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INSTITUTE NOTE

SERBIA AND CROATIA – RESURGENCE OF NATIONALISM?
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This conference brought together about 30 officials and leading experts from across Europe, including from Croatia and Serbia, to assess the meaning of the recent elections in the two countries for the prospects of continuing economic and political reforms, for the security and stability of the region, and for their relations with the EU. The main findings of the rich and lively discussions are summarised below, followed by more detailed accounts of the four sessions.

- ***Politics:*** The recent electoral successes of the HDZ in Croatia, and the Radical Party in Serbia, do not signal the return to the violently aggressive nationalism of the 1990s, directed against neighbouring successor states and minority populations of the former Yugoslavia. In both countries, extremism is fed by acute economic distress and disillusion with the outgoing coalition governments' ineffectiveness and internal bickering. In Croatia, top-down reform of the HDZ has begun – but not completed – the process of 'Europeanising' the party and channelling energies into the tasks set by integration into the EU and NATO. The prospects for early compliance with ICTY seem quite favourable here. The situation in Serbia is more worrying. The Radicals, an unreconstructed extremist party, has capitalised upon disillusion with the corruption and fractiousness of the outgoing government, as well as deep socio-economic distress. While a majority of voters opted for democratic parties, their inability to work together will mean continuing instability and a strong possibility of the Radicals winning the forthcoming Presidential election.
- ***The economic outlook*** for the region, apart from Croatia, looks very bleak. Relatively encouraging macroeconomic results cannot mask the incomplete nature of structural reforms, the absence of factors for self-sustaining growth (including in Croatia), and the already high levels of unemployment. Things will get worse before they get better.
- ***Security issues:*** Progress has been made in both countries on reform of the military and security sectors – in the past one of the key threats to security and stability in the region. But downsizing of the armed forces is a further challenge, sending many people with 'security skills' into the labour market, and potentially

into organised crime. Key 'unfinished business' remains on the regional security agenda, especially Kosovo and the viability of the Serbia-Montenegro Union (SMU), which will both rise once again to the top in 2005.

- ***EU policies:*** As long as EU accession remains a distant prospect (except for Croatia), the EU will need to provide some more immediate benefits to secure compliance with its conditionality. If it wants the SMU to survive, it will have to show more flexibility in its terms for the SAA, and will have to get more directly involved in internal state-building. In the short term, lifting the visa regime is probably the strongest card the EU has to play in the region.

I POLITICAL DYNAMICS: VOTERS, PARTIES AND LEADERS

The panel speakers agreed that the recent election results did not show a 'resurgence of nationalism', in the sense of a threat of violent aggression between nations. In ***Croatia*** voters chose the HDZ because they were looking for more effective government. The outgoing coalition was rejected because it was failing to deliver. The HDZ leadership had made a convincing start on reforming the party's image and removing the most compromised politicians from its previous period in power. It also ran a very good election campaign, presenting the image of a modern party with a determined leader ready to pursue a strong agenda of reform, prioritising the goals of NATO and EU accession. Croatian public opinion strongly supports these objectives. The HDZ has, moreover, drawn representatives of the Serbian minority into the new government. The results in ***Serbia*** could be seen as characteristic of a country only at the beginning of transition, which started late in 2000. An optimist would point to the fact that the democratic parties between them carried off more than 60 per cent of the vote. The vote for the extremist Radicals did not reflect a resurgence of nationalism, but protest against the corruption and sterile infighting of the outgoing government. A high proportion of Radical voters came from the poor, refugees and IDPs, and the Roma. Comparison was made with surprise electoral successes of unknown outsiders in early 1990s elections in Poland and Slovenia.

Some scepticism was voiced in discussion about these upbeat interpretations. In ***Croatia***, the HDZ now faces the key challenge of delivering General Gotovina to the ICTY. The HDZ leaders claim to be ready to do this, but will they carry their rank-and-file with them? If the nationalism of the 1990s has burnt out as a popular force, why is ICTY cooperation such a sensitive question for political leaders? Croatia has yet to complete the process of recalibrating its national identity with its sense of a European vocation. The Gotovina case presents the country with a clear historic choice, clarifying the full implications for both the elite and public opinion. The HDZ could well be better placed to deliver on this (and other difficult issues on the reform agenda), precisely because of its credibility and legitimacy as defender of the 'national interest'. The HDZ is now receiving useful advice from west European conservative and people's parties on how to revise it ideology and adapt to the demands of 'Europeanisation'.

There was felt to be less room for confidence about developments in ***Serbia***. The problem may no longer be nationalism; but the continuing inability of the democratic parties to work together is deeply destabilising. Even if the vote for the Radicals mainly reflects socio-economic distress, this does not of itself make it any easier to deal with. After all, the economic situation is not likely to improve rapidly in the near future. In the meanwhile, the failure of democratic politicians since 2000 to confront the legacies of the

war is symptomatic of a pervasive moral relativism that weakens popular resistance to the appeal of the Radicals or Milosevic's Socialists. The new government seems even less likely to take the necessary steps on either cooperation with the ICTY, or Kosovo, the two key political challenges it will face. Much hinges on the ability of incoming deputy Prime Minister Labus (of the reformist and pro-Western G17 Plus party) to persuade Kostunica of the urgent need to cooperate with the West. But the new government's dependence on parliamentary support from the Socialists is hardly a promising start.

In the short term, the retention of Boris Tadic as Minister of Defence at the level of the Serbia-Montenegro Union (SMU) would help to improve western perceptions. But it will be difficult for him to combine this with his position of leader of the Democratic Party (DS) in opposition in the Serbian parliament. It is essential for the democratic parties to put forward a common candidate for the Serbian Presidency, but is by no means clear that the strongest likely candidate, Kostunica, will be able to count on the votes of DS supporters. The favourite to win is therefore Tomislav Nikolic, the Radical Party's acting leader. In the given conditions, DS inclusion in the governing coalition should enhance the prospects of continued reforms, and build popular confidence in the capacity of the democratic parties to achieve results. Meanwhile, however, the Radicals and Socialists may well benefit politically from being the only opposition to a government that will have to implement very difficult reforms, with little prospect of quick 'success stories' in the economy, or a positive Feasibility Study from the Commission, or an invitation to join PfP.

II ECONOMIC PROBLEMS AND PROSPECTS

The difficult economic situation in both countries was clearly a major factor in their recent elections. The rather good macro-economic results – relatively good growth rates, progress in structural reform, and low/declining inflation across the region – have not yet trickled down to the population. Deep socio-economic distress largely accounts for the propensity of voters to opt for extremist political alternatives. And matters are not likely to improve in the foreseeable future. All speakers agreed the outlook is bleak.

Croatia's real GDP grew by about 5 per cent in 2003, but this was accompanied by a rise in the trade deficit to over 27 percent of GDP. Despite a very good year for tourism earnings, external debt rose to over 74 per cent of GDP, reaching about the same level in absolute terms as the whole of former Yugoslavia in 1989. Croatia is by far the main recipient of FDI in the region, but sustainable growth depends on development of the indigenous private sector and substantial improvement in productivity, both of which require more resolute pursuit of reforms by the new government: completing large-scale privatization and promoting small and medium enterprise; reform of public finances, administration, clarifying land ownership titles; further banking sector reforms; and, last but not least, strengthening the rule of law and tackling corruption.

Serbia's economy grew last year by 4 per cent – but GDP is still at only about half of its pre-war level. Only the services and construction sectors are growing, while deep de-industrialisation continues. Agricultural output last year was at an historic low, and the FAO has even issued a 'hunger alert' for the country. The debt service burden is growing, while the prospect of increasing exports in the short to medium term is limited. Much economic activity is unregistered, affecting data on private sector output and unemployment (officially 30 per cent). The informal sector is no doubt a lifeline for large

numbers of people. But its disadvantages are obvious, and not only because of tax evasion and its association with organised crime. Just as important is the fact that unregistered earnings are more likely to be spent on conspicuous consumption (thus increasing demand for imports) than on investment, building the basis for future growth and employment.

Structural reform came to a standstill in Serbia 2003. The political crisis held up large-scale privatization, bank restructuring and the passage of about 40 pieces of key economic legislation, which the newly constituted parliament needs to pass without further delay. The appointment of G17 Plus reformers Labus and Dinkic to key economic portfolios in the new government is encouraging. But Serbia will need to work hard to attract foreign investors. The problem for late-starters on the reform road in the western Balkans is that the world economy has moved on; Romania and Bulgaria have meanwhile overtaken Serbia in offering an attractive, low-cost location for potential foreign investors in the region. At the same time, it has to be recognised that there are no quick fixes for regions affected by de-industrialisation: neither the experiences of other transition economies, nor those of western countries, hold out much hope for rapid solutions.

The general picture of the region (apart from Croatia) is one of deepening decline. As one speaker put it, 'The region is dying'. There was some debate of the significance of the current 'brain drain' of young, well-qualified workers. In the short term – combined with very low birth rates – this is leading to a declining, and aging population. Those who do not leave simply adjust to their inexorably declining standard of living – and provide a sullen and embittered constituency for extremist demagogues. Others took a more positive view of the benefits to be gained from migration to the west, not only filling immediate gaps in western labour markets, but, in the short term, providing substantial financial transfers from remittances sent home to tide families over the difficult years ahead, while in the longer term transferring skills, entrepreneurial experience, and a more 'European' outlook, back to the countries of origin, to which many migrant workers are likely to return when they see prospects improving. In light of this, several speakers urged that the EU keep its visa policy towards countries of the region under constant review.

III SECURITY ISSUES

This session looked at two sets of issues: (a) reform of the military and security sectors in each country; and (b) the general implications of the elections for the 'unfinished business' on the regional security agenda.

(a) Military and Security Sector Reform

The military and security sectors have themselves posed a major security threat in both countries, illustrated most dramatically by the assassination of Serbian Prime Minister Dzindzic. In both countries, hesitant cooperation with the ICTY has been justified by politicians in part by reference to the difficulties of bringing this sector under proper political control. While Croatian participants in the seminar argued that pressure to comply with the ICTY had helped in this respect, in Serbia, fears of a backlash were still present. Security forces attached to the Milosevic regime had deeply penetrated the state and inhibited its capacities to control them, and thus to deliver on its obligation to comply with the ICTY.

Nevertheless, under SMU Defence Minister Boris Tadic, progress had been made in reform of military structures and leading military personnel from the Milosevic era had been removed. It was argued that younger officers in the army and police were ready to see their compromised seniors despatched to the Hague, and were keen to see their forces modernised with western assistance. Early accession to NATO's PfP would ensure acceleration of this. But control of civilian security and intelligence services remains in the hands of the two states.

One of the biggest problems for both countries (after ICTY cooperation) is downsizing the large armed forces and bloated military-related bureaucracies in conditions where alternative employment opportunities are not available. The danger is that many people with 'security skills' will find alternative careers in organised crime. Downsizing also has costly implications in terms of re-housing, re-training, the provision of financial incentives to potential employers and support for potential entrepreneurs. Some useful lessons can, however, be drawn from the Russian experience. One participant expressed deep scepticism about the desirability of accepting offers of SMU forces to assist in Afghanistan or Iraq. But it was explained that this had had a primarily political motive, as a gesture intended to impress the US of Serbia's will to rejoin the west.

(b) Regional security issues:

The western Balkans are slipping down the EU and US security agendas. The western military presence is decreasing significantly. When the EU takes over from SFOR in Bosnia-Hercegovina, it will be a much smaller force of about 7,000. The US will not leave the region altogether, but their interest is now focussed on the threat of terrorism. Yet 2005 will bring major unresolved issues in the region back to centre-stage: Kosovo and the future of the SMU. The election result in Serbia had only heightened apprehensions in both Kosovo and Montenegro. The situation in Kosovo is deteriorating rapidly, with mounting frustration. Major reforms, such as privatization, are blocked by the ambiguous status of the province. But Kosovar politicians also use the status question as an excuse for slow progress in fields where they do have the competence to act, such as much-needed reform of the Kosovo Protection Corps. While the recent elections in Serbia give little grounds for expecting new impetus towards a resolution of the Kosovo question, it was also argued that without at least some progress on refugee returns, any Serbian government would find it hard to move further towards a resolution.

It was reported that in Croatia the HDZ had changed its position towards the Bosnian Croats, and was now urging them to contribute constructively to strengthening Bosnia-Hercegovina as their state. Nevertheless, given that about 70 per cent of Bosnian Croats have Croatian citizenship, Croatia's coming integration with the EU is likely further to deepen their indifference to the fate of Bosnia-Hercegovina. Positive developments in Croatia's relations with Serbia were noted, including the impact of the Serbian minority's participation in the new Croatian government. But Croatia has to make further progress to convince Serbia – and western observers – of its commitment to encouraging refugee returns. Given that many refugees no longer wished to return, property issues needed to be addressed.

The question of the viability of the SMU entered the discussions at several points. Several participants shared the view that it was just not working, not least because of the uncertainties created by the possibility of a referendum on its fate in one or both constituent states in 2005 or 2006. The key was to find a way to prevent this obstructing

progress on other fronts, especially reforms and relations with the EU. It was pointed out, however, that the SMU in itself had little to do with Serbia's recent domestic political difficulties. It was important that this issue not be used by Serbian politicians as an excuse for delays in reform. It was by no means clear that the failure to reach agreement on the Union would have created a climate more conducive to political stability in Serbia.

IV POLICY CHALLENGES FOR THE EU

Despite the displacement of the Balkans from the top of the EU's agenda, the region will remain there in fourth or fifth place. Stabilization has made progress, but we now face complex and long-run challenges of state-building and economic development. The region is not yet firmly locked into the EU integration process and the situation in Serbia in particular could get worse before it gets better, and a coming array of Presidential and local elections will provide new opportunities for the Radicals to further enhance their strength. The discussion focussed on aspects of EU conditionality. As several participants noted, the EU is not a very strong player. The Western Balkans need the EU very much, but the EU is not able to offer very much in the short to medium term (except to Croatia). The EU needs to find some way of 'front-loading' the benefits of association and integration.

One participant voiced scepticism about the helpfulness of ICTY conditionality, but most others insisted that compliance was an essential indicator of governments' real commitment to leave the past behind and build states based on the rule of law as credible prospective members of the EU. Quick action by the new governments on ICTY cooperation is now vital to break the logjam. Croatia will not get a positive *avis* on its EU application without delivering Gotovina to the Hague. Croatian compliance will, moreover, have a significant impact on Serbian attitudes, and exert further pressure to Serbia comply.

EU conditionality related to the preservation and strengthening of the SMU received more critical attention. The EU had exerted enormous influence over its creation, and the Constitutional Charter makes frequent reference to the EU as the goal, the source of standards, and the monitor and arbiter of their implementation. This is not a traditional state but a peculiar union of two states, whose existence is almost wholly dependent on the will of the EU to preserve it. Yet the EU shows a reluctance to get more deeply involved in the internal problems of the state union, and moreover it also speaks with two voices: Solana's involvement was driven by the logic of regional security, but the resulting union is ill-equipped to meet the Commission's demands for compliance with the technical agenda of the SAA process. The member-states of the union are floundering in the internal harmonisation of agricultural tariffs. In the next two years the key is to prevent the union becoming just another source of frustration and delay. This calls for more flexibility and inventiveness on the part of the EU in negotiating the terms of the union's SAA.

A further point was that the economic problems of many parts of the region go beyond those of 'transition.' Some parts of the region were, economically speaking, hardly even touched by communist modernization policies and are now struggling harder than ever with problems of long-term underdevelopment predating communism, exacerbated by the impact of the last decade of war. Here, the standard recipes for 'transition' and

harmonisation with the *acquis communautaire* presuppose a complementary, comprehensive programme for socio-economic development.

On the question of what incentives the EU can offer in the short-term, discussion reverted to the question of the EU's visa regime. While EU member-states' resistance to liberalization here is clear, so is the negative impact of this on the achievement of other key EU objectives. The New Neighbourhood Instrument will focus on the promotion of cross-border cooperation with neighbouring states, which is impeded by the visa regime. The benefits of cross-border cooperation for rebuilding mutual trust and socio-cultural contacts between societies are important for regional security and stability. Cross-border cooperation can be a conduit for spreading the EU's values and understanding of its practices to its neighbours. A significant degree of economic interdependence has developed between border regions within new EU member-states and their counterparts in eastern and south-eastern Europe, which could be severely disrupted by the visa regime. Remittances from migrant workers from west Balkans countries working in the EU will continue to represent a sizeable contribution to the socio-economic stability of the region. Given that EU accession remains a distant prospect for most west Balkans countries, in the short-term, the promise of lifting the visa regime is probably the most powerful lever in the EU's hands to secure compliance with its conditionality.

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SERBIA AND CROATIA: NATIONALISM RESURGENT?

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