



# **Economic integration of the Eastern European countries through trade and FDI, with special focus on North Macedonia**

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# Introduction

- ♦ The beginning of the 90s (of the last century) was characterized by rapid expansion in global and regional trade
- ♦ Trade liberalization and removal of tariff and non-tariff barriers was a process in particular pertinent to the Eastern European Bloc, as an important cornerstone of the overall transformation towards fully functional market economies.
- ♦ The experience of the latest EU member states in the CESEE and Baltic countries group has confirmed that the best route to prosperity for small countries, especially for the Western Balkans is to integrate with the global economy.

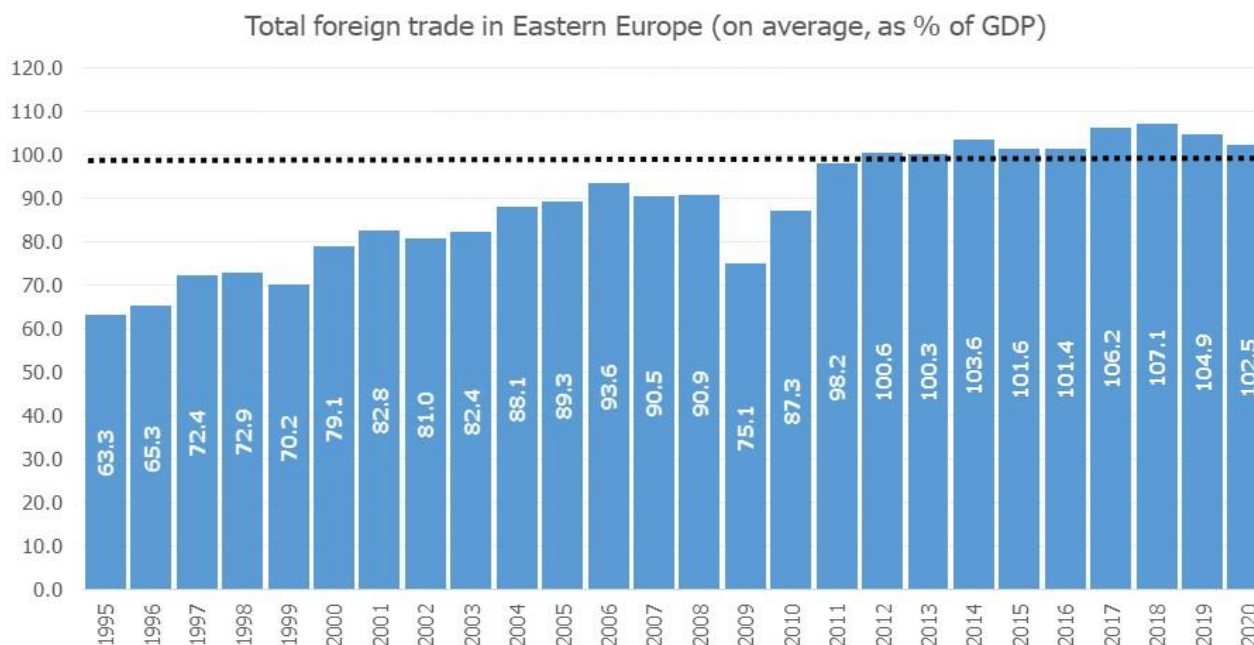


## Overall dynamics

- For the purpose of regaining access to international markets, Eastern European countries oriented towards a policy of concluding free trade agreements...

... with WTO starting as early as 1995, and by 2000 half of the region had joined - lowering tariff rates, harmonizing legislation, and signing up to independent dispute settlement mechanisms.

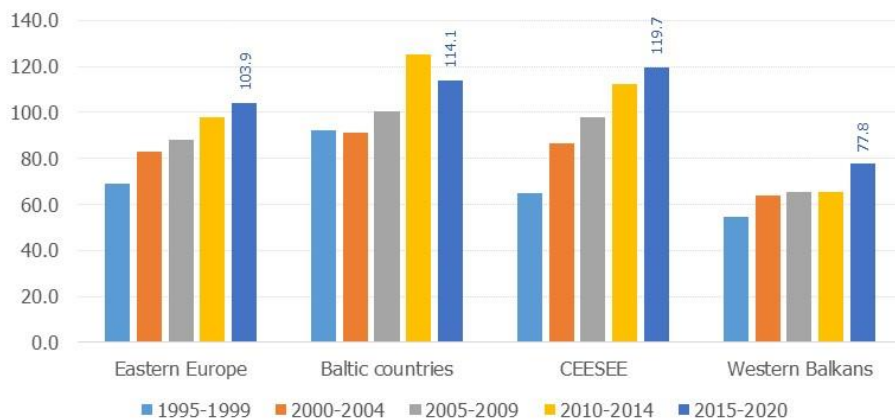
- Integration through trade and investment began almost immediately!
- Data show a constant upward trend in the overall foreign trade since the early 90s (excluding the Global economic crisis in 2009), surpassing 100% openness in 2012.



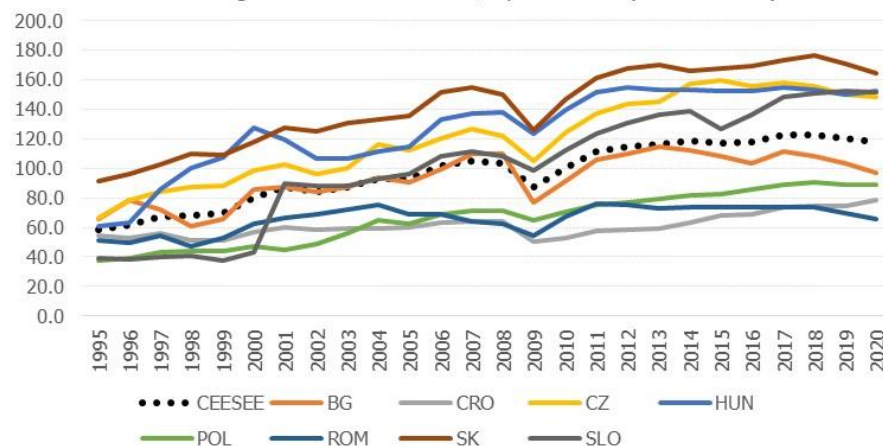


# Trade openness' dynamics, by group of countries

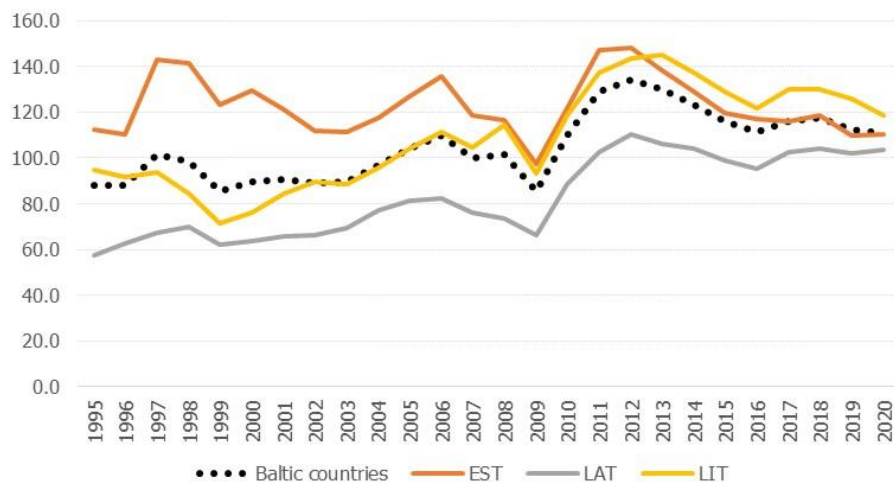
Total foreign trade in Eastern Europe, by groups of countries (on average, as % of GDP)



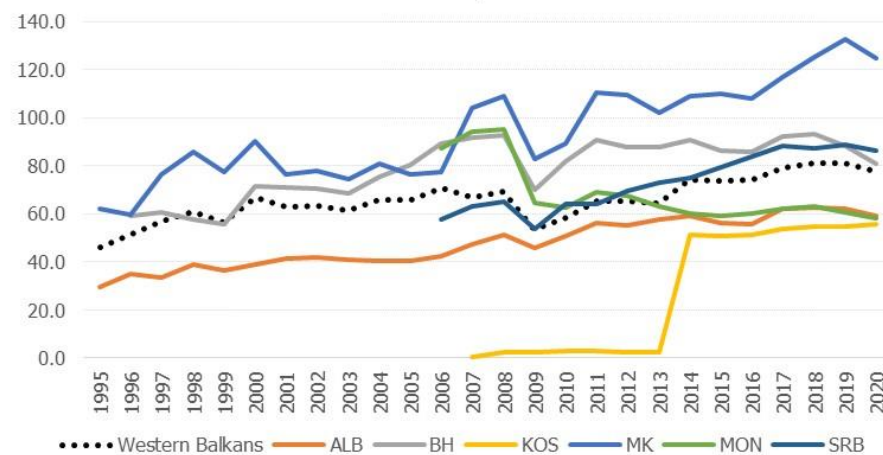
Total foreign trade in the CEESEE, by countries (as % of GDP)



Total foreign trade in the Baltic states, by countries (as % of GDP)



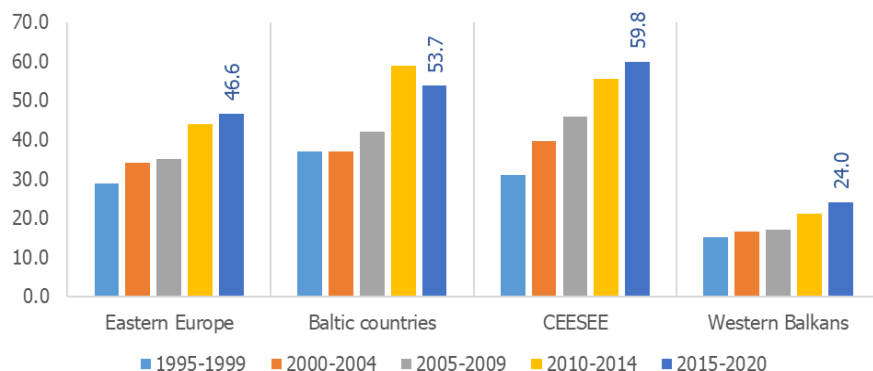
Total foreign trade in the Western Balkans, by countries (as % of GDP)



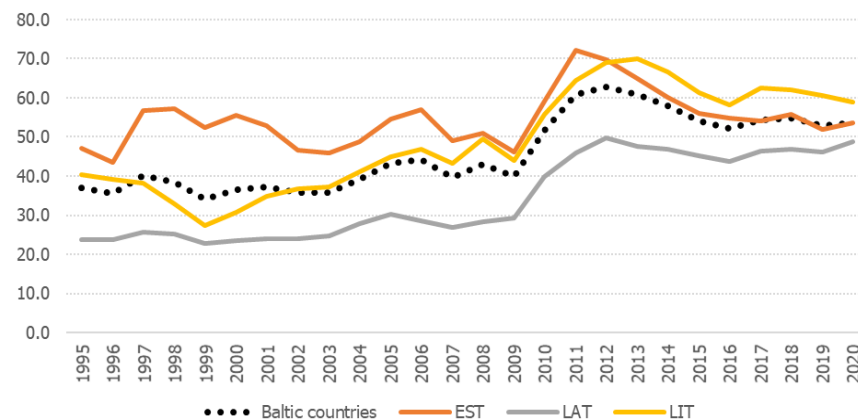


# Export of goods dynamics, by group of countries

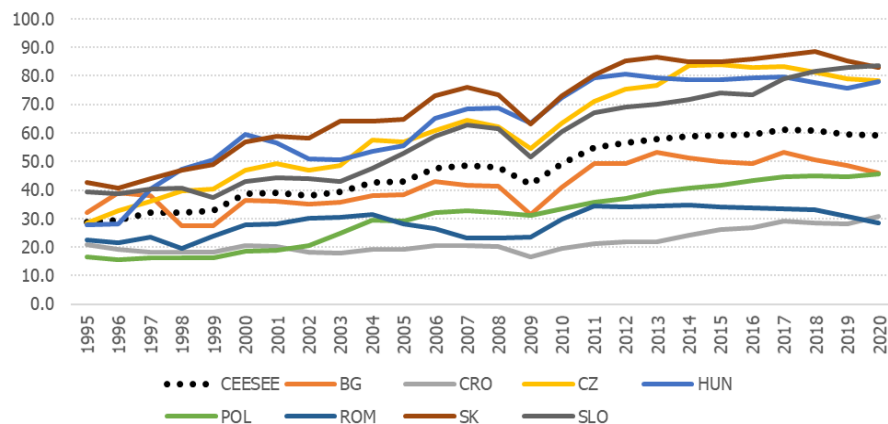
Total exports of Eastern Europe, by groups of countries (on average, as % of GDP)



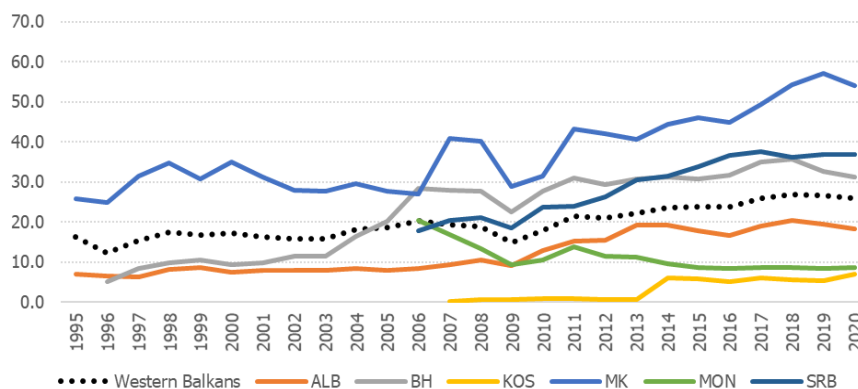
Exports in the Baltic states, by countries (as % of GDP)



Exports in the CEESEE, by countries (as % of GDP)



Exports in the Western Balkans, by countries (as % of GDP)



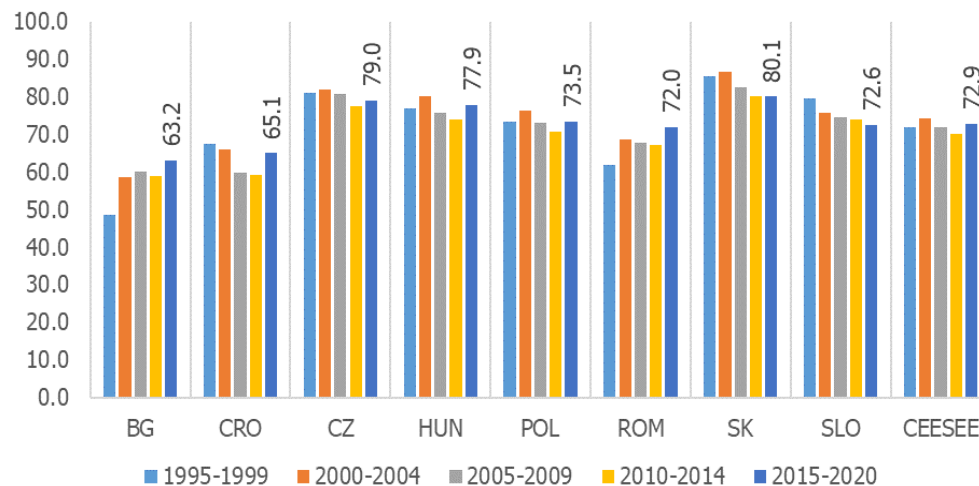




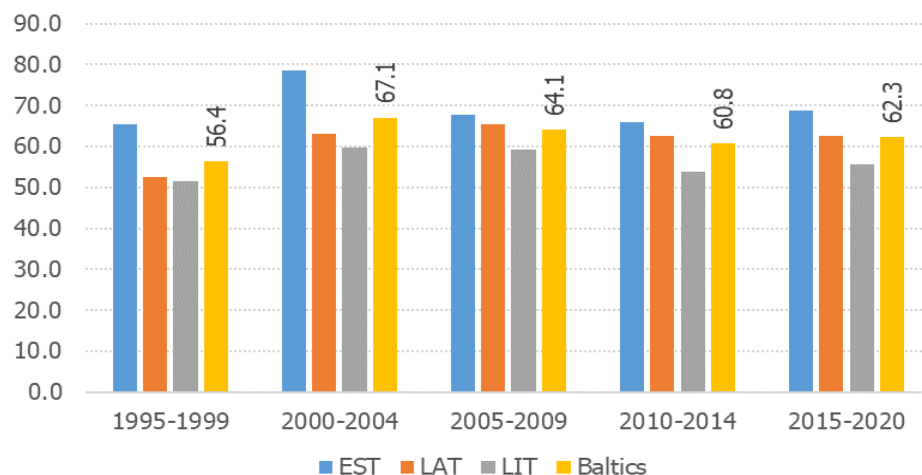
## Direction of trade: CESEE and Baltic countries

- The Central European countries, pioneered in both trade and financial integration with the EU economy, due to the faster reform process, as well as cultural and sectoral similarities and the geographical proximity, especially with Germany.
- CESEE countries, direct a large share of their export towards the EU averaging around 72%, with Czech Republic, Hungary and Slovak Republic surpassing the average in the latest analyzed period.
- Since the early 90s, they have strong supply chains with Germany, and the EU in general.
- The strongest link in this supply chain has been the automotive industry, mostly the outsourcing of the strong German automotive industry, a process that was largely supported by greenfield FDIs in the manufacturing sector.
- The Baltics' share of exports towards the EU is somewhat lower, averaging 62%, with Estonia being an outlier with around 7 p.p. higher share.

Share of total exports towards EU (in %)



Share of total exports towards EU (in %)





## Direction of trade: Western Balkan countries

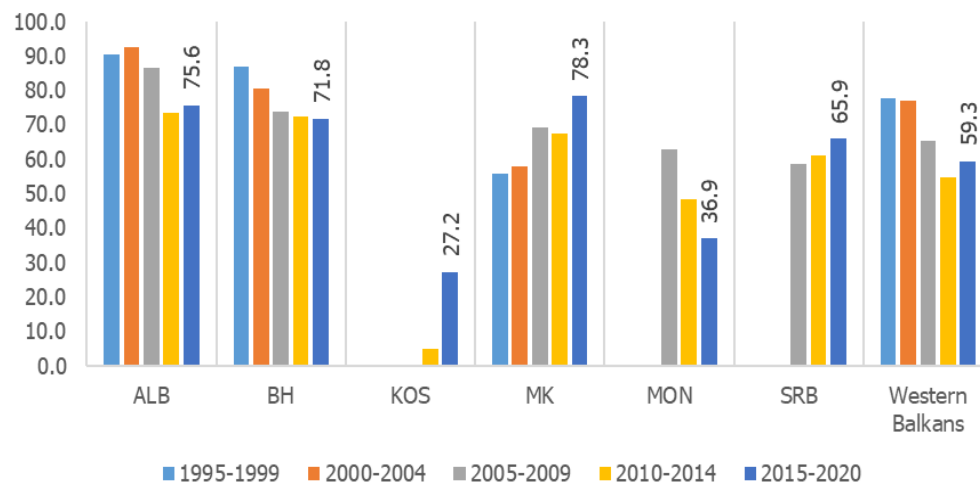
- Greater appeal of EU accession, rather than regions' trade initiatives, such as CEFTA agreement ...

... however, it differs throughout countries.

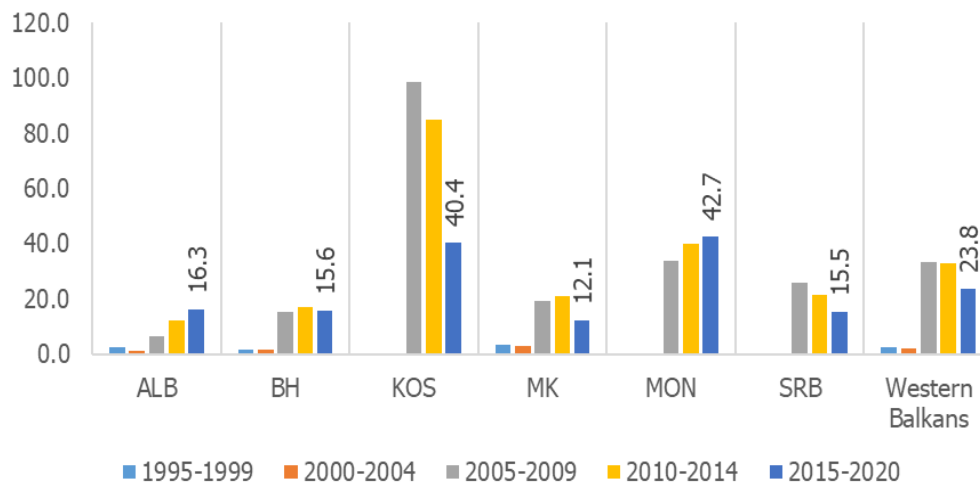
- Albania, Bosnia and Montenegro declined their share of export towards the EU and increased regional trade within the group...

... on the other hand, North Macedonia and Serbia are continuously increasing their export share to the EU.

Share of total exports towards EU (in %)



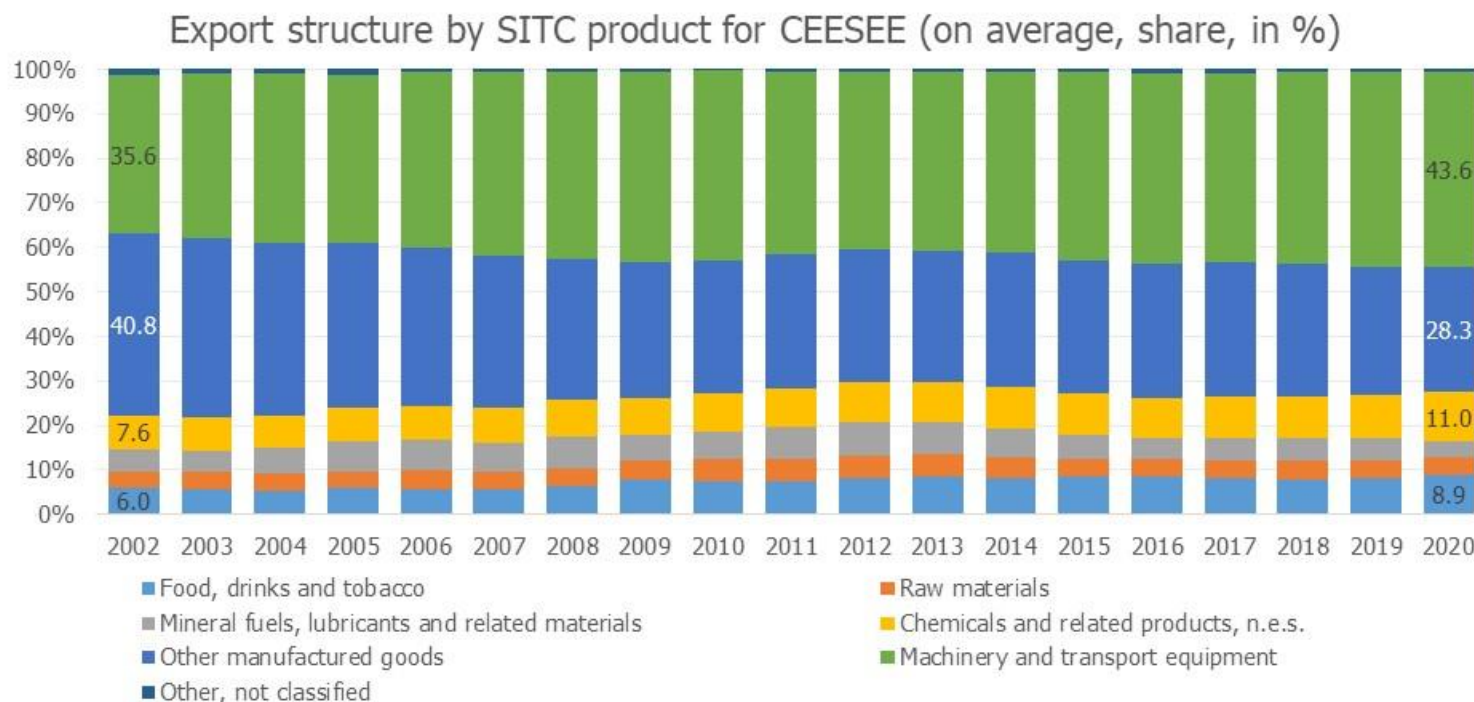
Share of total exports inside group (in %)





## Export structure, by SITC product

- For the CESEE region as a whole, 2 largest export shares consist of machinery and transport and other manufactured goods;
- From a dynamic point of view, this country group registers decline in other manufactured goods and at the same time an increase in machinery and transport equipment, as well as growth in the exports of food and chemical and related products.



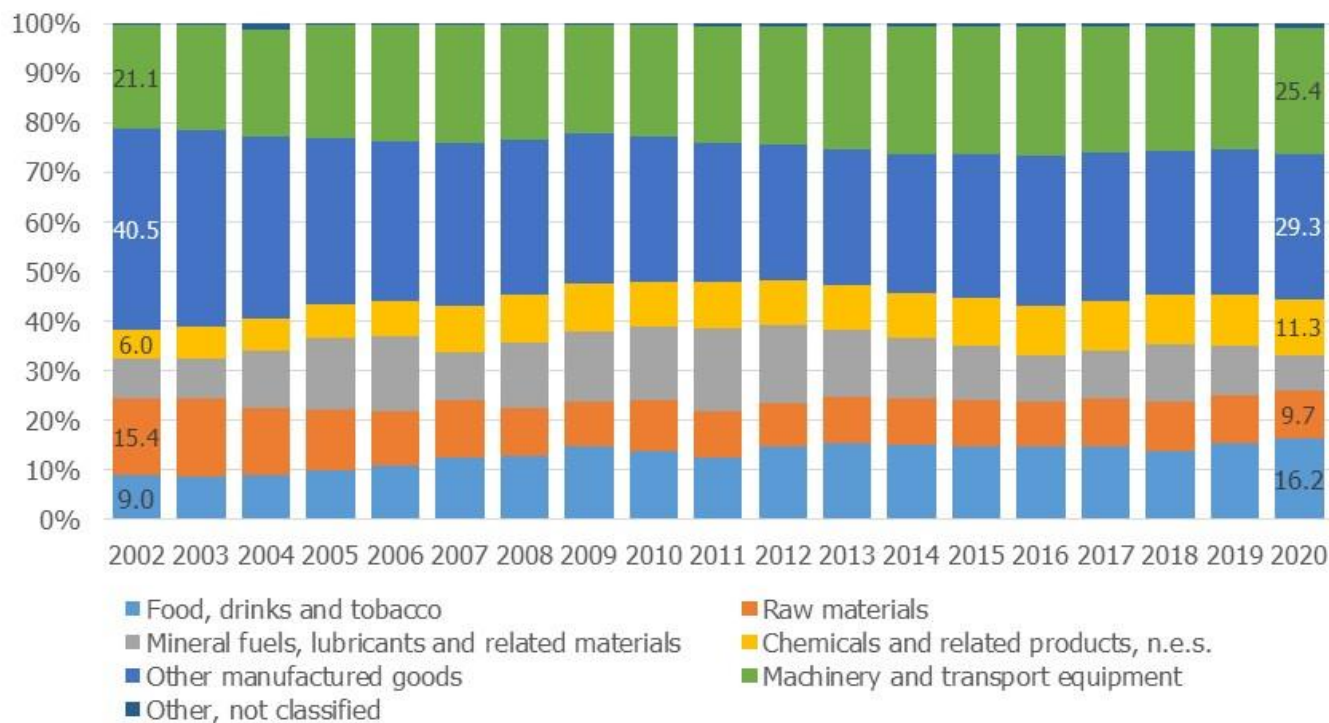




- The Baltic states mainly export other manufactured goods, machinery and transport, raw materials and food;
- Through out the analyzed period we observe a decline in the share of other manufactured goods and raw materials...

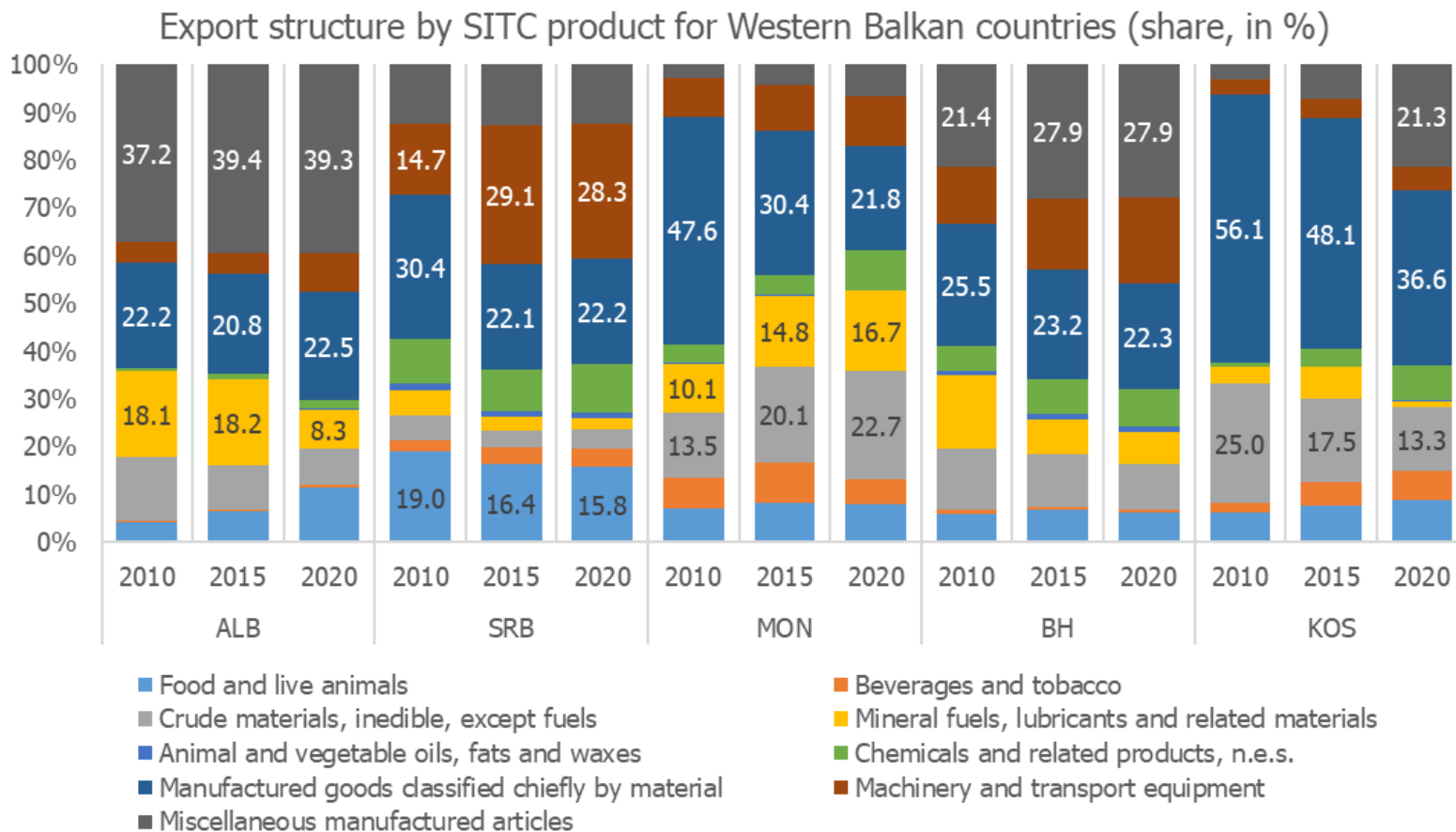
... whereas machinery and transport equipment, food and chemical and related products report an increase.

Export structure by SITC product for Baltic countries (on average, share, in %)



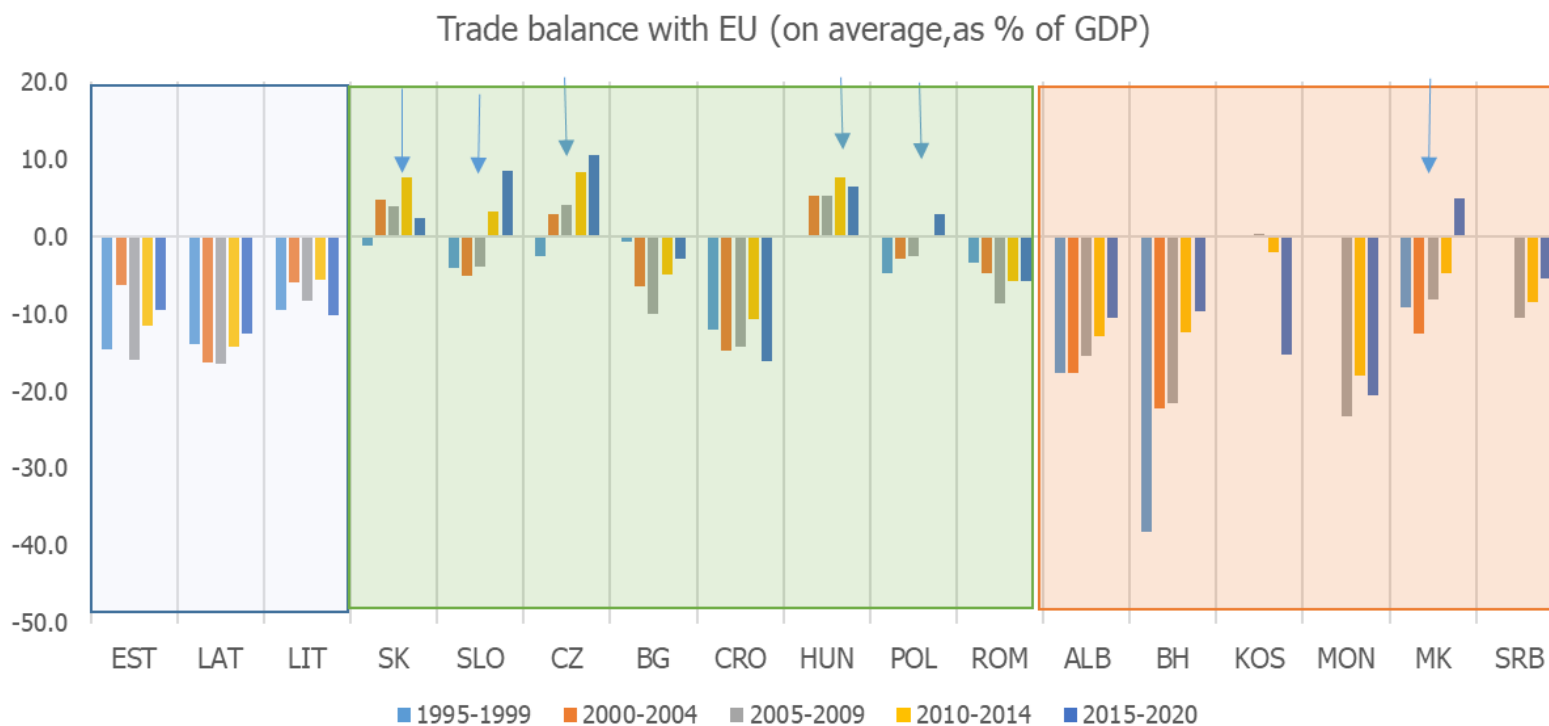


- The export structure of the Western Balkans differs immensely by countries...



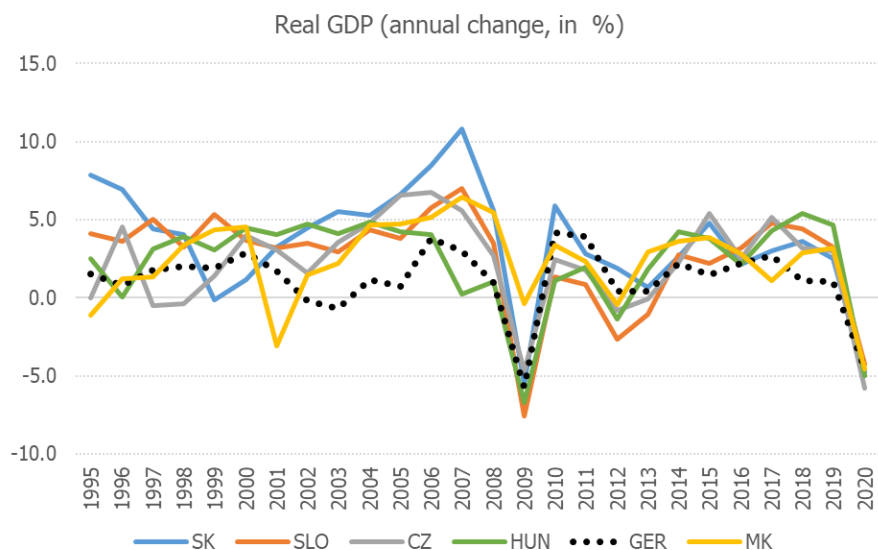


- Only five countries through out the analyzed period reported a surplus in the trade balance with the EU: Slovak Republic, Slovenia, Czech Republic, Hungary, Poland and North Macedonia.





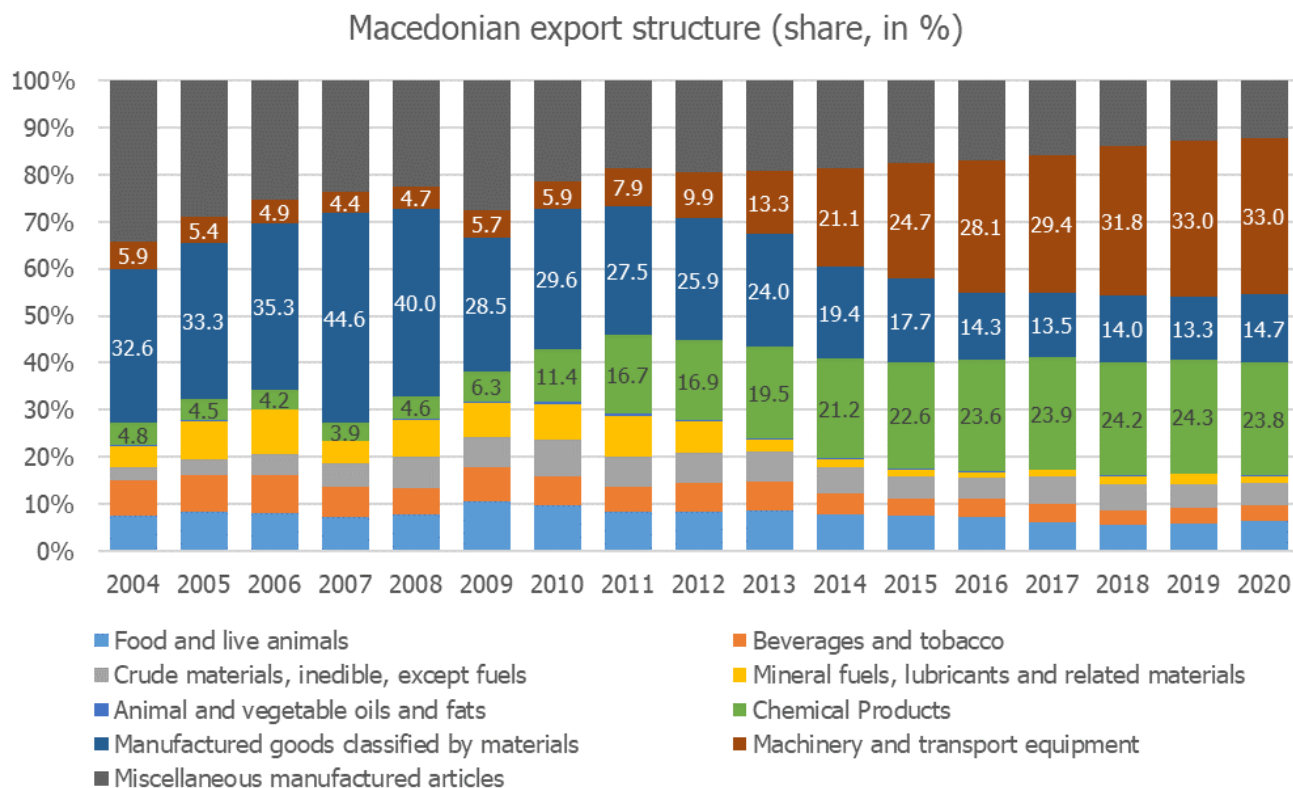
- **Macedonian export** diversification process resembles few high performing CESEE countries, such as Czech Republic, Hungary, Slovakia, and in the last couple of years, Romania.
- Significant portion of these economies export is classified as machinery and transport equipment and chemical products, as most of them are integrated into the global value chains through the Germany's automotive industry.





▪ Structural shift in the Macedonian export (by SITC categories):

- Significant increase in the share of higher-value products such as machinery and transport equipment and chemical products, while
- Large reduction in the share of traditional export sectors like iron and steel, food and tobacco and textile exports.

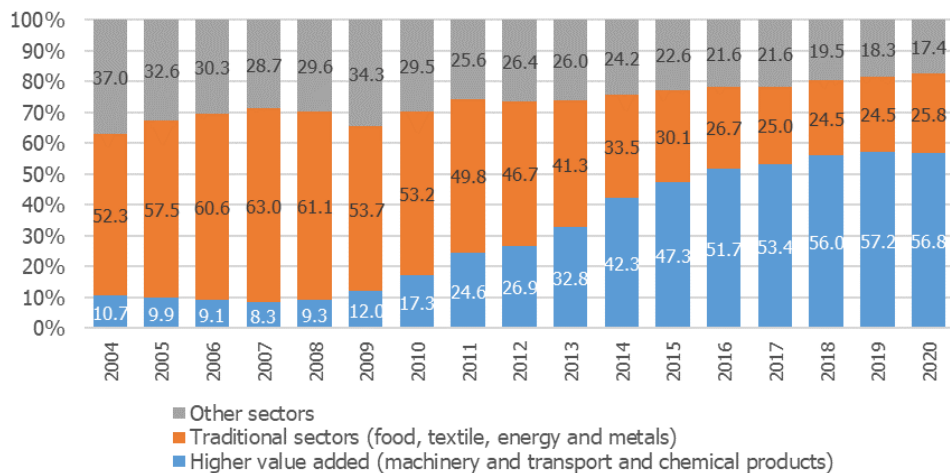




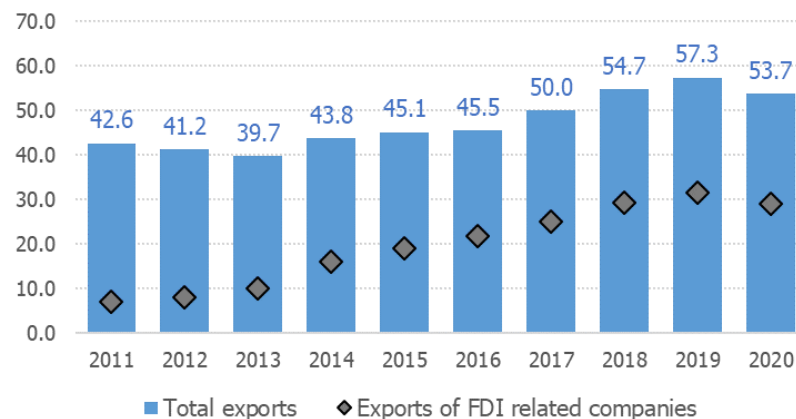


- Deeper integration into the global value chain has shifted greater export share towards knowledge intensive sectors, which include transport and electrical equipment, machinery and chemical products – the driving force behind the export growth in the period 2013-2019.
- The current share in 2020, of higher-value export is 56,8%, compared to 10,7% in 2004, a rise of 46.1 percentage points.

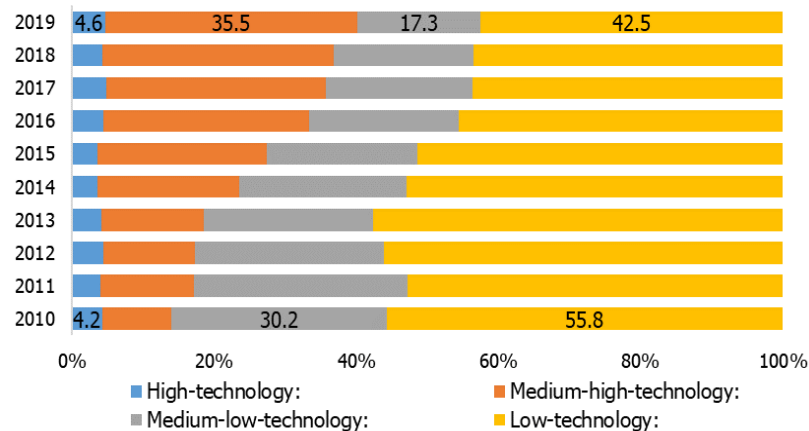
Shift in Macedonian export structure (share, in %)



Macedonian export of goods (as % of GDP)



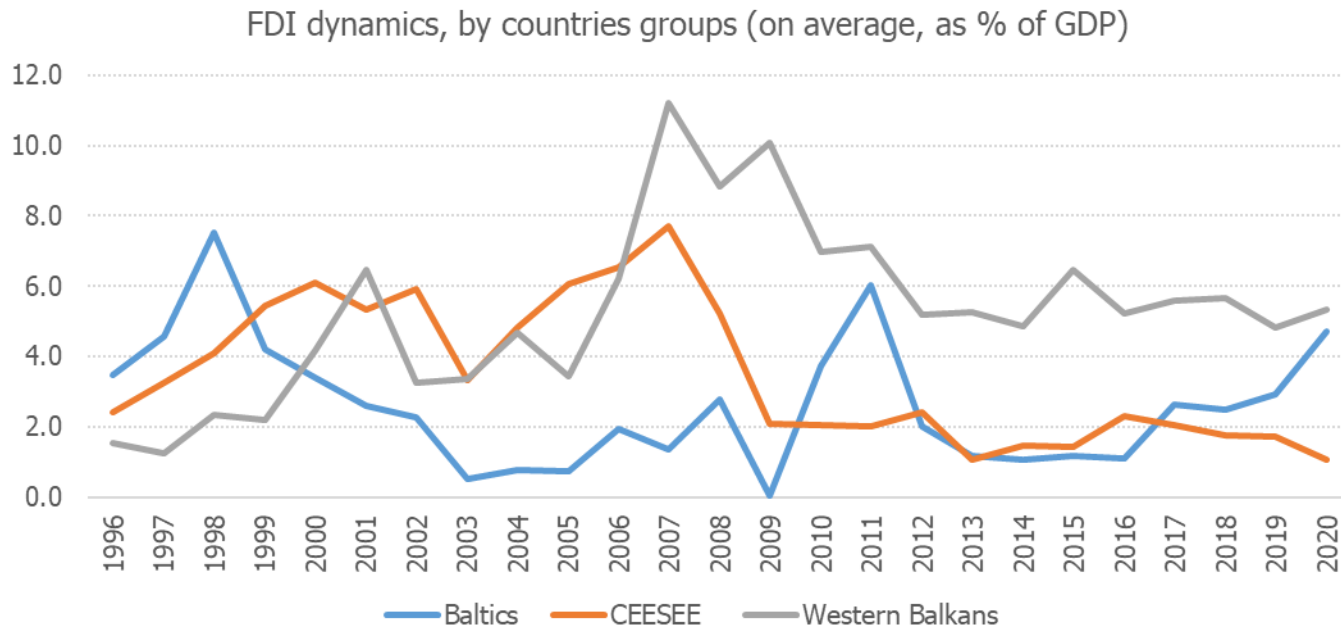
Macedonian industrial production, clasification by technology level (as % of total)





## Investment links in the region:

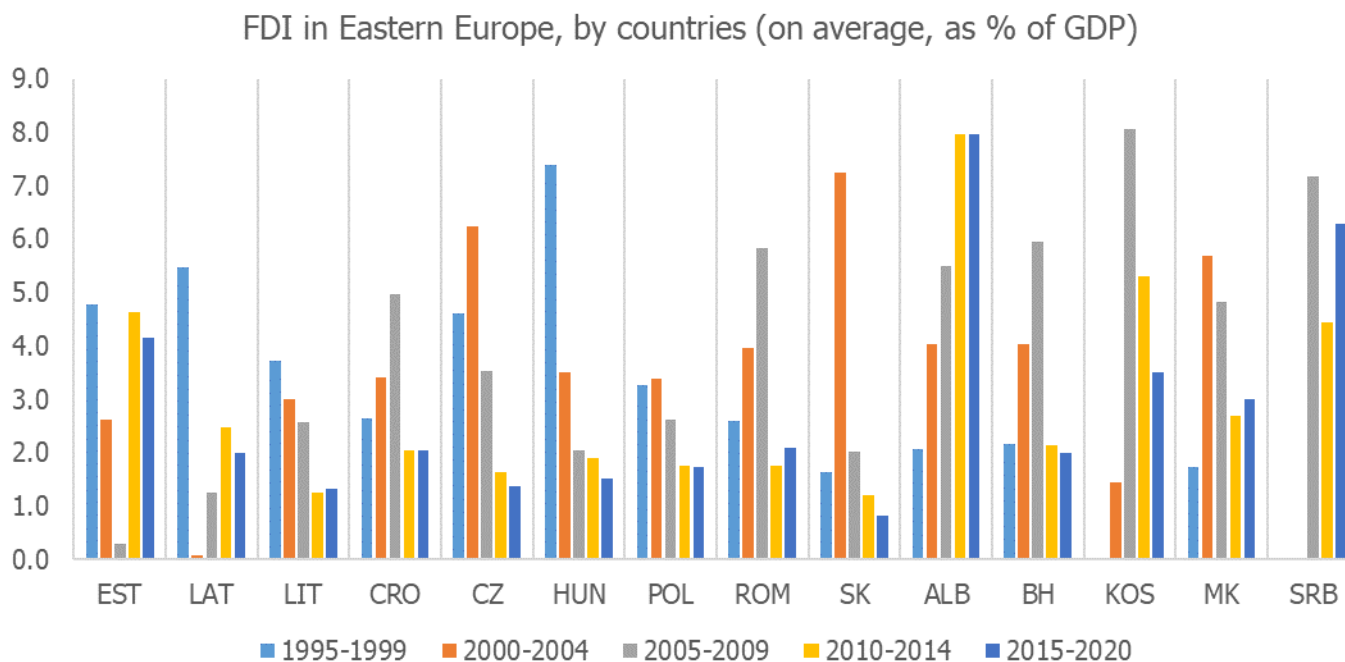
- Overwhelming investment needs, at the very beginning (1990s) - underdeveloped infrastructure and rundown industrial capacity;
- The bulk of external capital from Western Europe infused in the region in the form of FDI and cross-border bank flows;
- Dominance of FDI:
  - first through the large scale privatization that followed the transition
  - later on through Greenfield investment;
- Over the analyzed period of 25 years, Eastern Europe countries registered annual FDI net- inflows of around 4 percent of GDP on average.





## FDI dynamics:

- FDI inflows dynamics varied throughout the period, as expected;
- FDI upward trend in pre-accession and pre-crisis period for most of the economies (with new-EU countries pulling in more of the capital compared to non-EU countries);
- In 2009 and the overall post-crisis period, FDI influx slowed down considerably





### ***FDI structure in the Baltic states:***

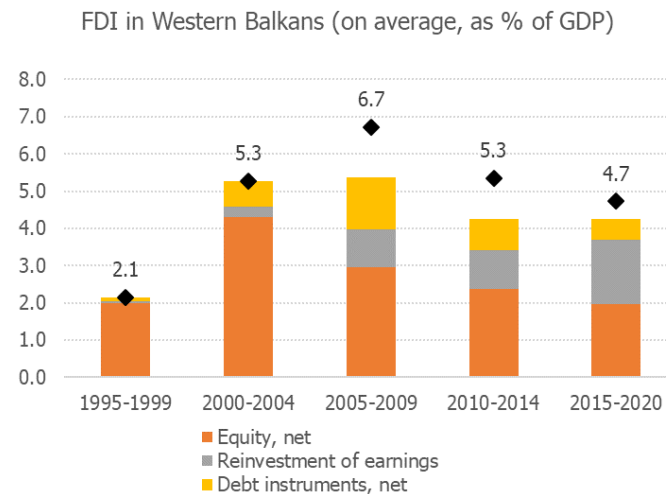
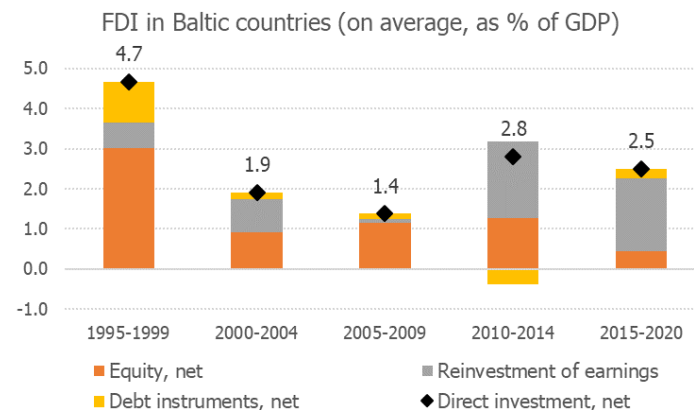
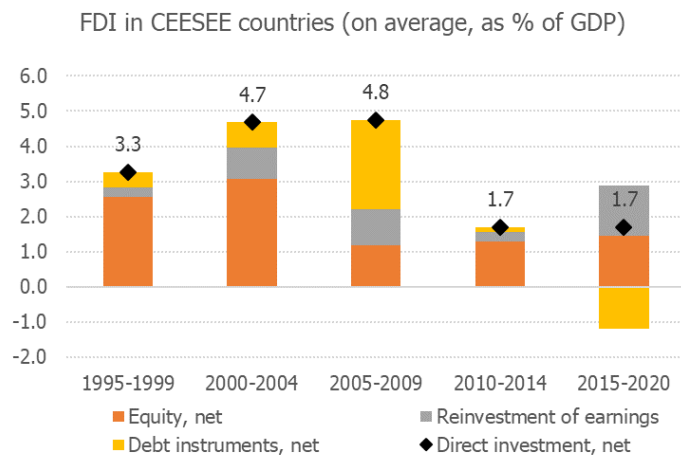
- Equity share dominating in the FDI structure, up to 2009 and the global crisis;
- In the last decade, a shift to reinvested earnings as a key component of the overall direct investment
- Later stage of the cycle of direct investment

### ***FDI structure in the CEESEE countries:***

- Equity share dominating in the FDI structure, up to 2004, followed by a period of financing through intercompany lending around the global crisis;
- Post crisis – outflows in debt instruments...

### ***FDI structure in the Western Balkan countries:***

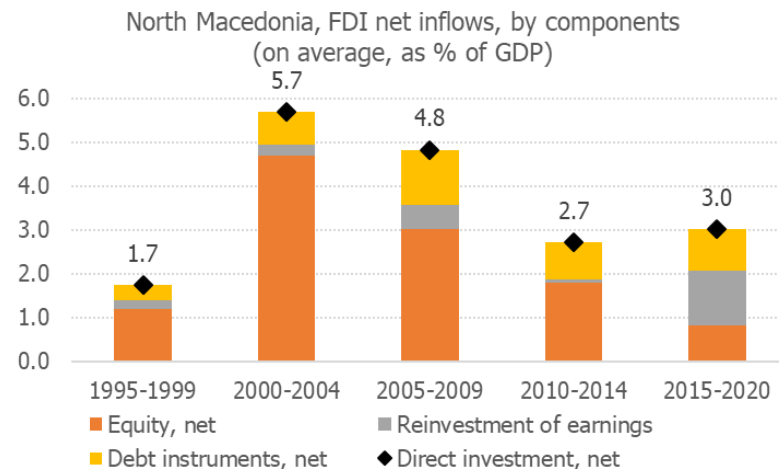
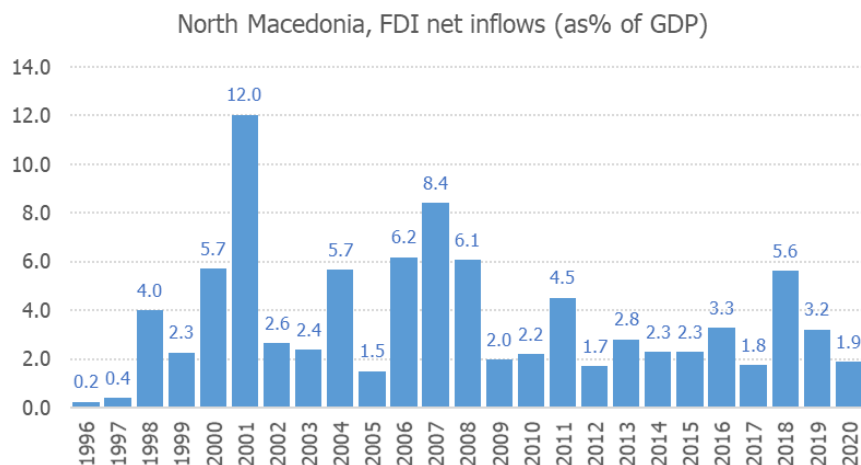
- Equity the largest component of the FDI structure...  
... with reinvested earning gaining momentum as of 2005, and reaching the peak in the latest analyzed period...





## North Macedonia FDI dynamics

- Historically (1996-2002), FDI inflows largely reflected the process of privatization
- Since the mid-2000s, greenfield investments have taken on an increasingly important role.
- Macedonia introduced major policy changes aimed at improvement of its business environment, as well as providing incentives to attract FDI in tradable sectors as a major component of the country's export strategy.
- Free economic zones offering tax and customs benefits have been established, providing new export platforms.

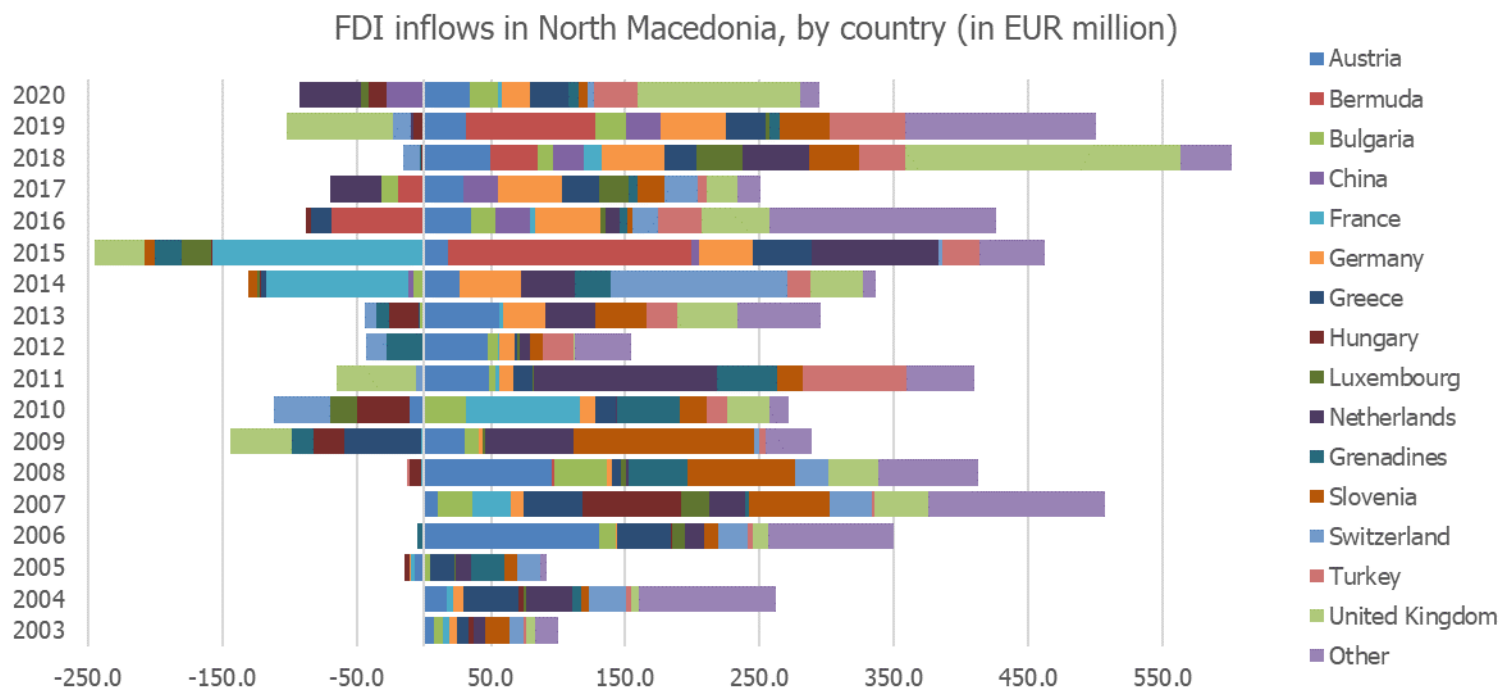






- FDI inflows in North Macedonia, by activity (in EUR million)







# Summary

- Structural changes in the export sector brought the Macedonian economy closer to the global value chains, increasing the country's trade openness, shifting the production towards higher value sectors and increasing the export share of higher-value products.
- Trade and financial integration among the plentiful benefits, also pose certain risks mainly by increasing the vulnerability of the economy through larger export concertation to external shocks and disturbances.
- Numerous challenges are ahead, some arising from the inevitable broad structural reforms and some coming from the global surrounding and the rising protectionism.
- Further reforms are needed, predominantly focused on increasing productivity, achieving further production and also export diversification, on higher value added products; greater focus on the service sector and its export potential.



**Thank you, for your  
attention!**



## Data sources:

- IMF DOT statistics ([Direction of Trade Statistics - DOTS Home - IMF Data](#))
- IMF BOP statistics (<https://data.imf.org/BOP>)
- IMF WEO Database October 2021 (<https://www.imf.org/en/Publications/WEO/weo-database/2021/October>)
- Eurostat (<https://ec.europa.eu/eurostat/data/database>)
- NBRNM ([https://www.nbrm.mk/eksterni\\_statistiki-en.nspix](https://www.nbrm.mk/eksterni_statistiki-en.nspix))
- SSO ([https://www.stat.gov.mk/Default\\_en.aspx](https://www.stat.gov.mk/Default_en.aspx))

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- 25 Years of Transition Post-Communist Europe and the IMF, Regional Economic Issues Special Report, IMF, 2014.
- Resilience to global headwinds? CESEE responses to changing trade and financial landscape – focus on the Macedonian economy, Vesna Stojchevska, NBRNM analysis, October 2019.
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