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Statement by the Hon. **PETAR GOSEV**,
Governor of the Bank for the **FORMER YUGOSLAV REPUBLIC OF**
MACEDONIA,
at the Joint Annual Discussion

**Statement by the Hon. Petar Gosev,
Governor of the Bank for the former Yugoslav Republic of Macedonia,
at the Joint Annual Discussion**

**THE REPUBLIC OF MACEDONIA-ACCOMPLISHMENTS IN THE PROCESS
OF TRANSITION**

Since it gained its political independence back in 1991, the Republic of Macedonia has been undergoing a process of complex economical and political reforms, directly towards development of a contemporary democratic society with a market-oriented economic system. In the process of transition Macedonian economy faced a large number of external shocks (trade blockades, economic sanctions imposed towards neighboring countries, security crisis in the region and in the country), which had an impact on the dynamics of the economic growth.

The process of macroeconomic stabilization commenced in 1994. Besides the restrictive monetary policy, it encompassed drastic reduction of the budget deficit. The fiscal consolidation, however, was to the largest extent rather a result of short-term measures than of the implementation of complex reforms. Despite the results accomplished on an aggregate level, the budget structure remained unfavorable from the aspect of providing more significant support to the economic growth. The Kosovo crisis from 1999 and especially the security crisis in the country from 2001, caused a deterioration of the fiscal position. The General Budget deficit in 2001 reached 7.2% of GDP, and in 2002 it remained at the high level of 5.6%.

Having in mind this situation, the main objective of the macroeconomic policy in 2003 was the fiscal consolidation. The General Budget deficit in 2003 is estimated to be reduced to the level of 2.5% of GDP which represents an impressive reduction of 3.3% of GDP in only one year. Not only has the objective been achieved in the first eight months of this year, but it has also been surpassed. The basic medium-term objective of the public finance policy is gradual reduction of the deficit at a level of around 1% of GDP. As opposed to the impressive Budget consolidation in 2003, directed towards establishment of initial discipline in the public finance, the further reduction of the budget deficit in the next years is achieved gradually. In parallel with this, the process of improvement of the public expenditure structure is going on. Thus, room for gradual increase of the capital expenditures and achieving a level compatible with the most advanced transition economies was being created.

The reduction of the Budget deficit is significant for the increase of the national savings, reduction of the interest rates, increase of the credits to the private sector, increase of the investment activity and reduction of the need for foreign financing. This is confirmed by the achievement sin 2003, when after the several-year rigidity, a reduction of the interest rates on debit balance of the banks was registered. This is also achieved by the measures for reduction of the costs of the banks and by providing increased foreign exchange crediting in the country. The fiscal consolidation and disciplined application of the monetary strategy to the targeting of the foreign exchange rate enabled maintenance

of the inflation at a low one-digit level which will not exceed 1-2% in 2003. As far as price stability is concerned, the Republic of Macedonia belongs to the group of most successful countries in transition with an average annual inflation rate of below 3% in the period 1997 – 2003.

The case of Macedonia is a clear example of the fact that the development is a much more complex issue than the achievement of the price stability, which is needed but not sufficient condition for dynamic growth. The analysis of the three basic components of the integrated development concept (sustainable economic, social and regional development), shows in the case of Macedonia that the economic components is the one that lags behind the most although the other two components heavily lag behind as well. The Republic of Macedonia was in fact much more successful in achieving and maintaining the price stability, reducing the budget deficit and changing the ownership structure in the enterprises, rather than in their efficient restructuring and realization of dynamic economic development.

The GDP growth rate was low during the whole transition period, so that in the period of political and security instability in 2001, the economy entered in the zone of recession, that also continued in 2002. By the end of 2002, there was a moderate revival of the economic activity that also continued in 2003. Still, Macedonia has not already reached the level of GDP that it had prior to obtaining its economic independence.

The poor dynamics of the economic growth is the reason for the biggest problem in the Republic of Macedonia – unemployment, which is estimated at the level of around 30%. Therefore, development of a new economic strategy is needed, the objective of which is realization of more dynamic and sustainable economic growth in a long run. The basis of this strategy should be strengthening of the private sector competitiveness and creation of new jobs.

In order to realize the commitments of the Government for increasing the employment, poverty reduction and increasing the standard of living, the Macedonian economy must realize more dynamic economic growth, which, on average should not be lower than 5%. In order to achieve this, a new development strategy is needed which is based on policies, that in accordance with the empirical results, show positive correlation with the growth: a) maintenance of low and stable inflation; b) control of the public expenditures; c) high openness of the country; d) compliance with the ownership rights and the law; e) development of the human factor and f) achievement of balanced regional development. Thereby it is very important these policies not to deteriorate the distribution of the income thus providing for the poorer layers of the population to feel the benefits of the economic growth.

I will elaborate more concretely on some of the most significant challenges:

1. Redefinition of the Government role

The Government should provide room for the private sector and favorable investment environment for development of entrepreneurship. That means strengthening of the institutional capacity of the Government institutions so that they can provide quality and efficient public services. I consider that the credibility of the Government and the capacity of the Government institutions are of key importance for the successful realization of the complex reform process. Therefore, the public sector reforms supported

by the World Bank are one of the priorities of the Government of the Republic of Macedonia.

The creation and maintenance of new jobs must be supported by the Government by labor market reforms, as well as via an efficient system of educational, health and social protection. The last element is especially important for mitigating the consequences of the structural reforms on the most disadvantaged layers of the population, as well as for providing public support for the implementation of those reforms. All these elements are an integral part of our three-year Country Assistance Strategy supported by the World Bank.

2. Openness towards the global financial and trade tendencies

The economic growth in the Republic of Macedonia as a small country with a market of 2 million inhabitants is to a large extent determined by the foreign demand for the Macedonian products. The degree of international openness of the Republic of Macedonia is satisfactory, whereby the share of the foreign trade in GDP is 90%. However, the balance between the export and import is very unfavorable. This refers to the need for achieving more dynamic growth rates of the export with respect to the import which was not a case in the past.

3. Post-privatization enterprise restructuring

This issue is closely connected to the problem of low growth and (in) competitiveness of the economic entities. The privatization process in the Republic of Macedonia has almost been completed. The change of the ownership, however, does not by itself ensure increase efficiency of the enterprises. Therefore, by the end of the year, all residual shares of the Privatization Agency will be sold at auction. Strengthened corporate governance will be stimulated through elimination of subsidies, strengthening of the collection of claims and simplification of the liquidation procedures. Simultaneously, this process encompasses completion of the process of restructuring of the thirty loss-making enterprises which is accomplished within the framework of the FESAL project of the World Bank.

All these activities mean finalization of the passive process of restructuring. The second stage of active restructuring of the enterprises is much more important from the aspect of strengthening the competitiveness. The Government plays the role of a supporter of this process by stimulating various projects and investments, support of the newly established hi-tech enterprises, support of the entrepreneurship, etc. To that end, the establishment of Agency for Entrepreneurship promotion is underway, as well as the other taking of measures for simplification of the procedures for registering new enterprises in accordance with FIAS recommendations. It should also be added that the firm commitment of the Government for fight against bureaucracy and corruption for which an anti-corruption strategy is uncompromisingly implemented.

4. Intensification of the investment activity

The investment activity in the previous period was at a very low level. In order to accelerate the economic growth the achievement of an investment rate of 25 – 26% of the GDP and savings rate of 20 – 21% of the GDP, which is by 10 or so percentage points higher than the existing level, is set as a medium-term objective of the macroeconomic policy. The disciplined public spending and development of long-term instruments for saving (pension system reform, issuance of government bonds) will contribute to the

increase of the domestic savings and improvement of the development potential. This also anticipates more efficient allocation of the savings, which requires further strengthening of the banking system competitiveness.

What is especially required for creation of new jobs are investments in new export-oriented enterprises (what are known as “greenfield investments”). In this context, as a Minister of Finance of a small country, I would like to publicly support all initiatives within the World Trade Organization (the trade negotiations in Doha, Monterey, Cancun etc.) for opening of the developed countries markets for the products of the developing countries to a greater extent. If the developed countries pass from rhetoric to action, more long-lasting and more dignified source of development and poverty reduction will be enabled than in the case with the official donations. Then, we might say that the globalization is a process that really creates equal opportunities for development of the undeveloped and developed, poor and rich countries.

Thank you.