Analytical Brief[1]

Beyond Convergence: Innovation, Institutional Capacity and the Strategic Future of the Western Balkans

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" Draghi's warning for Europe is even more consequential for the Western Balkans. EU integration can open markets and mobilise capital, but convergence will remain slow unless the region develops the institutional capacity to convert knowledge, entrepreneurship and external integration into productive scale.

Accession Does Not Guarantee Convergence

The Western Balkans are usually discussed in Europe through the language of enlargement. That is understandable, but economically incomplete. Accession is a political destination; convergence is a productive process. The two are related, but they are not the same. A country can become increasingly aligned with European rules, trade deeply with the Single Market and receive substantial external investment without necessarily developing the domestic capabilities required to generate high-productivity firms, technological upgrading and sustained income convergence.

This distinction should now become central to the region's economic strategy. The OECD's 2025 Economic Convergence Scoreboard shows that GDP per capita in the Western Balkans, adjusted for purchasing power, rose from USD 9,725 in 2003 to USD 21,305 in 2023. Yet after two decades of progress it remained just below 40 per cent of the EU average. Earlier OECD analysis warned

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that, at the prevailing rate of convergence, closing the gap with the EU and OECD could take at least half a century (OECD, 2024; OECD, 2025).

The problem is therefore not that the region has failed to grow. It is that growth has not yet been sufficiently transformative.

This matters even more because the European economy into which the Western Balkans seek deeper integration is itself confronting a structural competitiveness problem. Mario Draghi's report on European competitiveness identified weak productivity, insufficient technological scale, fragmented capital markets and an additional annual investment requirement of approximately €750–800 billion. For Brussels, this is an internal competitiveness challenge. For the Western Balkans, it is also an external constraint. A region whose convergence model depends heavily on integration with Europe cannot assume that European demand, capital and technology will automatically pull it towards the frontier if Europe itself is struggling to reproduce its technological and industrial leadership (Draghi, 2024).

The strategic question for the Western Balkans is consequently deeper than accession: how can the region use European integration to build capabilities that remain valuable even when the European growth model is under pressure?

I would frame this as a problem of institutional conversion capacity. The relevant measure of an economy is not simply the resources it possesses or the programmes to which it has access, but its capacity to convert those resources into productive outcomes. Universities must be able to generate commercial knowledge. Entrepreneurs must be able to build firms. Capital must reach companies capable of scaling. Infrastructure must reduce economic distance. Regional integration must enlarge markets in practice rather than only in legal form. Foreign direct investment must generate domestic capability rather than enclaves of production.
Without these conversion mechanisms, convergence risks becoming a process of integration without transformation.

The Western Balkans do not primarily lack entrepreneurial potential

The conventional explanation for the region's innovation weakness is often that it lacks capital, research intensity or sufficiently sophisticated firms. Each observation contains truth, but the deeper problem is how these weaknesses interact.

The Western Balkans invest far less in research and development than the European Union. OECD data indicate that gross expenditure on R&D across the WB6 averaged roughly 0.56 per cent of GDP in 2022, compared with approximately 2.25 per cent in the EU. North Macedonia's R&D expenditure has been particularly low, with the OECD reporting overall investment of around 0.38 per cent of GDP in the latest available country data (OECD, 2024). Such differences matter because sustained innovation requires a knowledge base. But simply increasing public research expenditure would not be enough.

The region already contains signs of entrepreneurial and technological dynamism. ICT service exports increased from 8.2 per cent of total service exports in 2018 to 13.0 per cent in 2022. Governments have created innovation funds, technology parks, accelerators, digital innovation hubs and start-up programmes. The 2025 regional study prepared by the Regional Cooperation Council, the European Institute of Innovation and Technology and the Enterprise Europe Network describes a start-up ecosystem with genuine potential, supported by a growing ICT sector and a young skilled workforce (OECD, 2024; Regional Cooperation Council, 2025).

Yet the same evidence identifies funding shortages, fragmented markets and talent migration as persistent constraints. These are not three unrelated problems. They form a conversion chain. A promising entrepreneur in Skopje, Tirana, Sarajevo or Pristina operates in a market that is small in national terms. To scale, the firm must internationalise early. Internationalisation requires management capability, networks, regulatory knowledge and capital. But venture and growth finance is shallow, while regional fragmentation increases the cost of reaching neighbouring markets. At the same time, skilled employees have credible opportunities to leave for higher-income EU economies. The company therefore confronts a financing problem, a market-size problem and a talent problem simultaneously.

Brain drain in this context is not simply a demographic issue. It is an institutional signal. People leave where the expected return to their human capital is higher elsewhere. The policy response cannot therefore be reduced to appeals for talented citizens to remain. The region must create firms and institutions capable of generating opportunities commensurate with the skills it produces.

This is why entrepreneurship should be understood as part of national and regional capacity rather than as a narrow private-sector agenda. Entrepreneurs are one of the mechanisms through which knowledge is recombined, uncertainty is explored and new productive activities are discovered. A political economy that systematically loses its most ambitious entrepreneurs, engineers and researchers is not merely losing individuals; it is losing part of its future adaptive capacity.

For the Western Balkans, innovation policy should therefore move away from treating start-ups as isolated beneficiaries of grants and towards constructing a complete entrepreneurial system. The relevant question is not how many start-ups are registered, how many innovation programmes exist or how many technology parks have been opened. It is how many firms can move from local experimentation to regional scale, and from regional scale to internationally competitive production.

Europe is the region's anchor - and therefore part of the constraint

No serious Western Balkan growth strategy can be built outside Europe. The EU is already the region's dominant economic partner. In 2022, 67.2 per cent of Western Balkan merchandise exports went to the European Union, while the EU accounted for 51.9 per cent of merchandise imports. The region is therefore deeply connected to European demand and European value chains long before full accession (OECD, 2024).

This is an enormous advantage. But it creates a strategic dependency as well.

A convergence strategy based largely on exporting labour, supplying cost-competitive production and receiving external investment can generate growth without necessarily producing the institutional capabilities required to move towards the technological frontier. The danger is a developmental equilibrium in which Western Balkan economies become increasingly integrated into European production while remaining concentrated in lower-value functions within those production systems.

This is where Draghi's diagnosis becomes directly relevant to the Balkans. Europe itself is trying to escape a structural innovation and productivity problem. It has world-class research, substantial savings and a vast market, but struggles to convert these advantages into sufficient numbers of globally scalable technology companies and new industrial capacity. If the Western Balkans integrate into Europe mainly as peripheral suppliers to mature European industries, they risk importing not only the strengths of the European economic model but also its structural weaknesses.

The answer is not to turn away from European integration. It is to make integration more demanding.

Foreign direct investment should be evaluated not only by the capital it brings or the number of jobs created, but by whether it generates supplier upgrading, managerial learning, technology transfer and entrepreneurial spillovers. Universities should not measure internationalisation merely through participation in European programmes, but through the extent to which such participation strengthens domestic research teams, commercialisation capabilities and industrial partnerships. Infrastructure should not be assessed only by kilometres of motorway or railway constructed, but by whether it reduces the transaction costs facing regional firms.

This distinction between access and absorption is central. Economies benefit from integration only to the extent that domestic institutions are capable of absorbing and recombining the knowledge, capital and opportunities integration makes available.

The EU's Growth Plan for the Western Balkans recognises part of this challenge. It offers a €6 billion Reform and Growth Facility for 2024–27 and aims to accelerate socio-economic convergence by bringing some benefits of the Single Market forward before accession. The Commission estimates that the Western Balkans currently operate at roughly one third of the EU's average economic level and argues that the plan could help double the size of the region's economies within a decade if reforms are implemented (European Commission, n.d.-a).

But money and market access cannot substitute for conversion capacity. They can only amplify it.

The region itself must become a market

The scale problem is especially important. The six Western Balkan economies are individually small. This places a structural constraint on firms attempting to grow in sectors characterised by high fixed costs, network effects or significant R&D requirements.

The Common Regional Market is therefore not merely a diplomatic exercise associated with the Berlin Process. It is an innovation institution.

The European Commission describes the initiative as an effort to create a common market of around 18 million people based on the four freedoms and aligned with EU rules. The economic cost of the existing fragmentation is not trivial. Trucks spend an estimated 28 million hours waiting at borders across the region each year, imposing costs equivalent to around 1 per cent of regional GDP (European Commission, n.d.-b).

Those waiting times are normally discussed as a trade problem. They are equally an innovation problem. Fragmentation raises the minimum organisational capacity required for a young company to expand. It makes a region of 18 million consumers behave more like six small markets than one meaningful home market. It discourages investment in business models that require scale and increases the relative attractiveness of moving directly into the EU.

A functioning regional market would therefore do more than increase trade. It would create a larger experimental space for Western Balkan firms. A company born in North Macedonia should be able to treat Albania, Serbia, Kosovo, Montenegro and Bosnia and Herzegovina as extensions of its early home market rather than as separate internationalisation projects.

This is where regional cooperation becomes geo-economic rather than symbolic.

If the Western Balkans can reduce commercial fragmentation before accession, the region becomes more attractive to capital and more capable of producing firms that enter the EU Single Market from a position of greater scale. If it cannot, each economy will continue competing separately for foreign investors and skilled workers while much of the region's entrepreneurial value is captured elsewhere.

The strategic value of regional integration is therefore not regionalism for its own sake. It is the creation of sufficient economic density to allow innovation to compound.

From convergence policy to strategic capacity

The Western Balkans now face a historically unusual combination of opportunity and pressure. EU enlargement has returned to the centre of European strategy. The Growth Plan provides additional capital and conditional market access. The Common Regional Market is advancing. European institutions are deepening cooperation with the region in research, innovation and artificial intelligence. At the same time, geopolitical competition has increased the strategic importance of transport routes, energy systems, digital infrastructure and resilient production networks across South-East Europe.

This creates an opening for a different development model.

The region should not aspire simply to become a cheaper extension of the European economy. Its objective should be to become a strategically valuable part of that economy: a region capable of producing firms, technologies, skills and infrastructure that Europe itself needs.

That requires a shift in how institutional reform is understood. Too often reform is measured through formal alignment: whether legislation has been adopted, whether an agency exists, whether a strategy has been approved or whether EU standards have been transposed. These measures matter for accession, but they are insufficient measures of development.

Institutional capacity must ultimately be judged by conversion outcomes.

Can a researcher build a company around an invention? Can a successful small firm obtain the finance required to become a regional firm? Can a regional firm cross neighbouring borders without disproportionate administrative cost? Can foreign investment produce domestic suppliers capable of technological upgrading? Can diaspora capital return as productive investment rather than predominantly consumption and property? Can public procurement create first customers for innovative domestic firms? Can universities, investors, entrepreneurs and government institutions form networks dense enough for knowledge to circulate rather than leave the region?

These are not secondary questions to be addressed after EU accession. They are the economic content of convergence itself.

The World Bank's latest assessment illustrates the urgency. Growth in the Western Balkans is expected to remain subdued in 2026, with the Bank revising its regional forecast downward to 2.8 per cent and emphasising stronger institutional capacity, policy stability and better mobilisation of human capital as conditions for higher long-run growth (World Bank, 2026). A region starting at below 40 per cent of EU income levels cannot rely indefinitely on growth rates only modestly above those of mature European economies and expect rapid convergence.

Nor can the region rely on demography. Labour shortages are already emerging, while the OECD identifies continuing brain drain and skills mismatches as barriers to competitiveness. The traditional development model in which abundant relatively low-cost labour attracts investment becomes less viable when the labour itself is becoming scarce.

That changes the strategic priority from labour-cost competitiveness to productivity.

Productivity growth, however, is an institutional achievement. It requires firms capable of adopting technology, workers capable of using it, financial systems willing to fund intangible assets, universities connected to industry and governments able to deliver infrastructure and predictable rules. Entrepreneurship is not separate from this system. It is one of the mechanisms through which the system adapts.

This is where the Western Balkans can draw the most important lesson from Draghi. Europe's competitiveness problem demonstrates that even wealthy societies with strong formal institutions can struggle when the mechanisms connecting capital, knowledge and commercial scale become fragmented. The Western Balkans should not wait to reproduce the same institutional bottlenecks at a lower level of income.

Accession can provide rules. European funding can provide capital. The Single Market can provide demand. None can guarantee transformation.

The region's long-term position will depend on whether its institutions can convert those opportunities into capabilities that remain embedded locally: stronger firms, denser entrepreneurial ecosystems, more sophisticated exports, deeper technological competence and a workforce that increasingly chooses to build its future in the region rather than outside it.
This is why innovation in the Western Balkans should also be understood as a question of resilience and security. Economies that cannot generate new firms, retain critical skills or adapt their productive structures become increasingly dependent on external technology, external capital and external labour markets. Such dependence may be efficient in normal times, but it reduces strategic room for manoeuvre when the international environment becomes less predictable.

Entrepreneurship, innovation and institutional capacity are therefore not peripheral elements of security policy. They are part of the economic foundation from which resilient states are built.
The Western Balkans do not need another abstract strategy promising convergence. They need institutions capable of making convergence cumulative.

The defining question for the region is no longer whether it will be integrated into Europe. Economically, much of that integration has already occurred. The more difficult question is what kind of economic position the Western Balkans will occupy inside the European system.

Will the region remain predominantly a supplier of labour, cost-competitive production and outward migration? Or can it become a producer of technology, entrepreneurial firms and strategic economic capabilities?

The answer will not be determined in Brussels alone.

It will be determined by the institutional conversion capacity built in Skopje, Tirana, Sarajevo, Belgrade, Podgorica and Pristina.

For the Western Balkans, prosperity cannot be imported through accession.
It must be produced - and continuously reproduced - at home.

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