

International Institutions' Influence on Domestic Spheres: The Case of Croatia

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Abstract: Starting with the League of Nation founded after the World War One, international institutions emerge and develop quickly once people and their countries recognize the importance of interstate cooperation. Nowadays, most international organizations are constructed and driven by their member states. Some might conclude that only international organizations are influenced by their member countries. However, the possibility of international organizations having influence on their member states may also exist. This work aims to explore this possibility. It uses the case of Croatia as a member of the World Trade Organization (WTO) as the case to study and evaluate the possible impact of the WTO on Croatia's economy and politics. This essay focuses on how international institutions influence the domestic sphere of their member states, specifically in terms of reforms and policy changes. The study has concluded that the mechanisms of international institutions like the WTO are capable of encouraging cooperation between countries and facilitating development within member states.

Keywords: International Institution, WTO, Croatia, Domestic politics, Economy.

1. Introduction

Recognizing the importance of global stability and peace, in January 1920, the winning allied states of World War One designed the first institution of global governance the League of Nation. Although it has long been criticized for unsuccessful regulations of member states and failing to provide security assurance to states in war, the emergence of this very first international organization clearly marked the beginning of “a modern era of cooperation, conflict resolution and institutional governance” [1].

Starting from the League of Nations, various international institutions began to emerge and go through a series of developments and reforms. Nowadays, international institutions are developed in a variety of fields including peacekeeping and global trade, gaining increasing importance and voices throughout the global stage. Moving to an era of interstate cooperation, more and more countries are willing to acknowledge the sovereignty of international institutions and being part of them. Indeed, no matter in which field, the special structure and principles of international institutions allow friendly and efficient cooperation between countries and reduces the possibility of unpleasant outcomes. In specific, centralization and independence, the two main properties of international organizations (IOs), allow IOs to perform a variety of functions such as facilitating negotiations, resolving disputes, and implementing norms and agreements [2]. On the other hand, according to Duffield, an international

institution has three functions: the constitutive function for creating institutional rules and norms, the regulative function for restricting or prohibiting several actions of member states, and the procedural function for allowing states to achieve mutual agreement [3]. Given these functions, countries have to make certain compliances and commitments in order to fit the standards and be able to join the institutions. International institutions, then, begin to play a crucial role in shaping the behaviors of states and bringing changes to the domestic sphere.

In part one, it briefly summarizes the history and development of international institutions and their general functions. In part two, it gives a general picture of the World Trade Organization (WTO), including its history and functions. In part three, Croatia as the case from the WTO is adopted and discussed for exemplification and analysis. In the fourth part, it draws the conclusion that the mechanisms of international institutions like the WTO are capable of encouraging cooperation between countries and facilitating development of member states.

2. The World Trade Organization as the Case

In this section, the prehistory and the development of the World Trade Organization will be introduced to give a basic insight on this international organization. In addition, some underlying principles and functions of the WTO will be discussed to justify the choice of using WTO as the case.

2.1. History before the WTO

Early in 1947, the General Agreement on Tariffs and Trade (GATT) was signed by 23 countries and was enforced on January 1, 1948. The treaty aimed at reducing trade barriers and facilitating economic recovery from World War II. The GATT is widely considered as the predecessor of the nowadays World Trade Organization, but it is created in support of the International Trade Organization (ITO), an international organization failed to officially form because of the U.S. withdrawal from the ITO concept [4]. During the execution of the GATT, negotiations about reforms of GATT occurred periodically from 1951 to 1986. In the 1980s, however, problems with GATT arose due to its flaws. The first problem came with its ineffective dispute resolution mechanism, resulting in continuous and unsolved disagreements between countries. Second, industries like agriculture, textile production and service were not regulated by GATT rules. Third, measure requirements such as antidumping and countervailing tariffs were said to adversely affect trade in certain sectors. Fourth, intellectual property rights were not well protected. Finally, rules regarding interstate investment engendered a wide controversy among countries.

To examine these issues, the Uruguayan Round, a new negotiating round, was started in 1986. Given the GATT treaty of 1994 ratified, the WTO, an international organization that oversees global trade and mediates trade disputes, was finally established in 1995.

2.2. Changes and Reforms done by WTO

From the initial 23 members signing the GATT agreement to 164 member states involved in the WTO, the WTO has gone through a series of changes and reforms despite similar basic principles with its predecessor GATT [5]. Compared to the GATT, the WTO has a wider scope of influences and regulations. Also, the provisions it requires are solidly applied to all members with specific agreements and obligations. Additionally, in response to the former issue of the GATT dispute resolution mechanism, the WTO has a more “automatic” settlement system with the “negative consensus” rule which states that the adoption of reports can only be stopped when all members involved disagree with the results of a dispute resolution. Furthermore, there is greater transparency in trade-related issues and supervision of the behaviors of member states, ensuring the obedience of commitments made.

2.3. Functions of the WTO

In summary, there are three main functions of the WTO. All of them help ensure the operation runs smoothly and function efficiently.

2.3.1. Regulating

The WTO was created to promote free trade and ensure global economic stability. Thus, requirements of economic reforms and measurements that guarantee fairer competition in international markets are the key thresholds of joining the WTO. Basic regulatory measures include similar GATT agreements in reducing protective tariffs and non-tariff barriers to get larger market access. Intellectual property rights are also protected by the Agreement on Trade-Related Aspects of Intellectual Property Rights (TRIPS Agreement) [6]. Further measures such as antidumping, countervailing tariffs and privatization of state-owned enterprises are needed too. Apart from liberalizing the global economy, these regulations assure that there is minimal governmental interference within the market, which is believed to cause disruption in the economy. If the regulating mechanism is functioning ideally, it should make sure that no one is gaining an unfair advantage over others.

2.3.2. Monitoring

After setting those rules and requirements, the WTO also functions to supervise its members whether they comply with them or not. To allow the members to have a clear picture of the trade policies of their trading partners in the WTO, the Trade Policy Review Mechanism (TPRM) is established during the Uruguay Round [7]. Knowing the information and the information being known are crucial for encouraging international cooperation, as states will be more likely to comply when they know others have done so as well. In addition, greater transparency the TPRM provides increases the cost of defection because of the concerns of retaliation, reducing the likelihood of cheating during trades. Member states can benefit from this instrument by examining each other's trade practices and thus reducing the level of information asymmetry. It also encourages smaller and under-developed nations to pursue appealing trade policies that advance their domestic economic prosperity [8]. Having this kind of mechanism, countries can perceive more accountable and predictable trading prospects.

2.3.3. Dispute Resolving

The WTO also forms its own dispute settlement mechanism that modified from the GATT system during the Uruguay round of negotiations. The Dispute Settlement Body, or DSB, with the mandatory jurisdiction for trade disputes settlement, marked a transition from the diplomatic approach to a rule-based institution [9]. When solving the dispute, as referred to Article 7, the DSB will form panels to investigate and examine the issues based on existing provisions, actions of actors and complaints against those actions. After the investigation, the panels may reach conclusions that either the actions of one country align with the WTO rules or the actions are inconsistent with the WTO norms. In the former case, the country will continue the actions as it is consistent with WTO rules. While in the latter case, the country shall stop behaving inconsistently. However, the panels have no right to make new norms for the member states, as the WTO is a member-driven organization. Countries on both sides of the dispute are expected to be mutually benefited and have more solid trade relations in the future. According to Bown and Hoekman, participating actively in dispute settlement activities can have positive externalities if trade barriers are successfully removed after the dispute is resolved [10].

3. Case of the WTO

In this section, Croatia as a WTO member will be used as the case of how international organizations influence the domestic politics and economy of its member countries. Croatia is a country located in the northwestern part of the Balkan Peninsula. Founded on 25 June 1991 and becoming a formal member of the WTO on 30 November 2000, Croatia has gone through a transition from a socialist country to a democratic country and transformation of economy during the late twentieth century and early twenty-first century.

3.1. A History of Croatian Politics and Economy

Before gaining independence in 1991, Croatia was a part of Yugoslavia, a country created after World War I which, according to Ivo Bičanić and Vojmir Franičević, has been long considered an “experiment” of socialism and frequent radical institutional reforms [11]. The formation of Yugoslavia was triggered by a series of events after the war. As parts of the Austro-Hungary and the defeated side of the World War One, Croatia, as well as Serbia, joined the winning side Serbia. Meanwhile, a social movement occurred in the former Austro-Hungarian monarchy, aiming to bring the separated nations together. Concerned about their safety under the potential threat from Italy on the West and Germany and Russia on the East, the supporters of the movement called for a state of strong military power to protect the territory from being invaded. Thus, the idea of Yugoslavism, a concept of forming a common South Slavic political entity, was born in Croatia and developed in both Croatia and Slovenia [12].

However, the reality was not ideal for the Yugoslavians. World War II stopped Yugoslavia from its gradual development as a federation, and the entire Yugoslavia was later under the control of the communist party. Influenced by the changing political situation, the economy of Yugoslavia under Communism went through a period of chaos, from a planned economy to a free market economy in 1964, and then to “collective bodies” in which all private interests were illegal and separate national economies, decreed by the constitution of 1974. Debts, disorder, and clashes arose from the failure of Yugoslav Communist Party. Although attempts were made after the death of the communist leader Tito to restore the country in the late 1980s, it was proved to be too late.

While the failing of Yugoslavia was concurrent with the transformation of Croatia and other successor states. In 1989, nearly all Yugoslav started to reform, given the evidence of The Enterprise Law and other legislation, including Croatia. Although the first radical transformation was turned out to be unsuccessful because of political constraints, problems with certain economic policies and the lack of international support (to be more precise, the EU support), it left several legacies to Croatia. Concerning the economy, it started the privatization of enterprises, entrepreneurship, and liberalization of the market. Concerning the politics, the transformation led to more pluralized political atmosphere, reducing political segmentation and ethnic tensions.

The second transformation of Croatia was after winning its independence in the Wars of the Yugoslav Succession in 1991. At this time the transformation was forced entirely by actors in Croatia, and it exemplified a successful reform. Firstly, with wide range of privatization, the share of private sector increased by 50 percent in the end of 1990s compared to the beginning of the decade. Secondly, a stability program issued in 1993 in response to hyperinflation addressed the problem successfully. Thirdly, sectors like energy and food are deregulated, and the energy prices approached international market prices. Fourthly, several transformation strategies were long-term, including liberalization of internal and global trade, introduction of value-added tax, and pension reform. Finally, the national budget became more transparent and international debt was kept under control.

Despite the seemingly effective economic reforms, the political economy of Croatia in the nineties was largely dominated by a capitalist system called Crony Capitalism. It refers to a phenomenon in

which companies gaining privileges and benefits from personal relationships between business and government, rent seeking, favoritism, clientelism, corruption and other similar features [13]. It was often suggested that crony capitalism emerges as a measure of facilitating economic recovery or growth under the situation of political instability. The condition was satisfied in 1990s Croatia, when it just became independent and was eager to transition from a part of a Socialist country to a multi-party system and a democratic country. The privatization process also stimulated the development of crony capitalism. This kind of capitalist system was not durable, causing trade deficit problem, Croatia second banking crisis, rising state spending, over-budget funds, and unwillingness of reducing armed forces. These crises then led to economic instability, stagnation, and economic inequality. People's wellbeing then decreased while social tensions increased. Thus, political and economic restructuring was of great importance to Croatia at the time.

3.2. Accession to the WTO

Croatia accession to the WTO can be reasoned as two main motives. The first one is to promote economic growth and encourage foreign investment. Both economic reform and crisis happened in the nineties left several challenges and restraints on Croatian economy. One of the many was the exports. Before Croatia was the second major exporting area in Yugoslavia, exporting mostly the industrial goods. However, the industrial sector simply collapsed in the early 1990s. Industrial production and employment dropped to a minimum of 49.6% and 73.9% of 1989 levels. The decrease in exports was mainly because of losing major trading partners involving the former Yugoslavia and Soviet Union. Croatian tourism and service sectors were also affected by wars and instability within the country. Therefore, to recover its important economic sectors, Croatia would need to join international organizations like the World Trade Organization to gain larger market access, expand its trade, and increase its participation in the global economy. The second motive would be the political consensus of joining the European Union (EU). The Croatia elections of January 2020 were won by a coalition of six parties led by Social Democrats (SDP) and Croatian Social Liberals (CSLP), which have reached the consensus on European integration. For Croatia, becoming an EU member enables it to enjoy the convenience of trade with other EU members. Although Croatia got the permission to join the EU late in 2013, its accession to the WTO in 2000 was one of the crucial steps for Croatia to meet the EU standard and join it successfully.

After joining the WTO, Croatia has been making voluntary commitments on its trade policies and sectoral regulation. According to the WTO report of Croatia reform program, Croatia has updated almost all its trade-related legislation in accordance with the EU trade policy and market rules and make a reduction in its simple average manganese tariff by 5 percent (from 12.1% in 2000 to 7.1% in 2009) [14]. Plus, Croatia has gradually removed non-tariff trade barriers and implemented measures including anti-dumping and safeguard measures. Note that Croatia also signed the Stabilization and Association Agreement (SAA) in October 2001 and became a member of the Central European Free Trade Agreement (CEFTA) in 2002 [15]. Both agreements allowed Croatia to have unlimited access to a larger market. In December 2002, Croatia and the European Communities (EU/EC, later known as European Union) reached the Interim Agreement on Trade and Trade-related Matters [16]. The agreement established a free trade area between the EC and Croatia over a maximum of six years, granting Croatia the free access to EU market before it gets a membership in the EU.

3.3. Influence on Croatia

The influences of WTO on Croatia can be seen as two parts. First, the WTO has obviously influenced Croatia in its economy. Croatia generally benefits from trade as an exporting country. This is because

that Croatia traded primarily in high value-added goods (usually manufactured or industrial goods) which the good itself has a greater value than the value of its imported components added together [17]. With trade liberalization and open market access after joining the WTO, as seen from Figure 1, Croatia exports constantly increased for years, from \$7.77 billion in 2000 to \$24.63 billion in 2008, until the 2008 global economic recession [18]. Croatia has also built stable relationships with its top trading partners including EU/EC, Bosnia and Herzegovina, Serbia, Turkey, and the United States [19]. With increasing global participation and economic stability, Croatia foreign direct investment (FDI) has increased by over \$4 billion from 1998 to 2008 [20]. Instead of stagnating in 5 years, Croatia Gross Domestic Product (GDP) showed a gradual increasing trend after 2000, as shown in Figure 2, with the accession to the WTO as an indispensable factor [21].

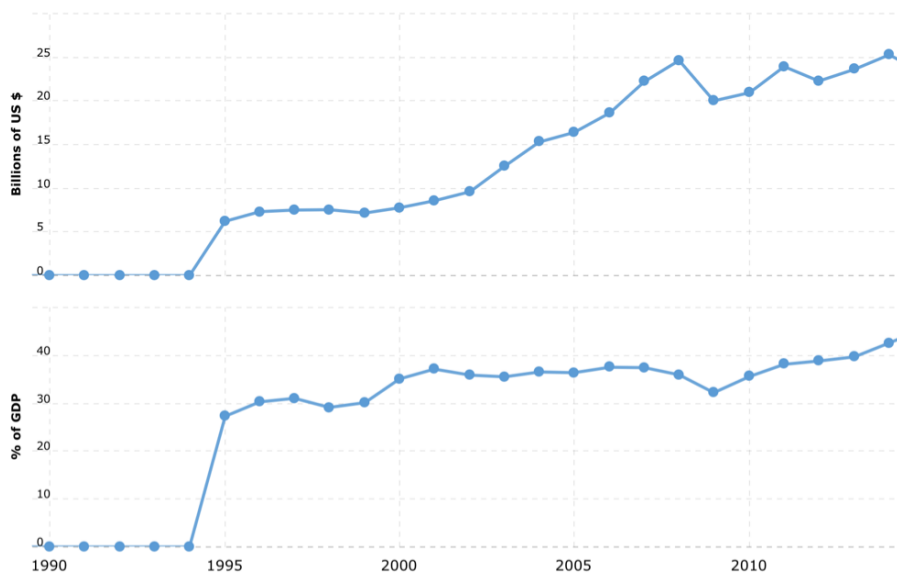


Figure 1: Croatia exports from 1990 to 2013 [17].

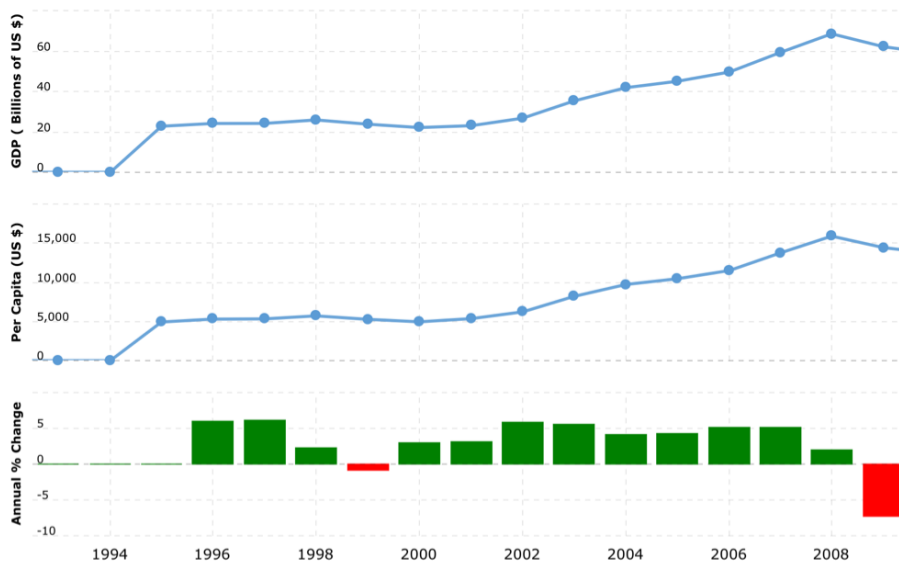


Figure 2: Croatia GDP from 1993 to 2010 [20].

The second major influence was on the politics of Croatia. For its domestic politics, the most direct change would be on Croatia economic policies, including elimination of protective tariffs and non-tariff barriers, anti-dumping, etc. While such trend of market liberalization also led to changing political preferences in Croatia. Most of these policies are neo-liberal with prevention of government intervention in economy, which are contrary to the former protectionist principle. Losing protection from international competition would inevitably cause competition among certain domestic sectors. Therefore, Croatian government at the time (mainly SDP) may have to confront challenges in proving its decision to join the WTO and possibly losing its supporters. Nevertheless, the election of 2000 ended the parliamentary and presidential dominance of Croatian Democratic Union (CDU), opening the era of the two-party system in Croatia [22].

For Croatia diplomacy, one main impact of joining the WTO was the successful gaining of EU membership in 2013. Croatia delayed its accession to EU because of a period of transition in its politics and economy. After becoming a member of the WTO, Croatia has continued to make reforms and achieve significant economic growth. With its large number of exports and tourism, Croatia was recognized as an economic asset by the EU and was thus granted EU membership on 1 July 2013. Membership of the EU is not only a symbol of economic prospects and security, but also the recognition of Croatia passing through the transition period [23]. It is not exaggerated to say that accession and compliance with the WTO played a crucial role in it.

4. Conclusion

In conclusion, the essay explores the influence of international institutions on their member states using the case of WTO member Croatia. As a country separated from a socialist country Yugoslavia, Croatia went through a period of transition in its domestic economy and politics during 1990s and 2000s. From a part of socialist country to a democratic one, from economic dislocation to an open market, Croatia is a country where successful reforms have been achieved. During its reform, the WTO acts as a facilitator, pushing Croatia toward liberalizing trade, aligning with international economic norms, and increasing global trade participation. Croatia achieved economic growth by expanding its trade with other WTO members. In addition, the accession to WTO indirectly affected the Croatia domestic and international politics. The more open and neo-liberal economic policies may cause temporary controversies among the public and within the parties, but they still implicitly ended the dominance of one-party ruling (CDU) and made the Croatia later election a more “democratic” two-party system. The accession and compliance with WTO rules also contributed to Croatia successful accession to the EU in 2013. While limitation exists from my analysis of the case. As Croatia has transitioned to a democratic country, its international relations and policies are likely to have influence on its domestic politics. However, the situation might differ in countries that have other types of government. Also, the influence of international organizations like the WTO on their member countries might be to different degrees depending on factors such as structure and degree of development. These topics are worth discussing in the future.

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