

## **A NEW ERA IN SOUTH EASTERN EUROPE? Grasping the opportunity to promote economic growth with equity**

**November 2000**

Oxfam is concerned that rising poverty and inequality in South Eastern Europe could derail the EU's long term efforts to "project stability" to the region. Our experience of working with poor and vulnerable groups throughout the former Yugoslavia and Albania concurs with the World Bank's assessment that "poverty is likely to have worsened dramatically in recent years."<sup>1</sup> Through most of the region, economic output has scarcely reached 75 per cent of prewar levels. Incomes have collapsed, as many people have lost their jobs through displacement and the closure of state-owned industries. Massive unemployment and reduced government spending mean that many people in South Eastern Europe are living in poverty, and lack access to basic services such as health care and education.

Two significant changes – the end of the Milosevic regime in Belgrade and the opening of EU markets through the recent Autonomous Trade Measures - should provide a significant impetus to economic recovery in South Eastern Europe. To ensure that recovery is sustainable, the majority must be able to benefit from economic growth. Without this, poverty will continue to feed the social and political tensions that have led to persistent violence in the region.

Poverty reduction requires careful targeting of assistance to ensure the creation of jobs and opportunities, particularly for marginalised communities and individuals. Efforts to stabilise the region in the past year have been significant. However, from Oxfam's experience of work with poor and vulnerable groups in South Eastern Europe, the funds pledged for economic reconstruction at the first regional funding conference in March have so far had little real impact on most people's lives. To grasp the opportunities brought by political change in Belgrade, we believe that more should now be done to secure economic growth with equity in South Eastern Europe.

For this reason, we call in this paper for a refocusing of international assistance to the region. Poverty reduction is a core objective of the EU.<sup>2</sup> Reducing poverty and promoting equitable economic growth in South Eastern Europe should now be made the explicit goal of Stability Pact signatories.

This report sets out why policies to combat the growth of poverty and to promote equitable economic growth are essential for the long term stability of South Eastern Europe. We then provide some suggestions, based on our own work in the region and globally, as to how such growth can be promoted through international assistance.

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<sup>1</sup> *The road to stability and prosperity in South Eastern Europe: A regional strategy paper*. The World Bank Europe and Central Asia region, Washington DC, 2000, p.31

<sup>2</sup> Javier Solana, 'Why Europe needs the military option,' *Financial Times*, 29 September 2000

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## Recommendations

- 1. The EU should draw up a strategy to ensure that recent trade concessions bring economic benefits to marginalised communities. Economic assistance to the region should be explicitly designed to promote job creation and skills, which will allow poorer people to capture a greater proportion of the benefits of access to EU markets.**
- 2. The EU, principal donors, and governments in South Eastern Europe should ensure that economic transition proceeds with the full involvement of civil society organisations and local communities.**
- 3. The Stability Pact should ensure that South Eastern Europe's governments invest in health, education and social protection during and beyond the difficult transition period. While the process of economic reform should be designed to benefit the poor, it must also be combined with a strong social safety net to protect those who lose from transition.**

## Why poverty matters

A recent World Bank report, *Making transition work for everyone*, describes a disturbing increase in poverty and inequality throughout Eastern Europe and Central Asia.<sup>3</sup> Throughout the region, transition to a market economy brought new opportunities for some; however, for many it resulted in loss of jobs or prolonged nonpayment of salaries, loss of savings, and a deep erosion of accustomed social supports such as low-cost or free health care, housing and education. Between 1988 and 1998, absolute poverty rates increased from 2 to 21 per cent. In the worst hit areas, such as the CIS, result has been “a virtually unprecedented increase in poverty and inequality.”<sup>4</sup> Even in Poland, which is often cited as the success story of post-socialist transition, poverty in 1998 was still higher than in was in 1991.

Growing poverty has had disturbing social and economic impacts in Europe and Central Asia. Those without secure incomes appear to be forming a permanent underclass, with very few prospects of improving their life opportunities. Among this class, educational standards have declined, and there is a disturbing deterioration in standards of both physical and mental health.<sup>5</sup> Crime has risen sharply. Social cohesion has deteriorated, leading to attacks against marginalised groups such as Roma.<sup>6</sup>

What does this mean for South Eastern Europe? Here too, poverty and inequality have clearly increased significantly during the past decade, though the transition to regulated market economies has been held up by war and sanctions. For South Eastern Europe as a whole, economic decline throughout the 1990s followed a decade of economic stagnation in the 1980s; as a consequence, per capita GDP fell from 33 per cent of the

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<sup>3</sup> *Making transition work for everyone : poverty and inequality in Europe and Central Asia*. World Bank, Washington DC, 2000. The poor are defined in this report as those people living on \$2.15 per day

<sup>4</sup>op. cit., p.16

<sup>5</sup> For example, there has been an almost 100 per cent increase in mortality rates of Russian men between the ages of 40 and 59. Tuberculosis and sexually transmitted diseases have risen dramatically.

<sup>6</sup> See e.g. *Hard Budgets, Soft States : social policy choices in central and eastern Europe*, Eatwell et al, IPPR, London 2000

EU average in 1990 to only 24 per cent in 1998. But poverty in the former Yugoslavia has also escalated due to the devastating impact of war. One and a half million people remain displaced from their homes. Millions have lost their jobs, pensions, assets and all their savings.

Rebuilding communities after years of war and isolation is difficult and painful. Persistent poverty and inequality further erode social capital, community cohesion and individual willingness to take part in a major reconstruction effort. Limited economic opportunities contribute to persistent violence against minority returnees in Bosnia, Croatia and Kosovo,<sup>7</sup> and fuel resentment against traditionally marginalised groups such as Roma. Poverty forces people to focus on their immediate welfare, making community efforts difficult to sustain. Oxfam's programme in rural Albania is working to ensure the maintenance of agricultural irrigation systems, by establishing local management committees. This is important for the economic good of the whole community. However, families who have scarcely enough to sustain themselves often feel unable or unwilling to co-operate in such community efforts. Throughout the region, this leads to the deterioration of public goods such as schools and health centres, as well as to rising levels of social tension.

People whose incomes scarcely cover the food needs of their families are often unable to pay taxes, so state revenues remain depleted. As one respondent to a recent Oxfam survey in Bosnia explained:

"My husband is officially still employed in a state enterprise in Banja Luka, but his status there is on hold, so he is not currently receiving a salary. We have two small children – four and six years old. The only way to survive is to work in the grey economy. For now, we do not consider paying taxes to the government, although we would like to be able to do so."

The survey also found that the cost of utilities as a percentage of many people's average incomes is striking; but also that many people are not paying their bills. As another Bosnian put it:

"You are asking me what percentage of my income goes on utilities. It is impossible to calculate as I have no income. Try yourself: any percentage of zero is still zero."

According to unofficial estimates, approximately thirty percent of the electricity supply in Republika Srpska is 'missing,' as people have found ways to divert it. Non-payment of bills is also a common coping mechanism among pensioners, the unemployed and social cases in Serbia. Unless the state manages to pay pensions, this will hit the new regime as hard as it hit the old one in terms of lost revenues.

States with high and persistent levels of poverty will be unable to raise the revenues needed to pay for the institutional reforms necessary to attract foreign investment and to become established trading partners with the EU. Training civil servants such as customs officials will be essential for the success of the Stabilisation and Association process, and states will have to bear much of this investment. States also need revenues to ensure that the next generation receives the basic education necessary to compete in a global economy – 'not so much to train workers, as to make them

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<sup>7</sup> UNHCR has repeatedly stressed the links between successful return and economic regeneration. See Humanitarian Issues Working Group documents, October 1999-October 2000.

trainable.<sup>8</sup> Unless states can pay for this, the economic benefits of a well educated workforce - currently cited as one of the region's few comparative advantages in a globalised economy - will be lost. Cuts in state spending hit the poor hardest, and one of the key benefits that they lose is the opportunity to send their children to school.<sup>9</sup>

Widespread poverty acts as a serious brake on business growth in South Eastern Europe. Very low average incomes that scarcely cover basic food needs in Bosnia, Serbia and Albania mean that domestic demand is very low; the market in the whole region is only the size of half that of Greece. Poverty can also contribute substantially to the failure of small, new enterprises, especially when – as is frequent in South Eastern Europe – people do not trust the banking system and community savings schemes do not exist. Oxfam research on small family enterprises shows that family crises such as the need to pay for medical care often destroy otherwise viable businesses.<sup>10</sup>

Insecurity, poor economic prospects at home and poor community services all encourage coping strategies based on migration. Family groups in the poorest parts of the region pool their resources to send family members to Western Europe, legally or illegally. In Bosnia, where old people only receive their pensions around four in every ten months, many depend almost entirely on remittances from abroad. EU countries see illegal immigration as a key problem, but for many families in the region it seems the only way to earn an adequate income. Migration is likely to damage the long-term prospects for economic regeneration in South Eastern Europe, however, as it also contributes to the massive 'brain drain' from the region as the best-qualified people leave their home countries, often permanently.

Without equitable, sustainable economic growth, people in South Eastern Europe will continue to suffer from the material and social costs the recent conflicts. Poverty in the region is also a problem for the EU: without equitable growth, social tensions will persist, states will remain weak, and South Eastern Europe will continue to be a destabilising factor.

Aid to South Eastern Europe could do much more to reduce current high levels of poverty and inequality. Below we provide some recommendations for a re-focusing of assistance to the region, to promote economic growth with equity.

- 1. The EU should draw up a strategy to ensure that recent trade concessions bring economic benefits to marginalised communities. Economic assistance to the region should be explicitly designed to promote job creation and skills, which will allow poorer people to capture a greater proportion of the benefits of access to EU markets.**

Mass unemployment is a serious and growing problem in South Eastern Europe. Unemployment is as high as 55 per cent in Bosnia and Herzegovina, 35 per cent in Macedonia, and around 40-50 per cent in the FRY. Inequality has also risen

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<sup>8</sup> Mark Blaug, 'Education and the employment contract', *Education Economics* 1 (1), p.28 cit. World Bank, *Making transition work for everyone*

<sup>9</sup> In Macedonia, for example, the poor spent two times more on education (as a percentage of per capita expenditures) than did the nonpoor, but they spent less than half of what the nonpoor spent. World Bank 2000, pp 237-238

<sup>10</sup> Susan Johnson and Ben Rogaly, *Microfinance and poverty reduction*, Oxfam and Actionaid, London, 1997

significantly: in Macedonia, for example, the Gini coefficient rose from under 20 in 1993 to almost 30 in 1996.

Unemployment is a major cause of poverty in South Eastern Europe, as it is in other transition countries. In their detailed report on the causes of widespread and growing poverty, the World Bank found that the “poor in Europe and Central Asia cite loss of stable income as the overwhelming factor associated with poverty. Poverty is largely the result of bad labour market outcomes, such as the loss of a paying job, the failure to be paid for work completed, or insufficient income because of the lack of skills needed to compete in the new, more market-oriented economy.”<sup>11</sup>

Oxfam is concerned that if the poorer countries of the region, including Bosnia and Serbia, do not make rapid progress towards private sector development in deprived as well as relatively prosperous areas, privatisation will result in a massive drop in numbers employed, and also a decline in overall economic output. “Transition” implies a shift from a low productivity economy, which existed in pre-war Yugoslavia, to one in which workers produce more and are able to compete with strong and efficient EU firms. For Macedonia, which is ready to sign a Stabilisation and Association Agreement leading to eventual free trade with the EU, this has to occur within the coming decade, during which measures to protect domestic producers will be removed.

Moving workers from low-productivity jobs will only result in effective transition if they have higher productivity jobs to move to, however. As Joseph Stiglitz, former Senior Vice President and Chief Economist at the World Bank, states:

“Systematic reorganisation [of an economy] is different from reorganisation when a single firm has a problem... When there is already massive unemployment, firing workers moves them from a situation of underemployment to no employment – not necessarily a transfer that leads to an overall increase in the productivity of the economy, though it may improve the balance sheet of a particular firm... It cannot be the case that all firms are overstaffed – except if at the same time new firms can be *and are being* created to absorb the workers let go.”<sup>12</sup>

This shift from underemployment to no employment is likely to be made by thousands of workers in Bosnia next year, as privatisation proceeds. No clear assessment has been made of the social and employment impact of privatisation in Bosnia. However, 65 percent of Bosnia’s GDP is currently from the public sector. Some estimates suggest that up to 80 per cent of currently publicly-owned enterprises will not survive privatisation. Official and unofficial unemployment already stands at around 55 per cent in Bosnia. The impact of privatisation on families and communities in an already desperate economic situation is likely to be severe, both in terms of people’s incomes, and their loss of access to company-owned housing and services. The social impact of job losses will also be significant, as people finally lose the sense of inclusion and community they once gained through being part of a larger enterprise.

In the long run, the creation of sustainable jobs is the best way to keep people out of poverty, though this must be combined with adequate state provision of basic services and an adequate social safety net. The challenge to domestic and international policy makers is to ensure that new jobs are created to fill the gap left by the decline of the old

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<sup>11</sup> *Making transition work for everyone*, World Bank 2000, p.110

<sup>12</sup> *Whither Reform ? Ten years of the transition*. Paper prepared for the annual World Bank conference on development economics, Washington DC, April 1999

economies. The World Bank and the EBRD agree that private sector development will be the engine of economic growth and job creation.<sup>13</sup> It is therefore surprising that private sector development initiatives, and the institutional reform programmes necessary for their success, have received so much less support than infrastructure projects under the Stability Pact. In the Stability Pact's economic Quick Start Package, the promise of €1075m spending on infrastructure compares sharply with only €365 million for private sector development packages. Funds granted for a single "Quick Start" infrastructure project – the development of Sofia airport – are greater than the combined costs of all Stability Pact economic development spending on private sector development initiatives, economic reforms, business development, vocational training and education, environmental projects and social development.<sup>14</sup> While EU and bilateral country programmes do deliver additional assistance to small enterprise development,<sup>15</sup> the imbalance in the Stability Pact's focus is still striking.

Greater private sector development, particularly in marginalised areas, is essential for long term poverty reduction. Initiatives to foster private sector development can also have an impact in the short to medium term, in a way that infrastructure projects cannot. Rebuilding roads, bridges and airports takes a long time: eight months after the funding conference, only six of the thirty five proposed projects are under way. By contrast, most of the Stability Pact private sector development initiatives are already up and running.<sup>16</sup> The economic benefits of improved infrastructure are unlikely to be felt for several years, especially as many of the contracts – and therefore a large proportion of the profits from construction – go to Western European firms. When the projects do start, construction will result in some local jobs. However, the experience of Bosnia suggests that economic recovery driven by physical reconstruction is fragile and dependent on international aid;<sup>17</sup> it is therefore unlikely that the current focus on infrastructure elsewhere in the region will result in sustainable job creation.

Private sector development initiatives, carefully focused on poverty reduction, can bring immediate benefits to poor families. However, assistance that is driven mainly by the likelihood of short term commercial returns may result in the continued marginalisation of poor communities. The EBRD, which is responsible for private sector development initiatives under the Stability Pact, operates according to commercial principles. Through the Micro Enterprise Bank, the EBRD and its partners have helped small businesses in Bosnia and Kosovo to expand. However, the MEB's focus on relatively low risk enterprises and short term returns effectively excludes many enterprises in very deprived areas, such as small scale producers in rural Bosnia or Kosovo. People in these areas are often most in need of assistance.

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<sup>13</sup> See for example *The road to stability and prosperity in South Eastern Europe : a regional strategy paper*. World Bank, Washington DC, 2000, p.73 and Jean Lemierre, President of the EBRD, 'Making a quick start', *Financial Times*, 3 August 2000

<sup>14</sup> *Note on the status as of June 30, 2000 of pledges to the March 2000 Regional Funding Conference for South Eastern Europe and Stability Pact Infrastructure Projects : Implementation Status as of October 2000*, World Bank/EU Joint Office for South Eastern Europe, October 2000

<sup>15</sup> For example, the World Bank Local Initiatives Project and the European Commission Quick Impact Facility

<sup>16</sup> Jean Lemierre, 'Making a quick start', *Financial Times*, 3 August 2000.

<sup>17</sup> Bosnia has received euro 5.1 billion in assistance since the end of the war, yet unemployment remains as high as 55 per cent. High economic growth rates were achieved by the reconstruction effort, but 'achievements in this area are moderated... by the fact that recovery is fragile. Unemployment remains high, economic growth continues to be linked primarily to reconstruction, and refugees and the internally displaced have not yet returned in the numbers hoped.' *Lessons for rebuilding South Eastern Europe, the Bosnia and Herzegovina experience*, World Bank, 1999

How can the development of economic growth to benefit the majority – including those in deprived areas and communities - be achieved? One successful effort to encourage the development of small agricultural production has been assisted by ALDI, a micro-lending and small business support venture supported by Oxfam and based in Gorazde, Bosnia. ALDI assists local businesses in developing plans and linking their production efforts to larger partners. One successful project helps soft fruit producers to sell their produce to a nearby freezing factory, which then sells the frozen blackberries and raspberries to the larger markets in Austria and Italy.

Assistance in developing reliable market links is important for producers around Gorazde, as the area remains cut off from pre-war markets by the IEBL. Without the assistance of ALDI in identifying larger partners for business expansion, local small farmers would have to rely on the very limited local market. Ibrahim Imamovic, the manager of ALDI, points out that limited market and bureaucratic hurdles make it very difficult for people to establish viable businesses from Gorazde. However, he also claims that one of the biggest problems with business development is “in people’s heads.” Of 11,000 people employed in Gorazde before the war, 8,000 worked for the government or in state owned companies. People lack the skills necessary for entrepreneurial activities, so the business planning aspect of ALDI’s work is essential.

Businesses also need assistance in marketing their goods, both domestically - where they have to compete with mass imports from EU countries - and also for potential export. One Oxfam project in Serbia enabled groups of women refugees from Krajina to establish a successful clothing production business. Single women and women who lost their husbands during the war suffered heavily from displacement; providing skills to enable these women to sustain themselves and their children is therefore particularly important. Assistance has been focused on training in management, and ensuring that the high-quality, hand made garments were carefully designed and marketed. In the six months to September 2000, one of the groups generated a good income of DEM14,000, and also lobbied to municipal authorities in Kragujevac to let them establish a shop in the centre of town. One of the most important outcomes of the project is that the women realised their efforts in the beginning had paid off. Now they have determination and skills to ensure the project can sustain itself. As one woman put it:

“We have to support our families; we have to fight now that we have the strength for that. And we can see the results!”

Relatively small scale, low budget projects such as these can enable existing producers to expand their enterprises, to make enough money to pay for school books, or to enable families to save a little to enable them to cope with future crises such as the need to pay for medical care.

The European Commission admits that it finds administering these kinds of projects difficult and labour intensive. Without this kind of assistance, however, people will be unable to benefit from the EU’s new trade concessions which should, in theory, provide a boost to economic growth. The political achievement of pushing through the trade concessions will be meaningless unless these measures result in new opportunities for the people of South Eastern Europe. The autonomous trade measures should therefore be accompanied by renewed efforts to equip small producers with the skills and information needed to compete with EU firms, both domestically and in the EU market.

This would ensure that the new trade opportunities with the EU make a real difference to the economic prospects of people in South Eastern Europe.

### **2. The EU, principal donors, and governments in South Eastern Europe should ensure that economic transition proceeds with the full involvement of civil society organisations and local communities.**

Transparent, accountable and competent institutions are essential if economic development in the region is to succeed. In its strategy paper for South Eastern Europe, the World Bank states this very clearly:

'Building large infrastructure without sound policies and institutions for private sector development and social cohesion and inclusion, means wasting large amounts of resources without achieving the objective of sustainable economic growth and prosperity for the region.'<sup>18</sup>

Government corruption at all levels is still a key reason for business failure throughout the region.<sup>19</sup> The Stability Pact has established measures to combat corruption and to improve the business environment: the OECD is working with countries in the region to ensure implementation of the Investment Compact, which should establish a better legal environment for privatisation and economic development. However, few resources have been committed to institutional reform in the region.<sup>20</sup> Even if more resources were made available, the establishment of professional, competent and modern civil institutions would take some time.<sup>21</sup>

Economic reform in South Eastern Europe will not be postponed until the institutions necessary to regulate it are developed. Civil society institutions cannot substitute for competent and transparent state structures; however, together with international technical assistance and reform efforts from the top, they are an important instrument in fostering transparent, accountable and consultative state institutions. Strong and active civil society institutions have helped to prevent the capture of state assets by corrupt political elites in other transition states. Assessments of the experience of transition elsewhere also show that states with developed civil societies and a tradition of collective action influencing the political process were also more likely to be committed to poverty alleviation and ensuring the provision of basic services to the most vulnerable.<sup>22</sup>

Civil society organisations can help to pressure governments to implement reforms, and demonstrate the effectiveness of citizens' engagement with governments. They are positive role models which help to demonstrate to others the potential of acting together to promote change. Civil society organisations can also provide governments and international organisations with expertise, enabling them to target economic assistance more effectively to those in need.

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<sup>18</sup> *The road to stability and prosperity*, p.119

<sup>19</sup> See for example Oxfam survey on the business environment in Bosnia and Herzegovina, October 2000, and *Why will no-one invest in Bosnia and Herzegovina?* International Crisis Group, Brussels, April 1999

<sup>20</sup> See *Stability, Institutions and European Integration*, EastWest Institute/ESI discussion paper, 31 October 2000

<sup>21</sup> 'There are two very clear lessons from experience with government reform: institutional reform is very difficult, and even seemingly 'tractable' institutions such as budgetary processes or legal and judicial arrangements are hard to fix.' *The Road to Stability and Prosperity in South Eastern Europe: a regional strategy paper*, World Bank 2000, p.106

<sup>22</sup> *Making transition work for everyone*, p.118-9

One very positive example of civil society action which has performed these roles is the Kiri Herb Association in Northern Albania. The Association, which is supported by Oxfam, has brought villagers together to collect and market wild herbs in an area where there are very few other economic enterprises. The Kiri Herb Association, working with Oxfam in Albania, found a buyer for the herbs on the Internet, and now the members of the Association export their herbs to France. This has brought added incomes to the very poor households in the area and has also enabled the villagers to use the profits for a small scale community electricity scheme. The Association has also been effective in drawing the government's attention to a particularly deprived area, and this has brought further economic benefits: recently the Association also won a tender for a government/NGO reforestation project.

Civil society organisations can also help to foster a sense of ownership of the reform process, by giving people a voice in the decisions that affect their lives. Ensuring popular support for the transition process is essential for its success. Thousands in South Eastern Europe have already lost their jobs as a consequence of the closure of state-owned industries, and see little of benefit from transition. Many people are also angry about the way privatisation has proceeded so far. Insufficient regulation, limited sources of legitimately-owned private wealth, and frequently obvious links between political elites and the new owners of previously "socially-owned" assets understandably make people very angry and resentful of the whole process of privatisation.

Clearly the best way to gain public support for the reform process is to ensure that people experience the benefits themselves, and gain greater material security from transition; so more jobs are crucial. However, economic restructuring will involve painful decisions. Many people will have to learn new skills, and also to move to new areas to find work. More people in the region might be willing to support economic restructuring, and the challenges it brings, if they were given a greater opportunity to take part in and understand the process. Local communities and civil society organisations may be able to offer enterprising alternatives to complete closure of factories or companies. Workers are at least more likely to accept the difficult decisions that lead to job losses if they know that all options have been fairly assessed. Enabling people to discuss the problems they face with local government officials – for example, the fact that employment agencies in Bosnia hardly function so that people are unable to look for work elsewhere – might produce effective and relatively low-cost improvements to government employment and labour policies.

This dialogue does not exist at present, because governments do not seek advice from civil society organisations or local communities. Because most civil society organisations have limited experience in lobbying for greater transparency, they often do not push their governments towards consultative practices. Slavko Klisura is the head of Cinvos, a network of local NGOs in Eastern Bosnia. He says that people have to learn how to lobby their government at the local level to ensure the delivery of the services they need. Many of the local NGOs in the region are relatively young and weak. While they resent the fact that the government doesn't listen to them, he also feels that civil society organisations need help in using local media, seeking meetings with officials, and presenting their case to lobby for change.

National and municipal governments in South Eastern Europe need to be proactive in engaging with civil society. However, the international agencies working in the region also need to lead from the front in seeking the advice of local non-governmental

organisations. So far, their engagement with civil society at regional and local level has been limited. Slavko Klisura says that the international agencies working in Bosnia are as unresponsive as the local Bosnian authorities to civil society organisations: for example, the local OSCE democratisation office has never contacted him to ask about the Civos network. The Stability Pact, too, has been slow in engaging with civil society in the region. An “NGO Charter” was signed at the last Stability Pact Working Table I meeting, but so far there is no action plan to ensure that appropriate civil society partners are included in the design or implementation of Stability Pact work. Disappointingly, the Charter specifies only that civil society organisations should be involved in Working Table I (democratisation and human rights) projects, not economic reconstruction and development.

In June 2000 Oxfam pointed out that, by ignoring civil society organisations in South Eastern Europe, the EU and other donors were wasting regional expertise, as well as denying people a voice in the reconstruction process.<sup>23</sup> Regional civil society organisations have much to contribute towards ensuring economic reforms are appropriate to the specific needs of their communities, and to pushing governments towards their implementation.

To ensure that civil society can play its part in providing expertise and encouraging responsive and accountable government, more must now be done to promote a culture of dialogue between civil society, governments, and international organisations. Serbia is a good place to start. In conducting its needs assessment for Serbia, the EU and the World Bank should seek input from organisations at local as well as government level. Consultations with associations of farmers, trades unions, refugee support associations and a range of other community groups should enable the international team to understand better the economic needs and concerns of people throughout society. Ensuring a fully participative assessment process also sets an example to governments throughout the region about the potential for garnering expertise throughout society, towards more efficient and community-led reconstruction.

**3. The Stability Pact should ensure that South Eastern Europe’s governments invest in health, education and social protection during and beyond the difficult transition period. While the process of economic reform should be designed to benefit the poor, it must also be combined with a strong social safety net to protect those who lose from transition.**

Since its inception in July 1999, the Stability Pact has been the subject of extensive criticism. Governments in the region complain that the Pact has not delivered on its promises of rapid assistance. Donors complain that it is still unclear where the Pact “adds value” to the EU-World Bank partnership, the Humanitarian Issues Working Group, the Higher Level Steering Group, and other co-ordinating mechanisms for assistance to South Eastern Europe. Many people from the region feel that the Pact has had no impact on their lives, and that the promises made in Sarajevo after the Kosovo war remain unfulfilled.

One reason for this criticism is that the Pact seems simultaneously to be responsible for everything and for nothing. It is telling that the Stability Pact is often defined by what it is not: key participants are eager to stress that it is not a fundraising mechanism, nor is it

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<sup>23</sup> *Winning the peace? Some lessons from the EU’s aid to South Eastern Europe, June 1999-June 2000.* Oxfam International policy paper, June 2000. See [www.oxfam.org.uk](http://www.oxfam.org.uk).

a donor co-ordination mechanism. However, eighteen months after its inception, the Stability Pact's potential as well as limits are becoming clearer.

One important achievement for the Stability Pact is that it has succeeded in bringing the leaders of South Eastern European countries together regularly, and started a dialogue about priorities for stabilisation. This networking and priority-setting role is, and will continue to be, important in the reconstruction of the region. Bringing the governments of the region together enables the Stability Pact to use "peer pressure" to push them towards espousing publicly a common set of practices and values, with eventual EU accession as the final goal. The Pact has taken formal steps to consolidate this: for example, all countries of the region have signed an Investment Compact, committing themselves to a set of measures to improve the domestic and international climate for economic development. All countries have also agreed to participate in an anti-corruption initiative under the Pact. Implementation of these initiatives has a long way to go. Nonetheless, the Stability Pact, together with the EU through the Stabilisation and Association Process, can send public messages to the governments of the region, setting out the common values that South Eastern European countries need to practice in order eventually to become members of the EU's institutions.

The message that the Stability Pact has sent most strongly in the past year is that economic development is crucial, but that this depends mainly on physical rebuilding. So far, the main "theme" of Pact projects has been high profile infrastructure. This was perhaps a consequence of the Pact's wish to have – literally – concrete results to demonstrate commitment to the region.

Oxfam suggests that the Stability Pact adopt a different "theme" during the coming year. The Pact should use its public profile and its role as a regional forum to push donors and regional governments towards poverty reduction, promoting equitable economic growth, and ensuring that social justice is regarded as a central aspect of the move towards European integration.

The Social Cohesion Initiative, which was signed by Stability Pact participants at the October 2000 Working Table II meeting, represents a first step towards highlighting the links between economic growth, job creation, poverty reduction and long term regional stability. At the inception of the Social Cohesion Initiative, Stability Pact signatories emphasised that "the creation of employment and promotion of decent work for men and women are fundamental for achieving lasting stability and social cohesion." Pact signatories also agreed on priority measures to promote social cohesion in South Eastern Europe, including "taking measures to ensure equal access to social protection, public utilities, health care, housing, employment opportunities, educational and training facilities for all members of society."

The Social Cohesion Initiative must not be shelved as another empty declaration. The Stability Pact now needs to turn the principles set out in the Social Cohesion Initiative into regional action to reverse the growth of poverty and inequality. This means that that states must take responsibility for ensuring that the most vulnerable are protected during and beyond the difficult transition period, by providing an adequate safety net and universal access to basic services.

This will be difficult: given limited revenues due to economic stagnation, governments in the region are under heavy pressure to reduce expenditures. Social spending has

already been hit hard. The result has been a significant decline in public spending on key services such as education and health care. In Albania, for example, public spending on education declined from 3.8 per cent of GDP in 1995 to 2.8 per cent in 1999. The result has been declining enrollment at schools, and a fall to under ten years spent in formal education. Spending on health is also inadequate: at under 2.1 per cent of GDP, Albania's health spending is one of the lowest in Eastern Europe and Central Asia. Over 30 per cent of health centres are not functioning, and there is a serious shortage of physicians and nurses.

Social spending is an essential component of the process of stabilisation and economic development. Experience elsewhere shows that public investment in human development is essential for economic growth.<sup>24</sup> One of the positive legacies of Socialist Yugoslavia was a highly educated and literate workforce, which should be one of the region's key assets as it moves towards integration with the EU and the global economy. However, without continued investment in education, and with the persistent "brain drain" of educated people from the region to Western Europe and North America, these benefits are likely to be lost. The children of the poor are most likely to suffer from cuts in state spending, as their parents are unable to pay for school books, clothes, and the extra tuition often needed to ensure that they can gain qualifications. Donors must work with regional governments to ensure that access to education is universal, to enable the next generation to contribute to economic revival.

Market mechanisms are unlikely to ensure that those made vulnerable by war and displacement have access to essential services. Poverty is undoubtedly extremely high among refugee communities. One and a half million people remain displaced from their homes in South Eastern Europe. These people have lost their livelihoods, their savings and their homes. Most currently remain dependent on humanitarian assistance. States in South Eastern Europe need to ensure that those unable to benefit from market led reconstruction, including refugees, pensioners and the disabled, are able to access basic services and live with dignity.

Commitment to supporting the most vulnerable, and ensuring universal access to basic services such as health and education, are values that unite the members of the European Union. In reconstructing South Eastern Europe, the importance these values must not be forgotten, either by governments in the region or by their partners in the EU.

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<sup>24</sup> K Watkins, *Economic growth with equity : lessons from East Asia*, Oxfam, Oxford, 1998