Economic Costs And Benefits Of The Eu Enlargement: The Impact On The Eu And Seec’s

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Abstract

The South-eastern enlargement of the European Union will be the sixth enlargement since establishing the European Community in 1957. The research uses the Gravity model, and measures the factors that have an influence on trade. The Gravity model involves coefficients that explain the pattern of trade with GDP, geographical distance, population, and several dummy variables. Trade that is explained by Gravity model includes two regions, EU-15 (inclusive Bulgaria and Romania) and SEEC's. The reason why Bulgaria and Romania are included, even if they are part of the SEEC's, is to acquire as accurate pattern of trade as possible. Comparing the data from 2010, the gravity model describes trade flows between 23 countries. Thus, the purpose of this study is to analyze trade flows between two regions.

Taking into consideration the costs of enlargement, this research examines the effects of the trade, its significance on the development of SEEC's after enlargement, well-being of countries that are not part of the EU, as well as it offers a solution for the South-east European countries. Therefore, the solution that this research proposes is a model based on creation of the Balkan Union.

Keywords: EU-Enlargement, Gravity model, South-eastern Europe, European union, Trade flows.

1.INTRODUCTION

The South-eastern enlargement of the European Union (EU) – the sixth since 1973 – is a huge test for the EU, as well as for the applicant countries. The European Union consists of 27 members. Besides incumbent members, there are candidates, as well as potential candidates. Inclusive candidates: Croatia, Macedonia (FYR), Montenegro, Iceland, Serbia and Turkey, the potential candidates will comprise the next enlargement of 9 countries. The potential candidates are Albania, Bosnia and Herzegovina, and Kosovo. This enlargement will increase the EU area by 25%, the number of population by 19%, and absolute GDP by 5%. Although, the exact time pattern of accession is not clear yet, the European Commission plans to start with a group of 3 states that consist of Croatia, Montenegro and Iceland. Turkey is not sure yet, whether to access the Union or not, because the country has strong economy, and many analytics think that joining the Union would hurt Turkish economy.

On the other hand, the applicant countries of South-eastern Europe are relatively poor countries with a GDP per capita below the EU average. Hence, the average GDP per capita of nine countries is $10,490 that would be 3 times lower compared to EU-27 or 4 times lower compared to EU-15.

Similar to the third EU enlargement, the next enlargement would be a new challenge for the EU countries, as the integration of poor with rich countries increases heterogeneity. The South-east European countries will enter the EU on the basis of the Treaty of Accession. Once they access the EU, the members are part of a union and a single market. One union of 27 countries with over 501 million consumers, which have access to a single market, is of huge importance for customers. Construction of a single market of the European Union has brought the new impact, and improved the emergence of a common EU policy such as competition policy. The EU constantly works on improvement of common policies, especially, on a common market. Those policies have gained great importance that increases over time. The policies are important, since they strengthen mutual trade, improve the quality of products and services, then they expand a single market, and the most important thing is that they reduce trade barriers and increase positive effects of the common market. As a result, the EU policies preserve the good functioning of market, and the European Commission prevents or corrects the non-competitive behaviour of companies. When it comes to South-east European countries (SEEC's), the fact is that its consumers enjoy a freedom of choice that is diversified by almost the same prices, lower quality and a fewer innovations comparing to the EU standards. The competition is present between SEEC's, but they are not competitive to the EU single market. Those companies cannot achieve scale of economies or competitive advantages as the EU countries do. Thus, this research shows economic costs and benefits that the EU enlargement brings to SEEC's. It presents gains from trade for both, the European Union and South-east European Countries. This paper looks at the economic costs and benefits of the enlargement of the EU, as well as the impact that the enlargement would bring to the South-east European countries.

2.MAASTRICHT TREATY, EUROPEAN UNION, SINGLE MARKET, AND SINGLE CURRENCY – EURO

In order to improve trade, six countries (Belgium, France, Germany, Italy, Luxembourg and the Netherlands) have adopted first four regulations for a common market in agriculture, finance and regulation of governing competition. On 1 January 1973, Denmark, Ireland and the United Kingdom joined the EU. Greece became the 10th member of the EU in 1981 and Spain and Portugal join Union five years later. The situation was stable until the Berlin Wall fell in 1989, so the European Economic Community (EEC) member states were negotiating over a new treaty at Maastricht in December 1991. However, it included intergovernmental cooperation in foreign policy and internal security that resulted in the Maastricht Treaty, which created European Union on 1 November 1993. The collapse of communism throughout Central and Eastern Europe has connected Europeans. As a result of that, in 1993 the Single Market was completed with freedom of movement of goods, services, people and money. Three new members came in 1995, Austria, Finland and Sweden.

The euro, Europe's single currency replaced the old currencies on 1 January 2002, when 12 EU Member States adopted it as their official currency, creating the euro zone. The euro zone makes life easier for business, consumers and travellers. On 1 May 2004, 10 countries got memberships in the EU: the Czech Republic, Cyprus, Hungary, Malta, Poland, Slovakia, Estonia, Latvia, Lithuania and Slovenia, while Bulgaria and Romania on 1 January 2007. Today, the EU has 27 member states. Enlargement to 27 was one of the most important steps in the history of European integration. 12 new countries in the EU, not only have expanded geographical size and population, but they have created an end for splitting the continent into two since 1945. As the idea of the EU says, democratic freedom was settled in 12 new member states. The creation of the single market gave European Union countries a strong incentive to liberalize previously protected monopolistic markets. Within the Union, Member States have removed all tariffs on trade, while having unified tariffs on imports from outside the EU. It means that no matter which country is the importer, the tariff paid on products is the same, and once customs procedures are completed, goods can be shipped throughout the EU without additional duties. In accordance to rules and regulations of the European Union, member of the Union should be guaranteed:

- Price stability,
- Stability of currency,
- Limitations of public debt, 60% of GDP,
- Economic balance with limited deficit of national budget,
- Investment stability, in sense of level of long-run interest rates, and

- 3% of GDP.

The European Union is formed on the principles of liberty, democracy, respect for human rights and fundamental freedoms, and the rule of law, principles that are common to the Member States. The EU has a motto, 'United in diversity', and May 9 is commemorated each year as Europe Day. By singing the Treaty of Rome in 1957, the EU members promised to abolish barriers to trade freely across the European continent. In Tupy (2003), the benefits of free movement of goods are seen as major benefits of consumers. Generally, the European Union has integrated the market, and established common rules. Those rules are implemented through technical standards of consumer protection, environmental standards, competition policy, and fairness in the workplace (Tupy, 2003, p. 6). Thus, for the SEEC's the common market could be a place for integration of every aspect of the state. Once the boarders are opened to flow of goods and capital, people would look at historic events less, and they will go for personal interest.

3.EUROPEAN UNION TODAY

Today, European Union exists as a union that aims to increase economic and political circumstances. The logic behind that is to deliver a peace, stability, and prosperity, to help improve living standards, promote a single currency that will build a single market, where people, goods, services and capital could move within the European Union. It is not a government or state or international organization, but a novel entity which respects human rights. Many countries, a huge single market, and single currency provide many benefits, but for whom? As a single market, the EU is a major world trading power. The single market aims at putting down barriers and simplifying rules to enable everyone in the EU to take advantage of the opportunities given to them by having access to 27 countries and 501 million people. Looking from economics perspective, small countries from Europe cannot achieve growth and prosperity without the EU. Therefore, in order to compete on the world stage and achieve economies of scale, the European countries need a broader base, and the European single market provides it. The single market is one of the European Union's greatest achievements. Restrictions on trade and free competition between member countries have gradually been eliminated; therefore, the whole system helps standards of living to rise. Within the EU, all border controls on goods have been eliminated, together with customs controls on people, but the police still conduct random checks as part of the fight against crime and drugs. When it comes to tax barriers, then tax barriers have been reduced by partially aligning national Value Added Tax rates, which must be agreed by the EU member states.

There is also the EU's competition policy that tries to ensure that within the European single market competition is not only free but also fair. Therefore, in the EU single market there is no cartel, or unfair monopoly.

The European Union was created to succeed in political objectives, through achieving economic cooperation. In modern terms, people call it as an "area of freedom, security and justice", where every citizen has an equal justice and protection by the law.

The European Commission represents the EU in international negotiations at the World Trade Organizations (WTO). Right now, the EU would like to put more emphasis on quality of food, precautionary principle ("better safe than sorry") and animal welfare.

The EU has regional policy stating that European Funds should be used to improve development in regions that are lagging behind, to increase standard of living in areas that are in decline, to help young people and the long-term unemployed find work. One important and interesting thing is that European Funds are also allocating funds to farming and to less-favoured rural areas.

In order to fund its policies, the European Union has an annual budget that in 2010 amounted to more than € 140 billion. The budget is financed from the EU's own resources that cannot exceed 1.23 % of the total gross national income of all the member states (Fontaine, 2010, p. 35). The resources are mainly collected from:

- Customs duties on products imported into the EU,
- A percentage of the value added tax (VAT) levied on goods and services throughout the EU, and
- Contributions from the member states, reflecting the wealth of each country.

The European Union has more influence on the world stage when it speaks with a single voice in international affairs such as trade negotiations.

4.European Enlargement

On January 1, 2007, the EU recorded the fifth enlargement. Bulgaria and Romania became new members of the EU. Before that, on May 1, 2004 the EU enlarged from 15 to 25 member countries. In the period from 1990 to 1999, the EU invested more than $85 billion to support the new Member States during the accession process (Delegation of the European Union to the United States of America, 2011, p. 21). Every new enlargement of the European Union is seen as a historic step toward long-term objectives of the union. Thus, any country that respects liberty, democracy, human rights and fundamental freedoms, and the rule of law is qualified to apply for EU membership. Applying for the EU membership is the start of a long and rigorous process. Once a country submits an application to the Council of the EU, it activates a sequence of EU procedures that may, or may not, result in the country being invited to become a member. After applying for membership, the process starts with accomplishing the Copenhagen Criteria. There are not many criteria, but, in essence, every country has to work on it, since the criteria are detailed. Fontaine (2010) mentions these criteria as follows:

- Institutions that provides high democracy, the rule of law, human rights and respect for and protection of minorities.
- Strong market economy and the ability to cope with threats and pressure within the Union.
- Ability to take on the obligations of membership, accomplishing the aims of the Union (Fontaine, 2010, p. 16).

Once the Council unanimously agrees to begin accession negotiations, discussions may be formally opened. The negotiation has got 35 separate policy areas that are called “chapters”, and each candidate country proceeds separately from one stage of the process to next. Each stage must satisfy all conditions, and then the candidate country could move on. Thank to this process, the prospect of accession acts as a powerful incentive for reform, providing simultaneously benefits to the EU and to its acceding members.

A candidate country is one whose EU membership application has been accepted by all relevant EU institutions, allowing it to begin accession negotiations. Once negotiations are concluded to the desired level for both sides, a comprehensive Draft Accession Treaty is submitted for approval by the Council of the EU, the European Commission, and the European Parliament. After the treaty is approved, it is signed by the candidate country and the representatives of all EU Member States. Afterward, all Member States and the candidate get the treaty for ratification. Once the ratification process is done, the treaty enters into force on its scheduled date, and the candidate country becomes an EU Member State.

5.Enlargement of the South-eastern Europe

The next enlargement in the EU is related to Western Balkan region. The structure and procedures to be applied on the Western Balkan region are the same as it was for the former candidates. A first significant step in this process is the establishment of European partnership with Albania, Bosnia and Herzegovina, Kosovo, Montenegro, and Serbia. It would be a very important factor that assists the Western Balkan states in preparing for membership within rational framework and in developing action plans with timetables of reforms.

"The main instrument that created by the European Union for Balkan integration is the Stabilization and Association Process (SAP), launched in 2000, that was established as a long process in order to establish development of the Western Balkans both in terms of political effort and financial and human resources" (Montanari, 2005, p. 59). The aim of the SAP is to create conditions that alike to the EU. Thus, the candidates work on preparation for future EU standards.

When it comes to SEEC's enlargement, conflicts can arise between European Union members as a result from its redistribution effects. EU members observe SEEC's as a geographical area for expanding single market that can import more goods and services from the current EU members. Once the union is enlarged, there is a new distribution of income that can create lower income for some of the EU 27. That is not the only threat for EU 27, high unemployment is another one. Taking this fact into consideration, when more immigration happens, the neighbouring countries of the SEEC's might be affected more. First targets are Slovenia and Hungary as very close countries to candidate of the EU. Previous five enlargements are observed if they were Pareto efficient for all member states and the candidate states, and evidence suggests that enlargements were not Pareto efficient in every enlargement round (Schneider T. P., 2007, p. 570). Thus, as Schneider (2007) states, the next enlargement is going to be very complicated from aspects of EU redistribution and from the free movement of labour. Thus, "the EU Eastern enlargement will adversely affect labour-intensive and low-tech sectors in the EU member countries but will stimulate growth of skill-intensive service industries and some capital-intensive and high-tech industries in Western Europe" (Schneider T. P., 2007, p. 572).

Table 1

Basic Socioeconomic Indicators for South-eastern Europe (2010)

	Population (millions)	Per capita GDP (current US$)	Unemployment 2009 (percent of labour force)

Albania	3.20	3,678	-
Bosnia and Herzegovina	3.76	4,409	-
Bulgaria	7.54	6,325	6.8
Croatia	4.42	13,754	9.1
Kosovo	1.82	3,059	45.4
Macedonia	2.06	4,460	32.2
Montenegro	0.63	6,510	19.1
Romania	21.44	7,538	6.9
Serbia	7.29	5,269	16.6

Sources: World Bank, *World Development Indicator.*
Monstat, *Department of statistics of labour market, life conditions, social services and household consumption.*

As a result, the candidate countries would have an incentive to export workers, rather than to attract them. Table 1 shows the unemployment rate, population and GDP per capita for SEEC's from 2010. From the table it is obvious that for relatively slow countries the unemployment rate is high. Kosovo has unemployment of 45.4%, but the real unemployment rate is around 25%, since the country has a problem with a gray economics. The other countries have acceptable rates, but still high that is a threat for labour migration and labour inflows in the EU. Two biggest countries of the SEEC's became the EU members, and remaining 7 will bring 23 million new customers to the single market. If we take into account GDP's of SEEC's than it is obvious that states have relatively low ones, comparing to the EU-15 (4 time lower), and EU-27 (3 time lower). Some of the candidate countries are economically weak, with high unemployment rate and low wages, and they will be ready to adapt to the system of free movement of labour. However, the Union could apply the potential limitations on the free movement of workers of new member. There was a case when the United Kingdom joined the Union in 1973. The state had to accept the limitations on the free movement of its workers within Belgium, France, Germany, and Luxembourg (Schneider T. P., 2007, p. 574). This clause could be used when accepting SEEC's to the Union, where Austria, Slovenia, and Hungary might ask for limitations of free movements of these three countries' workers in order to sign accession treaty.

Within the EU, the gains from the enlargement could be redistributed from the either relative winners of enlargement (members of the Union or the candidates) to the relative losers of enlargement that can also be state from these two groups.

When it comes to trade flows in 2010, than from Table 2 we see that Croatia is a main exporter to the EU-15 (BG+RO). The total import for the EU-15 (BG+RO) is 32.42% of total of the SEEC's. On the other hand, Croatia is the leader in imports, as well. The total export from the EU (BG+RO) to Croatia is 39.32 of total of the SEEC's exports. From that fact, it is not surprising that the country is the first to access the union. After enlargement the imports will be higher for each country, the members of the EU will export to SEEC's and try to import less. Croatia and Serbia to some extent manage their resources properly, but the rest have to increase an export that is almost 40% of overall exports to SEEC's.

Table 2

EU-15 + BG and RO trade with South-eastern Europe by Country (2010)

	EU-15+BG and RO Imports		EU-15+BG and RO Exports	
	Million US$	Percentage of Imports from SEEC's	Million US$	Percentage of Exports to SEEC's
Croatia	4,149	32.42	9,069	39.32
Serbia	3,867	30.22	6,414	27.81
Macedonia	1,738	13.59	2,081	9.03
Bosnia and Herzegovina	1,732	13.53	2,557	11.09
Albania	1,157	9.04	2,442	10.59
Montenegro	152	1.19	500	2.17

6.Strategy

The strategy of the EU for creating sustainable growth and jobs encourages innovation within businesses and investment in people that can design a knowledge-based society. Not only that, but the idea is to attract more people into employment, and keep them in work longer as life expectancy rises. Besides, the adaptability of workers and enterprises, provide better education and skills, globalization and mobility would increase the well-being of the society. By 2020, the EU aims to have accomplished the following targets:

- 75 % of the population aged 20-64 should be employed,
- 3 % of the EU's GDP should be invested in R&D,
- The “20/20/20” targets in terms of reduction of greenhouse gas emissions, renewable energy production, and energy efficiency should be met.
- The share of school dropouts should be under 10 % and at least 40 % of the population between the ages of 30 and 34 should have a degree of diploma.
- 20 million fewer people should be living below the poverty line (Delegation of the European Union to the United States of America, 2011, p. 38).

In order to accomplish the objectives, the EU adopted a proposal to re-focus R&D and innovation policy on major challenges; enhance the quality and attractiveness of Europe's higher education system; deliver sustainable economic and social benefits from a Digital Single Market; enable the EU's industrial base to become more competitive, promote entrepreneurship, and develop new skills for workers; and ensure economic, social and territorial cohesion by helping the poor and socially excluded.

7.COSTS AND BENEFITS OF THE SOUTH-EASTERN ENLARGEMENT

7.1.The Overall Economic Impact of the Enlargement

Taking into account the economic costs of enlargement, as well as the distribution of gain among incumbent Member States, we should consider the broader benefits and costs for the Union's economy that would take place after the enlargement.

The countries of the last EU enlargement were highly welcomed in the EU alliance because they belong to those of the developed countries in the EU, and, hence, did not only cost nothing, but contributed to the EU budget with significant amount. In a case of the South-eastern enlargement, the EU incumbents are firstly concerned about the costs, rather than the possible benefits.

Typically, this enlargement would enable consumers and companies to arrange their businesses more efficiently, so that there would be higher output and income. Taking into consideration the costs of enlargement the question is how the distribution of gains is shared among the EU members. Those countries that have strong trade relations with the SEEC's will benefit.

The European enlargement process is by no means a win-win project, but relatively unpredictable condition that creates both winners and losers. Due to the huge wage-gap between East and West sides of Europe, there might be a migration wave from East to the West, as a result of full involvement of East side of Europe in the single market.

On the other side, there are almost certain gains for some new members. Thus, the incumbent members prolong the acceptance of those candidates. One obvious case is Turkey. The country has applied for the European Union, and almost 17 years later in 2004, the EU finally decided to open accession negotiations. This news was a real shock for almost each member of the Union. That was in the period when Turkey was becoming stronger in its economy. The country was showing signals of real and healthy economy. Thus, many EU states appeared unwilling to accept Turkey to the European club. Immediately, some of them emphasized that the applicant would have to accept few exceptions from the common policies. Germany asked for permanent restrictions on the free movement of labour while France and other members of the EU called for refusing an allocation of agriculture subsidies to Turkish farmers (Schneider C. J., 2007, p. 85). Thus, from the case of Turkey, it is obvious that EU members are only looking for distribution of gains. Current members will question enlargement if a new state is to decrease the gains.

In this context, economic integration with the European Union is a challenging issue. Official unemployment rates are very high, while "unofficial" estimates of unemployment that include the large gray economy could be lower for 20%. Thus, it is obvious that SEEC's will benefit from the enlargement. They can export workers to neighbouring countries, even they can increase net trade, but the costs will be imposed on the current members of the EU.

Table 3

EU-15 Countries' Imports + BG and RO from South-eastern Europe (2010)

Country	Million US$	Percentage of the EU total imports from the SEEC's

Italy	4,426	34.61
Germany	3,047	23.83
Austria	1,680	13.14
Greece	744	5.82
Romania	488	3.82
Spain	411	3.21
France	396	3.10
Netherlands	378	2.96
United Kingdom	344	2.69
Bulgaria	338	2.64
Belgium	267	2.09
Sweden	106	0.83
Denmark	60	0.47
Portugal	41	0.32
Finland	27	0.21
Ireland	23	0.18
Luxembourg	11	0.09
Total	12,787	

Source: IMF, *Direction of Trade Statistics.*

When it comes to patterns of trade in the past few years, the EU trade with the South-eastern Europe has been in surplus; expressed in U.S. dollars. The largest trading partner of the SEEC's is Italy, which absorbs 43 percent of EU imports from the region and accounts for 33 percent of the exports (Montanari, 2005, p. 7). This suggests that geographical distance plays a considerable role in determining trade patterns. Table 3 shows that in 2010 Italy accounts for 34.61% of total imports from SEEC's to EU-15 (BG+RO). That is the main reason why SEEC's trade mostly with their neighbouring partners. Behind Italy are Germany, Austria, Greece and Romania. It shows that distance between capitals plays considerable role in international trade. Countries that are away from the SEEC's take account of around 10% of total imports.

7.2.The Costs of Enlargement

When it comes to costs of the enlargement, then the most significant ones are: the costs for public finances, the costs of labour market disruption, and the costs of wage competition (Grabbe, 2001, p. 33). On the other hand, we have to take into account costs of the expansion of membership as well. It means that the EU bureaucratic machinery is likely to grow to be unmanageable. There is the added cost of preparing translations of all EU documents in language of member state. However, the cost of preparing is in second place, behind the reaching decisions.

Reaching decisions on a unanimous or qualified-majority basis is likely to become more difficult (Richard E. Baldwin, 1997, p. 172). South-eastern countries have problems in reaching decisions in their parliaments, and accession to the EU would make things worse, since the new members would, very often, go for personal feelings, rather than for well-being of the society. Voting prolong, and not reaching decision on time, would increase the costs of bringing people to the parliament, and most important is the time spent while new regulations could have already taken place.

Nowadays, the situation of Croatia and its accession to the European Union is related to neighbouring countries. Many analysts of macroeconomic issues warn saying that if Croatia enters the EU; many mechanisms will change, especially for Bosnia and Herzegovina and its exports and imports, because the EU asks for high criteria of product quality. As a country with cheaper labour, Bosnia is going to be a place where Croatia produces licensed products that are expensive to be produced in the EU. There are Croatian media, who speak about negative consequences of accession to the EU. If Croatia joins the Union, it would become small, political and economical unessential province inside the European giant countries (R.I., 2012). The European Union is not a single country, but Union of different people and countries (big and small), where member states represent their own interests on European level better and more efficiently, then in a case they would, in today's globalized world, without the Union.

Table 4

EU-15 Countries' Exports + BG and RO to South-eastern Europe (2010)

Country	Million US$	Percentage of EU total exports from the SEEC's
Italy	6,116	26.52
Germany	5,428	23.54
Austria	2,775	12.03
Bulgaria	1389	6.02
Greece	1,344	5.83
Netherlands	1,332	5.78
Romania	1,120	4.86
France	904	3.92
United Kingdom	785	3.40
Belgium	568	2.46
Spain	548	2.38
Denmark	254	1.10
Sweden	191	0.83
Ireland	149	0.65
Finland	109	0.47
Portugal	32	0.14
Luxembourg	15	0.07
Total	23,059	

Source: IMF, *Direction of Trade Statistics.*

Table 4 shows almost the same results as Table 3. Italy, with 26% is a leader in exports from SEEC's, where Germany, Austria, Bulgaria and Greece come after. One half of the countries from the table have a total of 15% of overall exports that explains again importance of distance between capitals.

7.3. The Economic Benefits of Enlargement

After enlargement, benefits will accumulate, not only to the member states of the Union, but also to us, individual citizens. One of the principles on which the EU is based is that it will improve the welfare of its member states and their citizens. This process does not have appeal to the government of the member state which have initiated the accession process; it is also expected to have an influence on the citizens and their readiness to assist integration process. The main economic benefits after enlargement are the classical ones generated by integration processes. Thus, those benefits can be generated from expansion of the Single Market, strengthening of the Union's position in global markets and catching up with EU living standards. When SEEC's join the Union they will be passing from a free trade area for manufactured products to a single market. The major benefit is free movement of workers, which is a highly sensitive issue.

Enlargement will be good for the European economy. Enlargement will add over million consumers to the single market that will create many new jobs in both the applicant countries and the incumbent member states. Looking from perspective of European companies, they are looking forward to seeing more states on the EU single market that would possibly reduce the risk of doing business in the other half of the continent.

In the long-run, the applicant countries will need help from the EU in order to increase private investment that will meet the EU environment and transport standards. The main economic benefit of EU membership is a potential improvement in the investment climate of the South-east European countries.

When the SEEC's join the EU, participation in the single market should involve the end of contingent protection (anti-dumping and safeguards). In1999, the total number of anti-dumping investigations opened was 86 (Nello, 2002, p. 296). It is obvious that some countries will be better-off and some worse-off. Bosnia can increase the sale of its domestic tobacco company`s products if it proves that the Croatian tobacco company is dumping in Bosnia (this case was speculated in media in 2010).

The EU imposes environmental regulations that take into account environmental quality protection, production processes, and products (Tupy, 2003, p. 9). One of the significant benefits will be quality in the countries of South-eastern Europe. It will affect local producers, and decrease their profits, but more importantly, the customers will be better-off. Besides, citizens will enjoy higher air quality, water protection, pollution controls, and all other things that create negative externality. For instance, people from Zenica (Bosnia and Herzegovina) could have higher air quality, when Environmental Regulation Agency introduces pollution control to Metal company.

8.GRAVITY MODEL

8.1. Gravity Model of EU-15 (including Bulgaria and Romania) and SEEC's

The aim of this research is to analyze trade patterns between the EU and SEEC's. Thus, the research devotes much time analyzing trade between the European Union and South-eastern Europe, and it uses one of the most popular models in International Economics – Gravity model. Therefore, it is attractive to evaluate whether there could be a potential for trade growth between the two groups. The answer to this question can be obtained by estimating a gravity model of trade. Such model as gravity is very often applied to research trade patterns between countries. The model that is used in this research is very similar to one that Montanari (2005) uses while explanating trade patterns. Gravity model describes bilateral trade patterns in accordance with socioeconomic and geographical characteristics of the countries measured (Montanari, 2005, p. 60). The gravity model is used to measure bilateral trade flows between EU-15 and SEEC's.

The countries included in the analysis are divided into two groups. First group consists of the EU-15, while the other includes countries from the South-eastern Europe. Even if, Bulgaria and Romania are the members of the SEEC's, the research uses them as the EU members, to get more precise results. EU-15 does not include Bulgaria and Romania, but EU-27 does, so we obtain a real potential of the SEEC's only if we include two countries into the first group. Greece was a part of the EU-15, and, therefore, it counts in the first group of the model.

This research uses the data as from 2010. Thus, there are separate indicators for Montenegro and Serbia. Due to lack of data, the analysis excludes Kosovo.

The equation of the Gravity model is as follows:

$$\ln X_{EUp} = c + \ln gdpexp + \ln gdpimpo + \ln dist + BOR + CU + U_{EUp} \qquad (1)$$

X_{EUp}: is the export flows from EU-15 countries (including Bulgaria and Romania) to SEEC's. We take data for exports (2010) that are measured in current US Dollars, Millions.

$gdpexp$: represents the GDP of the exporting country expressed in current US Dollars, Millions.

$gdpimpo$: is the GDP of the importer country expressed in current US Dollars, Millions.

$dist$: is the distance between capitals of exporter and importer in kilometres.

BOR: is the dummy which has 1 if exporter and importer share a common border and 0 otherwise.

CU: is the dummy variable which is 1 if exporter and importer countries use a common currency and 0 otherwise.

$bilateral$: is a dummy variable which takes 1 for a specific importer and exporter country and is used to capture the effects of any political, historical or cultural event between two countries.

U_{EUp}: describes error term.

Appendix A mentions data sources used in the model and explain the functions of the gravity model. The model says that trade increases if countries have the same border, or they use the same currency. In a case of signing a bilateral agreement, like CEFTA, the trade barriers decrease and countries trade more.

8.2.The Basic Gravity Model

Table 5, which consists of 4 models, explains patterns of trade between the EU countries and SEEC's. In the first model, GDP of exporter country seems to have a positive effect on trade flows and its coefficient of 1.06 shows that when GDP of exporter increases by 1%, its exports increases by 1.06%. Similar result is given for the importer, where the coefficient of 0.78 shows the increase in trade flows when GDP of importer increases by 1%. There is negative coefficient for the distance saying that when countries are further they trade less. In order to decrease the cost of transportation, those countries trade mostly with neighbouring countries, and the model says that 1% increase in distance will decrease trade by 2.39%. Besides that, the model uses dummies such as common borders and currency. While common borders have a positive impact on trade with coefficient of 0.53, the common currency has a negative effect with -0.62. This negative dummy might be a result of not using Euro. Montenegro is the only one, who is a member of the Euro zone. The value of R2, 86%, shows that this model explains 86% of the variation in trade flows between the EU and SEEC's.

Table 5

Gravity Model: Regression Results

Variable	Model 1	Model 2	Model 3	Model 4
lngdpexp	1.06	1.06	1.06	1.06
	(0.07)	(0.07)	(0.07)	(0.07)
lngdpimp	0.78	0.78	0.89	0.76
	(0.11)	(0.11)	(0.09)	(0.11)
lndist	-2.39	-2.34	-2.52	-2.33
	(0.18)	(0.20)	(0.17)	(0.20)
BOR	0.53	0.58		0.58
	(0.35)	(0.36)		(0.36)
CUR	-0.62	-0.64		-0.74
	(0.30)	(0.30)		(0.33)
bilateral		0.00		
		(0.00)		
expfix			0.00	-0.01
			(0.02)	(0.02)
impfix			-0.01	0.04
			(0.05)	(0.05)
cons	-11.30	-11.72	-13.08	-11.54
	(3.28)	(3.35)	(3.07)	3.36
R^2	0.86	0.86	0.85	0.86
RMSE	0.81	0.81	0.84	0.81
AIC	249.31	250.81	255.99	252.13
BIC	265.00	269.11	271.68	273.05
N	101	101	101	101

8.3.Bilateral Effects Model

The equation used to estimate column 2 is:

$$\ln X_{EUp} = c + \text{lngdpexp} + \text{lngdpimpo} + \text{lndist} + BOR + CUR + \text{bilateral} + \quad U_{EUp} \qquad (2)$$

where bilateral is a dummy variable which takes 1 for a specific importer and exporter country and is used to capture the effects of any political, historical or cultural event between two countries on their trade flows, and all other variables are the same as Equation 1.

Second model has the same coefficient of GDP as the first one. Thus, if there is any increase in GDP of exporter and importer countries, the trade would also boost. In the second model, there is a slightly lower coefficient of distance, because the bilateral variable is included. The coefficient of common borders says that trade increases if two countries share the same border.

8.4.Main Effects Model (Exporter and Importer Fixed Effects)

The equation used to estimate Model 3 is:

$$\ln X_{EUp} = c + \ln gdpexp + \ln gdpimpo + \ln dist + expfix + impfix + U_{EUp} \quad (3)$$

where $expfix$ equals 1 whenever a country is exporting and 0 otherwise and $impfix$ equals 1 whenever a country is importing and 0 otherwise. These dummies might differ depending on the countries' tendency to export and import.

This model does not include dummies and bilateral effects variables, but it has exporter and importer fixed effects. In general, the model does not give a better picture; R2 is lower than the first and second models, and even, Akaike`s information criteria (AIC) are worse.

8.5.Main Effects Model with Dummies

When we enlarge Model 3 with common border and common currency variables, the model becomes the following:

$$\ln X_{EUp} = c + \ln gdpexp + \ln gdpimpo + \ln dist + BOR + CUR + \quad + expfix + \ln impfix + U_{EUp} \quad (4)$$

The model has a higher R2 with 86%. The distance has a negative coefficient as usual. The model says that neighbouring countries trade more with each other than other countries.

The results show that trade increases with economic size, measured by GDP in our model while it decreases with distance between them. This kind of model could be very useful for analyzing international trade; it is seen in the straightforwardness of explanation of trade patterns that can be used to test the impact of new policy measures.

8.6.Results

Measuring overall economic impact of EU-enlargement is almost impossible task given that there are problems of global economy, uncertainties, which could change the whole process. The main benefits of enlargement for incumbent countries are not economic, but rather they are related to stability and security. The economic benefits to the EU-27 will not be significant in the short-run, neither the costs. However, in the long-run the whole European economy will gain significantly from enlargement.

Table 5 presents four different models, where each of them consists of various variables. Each model uses GDP of exporting and importing countries. By becoming a part of the single market, there would be increase in the outputs and the growth of imports and exports that lead to an increase in GDP. As a result, according to the results of our models, if SEEC's access the union, GDP's will become higher, trade will increase, and at the end export flows become larger. Therefore, households would benefit from the European enlargement and from the removal of tariffs. Removal of tariffs would lead to reduction in import prices, and will affect the allocation of household income.

The removal of trade barriers would have a clear impact on price setting. As a result, the scenario would be a reduction in prices. Conversely, the increased demand should be taken into account, together with the removal of trade tariffs, which at the end will provide a positive output.

The European Union has to manage enlargement appropriately if it wants to gather all the potential benefits. Flourishing management depends on developing political strategy that is behaving in interest of enlargement as a way of gains for the public and for interest groups.

Comparing previous enlargements and next ones, there are significant differences. For instance, Greece, Portugal and Spain became members of the EU before the single market and monetary union programs were implemented. Thus, they became members when the EU was a much less integrated and smaller market. Today, the EU economy is experienced and it has a faster growth trade than it was in time of accession period of Portugal and Spain.

The main benefits of enlargement for the SEEC’s are not only economic, but they are more oriented to provide stability and security. The major risks are concerns of large migration flows, wage competition, and the costs to the EU’s budget.

Results show that there is a room for trade to increase, especially, in neighbouring countries. SEEC’s would have to invest in new technology in order to be competitive for the EU single market.

9.POLICY SUGGESTIONS

Yugoslavia was located in the South-eastern Europe, in the heart of the Balkan Peninsula. The heart connected two continents, Europe with Asia, and was the gate to the Black Sea. The country had resources and good geographical position to grow and become super power of Europe. Unfortunately, the country had not been unable to run resources properly.

The economy of Yugoslavia was oriented toward agriculture, so the whole national prosperity depended on the development of agriculture. The character of Yugoslavia is seen in the fact that out of 24,849,425 hectares of the whole territory, 11,500,000 hectares, or 46 per cent, account for agriculture (Roucek, 1933, p. 414). The country produced hemp, cotton, hops, opium, tobacco, etc. All these, and many other products, were high quality. The important thing is that no single part of Yugoslavia produced all these products. The country consisted of 7 parts that are today independent countries (Bosnia and Herzegovina, Croatia, Kosovo, Macedonia, Montenegro, Slovenia, and Serbia). Hence, each part of Yugoslavia was famous for the production of a particular good. Exports went mainly to France, Germany, and Switzerland. The interesting thing is that each province of Yugoslavia has its own special kinds of fruits. Different fruits and variety of foods and beverages are produced in a way that is traditional for every region of the country. Besides that, there were plenty of mineral resources such as coal, iron, copper, etc. Yugoslavia could, by its richness of iron, take a place as one of the leading countries in Europe. The main importers of Yugoslavian products were Italy (28.31%), Austria (17.68%), Germany (11.66%), Hungary (7.18 per cent), Greece (6.05%), etc. (Roucek, 1933, p. 420). The main products of exports were wood, cement, cereals, and ores.

The economic situation of Yugoslavia gave a real situation of the country, the country`s potential, and prosperity. Today, the former parts of Yugoslavia need a stabilization process that would bring them to previous conditions. It is obvious that countries need capital and investment in infrastructure.

Taking all of these facts into consideration, a solution for the SEEC's, among the one of the European Union, might be the creation of the Balkan Union. The union would consist of 7 countries (Albania, Bosnia and Herzegovina, Croatia, Kosovo, Macedonia, Montenegro, and Serbia). In that case, the members of the Union would be oriented towards a kind of closed economy. They would trade more between each other, and try to decrease imports from countries out of the Balkan Union.

The construction of the Balkan Union would look like the European Union. There would be institutions to regulate the union, but mainly, ones for culture, education, and trade. If each member specializes in production of particular goods and services, and achieves comparative advantage with economies of scale, then that product would be easy to sell, or to exchange for something else, of course from one of the Union members.

The Union would need to have a supervisor. Currently, the only state that has incentives and interest to regulate these countries is Turkey. If all countries agreed, Turkey would be the supervisor and manager of the Union. Even more, as a state with high FDI in South-eastern Europe, Turkey will be responsible for infrastructure, growth and development of the Union.

Developing countries, as "members" of the Balkan Union, must diversify their productive structure and strengthen domestic demand. People should buy more domestic products, and stop buying the similar foreign products, thinking foreign is better. Still, there are many foreign products that are better, but at least beverages and foods have to be bought from domestic producers.

Today, the countries not only depend on agriculture and manufacturing, but on tourism. Thus, economic policy for each country should be taking advantages of potential, which they have. There are countries such as Bosnia and Herzegovina, and Montenegro that should be oriented towards tourism, specifically winter and summer tourism.

Recently, Minister of Turkey, Rifat Sait has called for establishing of Balkan Parliament, where, besides Turkey, there would be Albania, Bosnia and Herzegovina, Bulgaria, Greece, Kosovo, Macedonia, Montenegro, Romania, and Serbia (Bojadžić, 2011). With headquarters in Izmir, the initiative of Turkey and its leading party, AK party, would welcome academics, NGO, politicians, journalists, writers, representatives of private sector, etc. who could invest money in development of Balkans. The idea might seem unachievable, where some countries could reject supervision of Turkey, but it is the only country that does not look at historical problems that occurred on the Balkans, and it wants to establish regular connections with each state from the Balkans.

10.CONCLUSION

This study discusses economic costs and benefits of South-eastern enlargement of the European Union. The idea of the united Europe is not a recent idea. Thus, the research starts with brief overview of the idea of the European Union and its objectives. The purpose was to maintain a peaceful and prosperous life throughout Europe. At the beginning of the fifties in the last century, the EU has signed many treaties and brought new policies that would ensure a zone for free capital movement. Besides that, the Union had five enlargements and introduced a common currency. Creation of a single market, which today consists of 501 million of consumers, is to provide a better life for every citizen.

Next enlargement is of the South-east European countries. After accession of the SEEC's, the European Union will have more than 30 members, with diverse cultures, histories and languages. Can such a diverse union of nations create a common political "union"? The EU was a trial to unify Europe, but it is obvious that it is difficult, since it is impossible to connect Germany or Sweden with, let say, Mediterranean, and there is no surprise for the failure of Greece and Italy. Can citizens of the EU establish a sense of being European while deeply belonging to their country? In essence, they can, if incumbent members follow the example of the first European Community. The moral legitimacy of the European Community is based on compromise, while consolidating the peace between former enemies. It stayed within the principle that all members, large and small, had equivalent rights and respected minorities. Therefore, the next enlargement should bring equivalence to small countries, and more important, stable market. EU member states account for almost 1/3 of the entire global economy, so in that sense the common market is the preferable mean to the global market.

The research uses the Gravity model to test the trade relations between EU-15 (inclusive Bulgaria and Romania) and SEEC's. After adding dummy variables such as common borders and currency to the model, the results show that there is a space for growth of trade between them. Trade is positively affected by GDP of exporters and importers. Larger GDP means higher production and increased ability for trade. However, distance has negative effect, and in this model it decreases trade if country is far away from partner. On the other hand, common borders positively affect trade, so by diminishing trade barriers, quotas, and taxes countries could stimulate trade to grow. Since Montenegro is the only one who uses Euro, the currency seems to affect trade negatively, and this shows that if any of SEEC's adopts Euro it would stimulate trade.

Current situation of the EU shows that high unemployment is present in many EU countries, so the EU has to be focused on achieving growth and creating jobs. In order to make its economies more dynamic and increase social cohesion, Europe must invest more in research and innovation, education and training. Thus, President of the European Commission presented a strategy for next 10 years, which is called the Europe 2020 strategy.

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APPENDIX

DATA AND VARIABLES USED FOR THE ESTIMATION OF THE GRAVITY MODEL

The reporting countries that are used for the analysis are the members of the EU-15 (Austria, Belgium, Denmark, Finland, France, Germany, Greece, Ireland, Italy, Luxembourg, Netherlands, Portugal, Spain, Sweden, and United Kingdom). Since the Belgium and Romania are not parts of the EU-15, they are not included in the South-east European countries, but they are attached to the first group, the EU-15. There are six partner countries: Albania, Bosnia and Herzegovina, Croatia, Macedonia, Montenegro, and Serbia.

The data GDP and population were taken from the World Bank's World Development Indicators. First two figures are measured in current US Dollars, Millions. Bilateral trade flows, imports and exports, were taken from the IMF's Direction of Trade Statistics, year 2010. Thus, the reference year for estimating potential trade between the EU-15 + (BG and RO) and the South-east Europe is 2010.

Distances between capital cities of the countries were taken from www.viamichelin.co.uk. The most used routes for transportation of goods by trucks and by ship (in case of Italy and its partner countries) are taken for analysis.

Dummy variable BOR takes a value of 1 if country of EU-15 and its partner share a common border, 0 otherwise.

Dummy variable CURR takes a value of 1 if country of EU-15 and its partner uses a common currency, 0 otherwise.