Former Yugoslav Republic of Macedonia: Country Assistance Strategy

1. Visiting World Bank officials declared in May that Macedonia shared first place (with Estonia) for macroeconomic stability in Central and Eastern Europe. But despite adhering to the sound macroeconomic policy set by the IMF, economic developments in 1997 were disappointing. GDP forecasts at the beginning of 1997 predicted growth of 5%, but expectations were downgraded during the year and growth was about 1.5%. The current account deficit remained high, poor export performance promoted a major devaluation of the currency in July, and unemployment continues to be a very major concern.

2. But Macedonia may have turned the corner. GDP forecasts for 1998 are for 4-5% growth. The devaluation has triggered export growth, bank privatization is progressing, and structural reforms are beginning to move forward. The most recent trend is encouraging, though there is much work to be done, especially on the structural side.

3. This Country Assistance Strategy is a strong program. We are pleased with its focus and consider the major priority of accelerating recovery to be well designed to improve upon Macedonia’s emerging economic expansion. The high-, low-, and emergency-case scenarios appear to be well conceived and we appreciate efforts to identify projects that will be successful even in a deteriorating economic environment.

4. We applaud the efforts to identify those previous assistance strategies that have been most and least effective as presented by OED. These lessons are well incorporated into the current CAS. The CAS strategy appears to be well coordinated with, and a good complement to, the aid programs of the IMF, EBRD, and other bilateral donors.

5. Successful macroeconomic adjustment by the Macedonians has given them the solid footing to tackle structural reforms. But it is crucial that all parties remain determined to
maintain macro stability while reforms focus more heavily on the structural side. The continued high current account deficit (8.3% of GDP in 1997, up from 7.3% in 1996) is very troubling, but the government appears to have taken the right steps. Devaluation of the currency may be starting to show results. Moreover, with relations between Macedonia and most of its neighbors improving, and pending resolution of the unrest in Kosovo, exports should increase. Thus, we support CAS projects that will help support current account financing.

6. Over three-quarters of the total enterprises had been privatised by the end of 1997 and sales of a further 15% of state-owned assets were under way. However, the privatisation program has yielded only limited results in terms of restructuring and revenues. The privatization process was dominated by management and employee buyouts, which resulted in little inflow of new capital and virtually no restructuring. Focusing CAS resources on re-privatizing/restructuring is highly appropriate.

7. The banking sector continues to lend to loss-making enterprises, often because of the interconnected ownership structure between banks and enterprises. There exists an urgent need for continued bank privatization (in addition to the recent progress with Stopanska Banka, supported by IFC), liquidation of insolvent banks, and mergers of smaller banks, accompanied by western-style prudential financial regulations. Can IFC and Bank staff expand on their anticipated involvement in the banking sector as envisioned in the CAS?

8. The GOM plans to capitalize a new state-owned Development Bank. This does not seem to promote the reform program. What is the purpose of the Development Bank and what is the Bank’s position?

9. We strongly endorse the CAS focus on reform of the labor market. Unemployment is very high, officially 25-35%. Unemployment is especially high among newcomers to the labour force and those with higher education, storing up problems for the future and increasing the potential for social protest. Macedonia must eliminate the labour-force rigidities that it has inherited from the old regime in order to facilitate the flow of labor resources to their optimal use. The need to restructure enterprises, with the accompanying layoffs, makes labor-market reform all the more important.

9. The CAS goal of enhancing the efficiency of the State is a very important element of structural reforms. Only through civil service reform, institution building, and redefining the role of the state, can Macedonia expect to accelerate privatization and restructuring of the economy.

10. Commercial law is in great need of reform. The GOM lacks an efficient, coherent process for drafting, considering, and enacting new laws. It also lacks the requisite expertise to
do so. These reforms are a key element to overall structural reform. Legal reform should not be neglected. How, specifically, will the CAS support commercial-law reform?

11. There has been mention of setting up a one-stop agency to assist in FDI. Given Macedonia's poor showing in attracting foreign investment, this is a good step forward. This type of action has proved very useful in other transition countries. Will the Bank and IFC be involved in the setting up of this agency?

12. A significant share of Macedonian output derives from the agricultural sector. In addition, agriculture has performed relatively well during the transition. Given the importance of this sector, can staff more specifically elaborate on its goals for the agricultural sector?

13. Finally, I would like to commend staff for their excellent work in building with the GOM a coherent and effective CAS to support the national development strategy for Macedonia focused on promoting private sector led growth and job creation. We commend the consultative process and suggest that efforts be taken to make this CAS publicly available.