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Assessing Government Involvement in the Balkan Countries' Economies

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Abstract: *The extent to which the government intervene the marketplace and the government's role in the economy is an important factor, determining the economic results achieved by a country. In the academic literature, the question of whether the promotion of this participation contributes to an improvement of the development of a nation or, on the contrary, can contribute to a loss of competitive advantages, is debatable. This study focuses on the degree of involvement of national governments in the economies of the Balkan region countries. For the purpose of analysis, a cluster analysis is applied, through which the Balkan countries are divided into several groups (clusters), characterized by different degrees of government participation. Three periods are considered - before and in the first years of the global economic and financial crisis, as well as just before the current COVID-19 pandemic. The analysis is supplemented by an assessment of the impact of individual clusters on the economic development of these countries.*

1. INTRODUCTION

Economic literature has for a long time debated on the extent to which government should be involved in the redistribution of economic goods and resources. The two major schools of economic thought, the Classical and the Keynesian, have adopted diametrically opposed positions on the role of government and its ability to influence a country's economic development. While the representatives of the Classical school advocate the free market and a limited degree of state interference in the economy (mostly functions relating to protecting private property, maintaining public order and national security), J. M. Keynes and his followers see government and its policies as a major player influencing the national economy.

Steinberg and Saideman (2002) believe that the degree of state influence on the economy is determined by the ability of the state, and in particular on the government's decisions ability, to influence the main market forces of supply and demand, hence impact price levels. That involvement is based on two fundamental elements, namely, the state involvement in economic processes through various types of investment, government consumption and publicly owned enterprises, on the one hand, and by applying the instruments of taxation, implementing social policies and providing budget transfers and subsidies as forms of distributing and redistributing economic resources, on the other.

Currently, the dilemma of state interference or non-interference in the economy remains topical. Globally, there is a considerable array of examples illustrating the extent to which governments take an active part in managing a country's national economy. The influence of government during an economic downturn and in times of national or global crises when it attempts to mitigate such crises has a particularly strong impact. It is important to strike a balance between the extent to which the market can self-regulate, and the extent to which the state and its institutions intervene in economic

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processes. Theory focuses, on the one hand, on market system deficiencies, including the inability of the market mechanism to distribute the available resources most efficiently (Nita, 2011) and the generation of other exogenous negative effects, and the need for government intervention, and on the other hand, on excessive state interference, inefficient policies, corruptive practices, the additional cost of state oversight of the private sector and the ensuing government failures (Krueger, 1990). Stiglitz (1997) concluded that government interventions in East Asian countries and in the U.S. have had a relatively positive effect on economic development, which could be used as a good point of reference for other countries as well. He has identified six key roles through which the state has contributed to the significant growth of those economies, namely: investing in human capital by developing the educational system, promoting R&D, supporting the financial sector to mitigate the risk of financial instability, investing in infrastructure (including transport but also institutional infrastructure), ensuring environmental protection and providing for a social safety net. Tanzi (1997) pointed to several important factors influencing the government role in the economy, notably: public attitude, the level of economic development and the complexity of the functioning of the market, the openness of an economy, the level of technological development and, to a large extent, the expertise of the people engaged in public administration.

Research often addresses the issue of how the level of government intervention in the economy is measured. Most commonly, the indicators used aim to show the size of the public sector as measured by the size of government spending (in GDP terms) or based on revenue collected through taxation, social security contributions and levies (again, in GDP terms), considering that the second approach underlies the redistribution function of the modern state.

Despite the abundance of research on the size of the public sector in a particular country or a multi-country entity, it is hard to single out a specific level of government intervention in the economy that would be applicable to all countries and would universally facilitate the improvement of their economic positions. This study does not aim to discover such a critical point. Rather, the study sets out to analyse the degree in which the governments of countries in the Balkan Region are involved in managing their national economies and to group those countries by distinguishing between those that typically exhibit more substantial government involvement and those that rely to a larger extent on market self-regulation. The object of analysis in this study covers the following countries: Bulgaria, Greece, Serbia, North Macedonia, Romania, Montenegro, Slovenia, Croatia, Albania, Turkey and Bosnia and Herzegovina.

Countries in the Balkan region cannot be treated as similar to those having a high degree of government involvement if compared to certain countries in Central or Western Europe, let alone Scandinavian countries, where there is a high degree of redistribution of public goods and resources using the government budgets. The above-mentioned indicators for assessing the extent of government involvement in economic processes exhibit a certain rate of dynamics in the period 2004–2019. Figure 1 shows that, on the average, Balkan countries have registered a gradual, although smooth, increase in terms of the indicator that measures the size of public revenue in GDP terms (from 37.1 % in 2004 to 39.1 % in 2019). In that period, public spending reached considerably higher levels (as high as 43.4–43.5 % in 2009 and 2013), leading to budget deficits, i.e. through their actions, governments get actively involved in economic processes; moreover, they do so using additional domestic or international financing. This is particularly evident during the global financial crisis of the late 2008, and in the several years in its aftermath. The figure below illustrates that the dynamics in public spending is more notable than that in national revenues, with a gradual decline and convergence toward the amount of public revenue observed post-2013.

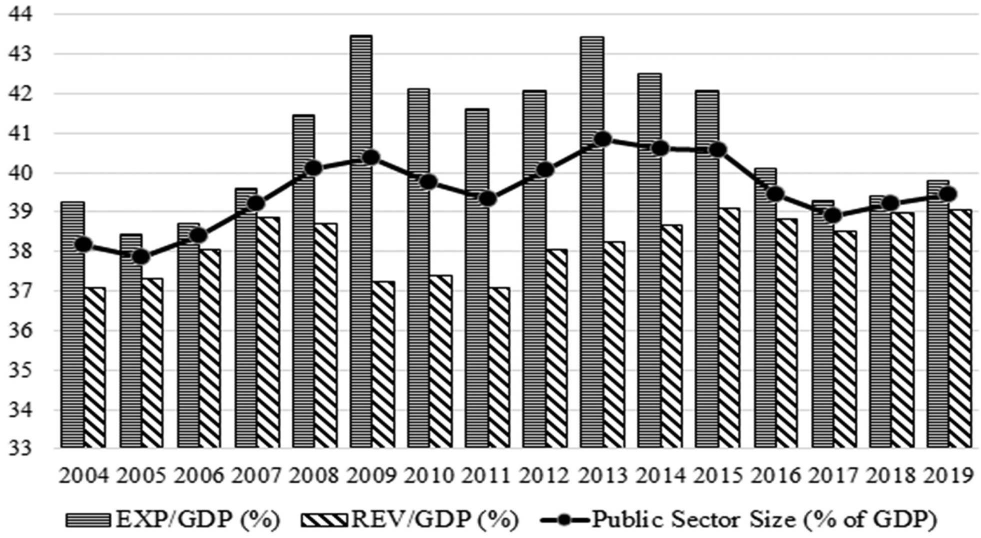

Figure 1. Size of public sector in the Balkan Region in the period 2004–2019

Source: Data on government budget implementation published by the finance ministries of Balkan countries

Based on Figure 1, it can be concluded that around 40 % of GDP in the Balkan Region was distributed through the public sector; following the global financial crisis, an intensification of the redistribution function of the state can be observed in the countries in the region, while there is a decrease in government consumption and investment.

2. DATA AND METHODOLOGY

The study uses an approach that involves a non-hierarchical clusterization procedure. The number of clusters is pre-determined, whereby the main purpose is to group countries into three clusters, which are:

- Balkan countries with a high degree of government involvement in managing the economy (Cluster 1),
- Balkan countries with a moderate degree of government involvement in managing the economy (Cluster 2), and
- Balkan countries with a low degree of government involvement in managing the economy (Cluster 3).

Clusterization used data about revenue (as a percentage of GDP) and expenditures (as a percentage of GDP) in eleven Balkan countries. The selection includes data for three years in the period 2004–2019, namely: 2004, 2009 and 2019. The aim in selecting those years is to compare the degree of government involvement at the start and the end of the period analysed above, while including 2009 as a reference year, i.e. to establish the effects of the global economic crisis.

3. RESULTS AND DISCUSSION

The data shown in Table 1 enable the conclusion that in countries such as Greece, Slovenia and Croatia, there is a considerable degree of government involvement in the economy. Those three countries fall into the first cluster in all three of the years analysed (2004, 2009 and 2019). While in 2004 only Croatia, Greece and Slovenia fell into the first cluster, in 2009 they were joined by another three Balkan countries: Bosnia and Herzegovina, Serbia and Montenegro.

Table 1. Cluster Membership

Country	2004		2009		2019	
	Cluster	Distance	Cluster	Distance	Cluster	Distance
Albania	3	5.007	3	0.000	3	5.892
Bosnia and Herzegovina	2	1.385	1	2.853	2	1.203
Bulgaria	2	1.155	2	2.733	2	4.025
Croatia	1	1.895	1	1.133	1	1.968
Greece	1	3.669	1	6.072	1	3.641
Montenegro	2	3.363	1	4.079	1	2.511
North Macedonia	2	3.368	2	2.628	3	0.567
Romania	3	3.590	2	2.869	3	2.578
Serbia	2	0.876	1	5.985	2	2.907
Slovenia	1	2.494	1	1.599	1	3.413
Turkey	3	1.686	2	0.045	3	3.190

Source: Authors' calculations based on SPSS

Towards the end of the analysed period, and particularly in 2019, Bosnia and Herzegovina and Serbia drop out of the group of countries having a significant government involvement in economic development. The main cause of that result may be the shrinking of government actions through the spending part of their countries' budgets. Greece also exhibits a shrinking of direct government involvement in the economy through the spending part of the budget; however, the role of the state in terms of revenue collected has increased (seeking to achieve fiscal consolidation of public finance in an effort to contain the growing government debt and in keeping with its commitments to international creditors (Nenkova and Angelov, 2020)), i.e. a strengthening of redistribution processes is observed. In Croatia and Slovenia, an activation of the state is also evident in the revenue part of the budget, along with retaining a stable position in terms of spending as a percentage of GDP. Of the three years examined, 2009 was the year when the scope of the first cluster was the largest, which confirms to a certain extent the data from Figure 1 above, indicating that the public sector involvement in economic development was most pronounced in the first years of the global economic crisis.

In 2004, the cluster of countries with a moderate government involvement in the economy included Bosnia and Herzegovina, Bulgaria, Montenegro, North Macedonia and Serbia. In 2009, Bulgaria and North Macedonia remained part of that cluster, while Montenegro, Serbia and Bosnia and Herzegovina dropped out. Simultaneously, Turkey and Romania joined this cluster. At the end of 2019, the cluster of countries with a moderate government involvement shrank, and comprised only three countries - Bulgaria, Serbia and Bosnia and Herzegovina. The data support the conclusion that, similarly to the first cluster, the number of countries in that cluster also went down at the end of the period under examination, which brings us to conclude that government involvement in economic processes has decreased in comparison to a decade earlier. Based on the analysis of the three years, the continuous presence of Bulgaria in the cluster of moderate government involvement clearly stands out. This is due to the relatively sustainable level of public sector involvement, with an increase in the public revenue/GDP indicator by about 4 p.p. in 2019 from the 2009 value, and a decrease in the public spending/GDP indicator by about 2 p.p. over the same period.

The third cluster, containing countries with low degree of government involvement in economic processes, typically features Albania. The low percentage of public revenue resulted in low levels of government involvement in the economy through investment and direct financing of activities through the government budget. In addition to Albania, that cluster included Turkey and Romania in 2004, while in 2019, as noted earlier, the cluster of countries with a lower degree of government involvement expanded the most, to include also North Macedonia, Turkey and Romania, i.e. largely due to the shrinking of budget expenditure, about 40 % of the Balkan countries qualified as countries with a lower degree of government involvement.

The overall dynamics of the three clusters in terms of the two indicators of the analysis that have been used in the clusterization can be traced in Table 2 below, showing the final cluster centres by year. Countries from the first cluster display a considerable upward shift in 2019 from 2009 in terms of budget revenue, while at the same time the direct government activity through the expenditure side of the budget declines. In the second cluster, there is a decline in the redistribution policy through the revenue side of the budget at the start of the economic crisis when compared to 2004, while 2019 saw a considerable government involvement of the countries from that cluster in their economies. The cluster of countries with a low degree of government involvement exhibits a gradual increase in the values of the analysed indicators towards the end of the analysed period, largely due to the inclusion of countries which had had a significantly higher level of government involvement and had gradually moved into the cluster of a lower degree of government involvement.

Table 2. Final Cluster Centre

	Cluster 1			Cluster 2			Cluster 3		
	2004	**2009**	**2019**	**2004**	**2009**	**2019**	**2004**	**2009**	**2019**
REV/GDP	42.46	42.03	45.91	38.49	32.82	40.75	29.31	26.14	30.96
EXP/GDP	47.74	48.86	45.93	38.07	38.00	39.67	32.69	33.21	33.77

Source: Authors' calculations based on SPSS

For the purposes of the analysis, it is important to observe what the differences among the clusters are in time. That can be done by examining the results of the differences among the final cluster centres shown in Table 3 below. In 2009, the differences between countries falling into the first and countries falling into the other two clusters grew. At the beginning of the global economic crisis, the degree of differences between the countries of the second and third clusters decreased. In 2019, the similarity among the three clusters in terms of government involvement in economic processes increased. The countries from the first cluster no longer stood out that sharply from the countries falling into the second and the third cluster. At the same time, the difference between the second and the third cluster grew as compared to 2009.

Table 3. Distances between Final Cluster Centres

2004				2009				2019			
Cluster	**1**	**2**	**3**	**Cluster**	**1**	**2**	**3**	**Cluster**	**1**	**2**	**3**
1		10.45	19.99	1		14.24	22.30	1		8.11	19.26
2	10.45		10.65	2	14.24		8.21	2	8.11		11.42
3	19.99	10.65		3	22.30	8.21		3	19.26	11.42	

Source: Authors' calculations based on SPSS

The purpose of this study is, on the one hand, to differentiate the individual Balkan countries based on the degree of government involvement in the management of the national economy and, on the other hand, to track the impacts of their higher or lower degree of government involvement on economic development. To that end, the average rate of real economic growth was traced throughout the period 2004–2019 (based on the annual change using data from the International Monetary Fund (2021)).

The data indicate that among the eleven Balkan countries included in our analysis, the three that display the highest average rate of real economic growth are indeed countries that, in 2019, belonged to the third cluster (Turkey, Romania and Albania), i.e. countries with a lower degree of government involvement in the economy. At the same time, the three countries characterized by the lowest economic growth rate are actually the three 'permanent representatives' of the first cluster, i.e. the cluster which includes the Balkan countries with a high degree of government involvement in the economy. Figure 2 below illustrates the linkage between the average rate of GDP growth for each one of the analyzed countries during the period 2004–2019 and the average size of its public sector (as a percentage of GDP) calculated by averaging the above-mentioned indicators for assessing the degree of government involvement in the economy during the period 2004–2019.

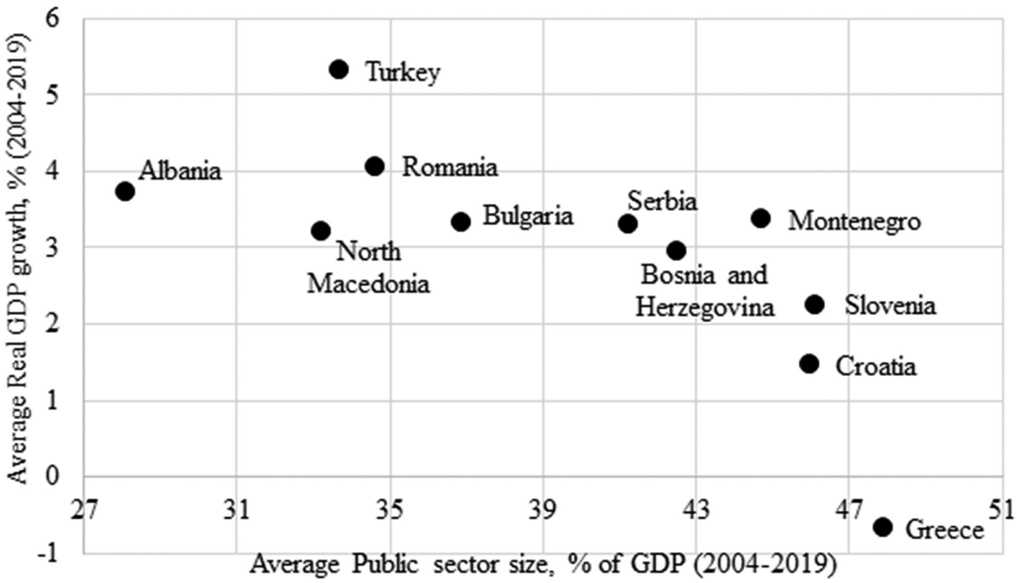

Figure 2. Relationship between the degree of government involvement and the economic growth rate of Balkan countries in the period 2004–2019

Source: Authors' calculations

It should be noted that the country featuring the lowest degree of government involvement, Albania, generated the highest growth in the conditions of the onset of the global economic crisis in 2009. It is important to point out that, there is a tendency to generate positive rates of economic growth over the period 2004–2019, paired with a relatively balanced government involvement in the economy of Albania. Angelov and Nikolova (2021) explained that trend with the low level of tax burden in countries such as Albania and the prevalent use of indirect taxation (especially until 2010, when the annual growth of Albania's economy is quite high and the share of revenues collected from indirect taxes is approximately 1.6 times higher than income tax revenues). In that context, one should not hasten to draw premature and definitive conclusions claiming that government involvement in the economy has, by default, a deterring effect, but rather explore an option where that involvement can be optimized in order to ensure conditions for a sustainable economic growth.

4. CONCLUSION

This study enables observation of the role of government involvement in the management of Balkan economies during the period 2004–2019. The analysed data reveal several periods of increasing government involvement and some periods of limited involvement. The results of the cluster analysis show that certain Balkan economies rely primarily on a more substantial government involvement, while in other countries, governments play much more limited functions, although the general tendency is for the role of those governments to increase gradually. It is noteworthy that at the end of the analysed period the countries in the Balkan Region exhibit a higher degree of similarity in terms of government involvement. Over the last three years (2017–2019) of the analysed period, the role of government in economic processes grew stronger. This development should be analysed in greater detail at some future point, especially in the context of the COVID-19 pandemic, where we have witnessed an even more active government involvement through a range of economic and social measures. It is recommendable for each Balkan country to seek for the optimal (potentially acceptable) level of government involvement that would facilitate the most favourable development of its economy, and to put more effort in boosting the efficiency of public spending and consequently improve the outcome of government involvement in economic processes on the Balkans.

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