Furthermore, such approach may also be inconsistent with the parties’ multilateral trade commitments at the WTO. In the same way, the CEFTA may hold back those countries which are willing to move forward in the integration of the EU Acquis. Furthermore, the CEFTA may also not be entirely consistent with the WTO agreements.

It is the merit of the author to address all these issues, to show how they are interlinked and to respond to the thesis’ ultimate question: is the CEFTA relevant to foster EU’s accession and should its full implementation be encouraged? The author skillfully and methodically responds to this question throughout her dissertation. She also uses relevant literature including several primary sources, such as the text of the CEFTA, the SAAs and original EU and WTO documents.

The author introduces very well the subject and she exposes her methodological approach, the relevance of the topic and the precise scope of her analysis. The tone is set: this will be a very methodical and logical paper, which is entirely dedicated to responding the key thesis’ question. The first chapter of the study sets the multilateral trade scene in which the CEFTA evolves. The second chapter then focuses on the EU-Balkan Trade Relations and reviews the existing trade relations of the EU with each of the eligible CEFTA parties for EU accession. The overall presentation is very systematic and clear. The author exposes very well all facets of the issue and she adequately raises the
question of whether adopting an individual approach with each country is of a nature to undermine regional integration and, consequently, the capacity of the CEFTA countries to integrate themselves economically. The third chapter then describes the CEFTA itself and the fourth chapter assesses whether it contributes to its members’ accession to the EU. Chapter 4 adequately exposes the relevant criteria used for the assessment and it applies them to CEFTA. It compares the CEFTA’s mandated degree of economic integration with the one of the EU. Chapter 5 then comments on the elements in CEFTA which are missing, namely provisions for the free movement of workers and the free movement of capital. Finally, the conclusion summarizes well the paper’s findings and it responds to thesis’ final question: it makes an overall positive assessment of CEFTA as a tool facilitating EU accession and it encourages its parties to develop the necessary political will not only to fully implement it but also to expand its scope to the free movement of workers and capital. The author thus concludes that CEFTA is a good way forward for EU’s accession and that its full implementation should be encouraged.

Trade integration of the CEFTA countries with the EU will thus be pursued de facto before their formal accession to the EU. In this context, the challenge for the CEFTA countries awaiting such accession is not only to implement the required adjustments to their policies, as implied by the accession process, but also to economically take advantage of their own trade integration area. Success in this regard will inevitably facilitate their future integration to the EU. Ms Mostetsching’s work is a positive contribution in this regard.
Introduction

This thesis analyses in detail the Central European Free Trade Agreement (CEFTA) and its Parties as regards their relationship with the EU. Taking into account that CEFTA was designed to be a preparatory exercise for the EU, the central question to be answered is whether the CEFTA constitutes an appropriate preparation for the EU Single Market.

The original Central European Free Trade Agreement (CEFTA) entered into force on 1 March 1993 and established a free trade area between its founding members, that is Poland, Hungary, the Czech Republic and Slovakia. In the course of the last 20 years other countries of Central and South Eastern Europe have joined the CEFTA. As of 2007, the 'new CEFTA' comprises Albania, Bosnia and Herzegovina (BaH), Croatia, Kosovo under UNSCR 1244 (Kosovo), the Former Yugoslav Republic of Macedonia (FYROM), Moldova, Montenegro and Serbia. In essence, all CEFTA signatories with the exception of Moldova are potential future member states of the European Union. Former parties are Bulgaria, the Czech Republic, Hungary, Poland, Romania, Slovakia and Slovenia; their CEFTA membership ended once they joined the EU.

The CEFTA is a regional trade integration initiative aimed at increasing cooperation among its members in order to prepare for the EU membership. The origins of the CEFTA in the 1990’s stem from the Visegrad countries’ efforts to join the EU as soon as possible. The EU signalled that regional cooperation and economic (re)integration would enhance the CEE countries’ case for a rapid move towards EU accession.1 In other words, the CEFTA was established as a consequence of the EU recommendation to the future members to prepare for membership by establishing free trade areas. This is why the original CEFTA Treaty of 1992 was modelled very closely on the Europe Agreements’ trade chapters, both as regards the contents and the timetable for transition to free trade between the CEFTA members.2 The CEFTA proved to be, and in its current form remains, a sort of preparatory exercise for or a precursor to the eventual integration into the EU single market:


2 Europe Agreements constituted the legal framework of relations between the EU and the Central European countries before their accession to the EU. In addition, they formed the framework for implementing the accession process for Poland, Hungary, the Czech Republic, Slovakia, Romania and Bulgaria. (See http://ec.europa.eu/enlargement/glossary/terms/europe-agreement_en.htm, last accessed on: 4 May 2011.)

3 Dangerfield Martin, op. cit., p. 312.
“Effectively implemented, the Agreement provides an excellent framework for the Parties to prepare for EU accession, thus continuing the tradition of the original CEFTA, whose founding members are now in the EU.”

In an attempt to analyse the aforementioned assumption in detail, this thesis is structured as follows: the first chapter will briefly introduce the WTO framework, in the context of which EU-Balkan trade relations in general, and the CEFTA in particular, will be further explored in chapters two and three respectively. Chapter four will conduct a detailed comparative analysis of the two similar but different trade integration models and seek to answer the question in how far the CEFTA can be considered an appropriate preparation for the EU Single Market. The methodology of the comparative analysis will follow a two-step approach: first, criteria for successful preparation will be established with a second step then assessing whether the CEFTA lives up to them. In chapter five, the analysis will focus on the two areas that the CEFTA fails to address in order to appropriately prepare its Parties for eventual EU accession. These two areas are: the free movement of workers and free movement of capital. The thesis will conclude with a brief summary of findings and their interpretation.

Relevance of the Topic

All the CEFTA members (apart from Moldava) are (potential) candidates for accession to the European Union. In other words, sooner or later, the Western Balkans will form part of the EU Single Market. When the Visegrad countries joined the EU in 2004, the CEE region presented itself as a relatively homogenous block in terms of economic development, and in addition it boasted high economic growth rates. Previous enlargements had, at least from an economic point of view, been an enormous success both for the “old” EU15 and the new Member States.5

The EU is of course interested to repeat this success in enlargements to come. The countries of the Western Balkan, however, face a different starting point: their economies are much smaller than the CEE economies, economic growth has been slowed down by the global financial crisis, they are poor exporters and some face growing trade deficits. International trade and regional trade integration thus play a central role in further economic and political stabilisation, as well as in achieving their common goal of EU membership. Taking this into account, the question whether the CEFTA is an

appropriate preparation for the EU Single Market is of great importance both from an EU enlargement and a regional point of view.

**Limitations**

This thesis will not undertake an analysis of the original CEFTA members which are today new Member States of the EU. Even though the cases of Bulgaria, the Czech Republic, Hungary, Poland, Romania, Slovakia and Slovenia would deliver empirical data about the convergence and adequacy of the CEFTA as a preparation for the EU Single Market, this thesis will only focus on the case of the current 'new CEFTA' Parties.

Another key limitation of the thesis is Moldova. Moldova has a very special position in the framework of the CEFTA. In contrast to all other Parties to the Agreement, it does not form part of the enlargement countries group, but part of the European Neighbourhood Policy (ENP). In 2004, the ENP was developed „with the objective of avoiding the emergence of new dividing lines between the enlarged EU and our neighbours and instead strengthening the prosperity, stability and security of all.“ At the moment, 16 of the EU’s closest neighbours form part of the ENP: Algeria, Armenia, Azerbaijan, Belarus, Egypt, Georgia, Israel, Jordan, Lebanon, Libya, Moldova, Morocco, Occupied Palestinian Territory, Syria, Tunisia and Ukraine. The ENP does not intend to prepare these countries for EU enlargement, but to develop stable and well-functioning neighbourly relations.

In 2006, negotiations on the ’new CEFTA’ started under the auspices of the EU and the Stability Pact for South Eastern Europe. The Stability Pact was launched in 1999 as an international instrument to stabilise the post-war Balkan countries and bring peace, human rights and economic stability to the region. The Partners of the Stability Pact were the countries of South Eastern Europe (except Greece), the European Commission and the EU Member States, International Organisations, International Financial Institutions and a number of regional initiatives.

The Stability Pact had a mandate to strengthen regional cooperation and eventually guide the region into taking over the responsibility and ownership for their future

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7  Albania, Bosnia-Herzegovina, Bulgaria, Croatia, Moldova, Montenegro, Romania, Serbia, Kosovo and The Former Yugoslav Republic of Macedonia.
8  UN, OSCE, Council of Europe, UNHCR, NATO, OECD.
9  World Bank, IMF, EBRD, EIB, Council of Europe Development Bank.
10 Black Sea Economic Co-operation (BSEC), Central European Initiative (CEI), South East European Co-operative Initiative (SECI) and South East Europe Co-operation Process (SEECP).
development. In transforming the Stability Pact into a more regionally owned initiative, negotiations for the 'new CEFTA' were launched. At that moment, it was obvious that all regional partners of the Stability Pact, including Moldova, would be included into the new CEFTA. However, while all other countries were offered an EU membership perspective, Moldova became hostage of the Ukrainian question\(^{11}\), and was denied accession to the EU and finally formed part of the ENP.\(^{12}\)

The main objective of this thesis is to explore the extent to which the CEFTA is an appropriate preparation for the EU Single Market. To that end, this thesis focuses to a great extent on the CEFTA Parties forming part of the EU enlargement process and thus excludes Moldova unless indicated otherwise. For Moldova, the research question is obsolete as it forms part of the ENP and does not have an enlargement perspective.

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\(^{11}\) Since the 'Orange Revolution' in the Ukraine in 2004, EU Member States have disagreed over whether to offer to Ukraine the prospect of membership, allured by Ukraine's economic potentials and energy resources whilst being scared of its size and communist past. The EU was torn over the question whether Ukraine would complete its democratic transition and embark on its Western European perspective rather than turning towards Russia again. In the end, the EU decided on offering Ukraine to form part of the ENP, thus denying the membership option.

\(^{12}\) Interview with Andras Inotai, Professor at the College of Europe, Academic Year 2010/2011, 11 March 2011.
Chapter 1. Regionalism in the Light of WTO Law

Any exploration of the individual trade regimes of the EU and the Balkan countries must take place within the larger scope of international trade rules. In order to fully comprehend international trade regimes, they need to be studied with reference to the international legal framework governing international trade, namely WTO law. Before turning to the analysis of how the bilateral trade relations between the EU and the individual Western Balkan countries and the CEFTA play together, some introductory remarks about regionalism within the WTO legal framework will be set forth.

1.1 General Principles

The WTO is the institution establishing and guarding international trade regulation. It was created in the course of the Uruguay negotiation rounds from 1986 to 1994 and emerged from the General Agreement on Tariffs and Trade (GATT), which entered into force after the Second World War in 1947. The WTO is governed by agreements, of which the most important are the Agreement Establishing the WTO, the GATT 1994 (for trade in goods), and the General Agreement on Trade in Services (GATS; for trade in services). However, the total list of WTO agreements is much longer, dealing with particular requirements of specific sectors or issues.

GATT 1994 is the most important WTO agreement, both regarding the scope and relevance as compared to other agreements. Its overall aim is to achieve multilateral trade liberalisation. GATT consists of two main legal doctrines: (1) the doctrine of non-discrimination and (2) the doctrine of removing barriers to international trade.

13 GATT 1994 is the amendment to GATT 1947.
14 For a more detailed overview of the WTO and its agreements, see http://www.wto.org/english/thewto_e/whatis_e/tif_e/agrm1_e.htm, last accessed on: 4 May 2011.
15 Hereinafter, whenever this thesis refers to GATT it is always in the sense of GATT 1994 unless indicated otherwise.
The doctrine of non-discrimination is mirrored in two principles. One is the “most favoured nation clause” (MFN) as laid out in Article I of GATT, stipulating that concessions granted to one trading partner automatically have to be granted to all other GATT/WTO parties. The other principle is the “national treatment clause” (NT) under Article III of GATT, providing that once a foreign product has entered the domestic market it is to be treated like all other domestic products.

The doctrine of removing barriers to international trade can equally be divided into two further principles. Whilst the first principle refers to the readiness to reduce tariffs (Article II GATT), the second principle provides for the prohibition of non-tariff barriers (Article XXI GATT), mainly dealing with the elimination of quantitative restrictions to trade.

1.2 Exception to General Principles: Preferential Trade Agreements

It therefore becomes evident that regional trade integration projects, such as the EU or the CEFTA, clearly violate the doctrines of non-discrimination and removing barriers to trade, as they are inherently preferential by their nature. However, to that end, the WTO rules include the possibility of establishing preferential or regional trade agreements legally compatible with GATT.

For the trade in goods, WTO rules provide an exception to the MFN clause in Article XXIV of GATT, allowing the formation of preferential trade agreements such as free trade areas (FTAs) and customs unions (CUs) under certain conditions. Another exception is the ‘Enabling Clause’¹⁶, designed to support developing countries. For the trade in services, Article V of the GATS allows to derogate from the doctrine of non-discrimination also applicable in the scope of trade in services.

In recent years, regional trade agreements have increased significantly. “The growth and development of RTAs [Regional Trade Agreements] today is fast-paced, complex and global, and mapping RTAs has become an increasingly difficult task.”¹⁷ Table 1 shows the total number of RTAs notified to the WTO and in force to be 297 as of May 2011,

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¹⁶ WTO, Differential And More Favourable Treatment Reciprocity and Fuller Participation of Developing Countries, Decision of 28 November 1979, L490/3.

of which the vast majority have been established in the form of free trade areas under Article XXIV of GATT.

Table 1: Regional Trade Agreements notified to GATT/WTO and in force

<table>
<thead>
<tr>
<th></th>
<th>Accessions</th>
<th>New RTAs</th>
<th>Grand total</th>
</tr>
</thead>
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<tr>
<td>GATT Article XXIV (FTA)</td>
<td>1</td>
<td>162</td>
<td>163</td>
</tr>
<tr>
<td>GATT Article XXIV (CU)</td>
<td>6</td>
<td>9</td>
<td>15</td>
</tr>
<tr>
<td>Enabling Clause</td>
<td>1</td>
<td>33</td>
<td>34</td>
</tr>
<tr>
<td>GATS Article V</td>
<td>3</td>
<td>82</td>
<td>85</td>
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<tr>
<td><strong>Grand total</strong></td>
<td><strong>11</strong></td>
<td><strong>286</strong></td>
<td><strong>297</strong></td>
</tr>
</tbody>
</table>

Source: WTO, as of May 2011

The largest number of RTAs is to be found in Europe. Despite the fact that the recent years have seen a consolidation of existing intra-European RTA networks, Europe continues to account for a large share of the preferential agreements in force and notified to the WTO. With the EU enlargements in 2004 and 2006, several RTAs with the now new Member States ceased to exist. South Eastern Europe followed the trend of consolidating trade agreements and turned about 20 bilateral free trade agreements into one multilateral agreement – the CEFTA 2006.

1.2.1. Trade in Goods: GATT Article XXIV

Article XXIV of GATT, paragraphs 4 and 5 read:

“(4) The contracting parties recognize the desirability of increasing freedom of trade by the development, through voluntary agreements, of closer integration between the economies of the countries parties to such agreements. They also recognize that the purpose of a customs union or of a free-trade area should be to facilitate trade between the constituent territories and not to raise barriers to the trade of other contracting parties with such territories.”

“(5) Accordingly, the provisions of this Agreement shall not prevent, as between the territories of contracting parties, the formation of a customs union or of a free-trade area or the adoption of an interim agreement necessary for the formation of a customs union or of a free-trade area (…)”

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19 Fiorentin Roberto V, Crawford Jo-Ann, Tocqueboeuf Christelle, op. cit., p. 45.
20 Ibid.
Article XXIV:5 of GATT further imposes three obligations on WTO members wishing to enter into a FTA or CU. To start with, there is (a) an obligation to notify the preferential trade agreement. Next, the parties entering into a FTA or CU are under (b) obligation to liberalise substantially all trade; and lastly, (c) an obligation not to raise the overall level of protection and increase trade barriers towards third parties. The latter obligations will be discussed in more detail below.

It has to be noted that Article XXIV GATT is receptive to transitional periods. This means that as long as the parties to a preferential trade agreement indicate that they plan to become a ‘full’ FTA or CU member in a "reasonable period of time" (Article XXIV:5 GATT), they can suspend the obligation to liberalise substantially all trade until the end of the transitional period.

There are two tracks available for reviewing the consistency of FTAs and CUs established under GATT Article XXIV with WTO law. Track one, the ‘multilateral’ track, provides for WTO members to enter into the Committee on Regional Trade Agreements (CRtA), which then issues reports on the (non-)conformity of FTAs with WTO rules. The second ‘bilateral’ track foresees that WTO members may challenge the consistency of a FTA through panel proceedings under the Dispute Settlement Understanding. The CRtA has not been very successful in exercising its mandate to verify the compliance of notified RTAs with the relevant WTO provisions. Fiorentin et al. found that at the time of the launch of the Doha Round in November 2001, the CRtA had made no progress on its mandate of consistency assessment, owing to the endemic questions of interpretation of the provisions contained in Article XXIV of GATT 1994.

With endemic questions of the interpretation of the provisions contained in Article XXIV of GATT, Fiorentin et al. are most likely to mean the provision on ‘substantially all trade’ and ‘no rise in barriers vis-à-vis third countries’. The situation remains unchanged today. Members of the CRtA are rarely able to reach a consensus on the consistency of the notified RTAs with the relevant WTO provisions. Up to date, the CRtA has only once taken a definite and unambiguous decision on the conformity of a preferential

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22 Ibid.
23 Ibid., pp. 555-556.
1. Regionalism in the Light of WTO Law

trade agreement with GATT law: the CU between the Czech Republic and Slovakia. Negotiations on how to remedy this situation are on the agenda of the Doha round. However, as the Doha round negotiations are currently stalled, there is also no progress on resolving the impasse of the CTRA.

1.2.1.1 ‘Substantially all trade’

Article XXIV GATT is a conditional exception to the general WTO principle of MFN. Article XXIV:8 GATT includes a provision that if a group of two or more countries decide to engage in regional trade integration (FTA or CU), they can only do so if the agreement covers ‘substantially all trade’. Article XXIV:8(a) applies to CUs while Article XXIV:8(b) targets FTAs and reads:

“A free-trade area shall be understood to mean a group of two or more customs territories in which the duties and other restrictive regulations of commerce (…) are eliminated on substantially all the trade between the constituent territories in products originating in such territories.” (emphasis added)

There is no consensus on how to interpret ‘substantially all trade’. The CTRA uses two approaches in examining regional trade agreements. The first one is a quantitative approach using statistics to determine the percentage of trade. The second approach is qualitative, and refers to the notion that no (major) sector could be excluded. The two approaches are not mutually exclusive. On the contrary, the Turkey Panel (Restrictions on Imports of Textiles and Clothing Products), suggested that a combined application of the quantitative and qualitative approach is to be favoured. Both methodologies, however, are controversial and lack clear criteria on what percentage of trade needs to be covered or how many sectors would need to be included. According to Petros Macvroidis, the WTO case law so far has not yet answered the question on how to interpret the meaning of ‘substantially all trade’.

27 Art. XXIV:8(b) GATT.
29 Ibid., pp. 234-345.
30 WTO, Report of the Turkey Panel, 31 May 1999, WT/DS34/R.
1.2.1.2 ‘No raise in trade barriers vis-à-vis third parties’

Article XXIV:5 GATT stipulates that members of a preferential trade agreement must not raise barriers towards third WTO parties. With this regard, the provisions are not the same for FTAs and CUs. In forming an FTA, constituents must not necessarily change their external tariffs vis-à-vis third countries. In CUs, on the other hand, constituents change their external tariffs in order to adopt a common external tariff.

With respect to FTAs, Article XXIV:5(b) GATT reads:

“(…) the duties and other regulations of commerce maintained in each of the constituent territories and applicable at the formation of such free-trade area or the adoption of such interim agreement to the trade of contracting parties not included in such area or not parties to such agreement shall not be higher or more restrictive than the corresponding duties and other regulations of commerce existing in the same constituent territories prior to the formation of the free-trade area (…)” (emphasis added)

Two issues in this Article are worth noting. Firstly, the provision does not generally prohibit WTO members participating in an FTA to modify their external tariff. They are only not allowed to raise it as compared to the state prior to the formation of the FTA. Secondly, the term ‘other regulations of commerce’ leaves room for interpretation. Here, again, there is lack of common understanding on how to interpret ‘other restrictive regulations of commerce’ in Article XXIV:5(b) GATT.32

For CUs, the requirement of not raising protection vis-à-vis third countries is twofold: at first, CUs must not raise the overall level of protection. In addition, countries forming a CU have the specific obligation to compensate in cases where customs duties in some constituents of a CU had to be raised in order to match the level of the common external tariff.33 The ambiguous notion of ‘other regulations of commerce’ reappears in Article XXIV:5(a) GATT:

“with respect to a customs union, (…) the duties and other regulations of commerce imposed (…) shall not on the whole be higher or more restrictive than the general incidence of the duties and regulations of commerce applicable in the constituent territories prior to the formation of such union or the adoption of such interim agreement.” (emphasis added)

32 Matsushita Mitsuo, Schoenbaum Thomas J, Macvroidis Petros C, op. cit., p. 563.
33 Ibid., p. 564.
1.2.2. Enabling Clause for Developing Countries

In 1979, the signatories of GATT 1947 decided to allow positive discrimination towards developing countries, offering them preferential market access in order to better integrate them into the international trade system. The decision on differential and more favourable treatment reciprocity and fuller participation of developing countries continues to be valid under GATT 1994. The ‘Enabling Clause’ poses an exception both to the MFN clause as well as to Article XXIV of GATT, as it authorises two things: first, this Decision authorises developed countries to accord a General System of Preferences (GSP) to developing countries, granting them non-reciprocal preferential market access. It is important to note that non-reciprocal preferences must be accorded to all developing countries equally and no discretionary selection of them is possible otherwise than through objective criteria. Second, the ‘Enabling Clause’ allows developing countries to engage in preferential trade regimes without liberalising ‘substantially all trade’ (GATT Article XXIV:5).

One of the conundrums deriving from the Enabling Clause is how to define a developing country. With this regard, the WTO refers to the UNCTAD list of ‘Least Developed Countries’ (LDC) in order to differentiate between LDC and developing countries; however, there are no objective criteria how to differentiate between developing countries and developed countries. This problem has become more and more pressing in recent times. China, for example, in its accession protocol, classified itself as a developing country. The question whether China should really benefit from the preferences accorded to developing countries, given its recent rise to a global economic power, remains unanswered.

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34 WTO, Differential And More Favourable Treatment Reciprocity and Fuller Participation of Developing Countries, Decision of 28 November 1979, L490/3.
35 See Report of the Appellate Body, „European Communities – Conditions for the granting of tariff preferences to developing countries, 7 April 2004, WT/DS246/AB/R.
36 For more detailed information on the criteria how the UNCTAD defines LCD, see http://www.unctad.org/Templates/Page.asp?intItemID=3618&lang=1, last accessed on: 4 May 2011.
37 China acceded to the WTO on 11 December 2011. See China’s WTO accession protocol, WT/ACC/CHN/49 and Corrigendum 1, WT/MIN(01)/3.
1.2.3 Trade in Services: Article V GATS

The General Agreement on Trade in Services (GATS), negotiated in the Uruguay Round, allows the WTO members which enter into a preferential trade agreement to deviate from the MFN obligation in their trade in services covered by the GATS.

Countries wishing to enter into a preferential trade agreement covering services have the obligation to notify their agreement to the WTO. Furthermore, they can do so under two conditions: pursuant to Article V:1 of the GATS they have to ensure the elimination of all discrimination within a framework of substantial sectoral coverage, and secondly, they have to agree not to erect new trade barriers towards WTO members not participating in the preferential agreement (Article V:4 GATS). Essentially, the conditions for establishing a preferential trade agreement with the scope of services mirror the provisions from the GATT.
Chapter 2. EU-Balkan Trade Relations

This chapter will take a look at the EU-Balkan trade relations in general. Two sets of regimes govern the trade relations between the EU and the Western Balkans. One is the regime of autonomous preferential treatment, possible due to a WTO waiver under the ‘Enabling Clause’. The regime of establishing reciprocal preferential trade agreements, on the other hand, forms part of the EU enlargement process. Almost all CEFTA members are (potential) candidate countries for EU accession and have concluded so-called Stabilisation and Associations Agreements. These reciprocal preferential trade agreements mainly govern the bilateral trade relations between the individual countries and the EU.

2.1 EU-Balkan Trade Relations after the Yugoslav Secession Wars in the 1990's

In 2000, the EU requested a waiver to Article I of GATT (MFN clause) from the WTO in order to set up a trade regime of autonomous preferential treatment with the Western Balkan countries in the aftermath of the Yugoslav secession wars in the 1990's. In doing so, it was suggested that the countries in South Eastern Europe found themselves in an exceptional (post-war) situation, recalling the EU's efforts for preservation of peace and economic reconstruction in the region. The General Council of the WTO decided to grant the waiver:

“(…) the provisions of paragraph 1 of Article I of GATT 1994 shall be waived until 31 December 2006 to the extent necessary to permit the European Community to afford duty-free or preferential treatment to eligible products originating in Albania, Bosnia-Herzegovina, Croatia, the Federal Republic of Yugoslavia and the former Yugoslav Republic of Macedonia, without being

39 The exception is Moldova, which forms part of the ENP and is not a (potential) candidate country. In the course of this thesis, Moldova will continue to play a particular role distinctly different from the other CEFTA Parties, due to the missing enlargement perspective.
required to extend the same duty-free or preferential treatment to like products of any other member." (emphasis added)

The waiver was granted under the conditions that such duty-free or preferential treatment would not raise new barriers to the trade of other WTO members. To that end, the EU has to report annually to the WTO on its trade flows with the Balkan countries. After its expiry on 31 December 2006, the General Council renewed the waiver upon the EU's request until 31 December 2011.

Even before 2000, the EU already had in place a liberal trade regime towards the Western Balkans, allowing more than 80 per cent of the countries’ exports to enter the EU duty-free. As the general level of imports from the Western Balkan countries remained very low (being less than 1 per cent of all EU imports), the EU decided in 2000 to further extend autonomous trade preferences by removing all remaining duties for industrial and agricultural products and by further improving access to the EU market for agricultural and fishery products. In order to extend the autonomous trade preferences, it was necessary to ask for a waiver from the WTO.

2.2 EU-Balkan Trade Relations in the Light of EU-Enlargement

2.2.1 The Perspective of Enlargement for the Western Balkans

In June 2000, the European Council held in Feira for the first time acknowledged that all Western Balkan countries participating in the Stabilisation and Association Process were potential candidates for EU membership and thus opened the door for enlargement towards the southeast. Only a few months later, the EU heads of state or government at the Zagreb Summit in November 2000 decided to launch the Stabilisation and Association Process with Croatia, The Former Republic of Yugoslavia (back then Serbia, Montenegro and Kosovo), Bosnia and Herzegovina, Macedonia and Albania.

42 WTO, Report of the European Union under the Decision WT/L/654, 12 July 2010, WT/L/799, paragraph 5.
43 Ibid., paragraph 6.
In the years to follow, the Western Balkans’ accession perspective was regularly reconfirmed in semi-annual European Council conclusions. In 2003, the ‘Thessaloniki Agenda for the Western Balkans: Moving towards European Integration’ was adopted and still today it provides the framework for the necessary steps the Western Balkan countries have to take on their way to future EU accession. The Thessaloniki Agenda reiterates the importance of the Stabilisation and Association Process, and thus the further strengthening of EU-Balkan trade relations.

The process of enlargement in the Western Balkans is based on the fulfilment of the Copenhagen criteria (1993), which are divided into three parts: the first two comprise general political and economic criteria, while the third part deals with the ability to assume the obligations of membership under 35 related chapters of **acquis communautaire**. After the enlargement round of 2004 and in particular of 2006, the European Council of December 2006 adopted new guidelines, the so-called ‘renewed consensus on enlargement’. According to them, the fulfilment of the political criteria, as set out in the Copenhagen criteria, becomes a precondition for opening accession negotiations. In addition, the Council takes a ‘regatta principle’ approach, implying that every (potential) candidate country will be evaluated on its own merits and may join individually once it sufficiently fulfils all the accession criteria. This aspect is of vital importance when later analysing the significance of regional integration in the enlargement process. And lastly, it puts a special emphasis on the conditionality of the Stabilisation and Association Process: “A country’s satisfactory track-record in implementing its obligations under a Stabilisation and Association Agreement, including trade related provisions, is an essential element for the EU to consider any membership application.”

At the Sarajevo EU-Western Balkans ministerial meeting in June 2010, the EU once more repeated its unequivocal commitment to the European perspective of the Western Balkans, pointing out that the future of these countries lies in the European Union.

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48 Ibid., p.3.

Likewise, all the CEFTA countries with an accession perspective make continuous efforts to join the EU as soon as possible.

**CROATIA** concluded accession negotiations in June 2011. On 1 December 2011 the European Parliament approved Croatia’s accession as the 28th member of the EU. Croatia and the EU signed the accession treaty on 9 December 2011. Following the ratification procedure in all Member States and Croatia, Croatia’s accession is foreseen for 1 July 2013.

The ratification of the Stabilisation and Association Agreement between **Serbia** and the EU started in June 2010. In October 2011, the European Commission delivered its Opinion on Serbia’s EU membership application. Serbia was finally granted candidate status in March 2012, however without opening accession negotiations.

**BOSNIA AND HERZEGOVINA (BAH)** signed a Stabilisation and Association Agreement in June 2008, however the ratification process has not been completed yet. Reforms in BaH have been going slow and the outstanding alignment of the Bosnian Constitution with the European Convention for Human Rights (ECHR) hampers further progress. BaH has not applied for EU membership yet.50

**MONTENEGRO** has been awarded candidate status in the beginning of 2011. Once it fulfilled outstanding benchmarks, the Council decided to open accession negotiations in June 2012.

**THE FORMER YUGOSLAV REPUBLIC OF MACEDONIA (FYROM)** became a candidate country in 2005 but the Council until now has not decided to open accession negotiations, mainly due to the unresolved name issue.51

**ALBANIA** has recently suffered a setback in its EU-integration efforts due to internal political problems and remains to be a potential candidate. Following Albania’s application for EU membership in 2009, the Commission has neither recommended to the Council to open accession negotiations with Albania, nor to grant candidate status like in the case of Montenegro and Macedonia.52

50 Ibid.

51 The name issue between FYROM and Greece arose in 1991, when the former Yugoslav Republic of Macedonia declared its independence under the name “Republic of Macedonia”. Greece opposes the constitutional name of its northern neighbouring country, invoking historical, cultural and territorial concerns resulting from the ambiguity between FYROM’s constitutional name and the adjacent Greek region Macedonia. Both countries remain engaged in talks under the auspices of the UN in order to resolve the name issue.

52 European Commission, Commission Opinion on Albania’s application for membership of the
**Kosovo** (under UN 1244) remains the main source of instability in the region. Until Kosovo’s status has been resolved, the EU has hardly any room for manoeuvre in terms of enlargement. However, in February 2010, the Commission proposed to start working on how to possibly extend the EU’s autonomous trade measures to Kosovo. Once all the relevant conditions are fulfilled – including the resolution of Kosovo’s status, bearing in mind that five EU Member States have not recognised Kosovo’s independence – the Commission will propose to negotiate Directives for a free trade agreement with Kosovo. In addition, a visa liberalisation dialogue is to be launched shortly.53

Taking into account all official EU positions towards enlargement on the one hand and efforts of (potential) candidate countries on the other hand, it becomes clear that the process of enlargement constitutes the major impetus for change and development in the Balkans. The prospect of EU membership and the process of enlargement connected therewith affords a powerful tool to implement international trade policies in these countries, as favoured by the EU. Discussion now turns to how the EU eventually implements its enlargement policy. It does so via a vehicle called ‘Stabilisation and Association Process’.

### 2.2.2 The Stabilisation and Association Process

In order to stabilise the post-war Western Balkan region and support its economic recovery, the EU came up with a programme called ‘Stabilisation and Association Process’ (SAP).54 The SAP is first and foremost an instrument to enhance bilateral relations between the EU and the participating countries. In addition, the EU also linked the SAP with the prospect of potential membership, however without a clear roadmap or timeframe. At the Feira European Council in 2000 it was acknowledged that all Western Balkan countries participating in the SAP are potential candidates for EU membership. The goal of the SAP is to progressively align the participating countries with the EU while also promoting regional integration. Essentially, the SAP has four pillars:

**Trade:** The SAP envisages a deepening of bilateral trade between the EU and the participating countries through preferential trade regimes.

**Financial Assistance:** The EU supports the participating countries with financial assistance. The current financial assistance programme is called Instrument for Pre-Accession (IPA).

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Regional Cooperation: The SAP obliges the participating countries to engage in regional cooperation with the aim to reconcile the post-war region.

Stabilisation and Association Agreement (SAA): The participating countries and the EU negotiate, sign and ratify an agreement called SAA. With an SAA, the parties enter into a more institutionalised and more advanced contractual relationship with the EU. The fulfilment of the SAA provisions is a pre-condition for all further progress in the accession process.

The SAP sets out a number of criteria to be fulfilled in order to establish a more advanced relation with the EU, such as within the more institutionalised contractual framework of a SAA. The conditions for SAA negotiations include the fulfilment of a number of political criteria such as full co-operation with the International Criminal Tribunal for the former Yugoslavia (ICTY), the respect for human and minority rights, a solution to the question of refugees and internally displaced persons and a credible commitment to regional cooperation. Once these conditions have been sufficiently fulfilled, the Commission launches SAA negotiations. After the signature of the SAA, an Interim Agreement enters into force until all Member States have ratified the SAA. Until EU accession, the SAA is the main institutional and contractual framework in place on which the bilateral relations between the associated country and the EU are based.

The content of an SAA is largely inspired by the Europe Agreements and is similar for all SEE countries having concluded such an Agreement. An SAA is generally implemented in two parts. The parts containing general trade and trade-related elements as well as other areas in which the EU is competent can enter into force via an Interim Agreement shortly after signature because it does not require ratification by the Member States. The other parts can only enter into force once the SAA has been ratified by each Member State individually. This may take considerably more time due to different Member States’ positions towards the associated country in question. The content of an SAA is structured as follows:

Title 1: General Principles. The first title comprises general commitments towards peace and stability, democratic principles, fundamental rights and the rule of law. For the countries concerned, it reiterates the obligation to fully cooperate with the International Criminal Tribunal for the former Yugoslavia (ICTY) and engage in regional cooperation. It further states that the association is to be realised progressively and fully within a certain period of

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time, which varies from country to country. The first title also contains an Article stating that the SAA shall be implemented fully in line with the relevant WTO provisions.

**Title 2: Political Dialogue.** The second title provides for regular exchanges and dialogue on the political level in the form of meetings, via the diplomatic channels, in the international fora and within so-called Stabilisation and Association Councils. Political dialogue does not only mean bilateral communication, but includes also regional integration and good neighbourly relations.

**Title 3: Regional Cooperation.** The third title obliges the associated country to seek active and close cooperation with its regional partners and neighbouring countries. It specifically calls on the country to cooperate in the areas covered by the SAA. It is important to point out that this title also contains an obligation to fully implement the CEFTA.

**Title 4: Free Movement of Goods.** The SAA establishes a bilateral free trade area between the associated country and the EU in conformity with GATT 1994 and WTO provisions. This free trade area is not to cover all trade between the associated country and the EU, but covers only industrial products, agriculture and fisheries.

**Title 5: Movement of Workers, Establishment, Supply of Services, Movement of Capital.** In the area of movement of workers, the SAA grants non-discriminatory treatment to the workers of the associated country legally employed in a Member State and vice versa, to Member States’ nationals employed in the associated country. As regards establishment, the associated country and the EU shall mutually facilitate the establishment of the associated countries’ companies and EU companies and treat them on a non-discriminatory basis.

The fifth title also provides for taking measures to facilitate the mutual recognition of qualifications. In view of supply of services, the SAA provides for a progressive liberalisation of the supply of services. The SAA allows for the associated country’s companies to provide services and for EU companies to provide services in the associated country. In line with this liberalisation, the parties shall permit the temporary movement of natural persons providing the service. This title also contains provisions on transport and the associated country’s obligation to align its legislative framework to the EU acquis in this area. With regard to movement of capital, the parties agree to ensure the free movement of capital as well as enable EU nationals to purchase real estate in the associated countries. The SAA envisages the full application of the EU’s free movement of capital and acquisition of real estate rules once a certain period of time after entry into force has elapsed.
Title 6: Approximation of Laws, Law Enforcement and Competition Rules. The sixth title requires the associated country to progressively align its legislative framework with the EU *acquis* and to implement and enforce the new laws. This title further contains rules on competition, intellectual, industrial and commercial property, consumer protection, and public procurement. As regards the latter, the parties decide to open up public contracts on the basis of non-discrimination and reciprocity.

Title 7: Justice, Freedom and Security. The seventh title has a focus on cooperation in the area of justice, freedom and security and the rule of law. It comprises provisions on asylum, migration, visas and boarder management, but also fight against corruption, crime and terrorism.

Title 8: Cooperation Policies. The eighth title provides for measures to be taken in order to promote sustainable economic growth and social development in the associated country. The country shall make efforts to establish a functioning market economy and to gradually stabilise its monetary and fiscal policies in line with the principles of the European Economic and Monetary Union.

Title 9: Financial Cooperation. The second but last title provides for the associated country to receive financial assistance from the EU and the European Investment Bank (EIB).

Title 10: Institutional, General and Final Provisions. In the final title, the institutional framework of the SAA is covered. It establishes a Stabilisation and Association Council of which the European Council, the Commission and the associated country’s government make part. This Council is to meet regularly and discuss the progress made as regards the provisions of the SAA. The decisions of the Council are binding. The Council is assisted by SAA committees, which may further create sectoral subcommittees. The final provisions also provide for the establishment of a Stabilisation and Association Parliamentary Committee, comprising both Members of the European Parliament and Members of the associated country’s National Parliament.

Overall, the SAP progresses at different speeds in different countries. Table 2 shows that bilateral relations between the EU and the countries of the region develop according to their individual pace of reforms. While some countries are already very much advanced (Croatia, Macedonia, Montenegro), others clearly lag behind (Kosovo, BaH).

Andras Inotai notes that the SAP might have contributed to aggravation of regional disparities rather than to promotion of regional integration.56 One the one hand, the

56 Inotai, Andras: *op. cit.*
EU has always insisted on the regatta principle while demanding regional integration and cooperation on the other. By insisting on strong conditionality and country-specific benchmarks, the EU has motivated the countries to individually progress as good and as fast as possible. This has led to some countries developing and implementing reforms at a faster pace without letting others to catch up. Then again, the SAP stipulates regional cooperation as one of its fundamental pillars. In summary, the conditions of the SAP/SAA further and hamper regional integration at the same time.

Table 2: Status of Bilateral Agreements Between the Western Balkans and the EU

<table>
<thead>
<tr>
<th></th>
<th>Croatia</th>
<th>Serbia</th>
<th>BAH</th>
<th>Montenegro</th>
<th>Macedonia (FYROM)</th>
<th>Albania</th>
<th>Kosovo (UN 1244)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Interim Agreement in Force</strong></td>
<td>Feb. 2010</td>
<td>July 2008</td>
<td>Jan 2008</td>
<td>June 2001</td>
<td>Dec 2006</td>
<td>-</td>
<td></td>
</tr>
<tr>
<td><strong>SAA in Force</strong></td>
<td>Feb. 2005</td>
<td>ratification started in June 2010</td>
<td>so far ratified by 25/27 MS</td>
<td>May 2010</td>
<td>April 2004</td>
<td>April 2009</td>
<td>-</td>
</tr>
<tr>
<td><strong>Date of Membership Application</strong></td>
<td>Feb. 2003</td>
<td>Dec. 2009</td>
<td>-</td>
<td>Dec. 2008</td>
<td>March 2004</td>
<td>April 2009</td>
<td>-</td>
</tr>
<tr>
<td><strong>Candidate Status</strong></td>
<td>June 2004</td>
<td>March 2012</td>
<td>-</td>
<td>2011</td>
<td>Dec. 2005</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td><strong>Accession Negotiations Started</strong></td>
<td>Oct. 2005</td>
<td>-</td>
<td>-</td>
<td>June 2012</td>
<td>-</td>
<td>-</td>
<td>-</td>
</tr>
<tr>
<td><strong>Accession Negotiations Concluded</strong></td>
<td>June 2011</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Sources: European Commission, DG Enlargement

*Montenegro became independent from Serbia in June 2006
In this context, the detailed analysis of the SAP clearly reveals its incongruence: it calls for regional integration and cohesion while at the same time hampers them with the ‘regatta principle’. The ‘regatta principle’ inherent in the SAP has to some extent fuelled competition between the candidate and potential candidate countries, rather than motivated them to engage in regional cooperation. In this respect, the CEFTA can be alternatively interpreted as a regional initiative very much necessary to counter regional disparities (in part) induced by the SAP. The CEFTA thus serves the EU’s preparatory intention in two ways: on the one hand it allows the countries to simulate the internal market situation and prepares them for the economic reality of the EU Single Market. At the same time, the CEFTA is also a measure to counter regional disparities caused by the ‘regatta principle’. The question arises whether the ‘regatta principle’ approach of the EU is adequate to enlarge to the Western Balkans, or whether it should not reconsider the ‘package solution’ it had applied in the previous enlargement round in 2004.

The arguments against and in favour of both approaches, ‘regatta principle’ and ‘package solution’, are numerous. The ‘package solution’ would discourage countries from reforming as their efforts are in vain as long as the other countries do not participate in reforms. The ‘regatta principle’ is an approach based on meritocracy, rewarding the countries on the basis of their individual progress. In the ‘package solution’, some countries will be punished for the failures of others. This thesis argues that the ‘package solution’ would be equally inadequate for the Western Balkans, as the countries are too different in their stages of political, economic and social development. However, the EU should be aware that in having made regional cooperation and good neighbourly relations a strict conditionality to join the EU, the ‘regatta principle’ inherent in the SAP is self-contradictory: it furthers and hampers regional integration at the same time.

With the SAP and its contractual instrument, the SAA, the EU relies on a traditional trade-oriented policy instrument in pursuing its goal of supporting peace and stability in the Western Balkans. The SAAs being very similar to the Europe Agreements already employed for the accession of the Central and Eastern European States, the EU copies an instrument invented for an already rather homogeneous region in a very different environment, such as the Western Balkan countries. The SAA is an instrument based largely on trade-related incentives, despite the fact that the EU does not have any significant trade interest in the Balkans. The overall trade volumes between the EU and the SEE countries remain at an almost negligible level, constituting less than 1 per cent

of the total EU imports and a little over 2 per cent of the total EU exports (see Table 3). All the Western Balkan countries are poor exporters with high negative trade balances. The region's total purchasing power is comparable to the one of the Czech Republic.

**Table 3: EU 27 Trade with Western Balkan Countries**

<table>
<thead>
<tr>
<th>Year</th>
<th>Imports</th>
<th>Share of total EU imports (%)</th>
<th>Exports</th>
<th>Share of total EU exports (%)</th>
<th>Balance</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Value (Mio. €)</td>
<td></td>
<td>Value (Mio €)</td>
<td></td>
<td>Value (Mio €)</td>
</tr>
<tr>
<td>2005</td>
<td>9,003</td>
<td>0.8</td>
<td>21,584</td>
<td>2.1</td>
<td>12,581</td>
</tr>
<tr>
<td>2006</td>
<td>11,573</td>
<td>0.9</td>
<td>25,204</td>
<td>2.2</td>
<td>13,631</td>
</tr>
<tr>
<td>2007</td>
<td>13,340</td>
<td>0.9</td>
<td>29,374</td>
<td>2.4</td>
<td>16,034</td>
</tr>
<tr>
<td>2008</td>
<td>13,928</td>
<td>0.9</td>
<td>33,029</td>
<td>2.5</td>
<td>19,101</td>
</tr>
<tr>
<td>2009</td>
<td>11,177</td>
<td>0.9</td>
<td>25,478</td>
<td>2.3</td>
<td>14,301</td>
</tr>
</tbody>
</table>

**Source:** WTO, Report of the European Union under the Decision WT/L/654, 12 July 2010, WT/L/799.

* Albania, BaH, Croatia, Kosovo, FYROM, Montenegro and Serbia.

The EU's main motivation in associating the SEE countries is political. The EU hopes to stabilise the war-ridden region by employing its well-tested strategy of exporting peace and stability via trade integration. To this end, and in contrast to the Europe Agreements, the SAP/SAA obliges the Balkan countries to engage actively in regional cooperation. Regional integration as a conditionality in the accession process is a new element absent in the previous enlargement rounds.

In this context, the main purpose of the CEFTA is revealed. The CEFTA serves three main goals: first, integrating the SEE economies and making them dependent on each other at the economic level reduces the risk of conflict. Second, the CEFTA aims at increasing economic growth via regional trade liberalisation and market integration. The individual SEE countries are too small to attract sustainable foreign investment, only their combined market share forms a market size big enough to attract foreign investments. And finally, regional trade integration and liberalisation prior to becoming EU members will have the benefit of making the countries better prepared for the EU
Single Market and thus more capable of coping with the competitive pressure within the EU.\textsuperscript{58}

2.2.3 SAAs and the WTO

Not all Western Balkan countries are members of the WTO.\textsuperscript{59} However, the EU is bound by its WTO membership and obliged to set up SAAs in conformity with WTO rules. Article 9 of the SAA between the EU and Serbia reads as follows:

"This Agreement shall be fully compatible with and implemented in a manner consistent with the relevant WTO provisions, in particular Article XXIV of the General Agreement on Tariffs and Trade 1994 (GATT 1994) and Article V of the General Agreement on Trade in Services (GATS).

Under the SAA, the Western Balkan countries individually establish free trade areas with the EU, notably only in restricted fields of trade such as industrial products, agriculture and fisheries. On that account, the EU as a WTO member is obliged to notify the establishment of a free trade area with another WTO member or third party to the WTO Committee on Regional Trade Agreements (CRTA). The EU has notified the SAAs as indicated in more detail in Table 4.

As long as the Interim Agreement of the SAA is in force, the EU and the associated country only enter into an FTA for goods. Once the SAA is fully in force, the FTA comprises goods and services and needs to be notified accordingly. All the SAAs have been notified under GATT Article XXIV for trade in goods and GATS Article V for trade in services.

\textsuperscript{58} Compare to an argument made by: Handjiski Borko (et al), \textit{op. cit.}, p. 45.

\textsuperscript{59} Albania and Croatia became WTO members in 2000; Moldova in 2001 and FYROM in 2003. BaH applied in 1999, and both Serbia and Montenegro filed their application in 2004. BaH, Serbia and Montenegro are not WTO members yet. Kosovo has not filed a WTO application yet.

Table 4: Notification of SAAs to the WTO

<table>
<thead>
<tr>
<th>SAA in force</th>
<th>EU-Croatia*</th>
<th>EU-Serbia</th>
<th>EU-BaH</th>
<th>EU-Montenegro</th>
<th>EU-FYROM*</th>
<th>EU-Albania*</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Coverage</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>Type of Agreement</strong></td>
<td>FTA + EIA</td>
<td>FTA</td>
<td>FTA + EIA</td>
<td>FTA + EIA</td>
<td>FTA + EIA</td>
<td></td>
</tr>
<tr>
<td><strong>Notified under Art.</strong></td>
<td>GATT XXIV, GATS V</td>
<td>GATT XXIV</td>
<td>GATT XXIV</td>
<td>GATT XXIV, GATS V</td>
<td>GATT XXIV, GATS V</td>
<td></td>
</tr>
</tbody>
</table>

Source: WTO61

Annotation: * = Country is a WTO member, FTA = Free Trade Area, EIA = Economic Integration Agreement (essentially means the SAA is in force)

In view of the non-reciprocal preferential treatment of the Balkan countries and their duty-free access to the EU market granted under the renewed waiver from the WTO,62 the SAAs and Interim Agreements allow „the continuation of the autonomous preferences where these provide more favourable conditions for the export of the goods originating in Croatia, the former Yugoslav Republic of Macedonia, Albania, Bosnia and Herzegovina, Montenegro and Serbia.”63

Trade barriers towards third parties (GATT Article XXIV:5)

Recalling that Article XXIV of GATT allows preferential trade agreements only if they do not raise barriers for trade with third countries, the question arises whether the arrangements stemming from the SAAs are damaging for the EU’s trade partners in the WTO. If so, the harmed WTO member may ask for compensation.

The question will be even more critical once the candidate countries and potential candidate countries join the EU. Pursuant to Article XXIV:5 of GATT, the enlargement of a customs union or free trade area must not lead to an increase of trade barriers as compared to the situation before such an enlargement.64 To give an example, before Sweden joined the EU in 1995, for certain goods it had lower tariffs than the EU’s Common External Tariff (CET). When acceding to the EU, Sweden had to adjust all its

61 Available at http://rtais.wto.org/UI/PublicAllRTAList.aspx, last accessed on: 4 May 2011.
tariffs to the CET, consequently raising the ones that were lower before accession. Sweden having to raise its tariffs constitutes a violation of Article XXIV:5 of GATT as it led to an increase of trade barriers (higher tariffs) as compared to the situation before enlargement. In this case, other WTO members are entitled to ask for compensation. Negotiations about these compensations pursuant to the enlargement of the EU’s customs union have not been concluded even for the 1995 enlargement to Austria and Sweden, let alone the enlargement rounds in 2004 and 2006. Regarding the recent enlargement, a number of trading partners of the EU claim that the 2004 EU enlargement raised trade barriers by extending the scope of its trade defence measures and its domestic regulations such as standards, sanitary and phytosanitary measures, etc. to the new Member States.\(^65\) The issue arising here is twofold: first, it is questionable whether the standards, technical regulations as well as sanitary and phytosanitary measures applied by the EU constitute trade defence measures. If they do, they are in themselves incompatible with WTO law and not only when they are extended to new member states. Secondly, it needs to be determined whether these additional measures constitute ‘regulations of commerce’ that are overall more restrictive as compared to those prior to the enlargement, pursuant to Article XXIV:5(a) GATT. Given the ambiguous wording of the aforementioned Article and the absence of case law on this matter,\(^66\) it is highly unlikely that this argument would hold in front of a WTO Panel.

Whether or not this is the case, the same complaint could also be brought regarding the SAAs. The SAA in its Title 6 (Approximation of Laws, Law Enforcement and Competition Rules) already obliges the associated countries to gradually align their legislative framework with the EU acquis, including their trade regimes and consequently their trade defence measures and domestic regulations. It can be argued that the SAAs, in extending the scope of the EU’s trade defence measures to the associated countries, have the same effect as enlargement. If this hypothesis is proven correct, the SAAs might be subject to complaints from other WTO members.

According to David Luff and Margarita Djordjevic, most WTO members agree that the EU enlargements have brought more benefits than downsides.\(^67\) This is because in acceding to the EU, most new member states had to substantially lower the vast majority of their customs duties rather than raise them. In addition, the enlargements

\(^{65}\) Ibid., p. 405.
\(^{66}\) Matsushita Mitsuo, Schoenbaum Thomas J, Macvroidis Petros C, op. cit., p. 563.
\(^{67}\) Luff David, Djordjevic Margareta, op. cit., p. 395.
were advantageous to the EU’s trading partners as they simplified and enhanced market access to the new member states as well as access to a larger EU internal market.\footnote{Ibid.}

This argument, as laid out above, cannot be applied to the SAAs. Whilst the accession of 12 new member states to the EU in 2004 and 2006 enlarged the territory of the EU customs union, the SAAs only establish free trade areas between the EU and the associated countries. This means that there is no need for the modification of customs duties. On the facts, it looks like the FTAs between the EU and its associated countries do not bring about any substantial benefits to the third party WTO members that might compensate for the extension of the scope of EU’s trade defence measures to the Western Balkans.

\section*{2.3 Implications of EU Enlargement for the CEFTA}

EU enlargement is the driving force behind the CEFTA. The CEFTA is one of the answers to the EU’s condition to enhance regional integration for further progress in the accession process. However, the countries of the region tend to interpret the process of EU accession more as a competitive game than understand the real need for regional cooperation. This means that the countries of the Western Balkans are very much concerned with their individual progress and further alignment with the EU rather than with regional integration and cohesion. Even though the SAAs in Title 3 (Regional Cooperation) oblige them to fully implement the CEFTA, regional integration does not yet receive the attention it should get.

All countries in the Balkans have an accession perspective and even though the timeframe of accession is neither clear nor predictable, it is evident that they will join at some point. Once they find themselves reunited in the EU, regional cooperation and cohesion is a must in order to fully exploit the benefits of the Single Market and avoid a Europe of different speeds.

\section*{2.4 Implication of the CEFTA on the EU Enlargement Process}

The implication of the CEFTA on the enlargement process has been rather limited until now. In interviews with European Commission officials, the CEFTA seems to have a low rate of visibility and influence. Commission representatives reiterate that efforts to make the CEFTA work more efficiently would be more than welcome. It has to be
noted again that the full implementation of the CEFTA is a provision in the SAAs with the individual CEFTA countries. In the course of the preparations of the Commission’s Opinion on Montenegro and Albania’s membership application delivered in November 2010, the CEFTA secretariat was a source of information thereon.  

3.1 Scope and Objective of the CEFTA

In 2006 Bulgaria, Romania\textsuperscript{70}, Albania, Bosnia and Herzegovina, Croatia, FYROM, Kosovo (under UNSCR 1244), Moldova, Montenegro and Serbia negotiated an agreement to amend and enlarge the original CEFTA and to form the CEFTA 2006. The negotiations were supported by the Stability Pact for South Eastern Europe and the European Commission.\textsuperscript{71} The ‘new CEFTA', also called CEFTA 2006, finally entered into force in July 2007.

CEFTA 2006\textsuperscript{72} aims at enhancing trade in goods and services, seeks to eliminate trade barriers between the signatories and attract investment to the region through fair, stable and predictable rules. The Agreement tries to harmonise its Parties’ regulatory framework with international standards. In doing so, it also covers issues such as the protection of intellectual property rights, competition rules and state aid. Article 1 of the CEFTA reads that the free trade area shall be established in a transitional period ending the latest on \textsuperscript{31st} December 2010. According to the CEFTA Secretariat, this goal has been achieved as by the end of 2010 about 90 per cent of all trade between

\textsuperscript{70} Even though Bulgaria and Romania still participated in the negotiations of a new CEFTA and signed the agreement, it was clear that by the time they join the EU (eventually in 2007), they would automatically cease to be members of the CEFTA.


\textsuperscript{72} Hereinafter, ‘CEFTA' shall mean ‘CEFTA 2006', unless indicated otherwise.
the Parties could be considered liberalised. However, given the fact that the quality of foreign trade statistics is very poor in the region, there is no hard evidence whether or not this objective has been indeed achieved.

The CETA is concluded for an indefinite period of time. The conditions for accession and possibilities to exit the Agreement are stipulated in Article 49 and 51 of the CETA respectively. “Accession to this Agreement may take place with the consent of all Parties.” A Party can withdraw from the CETA via a written notification and will automatically have to withdraw once it becomes a member of the EU. There are no specific membership requirements mentioned either in the Agreement or in the Decisions taken by the CETA Parties, since the CETA is an Agreement signed by its Parties and not an institution/organisation to which one could be a member.


74 Handjiski Borko (et al), Enhancing Regional Trade Integration in Southeast Europe, World Bank, Washington D.C., 2010, p. 18. Handjiski notes that “trade statistics in the SEE region reveal significant deficiencies in registering exports and imports by customs authorities, which is a serious handicap for conducting analysis as well as for policy making.”

75 Article 51 CETA.
76 Article 49 CETA.
77 Article 51 CETA.
3.2 The CEFTA Institutions

Chapter VII of the CEFTA comprises its functioning rules. Pursuant to Article 40 of the Agreement, a Joint Committee composed of representatives of the Member States and chaired by an annually rotating presidency is set up. The Members of the Joint Committee, usually represented by the trade ministers of the Parties, meet on a regular basis (obligatory at least once a year) and are tasked to supervise the implementation of the CEFTA. All decisions are to be taken by consensus. The Joint Committee is accompanied by three subcommittees: the subcommittee on agriculture, sanitary and phytosanitary issues, the subcommittee on customs and rules of origin, and lastly the subcommittee on technical barriers to trade and non-tariff barriers. The members have also formed working groups to discuss specific issues.

A permanent secretariat, located in Brussels, supports the Joint Committee in technical and administrative matters. In its 2011 work programme, the secretariat identified its main tasks to provide support to the Chair in Office, give technical advice and guidance, take care of the management and administration of the CEFTA and pursue promotional activities. The permanent secretariat was established in September 2008 and is financed jointly by the CEFTA parties and a number of donors, of which the main one is the European Commission. At the moment, the secretariat comprises three permanent staff members, recruited via international tenders.

The CEFTA also provides for a dispute settlement mechanism. Article 43 of the CEFTA provides for the formation of an Arbitral Tribunal to settle disputes between Parties that could have not been settled through direct consultation. This tribunal is to be set up according to Annex 9 to the Agreement and comprises three members. The structure of the CEFTA dispute settlement mechanism mirrors the WTO’s Dispute Settlement Understanding.

In summary, the institutional framework of the CEFTA is simple and in its very early stages. The secretariat has been operative for only three years, and taking into account its three full staff members its capacities are fairly limited. The simplistic institutional set-up of the CEFTA reveals the approach of negative integration only, mainly aiming at eliminating trade barriers via the reduction of duties rather than harmonisation.

3.3 Main Economic Elements of the CEFTA

The CEFTA is an example of economic regionalism in contrast to worldwide integration of national economies envisaged by the WTO. The main economic motivation and fundamental significance behind regional economic integration is to increase the actual or potential competition. More competition consequently leads to lower prices of goods and services, to a greater product variety and generally induces impetus for change and innovation.80

The process of economic integration refers to market integration and economic policy integration.81 This means that, on the one hand, different smaller markets merge into a single market with a single demand and supply curve. On the other hand, (national) economic policies are integrated, or at least discussed and optimally harmonised at the regional level. The concept of policy integration is much more complicated than market integration due to the fact that policy integration is always also a political process. The extent to which policy integration can be successful is strongly dependent on the political will of the individual parties concerned.

As regards the CEFTA, market integration is of crucial importance. The individual markets of the comparatively small states that have emerged after the break-up of Yugoslavia (apart from Albania) are too small to attract foreign capital and investment. In addition, all the states but Albania had already formed a single market prior to the dissolution of Yugoslavia, a fact that guarantees favourable preconditions for market integration, such as a common language, a similar culture and consumer preferences. Policy integration, on the other hand, is much more difficult to achieve. Due to the political situation and recent armed conflicts in the region, policy integration is a politically highly sensitive issue. To give an example, harmonised regulation is sometimes even a problem within a state. Bosnia and Herzegovina for instance, comprising of two separate entities (the Federation of Bosnia and Herzegovina and Republika Srpska) hardly manage to harmonise the legal framework between each other. Different business regulations in the two entities are a common problem in BaH impeding trade and investment. However, the CEFTA does oblige its members to engage in policy integration, at least in some areas. Chapter 4 of the CEFTA covers provisions on technical barriers to trade, and Article 13(3) reads as following:

“The Parties are strongly encouraged, without prejudice to the WTO Agreement on Technical Barriers to Trade, to harmonize their technical

81 Ibid., p. 6.
regulations, standards, and procedures for assessment of conformity with those in the European Community unless their use would be an ineffective or inappropriate means for the fulfilment of the legitimate objective pursued by the Parties.”

Economic integration can happen in different stages according to their degrees of intensity. This ‘stages approach’ was first defined by Bela Balassa in 1961. Table 5 presents the five Balassa stages:

**Table 5: Stages of Economic Integration**

<table>
<thead>
<tr>
<th>Stage</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Free Trade Area (FTA)</td>
<td>For imports from FTA members, tariffs and quotas are abolished. FTA members keep their individual external tariffs (and quotas) for third countries.</td>
</tr>
<tr>
<td>2. Customs Union (CU)</td>
<td>All tariffs and quotas within the CU are abolished. The CU members adopt a common external tariff in trade with third countries.</td>
</tr>
<tr>
<td>3. Common Market</td>
<td>A Common Market can be defined as a CU that also abolishes restrictions on factor movements, i.e. persons, capital and services. The Common Market attains the free movement of products, services and factors of production.</td>
</tr>
<tr>
<td>4. Economic Union</td>
<td>An Economic Union is a Common Market with a certain degree of policy harmonisation.</td>
</tr>
<tr>
<td>5. Total Economic Integration</td>
<td>Total Economic Integration unifies monetary, fiscal, social and counter-cyclical policies.</td>
</tr>
</tbody>
</table>


The CEFTA creates a free trade area, thus according to Balassa corresponds with the first stage of economic integration while the EU Single Market may be characterised as floating between stages three and five. The hybrid nature of the EU Single Market also points out to the weakness of Balassa’s stages approach; reality is not as clear-cut as Table 5 may suggest. Against this background, the CEFTA is clearly below the EU Single Market in terms of intensity of economic integration. In the context of the research question guiding this thesis, it must be noted that the CEFTA being an FTA covering goods only per definitionem cannot be a perfect preparation exercise for the EU Single Market demanding a far higher level of integration than an FTA.

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3.4 The CEFTA and the WTO

FYROM, as the chair of CEFTA, notified the agreement of and accession to CEFTA to the WTO in July 2006. It was notified as a FTA under Article XXIV of GATT covering goods only. It is again important to note that not all CEFTA members are WTO members. However, the text of CEFTA obliges all of its members, no matter whether they are members of WTO or not, to act in compliance with relevant WTO provisions. The CRTA has not reached a decision on the conformity of CEFTA with WTO rules. This means, that the ‘second track’ (see Chapter 1.2.1, page 16 for comparison) becomes applicable: if the CRTA does not reach a conclusion, WTO members may challenge the consistency of a FTA through panel proceedings under the Dispute Settlement Understanding. Until now, the CEFTA remains unchallenged.

This chapter established the CEFTA as a less intense or advanced form of regional economic integration in comparison to the EU Single Market. It was further concluded that in South Eastern Europe the market integration is of vital importance and easier to achieve than policy integration, which is hampered by the political reality in the post-war Balkans. In the EU, on the other hand, policy integration is very much advanced and central for the functioning of the Single Market. The institutional set-up of the CEFTA betrays an approach focused on negative integration, whereas a sophisticated institutional framework around the main decision-making triangle Commission-Council-Parliament governs the EU Single Market.

Chapter 4. Comparative Analysis of the CEFTA and the EU Single Market

This chapter now turns to a more detailed comparative analysis of the two similar, yet different trade integration models, focusing on particular chapters of the CEFTA and the EU Single Market acquis. In doing so, answers to the question on how far the CEFTA can be considered an appropriate preparation for the Single Market, will start to crystallize.

The methodology of the comparative analysis follows a two-step approach: first, criteria for successful preparation are established before applying them to the CEFTA to determine its success.

4.1 Criteria for Successful Preparation

In order to successfully prepare for the EU Single Market, the CEFTA would need to be as similar as possible to the EU Single Market acquis. This criterion, especially the phrase ‘as similar as possible’ needs further specification. Obviously, ‘as similar as possible’ does not mean ‘the same’. ‘As similar as possible’ acknowledges that CEFTA members, as developing countries, might not be able to commit to the same standards and degree of sophisticated trade integration legislation as EU members can. ‘As similar as possible’ also has to take into account that in certain areas, the CEFTA creates a free trade area and per definitionem cannot stipulate the same provisions as the EU Single Market. A free trade area focuses on the movement of products, while a single market allows for the free movement of all production factors, including labour, capital and products.84

In other words, even though the CEFTA should bring its members as close as possible to being able to meet their obligations arising from future membership in the EU Single Market, it cannot always be expected to do so with the entry into force of the Agreement. In the context of this analysis, ‘as similar as possible’ will mean that the CEFTA text needs

to cover – textually and substantively – the main elements of the EU Single Market, taking into account that certain elements will need a transitional period of time to be implemented. The following analysis will thus conduct a comparative analysis of the CEFTA text and the EU Single Market *acquis*, establishing whether the provisions are either (1) very similar, (2) only partly similar or whether there is (3) no similarity at all, and, within what time frame they are to be implemented.

(1) **Very similar:** The CEFTA provides for the realisation of the EU Single Market *acquis* (a) from the date of the Agreement's entry into force onwards or (b) within a clearly set time-frame.

(2) **Partly similar:** (a) The CEFTA provides for the partial realisation of the EU Single Market *acquis*, but thrives to complete realisation within a reasonable transitional period of time, including concrete deadlines. (b) The CEFTA provides for the partial realisation of the EU Single Market *acquis*, without the intention for further alignment in the future.

(3) **No similarity:** The CEFTA fails to include a substantive part of the EU Single Market *acquis*.

The EU Single Market is built on the four economic freedoms: free movement of goods, services, workers and capital. The four freedoms are considered to be the central economic corner stone of the Single Market, with other policies seen as supplementary to the economic priorities of market building. The comparative analyses of the two trade integration models will thus be conducted in the following areas: the analysis will first focus on the free movement of goods, persons, services and capital. Discussion will then turn to several functional and more specific provisions, those being public procurement and intellectual property rights, competition policy as well as agricultural policy.

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85 The webpage of the EU Directorate General for the Single Market reads: "The cornerstones of the single market are often said to be the 'four freedoms' - the free movement of people, goods, services and capital. These freedoms are enshrined in the EC (sic! Treaty and form the basis of the single market framework." Available at http://ec.europa.eu/internal_market/top_layer/index_1_en.htm, last accessed on: 4 May 2011.

4.2 The Four Economic Freedoms

4.2.1 Goods and Industrial Products

The first chapter of the CEFTA covers trade in goods. Article 2(1) of the CEFTA introduces the EU’s Combined Nomenclature of goods to uniformly classify all goods in trade between the CEFTA members. With this regard, it is worth noting that the Combined Nomenclature used by the EU itself is a translation of the Harmonised System of Classifications developed by the World Customs Organisation.

Even though the CEFTA aims to eventually abolish all customs duties within the bloc, the Agreement recognizes that this can only be achieved progressively within a transitional period of time. To that end, Article 2 CEFTA lays down the rules on how to define countries’ basic duty as a starting point from where the gradual reduction of tariffs should begin. Article 1 CEFTA provides for the transitional period to end on 31 December 2010. From 2011 onwards, all trade in the scope of the Agreement should have been fully liberalised.

With regard to reducing non-tariff barriers, Article 3 CEFTA abolishes all current and new quantitative restrictions on imports and exports as well as measures having equivalent effect in trade between the members. The abolition of quantitative restrictions and measures having equivalent effect is also to be found in the Treaty on the Functioning of the European Union (TFEU) Articles 34 and 35. In the area of prohibiting quantitative restrictions, the CEFTA provisions are almost identical to the provisions contained in the TFEU.

As regards exports to other CEFTA members, all customs duties, charges having equivalent effect and export duties of a fiscal nature are abolished (CEFTA Article 4). Again, there is an overlap with the European Single Market legislation in TFEU Article 30. However for imports, pursuant to Article 5 CEFTA, no new customs duties or charges having equivalent effect and export duties of a fiscal nature are to be introduced and those already applied must not be increased.


88 For further information on the Harmonised System of Classifications (HS) see http://www.wcoomd.org/hsharmonizedsystem.htm, last accessed on: 4 May 2011.
Chapter 2 CEFTA covers industrial products originating in the Parties’ countries. The Parties are to abolish all customs duties on imports, charges having equivalent effect and import duties of fiscal nature in trade between them upon the date of entry into force of the CEFTA. Annex 2 to the CEFTA provides for certain exceptions. The trade in industrial products between Macedonia on the one hand and Moldova as well as Kosovo on the other hand was fully liberalised in a transitional period of time from the entry into force of the CEFTA until 31 December 2008. There is no mention of exports in view of industrial products, like in Article 35 TFEU.

Article 17 of the CEFTA, finally, provides a general exception clause, very similar to Article 36 TFEU\(^89\). In the CEFTA, the prohibition or restriction of imports, exports and goods in transit can be justified on grounds of public morality, public policy or security, the protection of health and life of humans, animal or plants, the protection of national treasures possessing artistic, historic or archaeological value, protection of intellectual property or rules relating to gold or silver or the conservation of exhaustible natural resources.

**Non-Tariff Barriers: Technical Regulations and Standards**

With the abolishment of tariffs and quotas, technical regulations and standards are likely to become the next prominent obstacles to further trade integration in the CEFTA area.\(^90\) So, as countries have less opportunities to take protectionist measures in the form of import tariffs and quotas, they tend to increasingly disguise protectionist measures via technical barriers to trade and sanitary and phytosanitary measures.\(^91\) This trend was also confirmed in the EU. The European Court of Justice contributed significantly to the elimination of technical barriers to trade with its famous *Dassonville*\(^92\) judgement and later the *Cassis de Dijon*\(^93\) judgement. Nevertheless, technical barriers remain a major impediment to the free movement of goods within the EU.\(^94\)

\(^89\) Article 36 TFEU provides for possible derogations from Articles 34 and 35 TFEU on grounds of public morality, public policy or public security; the protection of health and life of humans, animals or plants; the protection of national treasures possessing artistic, historic or archaeological value; or the protection of industrial and commercial property.

\(^90\) Handjiski Borko (et al), *op. cit.*, p. xii.


\(^94\) Barnard Catherine, *op. cit.*, p. 95.
The CEFTA members agreed to apply the WTO Agreement on Technical Barriers to Trade, even though half of the CEFTA Parties are not WTO members yet. The Parties undertake to

“identify and eliminate unnecessary existing technical barriers to trade (…)”\(^{96}\)
and “not to introduce new unnecessary technical barriers to trade.”\(^{97}\)

Furthermore, the Agreement establishes a subcommittee on non-tariff barriers, which is tasked with overseeing the process of eliminating unnecessary technical barriers to trade. The CEFTA members have an obligation to notify any draft text for new technical regulation to the subcommittee. The subcommittee is further responsible to decide on remedies should any Party adopt a measure constituting an unnecessary technical barrier to trade. Article 13(c) CEFTA reads

“The Parties are strongly encouraged (…) to harmonize their technical regulations, standards and procedures for assessment of conformity with those in the European Community (…).”

This citation again confirms the preparatory notion of the CEFTA for the EU. Despite the crucial importance of eliminating technical barriers to trade, Boris Handjiski notices that the legal language in this area is quite weak.\(^{98}\) This ‘weakness’ of the legal language is the main difference between the CEFTA and the EU Single Market acquis. While the EU has enshrined the principle of mutual recognition in its case law\(^{99}\), the CEFTA only encourages the parties to harmonise their technical regulation and only obliges the CEFTA Parties to enter into negotiations on mutual recognition before 31 December 2010.\(^{100}\) The report of the Serbian CEFTA Chairmanship mentions that bilateral initiatives among BaH and Serbia, and BaH and Croatia to conclude a Protocol on mutual recognition of the conformity assessment have been reported during the Serbian Chairmanship in 2010.\(^{101}\)

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95 Article 13(1) CEFTA.
96 Article 13(2) CEFTA.
97 Article 13(3a) CEFTA.
98 Handjiski Borko (et al), op. cit., p. 25.
100 Article 13(3c) and 13(4) CEFTA.
4.2.2. Services

It will be recalled that the CEFTA was notified to the WTO under GATT Article XXIV as covering trade in goods only. Chapter 6 of the CEFTA, however, covers so-called ‘new trade issues’ and among them also provisions on services. Pursuant to Article 27, the CEFTA Parties

“will gradually develop and broaden their cooperation with the aim of achieving a progressive liberalisation and mutual opening of their service markets, in the context of European integration, taking into account the relevant provisions of the GATS and commitments entered into under GATS by Parties being WTO members.” (emphasis added)

The same chapter also includes an evolutionary clause aimed at upgrading the FTA within the scope of trade in goods only to a FTA covering both goods and services in accordance with Article V of GATS. The text of the Agreement mentions no time frame until progress should take place in the area of services. Here, the CEFTA’s provisions are far away from the EU Single Market acquis. The CEFTA does not include a legal obligation to liberalise services, nor does it oblige the Parties to develop a plan on how to possibly liberalise services in the long run. The CEFTA only formulates the goal to do so in the context of European integration (see Article 27 CEFTA as set out above).

However, one has to take into account that the free movement of services is not yet too advanced in the EU itself. The asymmetric liberalisation of goods and services is highly problematic as services nowadays account for more the 70 per cent of the EU’s GDP. The controversial Services Directive (123/2006/EC) tries to codify previous case law in the area of free movement of services. The Services Directive was to be implemented by EU Member States by 28 December 2009 at the latest with the aim to move in the direction of completing the Single Market for services. By June 2010, 12 member states had yet to fully implement the Services Directive.

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102 Article 29 CEFTA.
104 Barnard, Catherine, op. cit., p.348.
4.2.3 Persons

CEFTA does not envisage the free movement of persons. Labour migration takes place in the CEFTA area despite few formal mechanisms allowing and encouraging the mobility of workers. The EU, on the other hand, chose to allow the free movement of persons, subject to conditions, from its very beginning. The Treaty of Rome (1957) establishing the European Economic Community in its Article 3(c) reads

“(…) the activities of the Community shall include (…) the abolition, as between Member States, of obstacles to freedom of movement for persons, services and capital.”

Today in the Treaty of Lisbon and back then in 1957 in the Treaty of Rome, the scope of the provisions on free movement of persons remains limited. EU Law does not provide for general right of free movement of all people: to qualify, the individual has to be both a national of a member state, and be engaged in an economic activity as a worker (Articles 45-48 TFEU), self-employed person (Article 49-55) or as provider or receiver of services (Articles 56-62 TFEU). From the Treaty of Rome to the Treaty of Lisbon, the European Court of Justice had gradually broadened the scope of application of the right to free movement within the European Union. Its latest development is the application of Union citizenship, introduced with the Treaty of Maastricht in 1992, “destined to be the fundamental status of national of the Member States (…)”. In conclusion, the EU did not provide for free movement of (all) persons from the start. The right to free movement in the EU was established gradually through extensive ECJ jurisprudence.

An FTA has the primary purpose to allow the free flow of goods between members by reducing tariff and non-tariff barriers to trade. However, many FTAs and CUs include provisions on free movement of labour and even capital (i.e. Asia-Pacific Economic Cooperation (APEC), ASEAN Free trade Area, Caribbean Community (CARICOM), East Africa Community (EAC), Mercado Comun del Sur (Mercosur), North American Free Trade Agreement (NAFTA)).

106 Handjiski Borko (et al), op. cit., p. 54.
108 Barnard, Catherine, op. cit., p. 223.
110 Compare to chapter 3.3 'Main Economic Elements of CEFTA' and the Balassa stages.
111 It has to be added that just because these RTAs include provisions on cross-border movement of labour, it does not automatically mean that these rights guaranteed in the Agreements are also appropriately
Free movement of persons is a technically complex and politically sensitive issue due to its being intertwined with national sovereignty, immigration and third-country nationals, as well as social and health security and, consequently with public finances. Among the many reasons why the implementation of free movement of persons is difficult and delicate, the most important ones can be summarised as follows:

- Not only countries liberalising free movement of persons within their territories are concerned, but it also requires the consideration of so-called ‘third-country nationals’.\textsuperscript{112}

- In order for labour to move freely, qualifications need to be mutually recognised.

- Free movement of persons/labour comes with the question who takes over the financial burden for the emigrants, and the delicate question of social security, pensions and social benefits is connected herewith.

- High unemployment throughout the region may hinder labour mobility.

- It is difficult for the parties to agree on free movement of labour, as the benefits of labour mobility often spread unequally across member countries or within each country. Labour mobility may sometimes even contribute to regional disparities rather than to regional cohesion.\textsuperscript{113} “If FTAs encompass countries with different income levels, there is likely to be net migration to the higher-income states.”\textsuperscript{114}

- Free movement of persons requires positive integration. A number of institutions need to be set up; i.e. for individuals whose mobility rights have been violated.

It is not unusual for the free movement of persons to be implemented with a considerable time lag, on many occasions several years after free trade in goods.\textsuperscript{115} Yet, in the Balkans it might be easier to achieve due to the legacy of the Socialist

\textsuperscript{112} Ibid., p.xiv.

\textsuperscript{113} In order to remedy the regional disparities arising from free movement of labour, the EU set up the structural funds.

\textsuperscript{114} Handjiski Borko (et al), \textit{op. cit.}, p. 79.

\textsuperscript{115} Handjiski Borko (et al), \textit{op. cit.}, p. 22.
Federal Republic of Yugoslavia, that presupposes a common language, 40 years of a unified economic and political space, and inter alia similar education systems.\textsuperscript{116}

4.2.4 Capital

The CEFtA does not cover free movement of capital or the liberalisation of capital markets in the region. However, chapter 6 of the CEFtA, named ‘New Trade Issues’, includes investment. The Parties have concluded a number of bilateral investment agreements aimed at promoting and reciprocally protecting investments.\textsuperscript{117} These bilateral investment agreements continue to be valid pursuant to Article 30 of the CEFtA. Article 31 CEFtA stipulates that the Parties shall create and maintain stable, favourable and transparent conditions for investors of the other Parties and admit investment from the Parties in accordance with their domestic laws and regulations. Article 32(3) CEFtA contains a ‘national treatment’ clause:

\textit{“The Parties shall provide, as regards the establishment and operation of other Parties’ investments, a treatment no less favourable than that granted by each Party to investments made by its own investors, or than that granted by each Party to the investments by investors of any third State, if this latter treatment is more favourable.”} (emphasis added).

With regard to free movement of capital and the liberalisation of their financial markets, the CEFtA countries clearly lag behind the EU. The CEFtA furthermore does not include any provision that would remedy this situation. This is worrying as a stable financial market with intelligently regulated access to capital is vital for countries in transition. On that note, it has to be mentioned that in the EU the level of liberalisation of capital and the opening of the financial market herewith connected was not accompanied by sufficient regulation either. This account was proven correct in the light of the recent economic and financial crisis. The EU only started to adequately regulate its financial markets after the financial crisis starting in 2007 forced it to, and is now in the process of preparing and passing vast amounts of legislation. It agreed on a new supervisory structure (the European Banking Authority (EBA), the European Insurance and Occupational Pensions Authority (EIOPA), the European Markets and Security Authority (ESMA), the European Systemic Risk Board (ESRB)) and, inter alia, proposed legislation on Alternative Investment Fund Managers (i.e. hedge funds)\textsuperscript{118}

\begin{itemize}
\item \textsuperscript{116} Ibid., p. xiv and p. xv.
\item \textsuperscript{117} See Annex 6 to the CEFtA.
\end{itemize}
and regulation of insurance companies (Solvency II).\textsuperscript{119} However, there are many more proposals to come. The Commission is currently working on the implementation of Basle III,\textsuperscript{120} legislation concerning market abuse, corporate governance, European credit rating agencies, commodity derivatives, deposit guarantees, the amendment of the Markets in Financial Instruments (‘MIFID’) Directive\textsuperscript{121} and directors’ remuneration and capital requirements.\textsuperscript{122}

It can be observed that, whilst the expansionary dynamic of the liberalisation of the capital movements and financial markets dominated the EU’s development in this area up till the financial crisis, it has now taught EU regulators to increasingly control the seemingly unrestricted movement of capital and financial services. With all the EU legislation to come in this area, it will become more difficult to get access to capital. The CEFTA Parties have one lesson to learn from the EU’s experience with the financial crisis: the opening of financial markets and the full liberalisation of capital movements needs to be accompanied with adequate regulation.

Furthermore, it is important to distinguish between free movement of financial capital and payments in general. To that end, the CEFTA fully liberalises payments. Article 16 CEFTA reads:

\textit{“Payments in freely convertible currencies relating to trade in goods between the Parties and the transfer of such payments to the territory of the Party, where the creditor resides shall be free from any restrictions.”}

In fact, the Treaty of Rome also liberalised payments between the EU members right away, while liberalising the capital movement only to the extent necessary for the functioning of the customs union. Capital movement was fully liberalised only in 1988 in Directive 88/361/EEC.\footnote{Council Directive 88/361/EEC of 24 June 1988 for the implementation of Article 67 of the Treaty, OJEU, L 178.}
4.3 Functional Provisions

4.3.1 Public Procurement

The CEFTA obliges its members to open up the government procurement market. Article 35 CEFTA decrees that

“each Party shall no later than 1 May 2010 ensure the progressive and effective opening of its government procurement market so that, with respect to any relevant laws, regulations, procedures and practices, the goods, services and suppliers of the other Parties are granted a treatment no less favourable than that accorded to domestic goods, services and suppliers.” (emphasis added)

Public procurement is an essential part of the EU Single Market, as contracts awarded by public authorities account for a substantial part of total economic activity. In terms of market integration, it is therefore of high importance that firms from all EU Member States can compete for public contracts in the EU, as well as the CEFTA Parties for public contracts in the CEFTA region. This implies that principles of transparency, equal treatment and non-discrimination must be applied in all public procurement procedures. In the EU, this is guaranteed via Directive 2004/17/EC coordinating public procurement in the areas of water, energy, transport and postal services and Directive 2004/18//EC on public work contracts, public supply contracts and public service contracts.

The CEFTA’s provisions on public procurement are similar to the EU ones as they cover all laws, regulations, procedures or practices regarding procurement by central or sub-central government entities and further include a non-discrimination clause. However, the CEFTA chose not to apply the WTO Agreement on Government Procurement.

4.3.2 Intellectual Property Rights

The CEFTA ensures the protection of intellectual property pursuant to Article 37 of the Agreement. It obliges its Parties to grant and ensure adequate and effective protection as well as enforcement of intellectual property rights in accordance with international standards, in particular with the WTO Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS). Annex 7 to the CEFTA includes 25 international conventions related to intellectual property, to which all the Parties to the CEFTA are obliged to accede no later than by 1st May 2004.

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124 Article 34 CEFTA.
125 Article 35(2) CEFTA.
Article 118 TFEU establishes measures for the creation of European intellectual property rights and to provide uniform protection of intellectual property rights throughout the EU. With regard to the similarity of the CEFTA with the EU *acquis* in this area, the intellectual property rights provided for in the CEFTA largely correspond with the provisions of the TFEU.

### 4.3.3 Competition Policy

Chapter 5 of the CEFTA comprises several articles on competition rules. The CEFTA Articles 19 to 21 cover state monopolies, competition rules for undertakings and state aid. As regards state monopolies, the CEFTA Parties

> “shall adjust any State monopolies of a commercial character or State-trading enterprises so as to ensure that, in accordance with WTO provisions, no discrimination exists between enterprises of the members regarding the conditions under which products are marketed.”

For competition rules concerning both undertakings\(^\text{127}\) and state aid\(^\text{128}\), the CEFTA prohibits any behaviour that distorts competition and is incompatible with the proper functioning of the agreement as far as it may affect trade between the parties. The CEFTA further states that any practice contrary to Article 20 and 21 shall be assessed on the basis of the principles of competition rules applicable in the EU, in particular Articles 101, 102, 106 and 107 of the TFEU. In other words, the CEFTA essentially imports the EU’s competition policy, including relevant ECJ jurisprudence.

### 4.3.4 Agriculture

In many countries, the market for agricultural products has been a very sensitive sector ever since the vast industrial changes in the 20\(^\text{th}\) century and traditionally subject to state subsidies and defensive trade policies.\(^\text{129}\) The EU’s Common Agricultural Policy (CAP) is a good example for this trend. From its very beginning, the CAP has been controversial

\(^{126}\) Article 19 CEFTA.

\(^{127}\) Article 20 CEFTA.

\(^{128}\) Article 21 CEFTA.

\(^{129}\) Paarlberg Robert, “Agricultural Policy Reform and the Uruguay Round. Synergistic Linkage in a Two-Level Game?”, in: International Organization, Vol. 51/3, 1997, p. 417. Paarlberg argues further, that countries are more likely to engage in strongly subsidizing their agricultural sector, when the agricultural sector develops much slower than the industrial sector and thus the first becomes highly disadvantaged in comparison to the latter. This is the case in i.e. Germany and Japan, however less the case in i.e. the US.
and criticised both by third countries\textsuperscript{130}, and from within the EU.\textsuperscript{131} Over time, the CAP had become no longer sustainable for a number of reasons: first, it became too costly for the EU; second, it had severe consequences for the environment as the CAP subsidised too high a volume of production and thus supported the unsustainable exploitation of land; and thirdly, after the WTO Uruguay round negotiation were concluded, the EU was forced to comply with its negotiated commitments in the Agreement on Agriculture. During the Uruguay round, the EU was essentially obliged to reform the CAP and significantly reduce its subsidies as well as its tariffs on agricultural products.\textsuperscript{132}

For the CEFTA, chapter 3 on agriculture is of particular importance as most South Eastern European economies have a significant agricultural sector.\textsuperscript{133} The CEFTA in its Article 10 largely liberalises the trade in agricultural products by either abolishing or reducing customs duties on imports, charges having equivalent effect, and other import duties of the fiscal nature on these products according to Annex 3. Annex 3 to the CEFTA thus includes a table of duties and quotas for each CEFTA member, specifying the concessions for agricultural products. In view of export subsidies Article 11(3) CEFTA reads:

“\textit{(…)} all Parties shall refrain from the use of export subsidies, and abolish such existing subsidies, in their mutual trade.”

A sub-committee on agriculture, sanitary and phytosanitary measures is to meet annually and further facilitate trade in agricultural products within the region. The sub-committee is tasked to ensure that sanitary and phytosanitary measures as well as other technical regulations do not unjustifiably restrict trade in agricultural products.\textsuperscript{134}

There is however no provision for a common agricultural policy. Each member country may independently structure its agricultural policy, only with an obligation to inform the Joint Committee about changes that may affect the trade in agricultural products with other member countries.


\textsuperscript{131} Franz Fischler, European Commissioner for Agriculture and Rural Development writes, with regard to the Commission reform proposal on CAP ‘Agenda 2000’: “To put it plainly – without reforms, the CAP is likely not only to lose public support but also its capacity to help farmers.” (Introduction to Piccini Antonio, Loseby Margaret, \textit{op. cit.}, p. xv.)


\textsuperscript{133} Handjiski Borko (et al), \textit{op. cit.}, p. 27.

\textsuperscript{134} http://www.cefta2006.com/cefta-2006-sub-committees, last accessed on: 4 May 2011.
In conclusion, the CEFTA provisions on agricultural products differ from the EU’s agricultural policy. The EU pursues a rather protectionist common agricultural policy towards third countries, which relies, *inter alia*, on export subsidies (even after the recent reforms). The CEFTA countries on the other hand do not engage in a common agricultural policy. The agreement largely eliminates tariffs and quotas on agricultural products within the bloc,\(^{135}\) and abolishes export subsidies within the FTA. Further liberalisation was achieved through an additional protocol on agricultural products, signed in February 2011 by all the CEFTA members other than BaH and Kosovo, after two years of negotiations. With this additional protocol, the signatories abolished all customs duties on imports, charges having equivalent effect, and import duties of the fiscal nature in trade between them on further agricultural products, leaving only a small portion of trade in agricultural products to bilateral concessions.\(^{136}\)

As regards sanitary and phytosanitary measures, the CEFTA countries chose to be bound by the WTO Agreement on the Application of Sanitary and Phytosanitary Measures.\(^{137}\) Furthermore, CEFTA provides for the conclusion of agreements on harmonisation or mutual recognition in these matters; however, with this regard the Agreement does not lay down any specific deadlines.

In conclusion, the CEFTA does not copy the model of the EU’s Common Agricultural Policy in any of its provisions. The explanation for this circumstance is straightforward: first of all, unlike the EU, the CEFTA Parties do not have the budget to finance a common agricultural policy. Next, export subsidies on agricultural products as well as domestic subsidisation to the extent where it distorts international trade are prohibited in the framework of WTO law. This means that the CEFTA Parties who already adhered to the WTO cannot introduce export subsidies on agricultural products. Furthermore, the CEFTA Parties who are not members of the WTO yet, aspire to adhere. In their effort to do so, even the non-WTO members of the CEFTA cannot introduce export subsidies of any sort, including on agricultural products, as they are prohibited to do so according to the WTO Agreement on Subsidies and Countervailing Measures and the Agreement on Agriculture.

\(^{135}\) Handjiski Borko (et al), *op. cit.*, p. 27.
\(^{137}\) Article 12 CEFTA.
4.4 Discussion of the Results of the Comparative Analysis

The comparative analysis of the CEFTA and the EU Single Market *acquis* is summarised in Table 6 below. Out of the eight chapters under analysis, a majority exhibit partial or close similarities between the provisions in the CEFTA and the EU Single Market *acquis*. Only three chapters were found to almost completely lack in similarity. In the first cluster of the analysis, *viz* the four freedoms of movement at the very heart of the EU Single Market, close similarity is only to be found in the area of free movement of goods. The CEFTA chose, unilaterally and without all Parties being members of the WTO yet, to apply the relevant WTO agreements in all areas analysed with one exception; it will not be bound by the WTO Agreement on Government Procurement, albeit it decided to liberalise its public procurement sector.

**Table 6: Similarity Assessment of CEFTA and the EU Single Market acquis**

<table>
<thead>
<tr>
<th>AREA</th>
<th>SIMILARITY ASSESSMENT</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Free movement of GOODS</td>
<td></td>
</tr>
<tr>
<td>a. Elimination of tariffs barriers</td>
<td>a. Very similar</td>
</tr>
<tr>
<td>b. Elimination of non tariff-barriers (technical barriers to trade)</td>
<td>b. Partly similar</td>
</tr>
<tr>
<td>2. Free movement of SERVICES</td>
<td>Partly similar</td>
</tr>
<tr>
<td>3. Free movement of PERSONS</td>
<td>No overlaps</td>
</tr>
<tr>
<td>4. Free movement of CAPITAL</td>
<td>No overlaps</td>
</tr>
<tr>
<td>5. Public Procurement</td>
<td>Very similar</td>
</tr>
<tr>
<td>6. Competition Policy</td>
<td>Very similar</td>
</tr>
<tr>
<td>7. Intellectual Property Rights</td>
<td>Very similar</td>
</tr>
<tr>
<td>8. Agriculture</td>
<td>No overlaps</td>
</tr>
</tbody>
</table>

The comparative analysis showed that, overall, the CEFTA is a good preparation for the EU Single Market. Especially in the area of free movement of goods, the CEFTA appropriately prepares its Parties for future membership in the EU. Also, in the areas of public procurement, competition policy and intellectual property rights, the CEFTA provides for the realisation of the EU Single Market *acquis* from the date of the Agreement’s entry into force onwards. In the area of competition policy, the CEFTA even copies the EU’s provisions. In the area of free movement of services, however, the CEFTA lags behind the EU’s development, even when taking into account the fact that the EU itself is yet to fully liberalise services. Given the level of complexity of free movement of
services, it cannot be expected from the CEFTA that it decrees more measures than the present obligation to gradually develop the liberalisation of services.

However, the CEFTA leaves out two areas completely: free movement of persons and capital. Here, the CEFTA is not an appropriate preparation for the EU Single Market. All CEFTA Parties have relatively small populations and geographic areas. This makes trade, foreign direct investment and migration the key drivers of increased competition, creating larger markets and exploiting economies of scale that would sustain economic growth in the Balkans. In addition, these are two areas where the Balkan countries have a relative advantage in comparison with other regional trade integration projects. Both capital movement and labour migration are already happening in the South Eastern Europe, however without formal mechanisms to regulate and encourage it. The legacies of Ex-Yugoslavia, a common past and common language are significant advantages in formally implementing labour migration. As regards the liberalisation of capital movement, this thesis argues that liberalising the capital movement between the CEFTA Parties and thus its financial markets would help the Western Balkan countries to increase stability and attract investment. This hypothesis will be further explored in chapter 5.2 ‘Should the CEFTA envisage Free Movement of Capital?’

Every form of trade integration needs a minimum level of harmonisation to be successful. Trade integration will not work on a strict non-discrimination-only basis without a minimum will to harmonise; this is also seen in the WTO. The absence of harmonisation will, in one form or another, distort free trade. In this regard, the CEFTA obliges its Parties to undertake some harmonisation efforts, i.e. in the area of non-tariff barriers or sanitary and phytosanitary measures. However, the legal language of these provisions is weak and might not be sufficient to actually prepare the ground for harmonisation in these crucial areas, i.e. due to the absence of concrete deadlines by which the negotiations on harmonisation have to start. In addition, where the CEFTA stipulates harmonisation, it does so by applying external standards, such as WTO

138 Handjiski Borko (et al), op. cit., p. 56.
139 For labour migration, see Handjiski Borko (et al), op. cit., p. 54.; for movement of capital: Interview with ERSTE Group Bank AG, Vienna, Department ‘Projects & CEE Governance’, 29 April 2011 and chapter 5.2 ‘Should CEFTA Envisage Free Movement of Capital?’
140 The WTO Agreement on Sanitary and Phytosanitary Standards is a good example to illustrate the need for harmonization in the framework of the WTO. In Article 3 of the SPS Agreement, WTO members are encouraged to base their measures on international standards, guidelines and recommendations, where they exist. This facilitates harmonization, and in doing so, food safety, animal and plant health protection can be achieved without unduly restricting international trade. See http://www.wto.org/english/tratop_e/spse/spseq1_e.htm, last accessed on: 4 May 2010.
agreements or the EU acquis. On that note, Handjiski et al. observe that “(i)t seems to be more difficult for the SEE countries to pool their sovereignty over ‘most’ of their trade policy, however it tends to be easier to adopt external benchmarks imposed by the EU.”\(^{141}\) What is missing in the CEFTA is an intrinsic motivation to harmonise. To that end, this thesis argues that reforms are always more successful if they are intrinsically motivated rather than extrinsically. If the CEFTA Parties were able to take political ownership over their FTA as a trade instrument serving their interest irrespective of its preparatory notion for the EU, this would significantly increase the success of the CEFTA.

Finally, discussion turns to the complex relation between the CEFTA, SAAs and EU acquis. The CEFTA Parties should be ready to commit to the same level of trade liberalisation as they do in their SAAs. Both the SAA and the CEFTA pursue the same goal: to prepare the countries for eventual EU membership. The EU has made it clear that a positive track record on implementing both the SAA and the CEFTA is a condition for EU accession. In this regard, it seems incoherent that the countries refused to commit to certain issues in the framework of the CEFTA to which they did commit in the SAAs. It can be argued, of course, that it would be difficult for i.e. Croatia to commit to the same provisions it did with the EU as with Kosovo, as two very difficult situations are at stake. However, taking into account that the EU has reiterated on a number of occasions that the future of all countries of the Western Balkans lies within the EU, the CEFTA Parties are advised to reconsider their purely bilateral approach with the EU. They should adopt a long-term regional approach, envisaging that they will all find themselves reunited in the EU Single Market one day.

\(^{141}\) Handjiski Borko (et al), op. cit., p. xvi.
Chapter 5. Lessons from the Comparative Analysis of the CEFTA and the EU Single Market acquis

The comparative analysis in chapter 4 has shown that the CEFTA is an appropriate preparation for the EU Single Market in all its substantive areas, but for two exceptions: free movement of persons and capital. Chapter 5 will now be dedicated to the question whether or not the CEFTA should envisage further integration in these two areas, either via making use of one of the ‘evolutionary clauses’ or possibly even via an amendment to the current Agreement in force.

5.1 Should CEFTA Envisage Free Movement of Workers?

Handjiski et al. at the World Bank identify a number of reasons why the CEFTA is advised to envisage free movement of skilled labour. Negotiating agreements to liberalise skilled labour migration is less difficult to achieve because the numbers are relatively small while economic and public finance gains to receiving countries may be greater than the costs (social benefits) involved. In addition, skilled labour mobility generates positive externalities in the host countries.142 Besides the many difficulties and costs that labour market integration poses in general, the situation in the CEFTA encompasses several favourable conditions for skilled labour migration. Firstly, the common language and similar education systems as a heritage from the common past in the Social Federal Republic of Yugoslavia facilitate the mutual recognition of qualifications.143 Given the similar income levels in the CEFTA area (with the exceptions of Moldova and Kosovo at the low end and Croatia at the opposite one), free movement of labour is less likely to increase regional disparities as there is less chance for labour mobility from low income states to high income states.144

142 Ibid., pp. 80-81.
143 Ibid., p. 80.
144 Ibid.
Overall, the World Bank study finds that there is considerable potential for improving labour productivity within the region by relocating workers from low to higher productivity settings. Given small population numbers in the CEFTA countries, access to more labour is vital in order to exploit the advantages of economies of scale. In addition, irregular labour migration is already the reality in South Eastern Europe, *inter alia* due to a large number of people being displaced in the course of the Yugoslav secession wars in the 1990’s. By formalising these movements, migrants would also benefit from better protection. Handjiski et al. conclude that “(r)eviewing labour mobility provisions within CEFTA, presumably in conformity with EU requirements, should (…) prove beneficial in preparation for EU entry.”

145 Ibid., p. 83.
146 Ibid., p. 86.
5.2 Should CEFTA Envisage Free Movement of Capital?

Before turning to the main discussion of this section, viz the question whether the CEFTA Parties should consider introducing free movement of capital, a short paragraph will be dedicated to the explanation of the concept in question. What does free movement of capital mean?

In essence, free movement of capital means the unrestricted transfer of financial capital from one country to another. In the EU, the right to free movement of capital confers upon citizens the ability to undertake a number of financial operations abroad, i.e. opening bank accounts, buying shares in non-domestic companies, investing where the best return is, and purchasing real estate. Companies may invest in and own other European companies and take an active part in their management.\textsuperscript{147}

The free movement of capital is one of the four economic freedoms constituting the main pillar of the EU Single Market. Until the 1980’s, free movement of capital was not liberalised at the same rate as the other freedoms (goods, services and persons) in the EU.\textsuperscript{148} Only with the advent of the Single Market and the launch of the Economic and Monetary Union (EMU) in 1992 was the flow of capital fully liberalised. This demonstrates the importance of free movement of capital for EMU and emphasises the interconnection between monetary policy and free movement of capital. The EU finally agreed on the full liberalisation of capital movements in 1988 with Directive 88/361/EEC.\textsuperscript{149} Annex I to this Directive lists a classification of capital movements that fall under the scope of the Directive. By abandoning capital controls in the EU, the financial sector has undergone dramatic changes in the last 20 years. It is important to note that the Treaty of Lisbon abolishes all restrictions on capital movement between Member States as well as between Member States and third countries. In contrast to the other four freedoms, the \textit{ratione loci} does not apply to free movement of capital.\textsuperscript{150}

At first sight, it may seem somewhat premature to suggest that the CEFTA should consider establishing free movement of capital so shortly after its coming into existence in 2006, taking into account that it took the EU about 30 years to implement it. Regarding the main research question of this thesis, whether or not the CEFTA provides for an

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\textsuperscript{148} Barnard Catherine, \textit{op. cit.}, p. 559.


\textsuperscript{150} Article 63 TFEU.
appropriate preparation in the area of free movement of capital, the answer is clear: in the EU, capital movement is fully liberalised while the CEFTA does not cover free movement of capital but only cross-border investment. The answer would therefore be negative.

This thesis argues that the CEFTA should envisage liberalising capital movements in the medium-term (5 years) for two reasons. First, it would increase the preparatory effect of the CEFTA for joining the EU. And second, liberalising capital movement between the CEFTA Parties and thus liberalising its financial markets would help the SEE countries to increase stability and attract foreign and regional investment it so desperately needs to sustain economic growth. Discussion will now turn to exploring the latter assumption.

In order to analyse whether free movement of capital in the framework of the CEFTA would have an overall positive effect on the SEE countries, benefits and downsides of liberalising capital movement will be considered.

5.2.1 Advantages of Free Movement of Capital

Willem Molle summarises the advantages of free movement of capital as follows:

- Free movement of capital reduces the risk of distortion of money markets that tends to occur in small markets.
- Free movement of capital leads to an increase of supply of capital, because better investment prospects mobilise additional savings.
- Free movement of capital increases competition in the financial market.
- Free movement of capital increases the efficiencies of financial markets. It allows financial markets – the intermediaries between the ones offering capital and those in need of capital – to work more efficiently and benefit from economies of scale. It enables those who need capital to raise larger amounts in forms better tailored to their needs.

Kristin J. Forbes from the MIT School of Management arrives at a similar assessment:

"The free movement of capital can have widespread benefits. Capital inflows can provide financing for high-return investment, thereby raising growth rates. Capital inflows – especially in the form of direct investment – often bring improved technology, management techniques, and access to international networks, all of which further raise productivity and growth. Capital outflows

can allow domestic citizens and companies to earn higher returns and better diversify risk, thereby reducing volatility in consumption and income. Capital inflows and outflows can increase market discipline, thereby leading to a more efficient allocation of resources and higher productivity growth. In order to obtain these widespread benefits of free capital flows, most developed countries and many developing countries have lifted most of their capital controls.\textsuperscript{152}

Free movement of capital will also foster regional investment. At the moment, the whole Western Balkan region relies heavily on foreign investment, from non-regional countries. In at least some of the SEE countries, the level of foreign investment is unsustainable in the long run. Montenegro is a good example to demonstrate this: the economic boom after independence in 2006 was primarily fuelled by large FDI inflows and foreign credits to the economy, which to a large part are not sustainable. In the years before the crisis, more than one-third of capital inflows consisted of elements that are temporary and will dissipate over the medium term, including, in particular, purchases of (coastal) real estate by foreigners and external borrowing by the domestic banking sector.\textsuperscript{153}

Liberalising capital movement and financial markets within the CEFTA area would bring an impetus to regional investment.

5.2.2 Disadvantages of Free Movement of Capital

Willem Molle lists the following reasons why a country may wish to uphold capital controls:\textsuperscript{154}

- Capital outflows may foster regional disparities: capital may flow from the poor countries to economically prosperous countries, thus reinforcing the economies of other states to the disadvantage of their own (i.e. there is less domestic investment, so the government receives less tax on the ensuing revenue).

- The loss of currency reserves may jeopardize a country’s ability to meet its other international obligations.


\textsuperscript{154} Molle Willem, op. cit., p. 120.
International markets may lose confidence in the policy measures of politically unstable countries, for the reasons that the country gives up one instrument to effectively influence its macroeconomic and monetary policies.

Capital is power: capital in foreign hands means a loss of sovereignty. Capital movements are closely linked to macroeconomic and monetary policies. By allowing capital to flow freely, a country gives up one instrument to steer its macroeconomic and monetary policies. Free movement of capital, fixed exchange rates and coordinated macroeconomic and monetary policies form the so-called ‘holy trinity’. In other words, one does not work without the other two. If capital is allowed to move freely, countries need exchange and interest rates as adjustment mechanisms to react appropriately to the business cycle. In times of an economic boom, interest rates need to be high in order to control inflation and prevent the economy from overheating. In times of recession, interest rates need to be low in order to foster investment, which will then increase economic growth.

In the CEFTA countries, almost all currencies are pegged to the Euro and have very low fluctuation; Montenegro and Kosovo even use the Euro as official currencies. Only the Serbian Dinar was observed to be more volatile in 2010.\textsuperscript{155} This means that the majority of CEFTA Parties have limited power over their exchange rate as an adjustment mechanism in times of real shocks as well as asymmetric shocks. Montenegro and Kosovo even gave up their monetary policy by unilaterally adopting the Euro as their official currency. Supposing that the CEFTA would introduce free movement of capital, according to the ‘holy trinity’, the countries would be forced to coordinate their macroeconomic and monetary policies at least to some extent, similarly to the EU.\textsuperscript{156} Given the political reality in the Western Balkans, it is highly unlikely that the CEFTA Parties would commit to such a high level of integration.

5.2.3 Do the Benefits Outweigh the Costs?

On the facts, it is very difficult to assess whether the benefits of free movement of capital would outweigh its downsides in the CEFTA area. Whilst the benefits of free movement of capital are numerous, the loss of capital control to maintain economic equilibria in the particular countries may pose a problem in the SEE due to the majority of countries’ limited


\textsuperscript{156} The EU does so via the Maastricht Criteria and the Growth and Stability Pact.
exchange rate flexibility. In order to reach a conclusion regarding the net benefits, it would be necessary to assess the degree of liberalisation of capital movement already provided for in the national legislations of the CEFTA Parties. If the CEFTA Parties had already lifted capital controls to a major extent in their national legislation, the impacts of introducing regional free movement of capital on national economic and monetary policies would be less detrimental than if capital controls would still be widely spread.

The Commission DG Enlargement Progress Reports from November 2010 on its potential and actual candidate countries provide an assessment on the status of liberalisation of capital movements. The Commission’s evaluation can be summarised in the following table:
Table 7: Status of Liberalisation of Capital Movements

<table>
<thead>
<tr>
<th>Country</th>
<th>Status of Liberalisation of Capital Movements</th>
</tr>
</thead>
<tbody>
<tr>
<td>Albania¹</td>
<td>Essentially liberalised</td>
</tr>
<tr>
<td>BaH²</td>
<td>Relatively liberalised, restrictions remain on capital outflows by residents</td>
</tr>
<tr>
<td>Croatia³</td>
<td>Essentially liberalised</td>
</tr>
<tr>
<td>Kosovo⁴</td>
<td>Essentially liberalised</td>
</tr>
<tr>
<td>Macedonia⁵</td>
<td>Restrictions remain</td>
</tr>
<tr>
<td>Montenegro⁶</td>
<td>Essentially liberalised</td>
</tr>
<tr>
<td>Serbia⁷</td>
<td>Moderately liberalised, restrictions remain on short-term capital movements</td>
</tr>
</tbody>
</table>

Source: European Commission, DG Enlargement.


² “Bosnia and Herzegovina continues to apply relatively liberal rules on inward capital flows. Restrictions remain on outward transfers by residents. Residents may hold accounts abroad, but the amounts that may be transferred are limited. (…) Overall, preparations in the area of free movement of capital are moderately advanced. Further legislative initiatives are required in order to align the legal framework with the acquis and to ensure country-wide harmonisation and the creation of single economic space.” European Commission, Bosnia and Herzegovina 2010 Progress Report, Brussels, 9 November 2010, {COM(2010) 660}, p. 36.

³ For Croatia, in the course of its accession negotiations, the chapter on free movement of capital is already provisionally closed. That means, that the Croatian legislation as regards free movement of capital is almost completely aligned with the EU acquis in this area. See European Commission, Croatia 2010 Progress Report, Brussels, 9 November 2010, {COM(2010) 660}, p. 5 and p. 29.

⁴ “Kosovo already has a very liberal regime concerning capital movements. As regards free movement of capital, no restrictions exist on foreign ownership or investment in the financial sector or in other assets.” European Commission, Kosovo 2010 Progress Report, Brussels, 9 November 2010, {COM(2010) 660}, p.32.

⁵ For Macedonia, the EU concludes that “(t)here are restrictions on residents regarding portfolio investments. EU citizens are not allowed to purchase agricultural land. The ceilings on the amounts of transfers that non-residents can perform through their local currency and foreign exchange accounts remain. This represents an effective barrier to the free movement of capital. The restrictions imposed under the Law on foreign exchange operations on the amount of cash that may be carried across the borders have not been removed. Nationals are still not allowed to buy shares in non-domestic companies, open accounts in foreign banks, or purchase real estate abroad.” European Commission, The Former Yugoslav Republic of Macedonia 2010 Progress Report, Brussels, 9 November 2010, {COM(2010) 660}, p. 34.
6 “Capital movements in Montenegro are essentially liberalised, but further efforts are necessary to fully align legislation with the acquis. As regards payment systems, legislation is not yet aligned with the relevant acquis.” European Commission, Commission Opinion on Montenegro’s application for membership of the European Union, Analytical Report, Brussels, 9 November 2010 (COM(2010) 670), p. 58.

7 “Serbian legislation provides for the free movement of credit related to commercial transactions or to the provision of services as well as to financial loans and credit with maturity longer than a year. While simplifying procedures for foreign payments, Serbia retains restrictions on short-term capital movements. (...) Overall, Serbia is still moderately advanced in the area of capital movements. With certain restrictions, non-residents are free to make direct investments.” European Commission, Serbia 2010 Progress Report, Brussels, 9 November 2010, (COM(2010) 660), p. 32.

In conclusion, capital movement can be considered largely liberalised in all CEFTA countries aspiring to EU membership. With this in mind, it can be assumed that bringing freedom of capital into the scope of CEFTA would have a net beneficial effect. It would increase security and stability in the regional financial markets and consequently reduce risk for domestic and foreign investors. This view is shared by a representative of ERSTE BANK157, one of the major banks operating in all the CEFTA countries but Albania.

Interestingly enough, the ‘old CEFTA’ (the original Agreement of 1992) also contemplated whether or not to introduce free movement of capital. “One of the aims of CEFTA in 1992 had been to liberalize the movement of capital, but that was never accomplished.”158

157 Interview with Erste Group Bank AG, Vienna, Department ’Projects & CEE Governance’, 29 April 2011.

Conclusion

This thesis seeks to analyse in detail the Central European Free Trade Agreement (CEFTA) and its Parties as regards their relationship with the EU. It could be demonstrated that both the original CEFTA entering into force in 1993 as well as the 'new CEFTA' establishing a free trade area between BaH, Croatia, FYROM, Kosovo (under UN Security Council Resolution 1244), Moldova, Montenegro and Serbia, was initially designed to be a preparatory exercise for the EU. To that end, the central question to be answered was how far CEFTA fulfils its purpose and constitutes an appropriate preparation for the EU Single Market.

The CEFTA needs to be analysed in the complex framework of EU-Balkan trade relations, which are governed by the perspective of EU enlargement to the Western Balkan countries. In this regard, the EU employs an instrument called the Stabilisation and Association Process (SAP) to prepare potential and actual candidate countries of the Western Balkans for future EU accession. In the framework of the SAP, the majority of SEE countries have concluded, or are in the process of concluding, the Stabilisation and Association Agreements (SAA) which provide the legal framework for EU-Western Balkan relations in general, and its trade relations in particular.

However, the main motivations for the EU to pursue further enlargement to the South-East are not trade-related, but political. The EU seeks to progressively align the post-war region in order to eliminate a potential risk of open conflict in its immediate neighbourhood. In addition, the Balkan countries are of geopolitical importance in the area of transport. One of the EU’s energy supply projects, ‘Nabucco’, envisages transporting gas from the Caucasus and Black Sea region via the Balkan Peninsula to Western Europe. In pursuing its goal of political stability and security in 'Europe's backyard', as the Balkans are often referred to, the EU has a vital interest in fostering regional cooperation. The SAAs therefore include the obligation to fully implement the CEFTA, whilst the full implementation of the SAA itself is a pre-condition for entry in the EU.

Against this background, the main purpose of the CEFTA becomes apparent. The CEFTA serves three main goals: first, integrating the SEE economies and making them economically dependent on each other reduces the risk of open conflict. Second, the CEFTA aims at increasing economic growth via regional trade liberalisation and market integration. The individual SEE countries are too small to attract sustainable foreign investment, only their combined market share forms a market big enough to
attract foreign investment. Finally, regional trade integration and liberalisation prior to becoming EU members will have the benefit of making the countries better prepared for the EU Single Market and, consequently, more capable of coping with the competitive pressure within the EU.

The approach of enlarging the EU to the South-East according to ‘the regatta principle’ rather than in a package solution (as was done with the CEE countries in 2004) has led to the situation where the SAP advances at different speeds in different countries. Whilst some countries (i.e. Croatia) have now successfully completed accession negotiations and will join the EU in 2013, Kosovo has not even passed the initial step of starting SAA negotiations. With this regard, the SAP modalities foster and hamper regional integration and the necessary cohesion connected therewith at the same time. In this context, the CEFTA can be also interpreted as a regional initiative very much necessary to counter regional disparities (also) induced by the EU’s Association and Stabilisation Process.

Both regional trade integration projects, the SAAs in the context of EU enlargement on the one hand, as well as the CEFTA on the other, need to be analysed in the larger context of WTO law. Turning first to the free trade areas between the EU and the associated countries established by the SAAs, they continue the EU’s trend of engaging in regionalism and concluding an increasing number of preferential trade agreements. The conformity of the SAAs with Article XXIV GATT and Article V GATS (where necessary), has not been challenged by any other WTO member yet. The CEFTA, likewise, has been notified under Article XXIV GATT for trade in goods only. Both the SAAs and the CEFTA are in line with WTO law.

In applying the ‘Balassa model of economic stages’ to both the CEFTA and the EU, the analysis showed that the CEFTA constitutes a less advanced form of regional economic integration compared to the EU Single Market. Consequently it appears that the CEFTA could never be a perfect preparation for the EU Single Market due to their different objectives in terms of the intensity of integration. The CEFTA cannot attain the same level of market integration and policy harmonisation, firstly because an FTA per definitionem reaches a lesser degree of integration than a common market. Secondly, policy integration is hampered by the political reality in the post-war Balkans. Market integration via a non-discriminatory approach focusing on negative integration remains the prerogative of the CEFTA.

Against this background, the CEFTA achieves increased market integration in succeeding to liberalise about 90 per cent of trade in goods among its constituent Parties. The
comparative analysis demonstrated that the CEFTA appropriately prepares its Parties for future membership in the EU, especially in the area of free movement of goods. Additionally, in the areas accompanying the four freedoms constituting the EU Single Market, viz public procurement, competition policy and intellectual property rights, the CEFTA provides for a substantive realisation of the EU Single Market acquis from the date of the Agreement’s entry into force. The CEFTA thus lays the basis for an appropriate preparation for the EU Single Market in all its substantive areas but two fields, namely free movement of persons and capital.

A World Bank report found strong evidence in favour of considering labour mobility to be brought into the scope of the CEFTA.\(^{159}\) The CEFTA brings about very favourable conditions for implementing skilled labour mobility, which would help the CEFTA area improve labour productivity, exploit economies of scale and foster economic growth. With regard to free movement of capital, the evidence is not conclusive as to whether or not the benefits of liberalising capital movements within the CEFTA would outweigh the costs of doing so. However, in assuming that the capital markets of the CEFTA countries are already liberalised to a large extent, it is estimated that bringing freedom of capital into the scope of the CEFTA would have a net beneficial effect. It would increase security and stability in the regional financial markets and consequently reduce risk for domestic and foreign investors.

From a theoretical perspective, the comparative analysis could prove that the CEFTA can be considered to sufficiently fulfil the criteria for appropriate preparation for the EU Single Market. This conclusion takes into consideration that all CEFTA signatories are countries in transition. This implies that appropriate preparation does not mean that the CEFTA has to fully copy the EU Single Market acquis from the date of its entry into force, but needs to gradually prepare the countries in form of partial realisation of the substantive provisions, possibly including transitional periods. In a majority of areas analysed, the Agreement covers both textually and substantively the essence of the EU Single Market acquis.

From an economic perspective, the aforementioned World Bank report reaches the conclusion that intra-regional trade in the CEFTA area has indeed improved considerably in past years, however, the structure of the trade flows in the bloc do not indicate a high level of economic integration.\(^{160}\) This fact might be another incentive for the CEFTA

\(^{159}\) Handjiski Borko (et al), *op. cit.*
\(^{160}\) Ibid., p. 44.
Parties to upgrade either the legal framework or to improve the implementation of the current Agreement.

With this regard, the CEFTA Parties should be ready to commit to the same level of trade liberalisation as they do in their SAAs, taking into account that both trade integration initiatives pursue the same goal: to prepare the countries for eventual EU membership. Recalling that the EU insists on both a positive track record in implementing the SAA and the full implementation of the CEFTA, it is not coherent that the Western Balkan countries refuse to commit to certain issues in the framework of the CEFTA to which they did commit in the SAAs, despite the fact that the EU has reiterated on a number of occasions that the future of all countries of the Western Balkan lies in the EU.

From a political perspective, finally, the CEFTA Parties will need to step up their efforts in harmonising at least a minimum level of standards and technical regulations, as well as sanitary and phytosanitary measures in order not to distort trade. What is missing in the CEFTA is an intrinsic motivation to harmonise. To that end, this thesis argues that reforms are always more successful if they are intrinsically motivated rather than extrinsically. If the CEFTA Parties were able to take political ownership over their free trade area as a trade instrument serving their interest irrespective of its preparatory notion for the EU, this would significantly increase the success of the CEFTA.
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