Board Meeting of August 4, 1998
Statement by Pieter Stek, Executive Director

Macedonia - Country Assistance Strategy

1. The Government of Macedonia greatly values the collaboration with the World Bank Group. In the difficult years since independence the Bank has stood by Macedonia's side and helped to cushion it from adverse situations, events and policies in the region. This support has encouraged the Government to persist with market-oriented reforms, thereby creating a realistic base for its National Development Strategy for 1998-2000, described in paragraph 12 of the CAS. The CAS is fully in line with the national strategy and the Government regards its implementation as crucial to the creation of a well-functioning market economy and of the conditions for accession to the European Union.

2. It appears that the corner has been turned and, after a deeply painful decline, real per capita income and consumption are rising again. The key to further restoration of income levels lies in profitable private investment. The Government is fully aware of the fact that this requires a fundamental reorientation and down-sizing of the public sector as part of the creation of an environment that is conducive to private-sector activity. It is also aware of the fact that significant remaining ties between banks and businesses not based on market incentives must be dissolved. The FESAL II for this fiscal year has a major role in this respect. The short-term effects of such structural reforms are obviously painful; to carry them out at an unemployment level of 30% requires great determination and deserves generous support.

3. Hence, the Government and the Bank have recognized that social-sector reform is a necessary complement to the reform of the private and public sectors. The CAS correctly notes that the Government is deeply committed in this area and intends to focus on a wide range of policies (paragraph 25), some of which are essential to help prevent poverty, others to remedy it, and others again to make it less intolerable.

4. The engine of recovery, as noted, must be investment-led growth. The first cylinder of the engine is in good working order, namely the creation of stability: inflation is low and so is the fiscal deficit. The IMF Board recently approved the second instalment of an ESAF loan. On June
19 the milestone was achieved of acceptance of the obligations of Article VIII of the Fund Charter. The performance of the other five cylinders, i.e. structural reform in all its dimensions, is improving all the time. The authorities are taking all the advice they can get from within the World Bank Group and outside to create an enabling environment for business. Particularly valuable has been the extension of IFC's reach to the country. This has helped to unleash a significant amount of entrepreneurial activity. Also, the advice from FIAS has been found very timely and useful. MIGA and EDI too have played constructive roles, although in the case of MIGA transactions still have to materialize. The foundation has been laid for an inflow of foreign direct investment. Foreign interest was already demonstrated in the privatization of Stopanska Banka and may again be expected in the telecom privatization. Clearly, the return of stability to the region would catalyze much more interest for what is fast becoming one of the more hospitable environments in the region.

5. In the meantime, Macedonia requires significant support for the reasons mentioned. The reward for its conscientious reform policies is slow in materializing and neither the prevailing unemployment rate nor the current account of the balance of payments leave any margin of comfort. In these circumstances the continuation of blending of Bank support with IDA funds is welcome. Macedonia understands that it is a borderline case in terms of income per capita but trusts that graduation from IDA will not take place without careful judgment of its situation. The Government is proud of the fact that its use of IDA money is judged to be of the highest quality by IDA. The Government is pleased that, in the unhappy event of an externally brought on crisis, Management would seek emergency funding from IDA. I agree with the risk of such an event as described in paragraph 45. Clearly such a risk looms large in the public perception in the present state of affairs in Kosovo. It should be noted, however, that so far there has been no significant influx of refugees and that the Government is doing all it can to reduce tension in the local Albanian community. As the CAS notes in paragraph 30, public outreach is important to both the Bank and the Government for making the reforms understood, including their balance and their fairness. The Government appreciates the professional experience the public sector is gaining from the Bank's efforts.

6. I wish to end by noting the dynamic role of the Resident Mission. Not only is it deeply committed to its work but it is a highly respected partner of the authorities in their development effort. I was deeply impressed, moreover, by the quality of the local staff and the enthusiasm they displayed for their work. These remarks extend fully to the IFC representation on the same location.