

# Fiscal Decentralisation, Local Government and Policy Reversals in Southeastern Europe

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# Fiscal Decentralisation, Local Government and Policy Reversals in Southeastern Europe

- ▶ Volume edited by Will Bartlett, Sanja Kmezić and Katarina Đulić
- ▶ **Contributors:** 17 authors from 8 countries
- ▶ **Publisher:** Palgrave Macmillan, 2018

# The scope of the study

- ▶ **Subject matter:** political economy of fiscal decentralisation
- ▶ **Geographic scope:** 8 countries of SEE (former Yugoslavia and Albania)
- ▶ **Time frame (1990 – 2016)**
  - “tectonic” changes
  - political economy of transition
  - EU integration

# The subject matter of the study

- ▶ The political economy of all three decentralisation processes:
  - Territorial – Administrative
  - Political
  - Fiscal
- ▶ **The focus is on fiscal decentralisation:**
  - Decentralisation of revenues
  - Decentralisation of functions (expenditures)
- ▶ The goal:
  - to identify the variety of decentralisation approaches that have been adopted, and
  - to explain political and economic interests behind them.

# The main conclusion

- ▶ The book argues that decentralisation has attained only partial success in addressing the specific policy objectives of:
  - democratisation,
  - balanced economic development, and
  - post–conflict reconciliation of ethnic communities.

The main reason for this partial success – the impact of the crisis.

# Analytical approach

- ▶ The context and motivation differs across the countries. Three specific objectives can be identified:

- (1) post-war reconciliation in ethnically divided countries,
- (2) political democratisation, and
- (3) (balanced) economic development.

The decentralisation process has been underpinned by the parallel process of integration of SEE into the EU.

# Analytical approach

The countries were categorised in four groups based on major policy challenges that they tried to address via decentralisation processes:

1. **Europeanisation (Slovenia and Croatia)** – the absorption of EU funds at local level and attempts to achieve balanced economic development.
2. **Crisis and Local Government Debt (Serbia, Montenegro and Bosnia and Herzegovina)** – serious consequences of the global crisis led to drastic and reactionary policy reversals.

# Analytical approach

3. **Ethnic conflicts (North Macedonia and Kosovo)** – the political economy of ethnic relations and decentralisation as a policy of post-conflict reconciliation.
4. **Democratisation of the society (Albania)** – the legacy of half a century-long isolation, extreme centralisation, and absence of real local self-government.

# Analytical approach

- ▶ The book has identified (for all eight countries) three distinct phases that have triggered accompanying policy changes.
  1. **early 1990s – early 2000s – centralisation** (the exceptions are Slovenia and Albania)
  2. **early 2000s – 2008 – decentralisation**
  3. **2008 – 2016 (ongoing) – strong centralising and pseudo-decentralising policies**

# Theoretical background

- ▶ **The first-generation theory of decentralisation** – decentralisation creates allocative efficiencies and raises overall welfare compared to a centralisation.
- ▶ **The second-generation theories of decentralisation** – political actors have their own self-interests, which dictate the actual level of decentralisation.

# Theoretical background

- ▶ The book confirms the **relevance of the second-generation theories.**
- ▶ Political economy behind the process in the Western Balkans: clientelism, patronage networks, democratic backsliding, LG budgets' raids by central governments...

# Academic contribution

- ▶ The book contributes to the body of literature on the political economy of post-communist transition as well as to the literature on the role of fiscal decentralisation in post-crisis Europe.

# Findings for the first group – Slovenia and Croatia –

- ▶ **Europeanisation (Slovenia and Croatia)** – the absorption of EU funds at local level and attempts to achieve balanced economic development.
- ▶ The main issues: vertical imbalance in LG financing (Slovenia) and instruments of fiscal equalisation (Croatia)
- ▶ Despite more favourable economic conditions, Slovenia and Croatia ended up at a similar level of decentralisation as the rest of the region, which is significantly lower than the EU average.

# Findings for the first group – Slovenia and Croatia –

- ▶ Great fragmentation prevents the majority of LGs from taking advantage of the access to EU funds.
- ▶ This is particularly true for smaller and less developed LGs, which further deepens the development gap.
- ▶ Optimising the number of sub-national government units would be difficult since all parties are not ready to give up their preferential status and personal benefits.

# Findings for the second group – Serbia, Montenegro and Bosnia and Herzegovina –

- ▶ **Crisis and Local Government Debt (Serbia, Montenegro and Bosnia and Herzegovina)** –serious consequences of the global crisis led to drastic and reactionary policy reversals.
- ▶ The main issues: non-transparency of fiscal data (Serbia), volatile municipal revenues (Montenegro) and LG debt (Bosnia and Herzegovina).
- ▶ The most important trend – the reversal of the decentralisation discourse.
- ▶ The drastic drop in capital investment and the uncontrolled rise in liabilities, accompanied by the fall of local revenues, have become a ticking time bomb.

# Findings for the second group – Serbia, Montenegro and Bosnia and Herzegovina –

- ▶ To prevent a deeper economic crisis, the central governments need to: adopt harder budget constraints, raise the level of fiscal transparency, and improve the fiscal autonomy and capacity of LGs.
- ▶ The EU should be the key partner supporting the process within the Europeanisation framework.

# Findings for the third group – North Macedonia and Kosovo –

- ▶ **Ethnic conflicts (North Macedonia and Kosovo)** – the political economy of ethnic relations and decentralisation as a policy of post–conflict reconciliation.
- ▶ The main issues: LG efficiency and ethnic fragmentation (North Macedonia) and resolution of ethnic conflicts (Kosovo)
- ▶ The most difficult task—resolving deep ethnic cleavages and functioning in the post– conflict context with high ethnic tensions.
- ▶ Decentralisation accommodated the geographic distribution of ethnic communities, not taking into account the economies of scale.

# Findings for the third group – North Macedonia and Kosovo –

- ▶ The goal has been partly achieved – interethnic conflict has ceased, but it is questionable whether the outcome is sustainable.
- ▶ Decentralisation failed to ensure political accountability for and economic efficiency in providing public services. The general clientelistic practices are aggravated by the ethnic component involved.
- ▶ Yet, there are significant achievements in the domain of fiscal decentralisation.

# Findings for Albania

- ▶ **Democratisation of the society (Albania)** – the legacy of half a century–long isolation, extreme centralisation, and absence of real local self–government.
- ▶ The main issue: Aligning territorial and fiscal decentralisation
- ▶ The 50–year–long centralism and totalitarianism left the country deprived of the real local self–government.
- ▶ Albania has achieved dramatic progress in all aspects of decentralisation and LG reform, thus securing democratisation and economic development.

# Findings for Albania

- ▶ However, the central government has been interrupting the decentralisation process with frequent, ad hoc measures that express conflicting policy priorities.
- ▶ Although Albania looked to be the counterpoint to the former Yugoslavia countries at the beginning of the process, the trend of convergence is evident at the end of the period.

# Conclusions

- ▶ Decentralisation has been one of the key instruments for keeping peace and calming ethnic tensions in countries previously affected by conflicts.
- ▶ Municipalities in the region have obtained a far wider purview of responsibilities and functions, including important social sector services.
- ▶ Municipalities became a relevant partner in the process of European integration.

# Conclusions

- ▶ However, the shares of LG revenue/expenditure in total government revenue/expenditure and their shares in GDP are today only at the pre-crisis levels and well below the EU average.
- ▶ This vertical imbalance has led to extensive borrowing and to the rapid accumulation of arrears. The lack of transparent consolidated financial reporting has prevented both local and central governments from effectively controlling their total fiscal risks.

# Conclusions

- ▶ EU funds can be crucial for mitigating external economic shocks.
- ▶ Yet, significant territorial fragmentation weakens the fiscal capacity of LGs, reducing their potential to absorb these funds and increasing the regional development gap.
- ▶ Problems of economies of scale in providing local public services exist. The main obstacle – the political patronage networks (particularly when an ethnic component is involved).

# Conclusions

- ▶ The wave of fiscal decentralisation slowly receded after the post-2008 economic crisis.
- ▶ It may take a combination of the current economic upswing, a political revival of the idea, and stronger EU leadership to support a renewed surge in fiscal decentralisation in the region.