



ABSTRACT WORKING PAPER 5.11

Institutional Quality and Growth in EU Neighbourhood Countries

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The research has investigated the relationship between institutional reform and economic growth in the European Neighbourhood Policy (ENP) countries, and the extent to which formal and informal institutions have converged towards EU norms. Several key conclusions emerge from the analysis. Firstly, the ENP countries show a weaker institutional convergence to the EU than candidate countries. Secondly, political stability, governmental accountability, freedom of media and control of corruption are important for the success of economic policies. However, nominal adoption or transposition of EU norms and rules does not guarantee successful institutional performance as the continuing problems in Bulgaria and Romania demonstrate. Thirdly, although Ukraine and Moldova have shown considerable progress over the last eight years, they lag behind others in creating a stable rule of law, political and economic freedom, respect for minorities and free media and are still considered as only partly free societies with respect to political and civil liberties. The convergence target is not yet reached and the final outcome is far from certain. Fourthly, the EU has not yet played an important role as a “transformative power”, shaping faster institutional convergence and there is a danger that the reform processes will either stagnate or “run out of steam” if the EU does not take a more decisive role in the process. In sum, the process of institutional reform is incomplete due to an absence of a clear European perspective. Fifthly, in the ENP countries changes in the complementarity of institutional reform are positively related to growth, and changes in reform level and reform complementarity have a greater effect on growth than in other regions. A corollary is that reforms that reduce institutional complementarity are likely to have a significant negative impact on economic growth. In Ukraine and Moldova the consequence is an increase in corruption and in political instability. The change in formal institutions brought about by reforms should therefore not be allowed to outpace the (slower) change in informal institutions. Reforms should therefore focus as much on informal institutions as on formal institutions. For example, the development of institutions based around improvements in social capital that would counteract the deeply rooted tolerance for corruption would contribute greatly to the elimination of the “governance gap” between these countries and the EU. Finally, the research suggests that capacities for change are progressing based on the considerable improvement in the quality of education in Ukraine, and in the capacity for innovation in Moldova.