Republic of Macedonia

ECONOMIC REFORM PROGRAMME

2018 -2020

January 2018

РЕПУБЛИКА МАКЕДОНИЈА
МИНИСТЕРСТВО ЗА ФИНАНСИИ

REPUBLIC OF MACEDONIA
MINISTRY OF FINANCE

Table of contents

Abbreviations

BC	border crossing
CACM	Capacity Allocation and Congestion Management
CEFTA	Central European Free Agreement
CIP	Competitive Industrial Performance Index
COSO	Committee of Sponsoring Organization of the Treadway
CPI	Consumer price index
DEU	Delegation of the European Union
EAR*M*	Employment Agency of the Republic of Macedonia
EBRD	European Bank for Reconstruction and Development
EC	European Commission
ECS	Energy Community Secretariat
EE	Energy efficiency
EIB	European Investment Bank
ENER	National Electronic Registry of Regulations
ERP	Economic Reform Program
ESA	European System of Accounts
ESRP	Employment and Social Reform Program
EU	European Union
EUR	Euro
FAO	Food and Agriculture Organization of the United Nations
FDI	Foreign Direct Investment
FITD	Fund for innovations and Technology Development
GDP	Gross domestic products
GS	Government Securities
GVA	Gross value added
GWh	Gigawatt hours
ha	hectare
HACCP	Hazard Analysis and Critical Control Points
HICP	Harmonised Index of Consumer Prices
HS	Hydro Systems
IEP	Individual Employment Plan
IIP	International Investment Position
IMF	International Monetary Fund
IPA	Instrument for pre-accession assistance
IPA TAIB	IPA Transition Assistance and Institution Building Component
IPARD	Instrument for pre-accession assistance for Rural Development
ISO	International Organization for Standardization
IT	Information Technology
JSC ELEM	Macedonian Power Plants
km	Kilometer
MAFWE	Ministry of Agriculture, Forestry and Water Economy
MEPSO	Electricity Transmission System Operator
MES	Ministry of education and science
MF	Ministry of Finance
MISA	Ministry of Information Society and Administration
MR	Macedonian Railways
MTBF	Medium- Term budgetary framework
MTEF	Medium-Term expenditure framework
MW	Megawatt
NBRM	National Bank of Republic of Macedonia
NEER	Nominal Effective Exchange Rate
NQF	National Qualifications Framework
NTTO	National for Technology Transfer Office
OECD	Organisation for Economic Co-operation and Development

OP	Operational plan
OTC	Over the counter
PFM	Public Finance Management
PFMRP	Public Finance Management Reform Program
PIFC	Public Internal Financial Control
PISA	Program for International Student Assessment
pp	percentage point
PPL	Law on Public Procurement
RDI	Research, development and innovation and digital economy
REER	Real Effective Exchange Rate
RES	Renewable energy sources
RM	Republic of Macedonia
ROA	Return on assets
SAA	Stabilization and Association Agreement
SEE	Southeast Europe
SEE CAO	Coordinated Auction office in South East Europe
SIGMA	Support for Improvement in Governance and Management
SMEs	Small and medium-sized enterprises
SS	Substation
SSO	State Statistical Office
TAIEX	Technical Assistance and Information Exchange Instrument
TFP	Total factor productivity
TSO	Transmission System Operator
UNESCO	United Nations Educational Scientific and Cultural Organization
UNIDO	United Nations Industrial Development Organization
VAT	Value Added Tax
VET	Vocational Education and Training
WB	World Bank
WB6	Western Balkans Six
WBIF	Western Balkans Investment Framework
WEF	World Economic Forum
WTO	World Trade Organization
WTTC	World Travel and Tourism Council
ZELS	Association of the units of local self-government of the Republic of Macedonia

Introduction

As a candidate country, Republic of Macedonia has prepared a total of ten programs so far, seven Pre-Accession Economic Programmes and three Economic Reform Programmes.

The European Union (EU) introduced a new approach to the economic governance in the Enlargement Strategy as of October 2013, becoming the key pillar in the enlargement process. Main objective of this approach is to help the enlargement countries tackle the economic fundamentals first and meet the economic accession criteria.

New approach to the economic governance in the enlargement process is inspired by the European Semester process at EU level. This approach means a significant change in the dialogue on economic policies and better reporting to the end of providing clearer instructions for the reforms necessary for supporting long-term economic growth and competitiveness. As of 2015, the Western Balkan countries, among which the Republic of Macedonia as well, have been invited to improve their economic policies and economic governance by preparing Economic Reform Programmes (ERP) covering a three year period.

Economic Reform Programme 2018 - 2020 is the fourth document of this type prepared in line with the instructions given by the European Commission (EC). The Programme presents the medium-term macroeconomic and fiscal framework, as well as the sectoral structural reforms for promoting both competitiveness and growth.

The programme is prepared in line with the Government Programme 2017-2020, the midterm Fiscal Strategy for the period 2018-2020, and the annual 2018 Budget of the Republic of Macedonia, as well as other national strategic documents, such as the National Programme for Adoption of the Acquis Communautaire, the Stabilisation and Association Agreement and the national sectoral strategies: Public Finance Management Reform Programme 2018-2021, Innovation Strategy 2012-2020, Competitiveness Strategy 2016-2020 etc.

In addition, the Programme is in line with the EU Strategy for fast, sustainable and comprehensive economic development "Europe 2020", as well as the SEE 2020 Strategy of the Council for Regional Cooperation, called "Jobs and Prosperity in a European Perspective", which closely follows the vision of the "Europe 2020" Strategy.

EC recommendations indicated in the 2016 Progress Report on the Republic of Macedonia, as well as the specific recommendations of the Ministerial Dialogue as of May 23rd 2017, based upon the EC's assessment of the Economic Reform Programme 2017-2019, were also taken into consideration during the Programme preparation.

Ministry of Finance (MF) coordinated the entire document preparation process together with the relevant state institutions. The draft sectoral structural reforms were also shared with the social partners and the business community via MF's website, the consultative meeting in MF and the Economic and social council's meeting, held for providing opinions and suggestions. There was continuous cooperation with the EC and OECD during the ERP preparation through missions and workshops in order to improve the quality of ERP and to strengthen capacity of institutions for prioritisation and coordination of economic policies.

1. Overall Policy Framework and Objectives

Macroeconomic policy in the period 2018-2020 is aimed at developing the economy and raising the living standard of citizens, by supporting domestic enterprises, above all small- and medium-sized enterprises (SMEs), increasing employment through the active employment measures, increasing the level of wages, as well as by strengthening the social protection system.

According to the Fiscal Strategy 2018-2020, fiscal consolidation in accordance with the Maastricht criteria remains the main priority in the coming medium-term period. In the period

2018-2020, gradual reduction of the deficit level is envisaged: 2.7% of GDP in 2018, 2.5% of GDP in 2019 and 2.3% of GDP in 2020. Moderate and contained increase of government debt up to 42.6% of GDP is expected at the end of 2020, while public debt is expected to account for 53.5% of GDP during the same period.

In 2018, economy is expected to recover and an intensification of economic growth is expected. Political stability and restoring the confidence of investors are expected to contribute to growth of private investments. Increase of wages and employment in the private sector, supported by government measures, coupled with the expectations for low and stable inflation in the country will contribute to increased private consumption. Continuous solid export from the new production capacities, as well as the recovery of traditional export sectors as a result of the strengthened economic activity of the countries - trading partners, will contribute to boosted export of Macedonia and better utilisation of industrial capacities.

Real GDP growth is expected to increase to 3.2% in 2018, and to continue with somewhat higher pace in the next two years, i.e. to reach 3.5% in 2019 and 4% in 2020.

Private consumption is envisaged to be the main driving force of economic growth in this medium-term period, which is expected to experience 3% growth in real terms, while growth of gross investments in the period 2018 - 2020 is projected at 4.4% in real terms in average, as a result of the planned investments by the public sector, as well as investment activity of domestic and foreign enterprises. In the next medium-term period, export of goods and services is expected to experience 8.0% real growth in average, in conditions of solid activity of the export-oriented capacities, as well as expected increase of foreign demand, while import of goods and services is expected to experience 6.4% real growth in average in this period.

Envisaged growth of economic activity in the next medium-term period is expected to be accompanied by increase of employment, encouraged by the active employment measures and programmes, the support of domestic and foreign enterprises for job creation, as well as other measures aimed at reducing unemployment in the country, as a result of which the unemployment rate is expected to reach 19.5% in 2020.

In the next three year period monetary policy will remain oriented at maintaining price stability by keeping a stable exchange rate of the Denar against the euro.

In the period 2018-2020, inflation rate is expected to be low and stable, amounting to 2% annually.

According to the latest estimates of the external sector, BOP current account deficit is expected to remain relatively low and to experience gradual narrowing in the period 2018-2020, i.e. to reduce to 1.9% of GDP in 2020.

In the upcoming mid-term period Republic of Macedonia will remain committed to creating a functional and competitive market economy. Structural reforms will be aimed at strengthening human capital, stimulating innovation and creativity, improving competitiveness of the service and agriculture sectors, further improving transport and energy infrastructure and facilitating trade. Implementation of these measures complemented by active labor market measures, should contribute to increase of the competitiveness of the economy, creating jobs and reducing unemployment.

1.1. Measures taken to implement the targeted policy guidelines adopted at the Economic and Financial Dialogue in May 2017

G 1: Develop a proper fiscal consolidation strategy by defining and costing concrete revenue and expenditure measures on a multi-annual basis, whilst protecting growth-enhancing spending. Improve the efficiency and effectiveness of public spending by streamlining and better targeting transfer payments.

The Fiscal strategy 2018-2020[1] stipulates that fiscal policy in the coming medium-term period will be aimed at fiscal sustainability and gradual fiscal consolidation, maintaining macroeconomic stability, boosting competitiveness of the economy and increasing employment. In fact, the focus will be placed on creating favourable business climate, supporting domestic enterprises, above all SMEs, as well as supporting the economy with substantial investments in infrastructure projects. During the next medium-term period, special attention will be put on the commitment to gradual consolidation of public finances, to the end of maintaining the macroeconomic stability and controlling the level of indebtedness. Set basic postulates of the fiscal policy in the coming period provide for gradual reduction of the budget deficit level and its positioning at a level of around 2.5% of the projected GDP in 2019 and 2.3% of GDP in 2020.
G 2: Improve budget planning capacity, in particular through the introduction of a medium-term expenditure framework. Enhance fiscal transparency by including information in the budget documentation on the composition of deficit financing; the budgetary impact of new policy initiatives; payment arrears; and spending and borrowing by state-owned enterprises. Adopt fiscal rules, as an ordinary budget law if their constitutional embedding proves difficult.
The Project on Strengthening Medium-Term Budgeting for Efficient Public Finance Management was implemented in the period December 2015 – November 2017 through IPA TAIB 2011, the main activities of which were aimed at determining the programme classification of expenditures, strengthening the capacities for medium-term planning and reporting in line with the ESA Methodology. Within the Project, a Medium-term budgetary framework manual was prepared, whereby the concept for implementation of medium-term budgetary framework (MTBF) and medium-term expenditure framework (MTEF) is appropriately defined, and respective legal amendments and bylaws will be prepared accordingly. Hence, the Ministry of Finance begins the preparation of a new law organic budget law, which will include all planned reforms regarding medium-term budgeting, as well as the establishment of fiscal rules in law, rather than the Constitution. In order to increase transparency by creating better-quality information, easy and available to the broader public, Ministry of Finance set an accountability and transparency platform on its website and it also published the 2017 Citizens' Budget[2], including the 2017 Supplementary Budget, as well as the 2018 Citizens' Budget[3] including the 2018 Budget. The citizens, the research and the academic community can easily access the information related to the Budget and the budgets of the budget users, quarterly data on generated revenues and executed expenditures of the municipalities, macroeconomic data, debt stock and other publications, bulletins and similar. In addition, Law on Budget Accounting and Accounting at Budget User was modified and amended so as for the budget users to publish the Annual Budget Reports on their websites within 15 days following their submission to the Central Registry. In the coming period, Ministry of Finance will also work on increasing the transparency by publishing additional data, annexes, scenarios within the overall budget documentation, on regular and continuous basis: Budget of the Republic of Macedonia, Annual Budget Report, Fiscal Strategy, as well as Citizens' Budget. Already with the 2018 Budget and the Fiscal Strategy 2018-2020, the Ministry of Finance moved towards increased transparency by introducing additional tabular reviews, graphs and clarifications. Ministry of Finance published review on arrears as of 31st May 2017 inclusive, prepared on the basis of data submitted by the budget users, the Funds, the public enterprises and the municipalities to the Ministry of Finance. In order to introduce a unique platform on which the budget users, the spending units, the public enterprises at national and local level, the public health institutions and the municipalities can report their arrears, the Ministry of Finance has prepared a software/application solution through the Twinning Project for Strengthening the Medium-Term Budgeting for Effective Public Financial Management. On the basis of the data the institutions report on monthly basis, they will be sublimated in a form of reviews so as to provide for records on the stock of arrears at all times. Ministry of Finance, in cooperation with the World Bank, will prepare a Strategy aimed at improving the process of recording the arrears, preparing an action plan for their settlement, as well as establishing a system to prevent the future incurring of arrears.
G 3: Continue efforts to further strengthen the use of the local currency and to further foster NPL resolution by developing a comprehensive strategy to these ends, with the participation of all relevant stakeholders. The monetary policy stance should remain consistent with the exchange rate peg, using available scope within this framework in line with safeguarding price stability.
a) Non-performing loans in the banking system of the Republic of Macedonia rose since the beginning of the global crisis,

[1] http://finance.gov.mk/files/u6/Fiskalna%20Strategija%20na%20RM%202018-2020_0.pdf
[2] http://www.finance.gov.mk/files/u3/Gragjanki%20Budjet.pdf
[3] http://www.finance.gov.mk/mk/node/6810

but still preserved at a moderate and stable level of about 11% in the period 2013-2015. The National Bank has been monitoring the movement of non-performing loans in order to preserve financial stability, as well as to prevent any damage to the credit channel. In addition, the central bank has been undertaking activities to identify the reasons of the high persistence of non-performing loans, but also of the emergence of new ones (banks' analyses and surveys). Thus, in 2013, regulatory amendments were made to support loan restructuring by banks.

The NBRM analyses from previous years indicated a high concentration of non-performing loan portfolio of legal entities, where the 50 largest non-performing loans accounted for nearly 60% of the total non-performing loans to legal entities. More than half of the non-performing loans were fully provisioned. Banks' surveys indicated that they take standard measures to manage non-performing loans (increased personal contact with customers, adjusting the credit standards to the current financial difficulties), and do not write-off claims as long as there is the slightest possibility of recovery. Under such circumstances, in December 2015, the NBRM amended the Decision on credit risk management, requiring from banks, by 30 June 2016, to write-off all claims that have been fully provisioned for more than two years. In addition, banks are still allowed and required to collect these claims, although they are written off. Consequently, at the end of 2016, mainly as a result of this measure, the share of non-performing loans was reduced to 6.6%, and in September 2017 it remained at the same level.

During 2016, the NBRM took further actions aimed to explore possibilities and obstacles to efficient settlement of banks' bad claims, including a comprehensive questionnaire that was sent to banks. As a result, in order to further reduce non-performing loans, in 2017, the National Bank developed a draft-strategy, including draft measures and activities for improving non-performing loan management, including their sale, whose implementation requires an interinstitutional coordination. The National Bank started to undertake concrete activities for the implementation of some of the proposed measures, such as developing a registry of assets foreclosed by banks, clarifying the definition of write-off, and so on. The process of interinstitutional consideration of the Draft Strategy has already started.

b) In the period from mid-2009 to 2015, there was a trend of intensive *denarization* on both sides of the banks' balance sheet, which was mainly driven by the denarization on the liabilities side, followed by the denarization on the assets side. During this period, the share of deposits with foreign currency component in total deposits declined by about 18 p.p., while the share of loans with foreign currency component in total loans decreased by about 12 p.p.. The switch in the currency preferences of entities towards savings in denars can be explained by several factors. Besides credible macroeconomic policies oriented towards maintaining macroeconomic stabilityand safe and sound banking sector, there are also other factors such as: strengthened fundamentals of the domestic economy, higher yield on domestic currency instruments, crisis in the euro area, efforts made to develop domestic financial markets, and wide range of macro-prudential measures taken by the NBRM in this period aimed at promoting domestic currency.

The NBRM significantly supported the process of denarization mainly through changes in reserve requirement, which in this period has been actively used as a macroprudential tool and instrument to support denarization. Thus, in this period, further differentiation was made of the reserve requirement rates by currency (reduction in the reserve requirement rate on denar liabilities and increase in this rate on foreign currency liabilities) and introduction of a zero rate on reserve requirement on household deposits with contractual maturity of over 2 years and denar household deposits with contractual maturity of over 1 year. Uncertainty about the political situation and speculations about the exchange rate and the banking system stability during the second quarter of 2016 interrupted the positive trend. Yet, the share of deposits with foreign currency component slightly increased (1.5 p.p. in the second quarter of 2016), and then stabilized and got back to the pre crisis level. The set of measures for dealing with this situation, among other things, included a measure for maintaining the denarization process (by increasing the reserve requirement rate on denar deposits with FX clause). In this context, it is worth mentioning that the benefits of the multiyear process of deeuroization were maintained despite the external and internal shocks.

In the course of 2016, the NBRM prepared a list of draft measures to further support the deeuroization process of the economy, and in 2017, the NBRM drafted a deeuroisation strategy aimed at further strengthening of the confidence in the domestic currency, which is aimed at supporting the monetary strategy of targeting the denar exchange rate, and further maintaining of the financial stability. The draft strategy specifies several measures, as well as involvement of other competent institutions. The process of interinstitutional consideration of the Draft Strategy has already started.

c) Monetary policy in 2017 has been focused on preserving price stability by maintaining a stable exchange rate of the denar against the euro. After the increase in the policy rate in May 2016 (from 3.25% to 4%) due to the uncertainty about the domestic political situation and speculations, there was a gradual stabilization, which allowed gradual reduction of the policy rate on three occasions (December, January and February), whereby in February 2017, it was restored to the pre-crisis level of 3.25%. As of September, this interest rate remained unchanged amid low inflation, favourable balance of payments position, stable foreign exchange market developments, gradual positive developments in banks' deposits since the mid-year, but also uncertainty in the first half of the year, and need for attentiveness. The NBRM will continue to carefully monitor the developments, internal and external risks, and will remain ready to adequately respond and maintain price stability in the economy.

G 4: Adopt a comprehensive and credible public finance management reform programme. Prioritise public investments against clear policy objectives. Increase the transparency on the selection criteria for investments and on their impact on economic growth and on the fiscal path.

The Public Finance Management Reform Program[4] was adopted on the Government's session held on 19 December 2017. Seven priorities are established for this PFM Reform Programme: - Priority 1: Improved Fiscal Framework - Priority 2: Revenue Mobilization - Priority 3: Planning and Budgeting - Priority 4: Budget Execution - Priority 5: Transparent Government Reporting - Priority 6: Internal Control - Priority 7: External Control and Parliamentary Oversight. Within the Programme, one of the activities in the Priority - Planning and Budgeting, is to Conduct Public Investment Management Assessment (in collaboration with IMF). The Public Investment Management Assessment (PIMA) will estimate the efficiency of the country's public investment, will outline the relative institutional strengths and weaknesses, will provide practical recommendations to enhance the efficiency, as well as information on the projects included in the budget.
G 5: Reduce the use of the urgency procedure for legislation and make full use of the National Electronic Registry of Regulations (ENER) to ensure proper and systematic consultation of the stakeholders, and reinforce the independence and the capacities of commercial courts.
According to the Plan 3-6-9[5], at the Government session held on August 15 2017, the Rules of Procedure for amending the Rules of Procedure of the Government were adopted, whereby the maximum number of days for consultation of ENER was increased from 10 to 20 days. These amendments enable affirmation and improvement of the established practices for participatory policy creation supported by the governmental and civil sector. In addition, at its session held on July 4, 2017, the Government adopted conclusions obliging all ministries to comply with the Regulatory Impact Assessment (RIA) procedures and publication to ENER. Pursuant to the Rules of Procedure of the Government and the E-Government system, at the sessions of the working bodies and the Government materials are reviewed, that contain the necessary opinions in accordance with Article 68 of the Rules of Procedure, including the opinion of the MISA on the draft laws that are subject to RIA. At the 7th Meeting of the Special Group for Public Administration Reform between the EU and the Republic of Macedonia, held on 20 September 2017 in Skopje, the Government's commitment to take further concrete steps to increase transparency was emphasized, in particular by limiting the use of urgent and shortened procedures and systematic engagement of civil society in policy development and the fact that government reports will be timely accessible to the public. Regarding the recommendation for strengthening the independence and capacities of commercial courts, we point out that there are no separate commercial courts in the Republic of Macedonia, only departments for commercial disputes within the civil courts. Courts in the Republic of Macedonia act very effectively upon trade disputes. The effectiveness of the courts, within the Council of Europe, has been addressed in the European Commission for the Efficiency of Justice (CEPEJ) reports, where it is particularly observed through the clearance rate and the average time to resolve the cases (disposition time). In 2016, 1,258 cases in the field of commercial disputes were received in the competent courts, and during this period 1,432 cases were resolved. According to the above, the rate of cleared commercial cases in 2016 is 113.83%, and the average disposition time is 271.46 days. Regarding the independence of the judiciary, the Republic of Macedonia has incorporated in its legislation all international standards in this area. Thus, judges are elected by the Judicial Council, where the majority of members are judges elected among all judges in the Republic of Macedonia. Also, regarding judicial financing, its independence is ensured through the functioning of the Judicial Budget Council, which has key competences in the process of drafting and implementing the judicial budget. The independence of the judiciary is also ensured through the education of judges, which takes place within the Academy for Judges and Public Prosecutors.
G 6: Strengthen the outreach and coverage of active labour market policies towards the long-term unemployed, youth, and the low-skilled. Improve the qualifications of teachers and increase enrolment in pre-school education. Stimulate work-based learning in both initial and continuous vocational education and training.
a) In order to increase the scope and coverage of active measures, in 2017, amendments were made to the Operational Plan, and additional EUR 2 million were provided for financing active programs and measures for employment for 2017. The additional funds were used primarily for active measures to support the employment of young people up to the age of 29. Regarding the recommendation to increase enrollment in **pre-school education**, precisely the increase of capacities of institutions for preschool education and care, increase of coverage of children, as well as inclusion of a larger number of children with disabilities and children from non-majority ethnic communities in these institutions, are among key

[4] http://finance.gov.mk/files/u3/PFM%20Reform%20%20Programme__EN%20DEC%202017_final%20Vlada.pdf
[5] http://vlada.mk/plan-3-6-9

challenges in the past period. Continuous efforts are being made to expand the number and capacities of institutions responsible for care and education of pre-school aged children. Thus, only in 2016, 34 facilities were opened (13 kindergartens, 13 early childhood development centers, 2 private kindergartens, 6 kindergartens as part of legal entities and private schools).

Currently, there are 65 public institutions for children-kindergartens and 4 public early childhood development centers in the Republic of Macedonia, with a total of 270 facilities distributed in 59 municipalities, as well as 35 private institutions. Thus, pre-school education is realized in a total of 305 buildings, 65 of which are in rural areas and provide pre-school care and education for children from the rural areas as a special target group.

Increasing capacities increases the coverage of children, so in 2016 there is an increased coverage of children aged 0-6 by 8% compared to 2015, while for children aged 3-6 coverage in 2016 equals 42% and is higher by 21% compared to 2015. For comparison, the coverage of children of this age in 2006 was about 10.6%.

In the coming period, intensive activities to further expand the network of institutions for care and education of preschool children continue, primarily by increasing the investments for reconstruction, adaptation and construction of new kindergartens. As a result of these activities, the coverage of children in pre-school education is expected to further increase by 50% in the next four years.

Within the project "Capacity building of pre-school facilities for improving inclusive practices", capacities of pre-school institutions are being developed so as to realise a programme that meets the individual abilities, interests and needs of children with difficulties and provide a high level of support in inclusive environment.

In this direction, the project "Inclusion of Roma children in public pre-school education facilities", which has been implemented for several years in 19 municipalities and has significantly contributed to the promotion of inclusion of children from vulnerable categories in pre-school education, in this case Roma children.

Together with these measures and activities for increasing the coverage of children, measures are also being taken to develop capacities of employees in pre-school institutions through trainings of educators and other professional staff in those institutions, preparation of professional materials for work etc.

b) In September 2017, a three-year **dual vocational education** project was launched, according to the German example. The project will help companies working in the industry to obtain professional staff, having in mind that students will be preparing for work in a particular company during their secondary education.

The Government will pursue to implement the system of dual education in secondary vocational education. Companies will be able to provide scholarships for high school students who will be obliged to work in those companies for a certain period of time after their graduation.

The Ministry of Education and Science (MES) has developed and approved occupational standards, qualifications standards and curricula for vocational education, based on new methodologies harmonized with international standards. The qualification form is in line with the requirements of the Macedonian Qualifications Framework, while the vocational education curriculum is modularly designed and contains learning outcomes.

Within the project "Strengthening lifelong learning through modernization of vocational education and training system and adult education" for reforms of the two-year and three-year vocational education, MES provided **training for professional development of teachers in secondary vocational education** and training related to the provision of new modularized curricula for secondary vocational education. More than 350 teachers in 3-year and 2-year vocational education and training were trained. The focus of the training was on the learner and on the learning-outcomes approach, which will be essential for the effect of the reformed qualifications.

In order to systematically introduce learning through work in vocational education, amendments were made to the legislation that foresees the employer to achieve the practical training goals of the Curriculum, obligation for the student to regularly attend practical training and to fulfill the work obligations determined in the contract, the chambers of commerce (employers) participate in the final examinations in vocational education and training, employers can conduct practical training for students, if they meet the requirements related to equipment, spatial conditions and adequate staff.

VET Strategy has been prepared, as well as bylaws - Standard for Equipment and Spatial Conditions and Standard for Professional and Other Staff for Practical Training / Teaching - Learning through Work with an Employer and Contracts for performing practical training with an employer.

421 mentors in companies, where the students are performing practical classes, have been trained, out of which 400 are certified mentors, 161 teachers in practical training are trained in companies, and a program for vocational and didactic training of the trainers has been prepared by employers where practical training is realized.

Practical classes were realized - learning through work in 229 companies with certified mentors and learning through work at the request of companies.

For systematic data collection, the Register for verification of employers for conducting practical training is created, conducted by the Economic Chamber of Macedonia, as well as the Register of concluded agreements between vocational education and training institutions and employers for the practical training of students.

A separate National Body for systematic implementation of work-based learning has been established. MES adopts Teacher

Training Programs in primary and secondary schools each year, upon proposal of the Bureau for Development of Education.

Since there is no single system or database comprising all labor market information / data from the institutions, employers' organizations, chambers of commerce, local self-government and other stakeholders who produce statistics and labour market research, as a system through which the destinations of graduated students will be monitored, the Republic of Macedonia works on improvement of the situation in this area. Thus, since October 2015 **Skills Observatory** is being developed, which will be used to analyze the adequacy of skills of the secondary education students in relation to the labor market needs, in order to continuously improve the curricula, in compliance with the requirements of employers. The Observatory will also provide information on the employability of certain professions, the expected waiting time and the level of income per education profile, etc., which will, in large part, help future high school students and their parents when deciding to enroll in a certain secondary school.

To improve the **social inclusion** of the most vulnerable groups in society, vocational training in penitentiary institutions has been introduced, which should enable faster re-socialization of convicted persons and their easier inclusion in the labor market. So far, 115 convicted persons have been trained who have acquired the 1st level of professional qualifications and state recognized certificates of professional competence.

In order to increase the opportunity for greater cooperation between employers and secondary vocational schools and trainers verified by MES, for realization of trainings in accordance with the employers needs, in order to increase the economic activity in municipalities, in the 2017 Operational Plan it was envisaged that two pilot programs will be implemented - 5.2. Training for meeting the local needs of skilled workforce and 5.3. Vocational Training Center, where it is expected that in the first phase 80 young unemployed persons up to 29 years of age to be covered, of whom at least 50% are expected to be employed by employers who have declared themselves in need of a qualified and skilled workforce.

In order to increase employment of vulnerable categories, at the same time focusing on higher quality for students with disabilities in the educational process, 106 educational assistants and 34 personal assistants for children in education in 19 municipalities were supported within the program Municipal work. These persons are included in the regular primary and secondary education, and the support model can also be adapted to the children of pre-school age.

For more information, see measures 16, 17 and 18, as well as Table 11.

2. Macroeconomic Framework

2.1. Recent Economic Developments

International Economic Environment. Global economy in the first half of 2017 was featured with greater confidence of economic entities and creation of favourable financing conditions on the international market, which together with the growth of Manufacturing and trade is expected to have positive effects on the global economic growth, projected at 3.6% in 2017. Growth was mainly driven by the intensified economic activity in the fast-growing economies and developing countries, being to a great extent due to the increased trade activity in conditions of disappearance of the export obstacles of these countries.

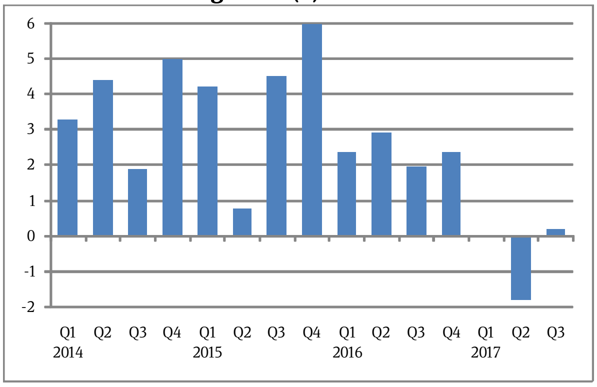
Positive economic trends were also seen in the developed countries, such as strengthened investment activity and solid growth of private consumption, which is expected to contribute to intensified economic growth in 2017, projected at 2.2%. European economy in the first half of the year experienced 2.3% activity growth, whereby economic growth of Germany, the largest economy in the EU, accounted for 2.0%. Main driving forces of the stronger growth of European economy in this period was the intensified activity of Manufacturing and the stronger export of goods in conditions of higher both employment and inflation. However, despite the inflation growth, the core inflation remained low and below the projected level by the European Central Bank, providing for smooth implementation of the accommodative monetary policy to the end of stimulating the domestic demand. Effects of the fiscal policy on the economy throughout the year are expected to remain neutral. Accordingly, growth is expected to remain at the same level of 2.3% by the end of the year, supported by the expected increase of private investments and increase in export in conditions of better utilisation of the production capacities and higher profitability of the corporate sector.

Positive trends in the global economy are expected to continue with higher pace during 2018, in conditions of increased investors' confidence, favourable trends in the global trade and positive developments on the financial markets. Hence, the global economy growth is expected to pick up to 3.7% in 2018. Positive trends are also expected in the European economy, in conditions of expected stronger export amid improved global trade conditions, as well as enhanced domestic demand under favourable financing conditions and reduced uncertainty with respect to the implementation of macroeconomic policies. Such trends are expected to cause for the economic growth in the EU to account for 2.1% in 2018, while the growth in Germany is projected at 1.8%.

Recent economic developments in the Republic of Macedonia.

Gross domestic product. During the first three quarters of 2017, economic activity was strongly influenced by the significant decline of the investment activity of economic entities and capital investments performance. Thus, GDP dropped by 0.4% in real terms in this period.

Chart 2.1. Real GDP growth (%)



Source: State Statistical Office (SSO)

Consumption registered 2.1% growth in real terms, driven by the increase in private consumption by 2.9%, while public spending decreased by 1.4%. Growth of private consumption was observed in conditions of increased household disposable income, increased employment and wages in the economy. Gross investments experienced 5.9% drop, amid significant activity decline in the construction sector, being the main reason for decreased economic activity in this period.

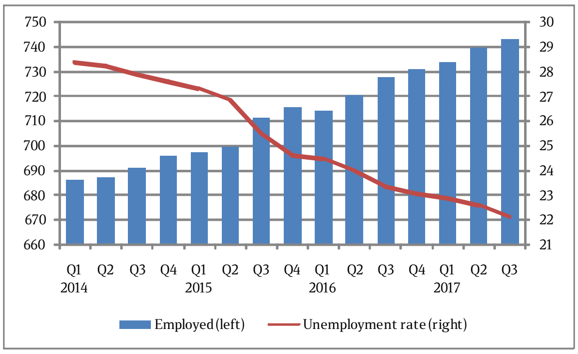
Export of goods and services increased by 8.1% in real terms in the first three quarters of 2017, in conditions of intensified activity of the new production capacities, favourable trends of external demand, i.e. growth of the economic activity in the EU, as well as positive developments on global markets. According to monthly data, growth of export in nominal terms was, above all, a result of the increased export of machinery and transport equipment by 20.8% and chemical products by 15.7%. Import of goods and services increased by 6.7% in real terms, which was mainly a result of the import of intermediary goods, surging by 15.2%. Higher growth of export than import in the first three quarters of 2017 indicates positive contribution of net export to growth.

Analyzed by sectors, construction activity, being the driving force of economic growth over the past year, dropped by 11.5% in real terms in the first three quarters of 2017. Drop was also registered in industrial sector by 3.9%, while agriculture and services sector grew by 4.2% and 1.1%.

Estimates for 2017. Given the drop of real GDP by 0.4% in the first three quarters of 2017, as well as the most recent forecasts pointing out to recovery of the economic activity, as well as the expectations for its additional intensification by the end of the year, real economic growth in 2017 is projected at 1.6%.

Labour market. Positive trends on the labour market continued in 2017. In the period January-September, number of employed persons was higher by 2.5% on annual basis. Higher employment was also seen at the services (being the highest in the trade activity), the industrial sector (being the highest in Manufacturing) and the agriculture, while construction sector experienced reduced employment.

Chart 2.2. Number of employees and unemployment rate



Source: SSO

Employment increase was accompanied by drop of the number of unemployed persons, by which unemployment rate in the first nine months of 2017 decreased to 22.5%, being lower by 1.5 p.p. compared to the same period in 2016.

Average net wage in the period January-September 2017 grew by 2.5% in nominal terms, i.e. by 1.3% in real terms. During this period net wages in the industry and the services sector surged by 2.9% and 2.8%, respectively in average, in nominal terms.

External Sector. The movements in the current account of the balance of payments in the first three quarters of 2017 followed the strengthening of the positive effects of the new production capacities on total exports, with simultaneous positive developments in some of the traditional sectors as well as with the movement of world prices of primary commodities. In the period January-September 2017, the current account registered a low deficit of EUR 61 million, which is by 59% lower compared to the same period of the last year. The narrowing arises mainly from the improvement in the secondary income and the trade balance in goods and services, while the primary income balance widened. Within the secondary income, currency purchased on the currency exchange market was higher by 12.4% compared to the same period last year, mainly reflecting the low base effect i.e. lower net purchase in the second quarter last year, due to the growing political uncertainty and speculative pressures.

Table 2.1. Balance of payments

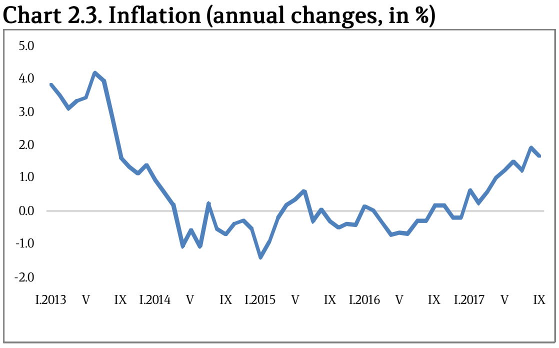
(% of GDP)	2013	2014	2015	2016	I-IX.2017
Current account deficit	-1,6	-0,5	-2	-2,7	-0,6
Goods, net	-22,9	-21,7	-20,1	-18,3	-12,7
Services, net	4,6	4,5	3,8	3,5	3,2
Primary income, net	-2,4	-1,9	-3,2	-3,9	-3,1
Secondary income, net	19	18,6	17,5	16	11,9
Financial account, net	0,8	5,1	-0,1	6,1	-1,5
(without foreign reserves)	2,8	2,3	2,2	3,2	0,5
FDI, net	2	5,6	0,7	4,4	-0,2
Portfolio investments, net					

Source: NBRM, SSO, NBRM forecast for GDP in 2017.

In the first nine months of 2017, inflows in the financial account were registered based on trade credits and FDIs. In the period January-September 2017, net FDIs were EUR 51 million, which is by 73.5% less relative to the same period last year, amid net outflows based on intercompany debt, as well as lower net inflows in shareholders capital (partly due to the prolonged political uncertainty) and reinvested earnings (significant amount of dividend payment in the second and third quarter).

At the end of September 2017, gross foreign reserves were EUR 2,271 million, which is a decrease of 13% compared to the end of 2016, mainly due to transactions for the account of the government (repayment of foreign debt in July, in the absence of external borrowing), price and exchange rate differentials and maturing of foreign currency deposits of banks with the NBRM[6]. Foreign reserves are maintained at an adequate level, providing an average import coverage of about four months in the next year.

Chart 2.3. Inflation (annual changes, in %)



Source: SSO

Inflation. At the beginning of 2017, the average annual inflation went out of the zone of negative annual changes, and in the period January-September 2017 it was 1.1%, with a trend of gradual acceleration. The inflation is influenced by fuel prices, in line with their movements in world markets, as well as higher prices in alcoholic beverages and tobacco, and communications.

The average core inflation, which excludes variable categories (food and energy), is 2.1% per annum (NBRM calculations), taking into account that it also contains the effects of one-off non-

[6] Introduced on a temporary basis during the political instability in the second quarter of 2016.

market price changes (higher excise taxes in tobacco). Thus, the average core inflation, excluding categories of unprocessed food, energy, liquid fuels and lubricants, and tobacco and alcoholic beverages is 1% (SSO calculations).

Monetary Developments and Exchange Rate. In 2017, the monetary policy continued to be focused on preserving price stability by maintaining a stable exchange rate of the denar against the euro. The gradual normalization of the monetary policy, initiated at the end of 2016, continued in the first two months of 2017. Namely, after the increase in the policy rate in May 2016 (from 3.25% to 4%), due to the uncertainty related to the domestic political situation and speculation about the exchange rate and the banking system, there was a gradual stabilization of market expectations, as well as favourable movements in deposits and the currency exchange market, as the most affected segments during the escalation of the crisis in the second quarter last year. This allowed a gradual reduction of the policy rate on three occasions (December, January and February), whereby in February 2017, it was restored to the pre crisis level of 3.25%. As of September, this interest rate remained unchanged amid low inflation, favourable balance of payments position, gradual positive developments in banks' deposits (mainly since mid-year), but also uncertainty, especially in the first half of the year, and need for attentiveness.

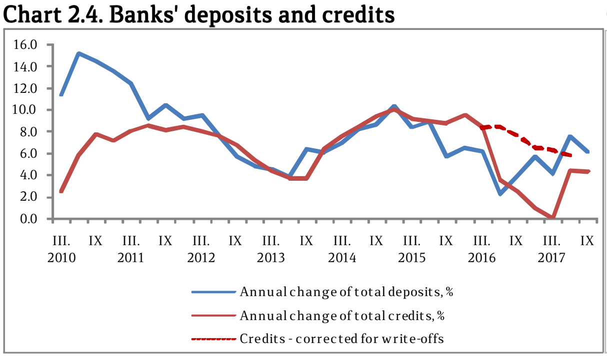
The annual growth of broad money M4 was 6.4% at the end of September 2017 (6.1% at the end of 2016) and accelerated mainly in the second quarter, reflecting the base effect, while the uncertainty and the slower economic activity adversely affected the monetary movements in the remaining quarters. Total private sector deposits that were higher in September by 6% on an annual basis slightly accelerated (growth of 5.7% at the end of 2016). Sector-by-sector analysis shows that this is mainly due to the acceleration in household deposits. Namely, due to the uncertainty about the domestic political situation and the speculations, in the second quarter of 2016, the annual growth of household deposits significantly slowed down, and after the measures taken by the NBRM and easing of the situation, it moderately strengthened in the second half of the year (2.5% in December), with the growth continuing in 2017 and accelerating in the second quarter, in line with the exhaustion of the base effect from last year. In September 2017, the annual growth of household deposits was 5.6%, with identical annual growth in corporate deposits (which increased by 13.4% at the end of 2016). In September, about two-thirds of the annual growth of total deposits resulted from the growth of household deposits.

Analyzing the currency, at the end of September 2017, faster annual growth was registered in denar deposits, including demand deposits (8%), as opposed to the growth in foreign currency deposits (3.3%), contrary to the dynamics at the end of 2016, when the political uncertainty and speculations switched the currency preferences (in December, growth of foreign currency and denar deposits of 8% and 4.1%, respectively). At the end of September 2017, the growth in denar deposits, including demand deposits, constituted over 70% of the annual growth of total deposits. Consequently, despite the moderate increase in the share of deposits with currency component in total deposits in the second quarter of 2016 (42.7%), their share in December 2016 decreased to 41.5%, and in September 2017, remained stable (41.4%), significantly lower than the level at the beginning of the global crisis.

Bank loans to the private sector in the first three quarters of 2017 increased moderately, amid favourable movements from the middle of the year, with uncertainty at the beginning of the year and slower economic activity. At the end of September, total banks' loans to the private sector were higher by 4.3% annually, entirely due to household lending. Compared to the end of 2016, when the credit growth was 6.5% per annum (corrected for the effect of transferring of non-performing loans fully covered by impairment for more than two years to the off-balance sheet records), the annual growth of total loans registered moderate deceleration.

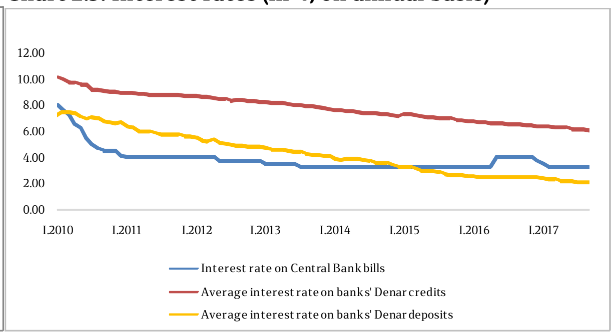
Interest rates in the banking sector registered a moderate decrease. Average weighted interest rates on denar loans and denar deposits were 6.1% and 2.1% p.a. in September 2017, which compared to the end of 2016 is a decrease of 0.3 p.p. and 0.4 p.p., respectively. Given the greater cut in deposit interest rate, the interest rate spread has expanded compared to the end of 2016 by 0.1 p.p., and reached 4 p.p.. In September 2017, average interest rates on foreign currency loans and deposits equaled 4.8% and 0.8%, respectively, which is a decrease of 0.4 p.p. and 0.2 p.p., respectively, since the beginning of the year, thus narrowing the interest rate spread by 0.1 p.p., to 4 p.p.. Interest rate differential between denar and foreign currency deposit interest rate narrowed by 0.2 p.p. compared to December 2016, and in September it equaled 1.3 p.p..

Chart 2.4. Banks' deposits and credits



Source: NBRM

Chart 2.5. Interest rates (in %, on annual basis)

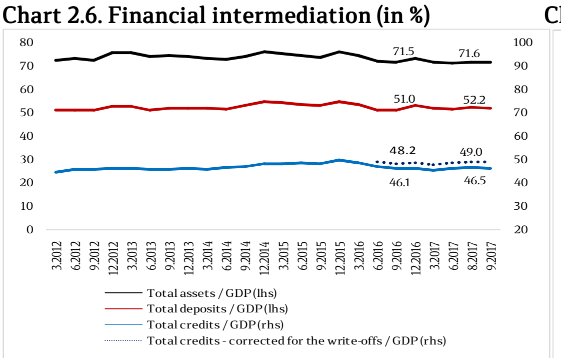


Source: NBRM

Banking System. Banks are the dominant institutional segment making up about 85% of the total assets of the financial system at the end of 2016. Fifteen banks operate in the Republic of Macedonia, of which eleven are predominantly owned by foreign shareholders, and six are subsidiaries of foreign banks. Foreign capital prevails (mainly from the EU countries), with share of about three-quarters of the total equity capital of the banking system.

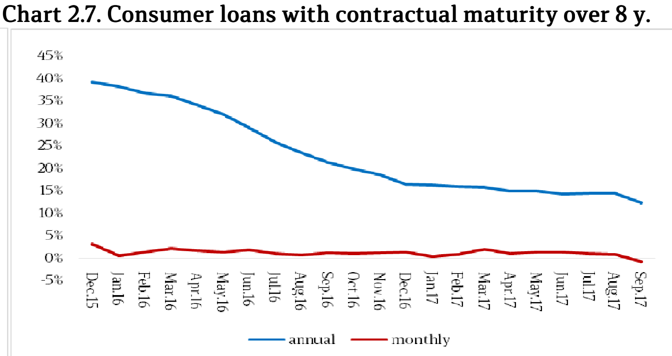
In the first three quarters of 2017, despite the domestic challenges, the banking system remained stable. At the end of September, the bank assets registered an annual growth of 4%. At the end of September 2017, bank assets to GDP ratio was 71.5%, which is unchanged on an annual basis. Considering the moderate acceleration of deposits, their share in GDP was 51.9%, with moderate annual growth. Analyzing credit market, there was a moderate increase in the total credits to GDP of 0.7 p.p. compared to the third quarter of 2016 (corrected for the write-offs).

Chart 2.6. Financial intermediation (in %)



Source: NBRM, SSO.

Chart 2.7. Consumer loans with contractual maturity over 8 y.



Source: NBRM

The NBRM Lending Survey for the first three quarters of 2017 indicates continued net easing of standards for approving corporate loans in terms of interest rate, non-interest income, with insignificant changes in the loan size requirements, collateral requirements and loan maturity. Also, there is continued net easing of standards for approving households loans, mainly in terms of interest rate and non-interest expenses for housing and consumer loans. With these changes, banks continue to facilitate private sector access to finance[7]. Banks have assessed the demand for

[7] WEF Global Competitiveness Report, 2016, ranks Macedonia at the 45th place by access to finance (up by 51 position compared to 2011).

loans by the corporate and household sector in the first three quarters of 2017 (same as in 2016) as moderate, probably reflecting the effect of the uncertainty about the political situation.

Credit risk. The effects of the amendment to the National Bank credit risk regulation (transfer of non-performing loans that are fully covered by impairment for more than two years to the off-balance sheet records) have been exhausted, namely, after the shock from the write-offs in May and June 2016, the subsequent monthly volume of write-offs has decreased. At the end of September 2017, non-performing to total loans ratio was 6.6%[8], which is by 0.8 p.p. lower compared to September 2016. Roughly 80% of the non-performing loans are corporate loans. The high coverage of non-performing loans with impairment, amid satisfactory volume and quality of the banks' own funds contributes to solid resilience of the banking system to contingent loan losses. In order to further reduce non-performing loans, the National Bank developed a draft-strategy, including draft measures and activities for improving non-performing loan management, including their sale, whose adoption and implementation require coordinated interinstitutional cooperation in the country.

Macro-prudential measure for slowing down the rapid growth of consumer loans with maturity equal to or longer than 8 years (a larger capital requirement was introduced on 1 January 2016) yielded results, because since its introduction, these loans have grown more moderately.

Corporate and household debt increased in 2016[9]. In 2016, the total debt of the domestic corporate sector registered an annual growth of 9.2% and reached 66.2% of GDP. As in recent years, the external debt component has been the generator of the corporate debt growth, which has determined over 88% of the annual growth of total debt, at the expense of the lower borrowing from domestic banks. Intercompany loans and trade credits dominate the debt to non-residents (as more stable and less risky flows), whose growth determined the overall growth of the external debt of the corporate sector in 2016. Domestic banks dominate in the domestic institutional funding of the corporate sector, whereas non-banking financial institutions have insignificant share. In 2016, amid favorable movements in the labor market and wages, household debt continued to grow moderately, reaching 23% of GDP (in 2015: 22.4%). Banks are the most significant lender to households, accounting for 93.9% of the debt.

Profitability and efficiency of the banking system were solid, although the earnings in the first nine months of 2017 were by 6.8% lower compared to the same period last year. Such a change in the earnings is due to the slower decrease in interest expenses, as well as the fall in interest income. Rates of return on assets and equity equaled 1.4% and 12.7%, respectively.

Table 2.2. Basic bank risks indicators (in %)

	2014 Q4	2015 Q4	2016 Q4	2017 Q3
Capital adequacy				
Capital adequacy ratio	15,7	15,5	15,2	16,2
Asset quality				
NPLs / gross loans (non-financial entities)	11,3	10,8	6,6	6,6
Total provisions to Non-Performing Loans (non-financial entities)	104,7	108,4	114,9	112,0
Profitability				
ROAA	0,8	1,1	1,5	1,4
ROAE	7,4	10,4	13,6	12,6
Operational costs / total income	55,5	51,6	49,8	50,0
Liquidity				
Liquid assets/total assets	33,2	31,4	30,9	29,5
Liquid assets to total short-term liabilities	59,2	54,9	53,5	51,7
Sensitivity to market risk				
Net foreign exchange position / owned funds	17,5	11,1	14,5	7,3

Source: NBRM.

[8] When controlled for the effect of write-offs, the share of non-performing loans in September 2017 was 11.5%.
[9] Source: Financial Stability Report for the Republic of Macedonia in 2016, latest available data.

The ***solvency*** of the banking system is high. Solvency and capitalization ratios of the banking system improved in the third quarter of 2017 due to the growth of capital positions (new subordinated instruments, while one bank transformed a hybrid instrument into shares). Capital adequacy ratio increased in the third quarter of 2017 to 16.2%, whereas the Tier 1 capital rate reached 14.6%. The new amendments to the Banking Law, adopted in October 2016, which started to apply from March 2017, are aimed at complying the domestic regulation with the international capital standard Basel 3, by introducing the new rules of the Basel Committee and the European regulations on the so-called capital buffers, whose fulfillment will further support the bank solvency[10].

Liquidity of the banking system continued to be maintained at satisfactory level. At the end of the third quarter of 2017, banks' liquid assets accounted for 29.5% of total banks' assets and covered 51.7% of total short-term liabilities and 55.8% of total household deposits, which is satisfactory and ensures smooth operations of the banks.

The regular quarterly sensitivity tests confirm the banking system resilience to the simulated shocks. The results of the stress tests that simulate a percentage increase of non-performing credit exposure moderately improved in the third quarter of 2017, compared to the previous quarter, due to the higher capital adequacy of the banking system prior to the simulation, as well as the lower sensitivity of some banks to the assumed shocks. Hypothetical shocks on the part of the credit risk made the greatest impact on the stability of the banking system. Simulations show that only in extreme growth of non-performing loan exposure to non-financial companies (of 181.6%) i.e. migration of 15% of the regular to non-performing credit exposure, the capital adequacy of the banking system would drop to 8%.

A regular macro stress test is also conducted on an annual basis, which for 2016 was based on two scenarios: the first suggests deterioration for one standard deviation of the basic macroeconomic variables from the official forecasts of the National Bank for 2017 and 2018, whereas the second is a historic scenario, which suggests that the trend of macroeconomic variables in 2001 and 2002 (at the peak of the security and political instability of the country) will also be mirrored in 2017 and 2018. Results suggest a satisfactory resilience of the total banking system.

2.2. Medium-Term Macroeconomic Scenario

Macroeconomic policy of the Republic of Macedonia is aimed at developing the economy and raising the living standard of citizens, by supporting domestic enterprises, above all SMEs, increasing employment through the active employment measures, increasing the level of wages, as well as by strengthening the social protection system.

Gross Domestic Product. In 2018, economy is expected to recover from the negative effects of the political uncertainty in the country during 2017, i.e. intensification of economic growth is expected. Political stability and restoring the confidence of investors are expected to contribute to growth of private investments. Increase of wages and employment in the private sector, supported by government measures, coupled with the expectations for low and stable inflation in the country will contribute to increased private consumption. Continuous solid export from the new production capacities, as well as the recovery of traditional export sectors as a result of the strengthened economic activity of the countries' trading partners, will contribute to boosted export of Macedonia and better utilisation of industrial capacities.

[10] For systemically important banks, these changes are introduced gradually (in stages) and should be fully implemented by March 2018.

Hence, real GDP growth is expected to increase to 3.2% in 2018, and to continue with somewhat higher pace in the next two years, i.e. to reach 3.5% in 2019 and 4% in 2020. The table below shows the real GDP growth projections of relevant international and domestic institutions.

Table 2.3. Comparison of GDP growth and inflation projections for Macedonia

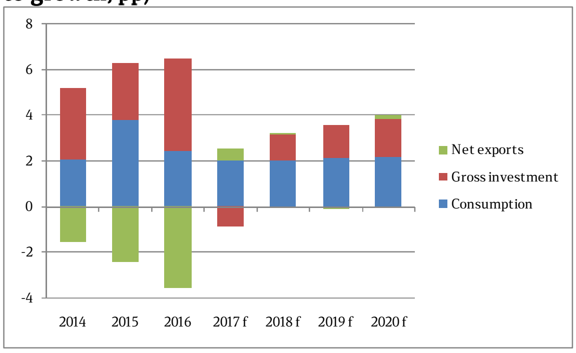
Institution	Real GDP growth (%)				Inflation rate (%)			
	2017	2018	2019	2020	2017	2018	2019	2020
IMF	1,9	3,2	3,4	3,6	1,2	1,7	1,9	2,0
World bank	1,5	3,2	3,9	/	0,9	1,6	2,0	/
European Commission	1,7	2,7	3,2	/	1,2	2,0	2,4	/
EBRD	1,5	2,5	/	/	/	/	/	/
Vienna Institute	1,8	3,1	3,4	/	1,0	1,5	2,0	/
NBRM	0,5	3,2	3,5	/	1,3	2,0	2,0	/
Ministry of Finance	1,6	3,2	3,5	4,0	1,4	1,7	2,0	2,0

Source: IMF (Article IV Consultation, October 2017), World Bank (Southeast Europe Regular Economic Report, November 2017), European Commission (European Economic Forecast, November 2017), EBRD (Regional Economic Prospects, November 2017), Vienna Institute (Forecast Report, November 2017) and NBRM (Quarterly Report, November 2017).

Private consumption is envisaged to be significant driving force of economic growth in this medium-term period, which is expected to experience 3% growth in real terms (see Chart 2.8 showing the contribution of the separate components to the GDP growth). Growth of private consumption is related to the expected increase of employment in the private sector, the gradual increase of the minimum wage, which will reflect on the growth of the average wage in the country, as well as the measures for strengthening the social protection, which will result in increase of the household disposable income. Private consumption is also expected to be supported by the envisaged growth of crediting to households. Growth of public consumption is projected at 1.3% in real terms in average in this period.

Growth of gross investments in the period 2018 - 2020 is projected at 4.4% in real terms in average. Planned investments by the public sectors, as well as the support of the investment activity of domestic and foreign enterprises are expected to have positive contribution on investment growth. Restoration of the political stability in the country will have positive effects on the expectations and the confidence of economic entities, which also mean a positive signal for the existing and the potential foreign investors. Chart 2.8. shows the contribution of gross investments to the economic growth.

Chart 2.8. GDP by expenditure method (contribution to growth, pp)



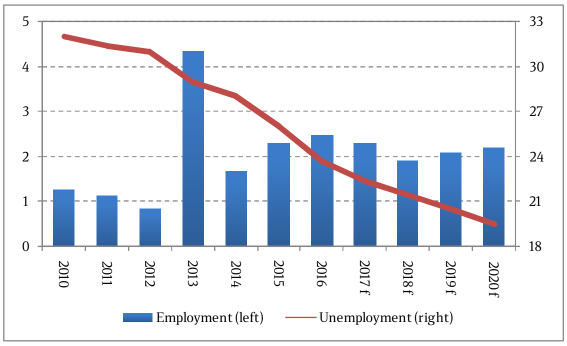
Source: MoF calculations based on SSO data, f – forecast

In the next medium-term period, export of goods and services is expected to experience 8.0% real growth in average, with prospects for certain growth intensification, in conditions of solid activity of the export-oriented capacities, as well as expected increase of foreign demand, particularly for higher value added goods the share of which in the domestic industry structure, increases. Favourable effects on export are also expected from the envisaged increase of prices of metals in the medium term. Projected growth of domestic demand and export activity provides for growth of import of goods and services which, in this period, is expected to experience 6.4% real growth in average.

Labour Market. Envisaged growth of economic activity in the next medium-term period is expected to be accompanied by increase of employment, encouraged by the active employment measures and programmes, the support of domestic and foreign enterprises for job creation, as well as other measures aimed at reducing unemployment.

According to the projections, number of employed persons is expected to experience average annual growth of around 2.0% in the period 2018-2020. Increase of labour demand in this period is expected to also reflect on the labour supply, projected to increase by 0.8% in average. Such trends on the labour market will provide for the average unemployment rate to drop to 19.5% in 2020. Average increase of net wage in this period is expected to range between 4.0% and 4.5% in nominal terms.

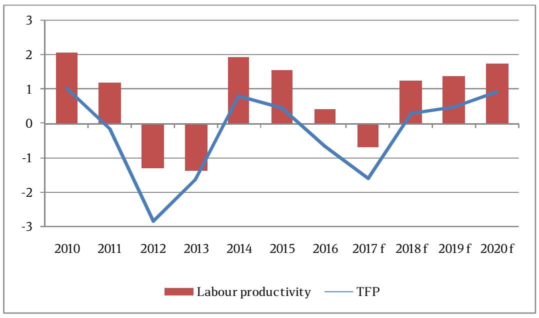
Chart 2.9. Employment growth (%) and unemployment rate



Sources of Growth. Total Factor Productivity (TFP)[11] is envisaged to have negative contribution to the economic growth in 2017, in conditions of expected decrease of investments in fixed assets and strong growth in the number of employed persons. Chart 2.10. shows the growth of both labour productivity and TFP in the period 2010-2020. In the period 2018 – 2020, growth of productivity of production factors is expected to shift to the positive zone. However, TFP contribution to growth in this period is relatively low and accounts for almost 16% in average. Labour is expected to contribute to economic growth with around 37%. Physical capital, according to the projections on investment growth, is expected to grow by 4.6% in average in the analysed period, contributing with almost 47% to total economic growth.

Potential Growth. Calculation of potential output is a basis for estimating the cyclical position of economy. Two methods are used to calculate the potential output. According to the first method, Hodrick-Prescott (HP) filter, which belongs to the statistical approaches group (a-theorethical) and is based only on historical data on GDP[12], potential GDP growth is estimated at 3.2%. According to the Production Function Approach (PFA), applied by the European Commission[13], potential GDP growth is estimated at 3.1% in the analysed period. Results from the calculation of potential output are presented in the charts below, as well as in Table 5 in Annex 3.

Chart 2.10. Labour productivity and TFP (growth rates)



Source: SSO and calculations of MoF, f - forecast

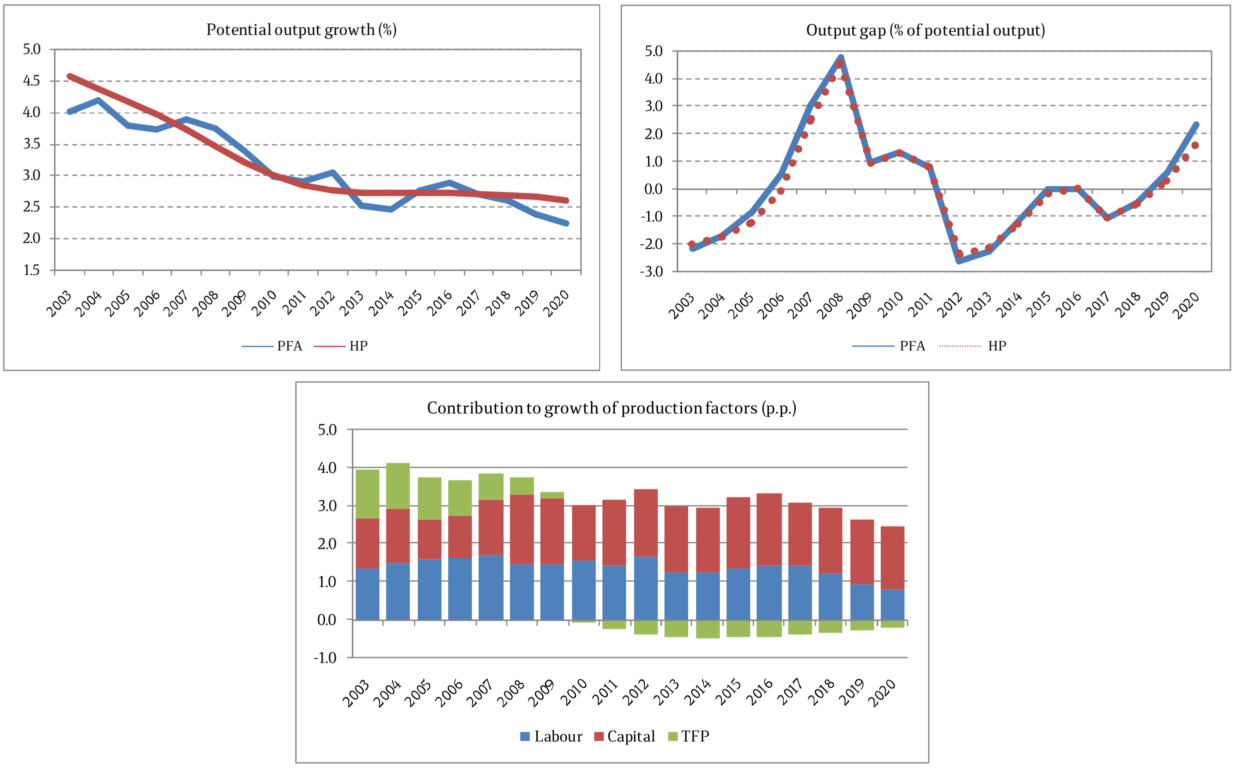
According to the projections on production growth in the coming medium-term period and the estimations on the trends of the potential output, cyclical component of output is in the negative zone in 2017. In 2018, output gap remains negative according to the both methods applied, however narrowed compared to 2017. In 2019, output gap is expected to shift to the positive zone and to remain positive in 2020, whereby calculations based on the Production Function Approach suggest a higher gap compared to the Hodrick-Prescott filter.

[11] TFP is residual of growth of other factors to economic growth, labour and capital. As regards the calculation of physical capital, the so-called perpetual inventory method has been applied (see Berlemann and Wesselhöft, *Estimating Aggregate Capital Stocks Using the Perpetual Inventory Method*, 2014), by applying 4% depreciation rate to the accumulated capital. Average value of the share of income from capital is estimated at 36%, while the remainder of the income is from labour.

[12] Trend value is assessed by minimising the gap between the real production and the trend and the variability thereof for the whole sample.

[13] Based on the study of Havik et al, *The Production Function Methodology for Calculating Potential Growth Rates & Output Gaps*, 2014.

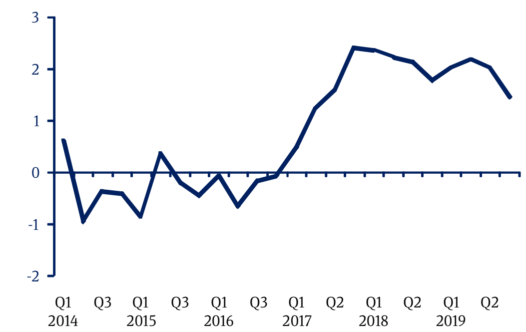
Chart 2.11. Potential output



Source: MF calculations

Inflation. Global and domestic factors of inflation in the medium term point to a moderate acceleration of inflation, after its low level in 2016, in line with the general downward trend of global prices of primary commodities. Foreign effective inflation[14] for 2017 is estimated at 1.8% (which is higher compared to last year's scenario of 1.3%). In 2018, foreign inflation is expected to decelerate moderately to 1.4%, and to accelerate to 1.7% in 2019.

Chart. 2.12. Inflation forecast (in %, annually)



Source: SSO, NBRM October forecast for the period

In the last quarter of 2017, the average annual inflation rate in the Macedonian economy is expected to remain low. Consequently, the average inflation rate in 2017 is expected to be around 1.3%. Analyzing the components, the higher average price level compared to the previous year is a reflection of the upward changes in energy prices (in line with the increased world fuel prices) despite the downward pressures last year, the almost neutral effect of food prices versus downward changes last year, as well as the higher core inflation (which in one part was driven by one-time non-market factors). Compared to last year's scenario, inflation expectations for 2017 in this scenario are unchanged.

In 2018, the inflation is expected to gradually increase by about 2%. The increase in consumer prices is expected to come largely from the intensification of food inflation, in line with the

[14] The calculation of effective foreign inflation is derived from a weighted sum of the consumer price indices of nine countries - major exporters of products for personal consumption in the Republic of Macedonia. Weighted structure is based on normalized shares of nominal imports from each country in the total nominal imports in the period 2010-2012.

forecast growth in world prices of some primary food commodities. Also, the core inflation will make positive contribution, amid improved domestic demand. On the other hand, energy inflation is expected to be negative and thus have a downward effect on total inflation, in line with the expectations for stabilizing the oil price on the world stock markets, after its significant growth in 2017. In the next two years, the rate of inflation is expected to stabilize to the historical average of around 2%. Risks to the forecast inflation trajectory are mainly attributable to the uncertainty about the movements in the prices of global primary commodities, especially in the context of geopolitical tensions and their potential effect on the global supply.

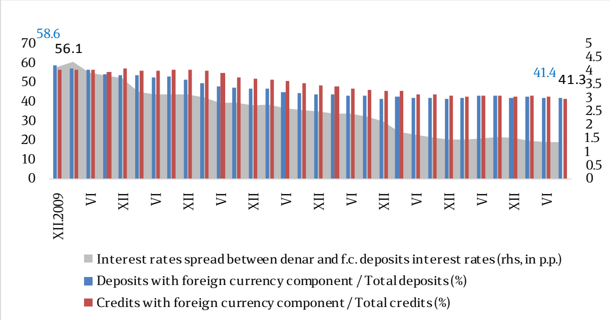
Monetary and exchange rate policies. Monetary policy is oriented towards preserving price stability by maintaining a stable exchange rate of the denar against the euro. After the increase in the policy rate in May 2016 (from 3.25% to 4%) due to the uncertainty about the domestic political situation and speculation about the exchange rate and the banking system, there was a gradual stabilization, which allowed normalization of the monetary policy with a gradual reduction of the policy rate on three occasions (December, January and February), whereby in February 2017, it was restored to the pre-crisis level of 3.25%. In the course of the year, the policy rate remained unchanged, amid low inflation (as expected), solid external position and stable foreign exchange market developments, positive movements in the banks' deposits (mainly since mid-year), but also uncertainty in the first half and need for attentiveness.

With respect to the set of instruments, in the peak of the political crisis in the second quarter of 2016, auctions of banks' foreign currency deposits with the NBRM were reactivated (at slightly more favourable interest rates compared to the current negative interest rates on the international markets), which increased the attractiveness for the banks and, consequently, boost foreign reserves. After the stabilization, at the end of October 2016, the foreign currency deposits auctions were terminated, and the placed deposits were gradually released according to their maturity, and by the end of August 2017, they became fully due.

The National Bank conducts ongoing monitoring of the movements in the currency structure of deposits and loans, as well as in the interest differential for instruments in domestic and foreign currency. In this regard, multiple changes have been made in reserve requirement rates in recent years, generally aimed towards cutting reserve requirement rates on denar liabilities (in a longer run). Potentially, the cost reductions would accordingly affect the interest rate differential in favor of denar deposits. Political instability and speculative attacks in the period April-May 2016 were assessed to have limited adverse effects on the currency structure of deposits (small increase in the share of deposits with foreign currency component of 1.5 p.p. in the second quarter of 2016 and thereafter their restoration to the pre crisis level), although the trend of denarization ceased. These impacts were limited by the set of measures that acted towards stabilizing household expectations, fueled by gradual, partial reconciliation of the political situation. The last increase in reserve requirement of deposits with FX clause in May 2016 was aimed at maintaining favorable trends in the deeuroization in recent years, which has in turn, increased credibility of monetary policy based on stability of the exchange rate of the denar against the euro. Additionally, in the course of 2017, a draft deeuroization strategy was developed including draft measures for a comprehensive treatment of this issue.

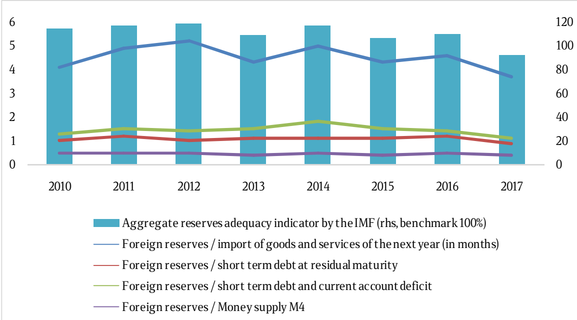
The measure that released banks from reserve requirements on loans to export and energy sector, which has been in effect since early 2013 and supported credit growth, has continued in 2017. Due to the positive effects on the bank lending, at the end of 2015, this non-standard measure was extended to the end of 2017, when considering moderate slowdown in lending, it was extended once again, by the end of 2019. In the previous five years, from sectoral viewpoint, the credits to net-exporters were dominant, while credits to the energy producers intensified since second half of 2016. Besides support to the credit growth, the favorable impacts of this measure for the clients are also related to the other aspects of lending to these sectors, including the banks' active approach towards increasing the credit support to these sectors, credit accessibility for larger number of companies, as well as easing in some of the credit conditions.

Chart 2.13. Currency structure of banks' deposits and credits and interest rate spread



Source: NBRM.

Chart 2.14. Foreign reserves adequacy indicators



Source: NBRM calculations, estimation for 2017.

In the next three years, the monetary policy will remain oriented towards preserving price stability by maintaining a stable exchange rate of the denar against the euro. The results of the evaluation models of equilibrium denar real effective exchange rate[15] as of the last quarter of 2016, did not indicate major deviations from the equilibrium, and were maintained within acceptable limits of +/- 3% in the period 2003-2016, and suggested moderate exchange rate undervaluation during 2016[16]. Regarding the conduct of monetary policy, it is important to mention the results of the monetary transmission models that, with the latest update as of 2016, indicate continuous improvement in the interest rate transmission channel from the policy rate to banks' interest rates (improvement in the transmission on lending and deposit interest rates amid higher transmission effect on deposit rates).

In the recent period of turbulent external environment, the monetary policy has confirmed its flexibility and appropriately adjusted its monetary instruments in order to encourage credit growth, strengthen the denar deposit base in a long run, while achieving its primary and intermediary monetary goal. In this context, the monetary policy provided sufficient incentive and revived the credit growth, and some of the measures, particularly those related to the currency structure and savings maturity, are expected to produce effects in the next period. In 2016, the monetary policy showed readiness to properly deal with the aftermath of the domestic political shock whose effects were short-lived. In 2017, the inflation remained low, under the dominant influence of global factors on the supply side and moderate growth in core inflation. Foreign exchange reserves have been maintained at an adequate level, as measured by different indicators, indicating readiness for absorption of any shock. According to the projections of the other segments of the economy, in the next three years, we can expect moderate inflation movements and generally favourable movements in the foreign exchange market, although accompanied by risks. Fiscal policy, and in particular the way of financing the budget deficit and the implementation of the announced fiscal consolidation in the period ahead, remains a significant factor for the environment for conducting monetary policy, which also emphasizes the importance of monetary and fiscal coordination. External sector developments, import structure and effects on the foreign exchange market and foreign reserves, will be crucial for the monetary setup in future. In addition, there will be regular monitoring of the pace and structure of credit growth in terms of consumer lending vis-a-vis investment lending, and of the movement

[15] According to the BEER (behavioral equilibrium exchange rate) approach for assessment of the equilibrium denar exchange rate, which is based on a narrower definition of the real effective exchange rate and is designed on the basis of the five major trading partners of the Republic of Macedonia from the European Union. Models (set by different specification and evaluated by various techniques), include differential in productivity, trade openness, public consumption and total net foreign assets, as independent variables.

[16] IMF's analyses also indicate no significant deviation in the real exchange rate (IMF Staff Report 2017 Article IV Consultation, November 2017, p.38).

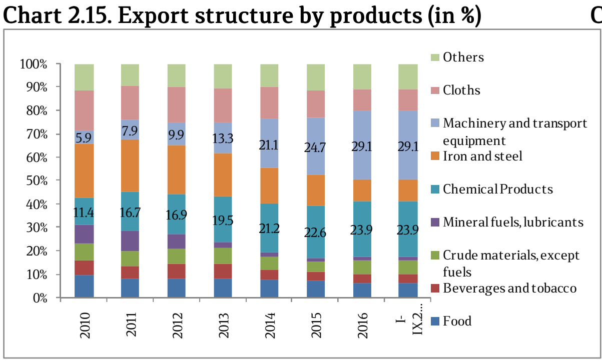
of deposits and interest rate spreads. Monetary authorities remain ready to take appropriate measures, if necessary, to maintain price stability in the economy.

A significant slowdown in the banks' deposit growth has been estimated for 2017 amid still incompletely stabilized expectations in the context of political upheavals in the country, with deposit growth estimated at 3.6% per annum (about 7% in the last year's scenario), with a high comparing basis at the end-year. However, by stabilizing the expectations of the economic agents, the growth of the economic activity, as well as the expected inflows through the balance of payments, over the next two years, it is assumed that the potential and the propensity for saving in the banks will increase, and hence the growth of deposit base will accelerate (growth of about 6.0% in 2018 and 2019).

In conditions of slower growth of the main source of financing the credit activity and prolonged uncertainty, in 2017, there has been a moderate slowdown in the credit growth, with expected credit growth by the end of the year of 4.6% (about 6% in the last year's scenario). The credit activity of the banking sector in the next three-year period is expected to be an important factor supporting the growth of private consumption and investments. In the period 2018-2019, the growth of credit activity is expected to accelerate to around 7%, reflecting the increased credit supply and the increased readiness of the private sector for additional borrowing. Thus, amid solid solvency and liquidity of the banks, with a more stable environment and sufficiently available sources of financing, banks are expected to provide greater credit support for both the households and the corporate sector. The growth in disposable income and favorable expectations is estimated to further support the credit demand and the creditworthiness of economic agents. The measures undertaken by the NBRM are still expected to produce favorable effects on the savings and credit activity.

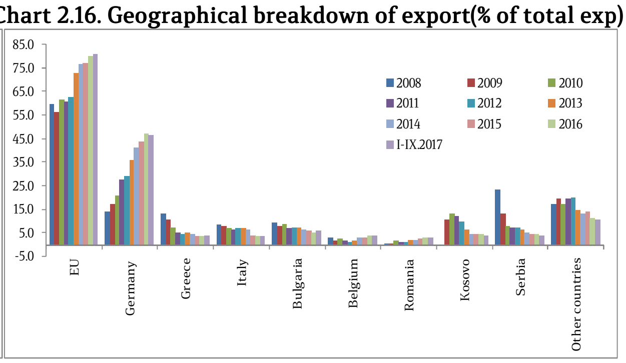
External Sector and Sustainability in the Medium Term. Movements in the current account of the balance of payments of the Republic of Macedonia have still reflected the structural changes in the economy in recent years, thus strengthening the export sector and improving the current account balance. The current account deficit in the last seven years (2010-2016) averaged 2% of GDP (compared to the previous seven-year average of about 6%). According to the trends and estimates for the last quarter of 2017, the current account deficit for 2017 is estimated at 2% of GDP, which is slightly narrower compared to the previous year (2.7% of GDP). The estimated deficit for 2017 is as expected in last year's macroeconomic scenario presented in the last year's ERP. Stable current account performance points to strengthened economic fundamentals and greater external sector resilience to shocks (domestic and external).

Chart 2.15. Export structure by products (in %)



Source: SSO.

Chart 2.16. Geographical breakdown of export(% of total exp)



Source: SSO.

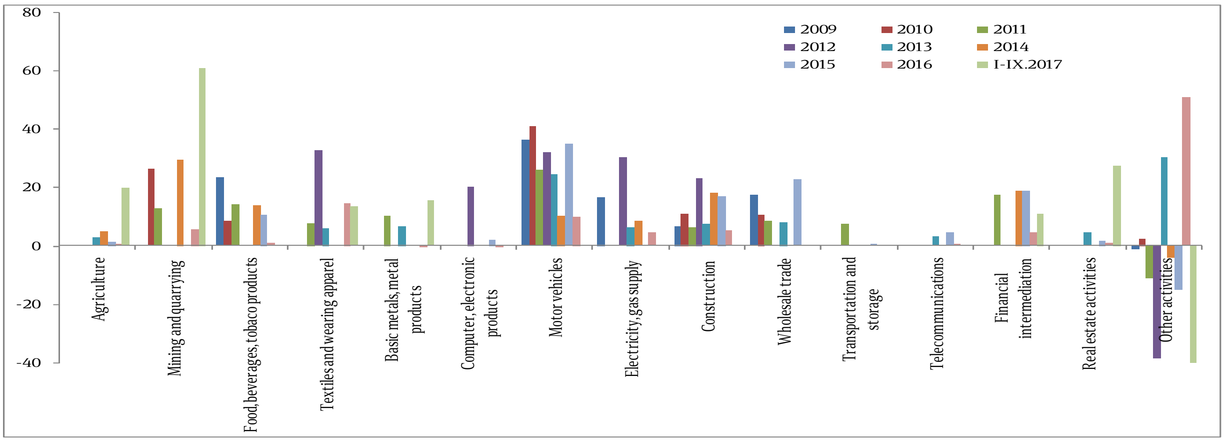
In the period January-September 2017, the total trade deficit[17] registered a slight widening of 1.2%, amid faster annual export growth of 15.1%, compared to import growth of 11.2% (although higher

[17] According to the foreign trade statistics, where the import is presented on c.i.f. basis.

absolute growth of import). The increase in exports is mainly due to higher export of machinery and transport equipment, and chemicals, which mainly reflects the effect of the new production facilities in the technological industrial development zones. Moreover, positive contribution was also made by some traditional sectors (iron and steel, ores, tobacco). The increase in imports was mainly due to the higher import of raw materials, equipment and energy (amid unfavorable price effect in energy). The highest trade deficit in goods in the period under observation was registered with Great Britain, and the highest surplus was registered in the trade with Germany.

Analyzing the structure, as a result of the new capacities in the economy, the export structure significantly improved. It is due to the gradual increase in the share of products with higher added value in exports, mainly chemicals, and machinery and transport equipment, which reached 53% at the end of September 2017. Changes in export structure correspond with foreign direct investment, which in the recent years, were mainly concentrated in these sectors. In the period 2009-2016, on average, about 60% of the new foreign capital was invested in the tradable sector, where one can expect its further contribution to export diversification. On the other hand, there is a decrease in the share of traditional export products - iron and steel, and textile products (with smaller reduction in textiles versus more distinctive decline in iron and steel), with their share from the dominant 40% in 2010 declined to about 18.5% at the end of September 2017, which confirms the export diversification and modernization of the export structure[18]. It should be considered that the unfavorable trends in export of iron and steel in recent years have been influenced by the unfavorable movements in the international market of metals and the fall in their prices, while in 2017, in line with the favorable price movements in the world market and the global recovery, their share in total exports has stabilized.

Chart 2.17. FDI, net, by activity (% of the total)



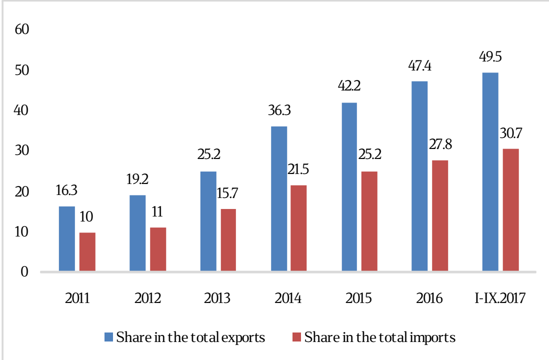
Source: NBRM.

Trade activity of new companies in foreign ownership has been intensifying. The share of exports of these companies in total exports of goods in the economy has grown steadily, reaching nearly 50% of total exports in the first nine months of 2017. Given that these companies import raw materials and equipment, the share of imports of these facilities in total import of goods also continued growing, but at a slower pace (nearly 31% share in the total imports in first nine months of 2017).[19] The new foreign-owned companies noted a positive net balance in the foreign trade, which averaged 0.5% of GDP in the period 2011-2013, while in the next three years, it intensified and reached about 3% of GDP.

[18] Exports of mineral fuels and lubricants have reduced their share in total exports in recent years, which mainly reflect the switch in the business orientation of the oil refinery (that had an effect on both sides of the trade).

[19] Source: NBRM. According to the foreign trade statistics (customs declarations), where export of goods is presented on f.o.b. basis, while imports of goods is on c.i.f. basis.

Chart. 2.18. Exports and imports of the new companies with foreign capital (% of the total)



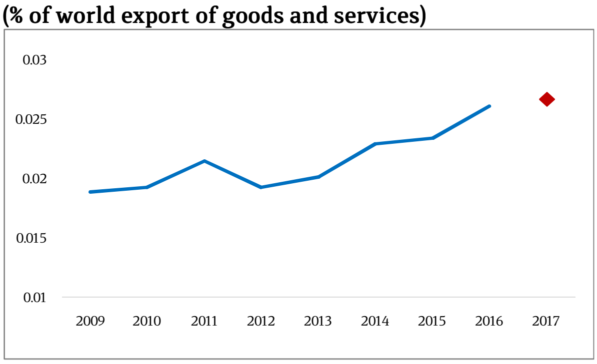
Source: NBRM and SSO.

Besides the direct effects on exports and employment, FDIs in the tradable sector have multiple positive effects on the economy. It mainly implies possibilities of transfer of new technologies, modernization of production, and increased demand for raw materials from local companies that improves the quality of local suppliers[20] (particularly by forcing implementation of standards in their businesses). This gradually increases the second-round effects of FDIs on the economy.

The analysis of geographic distribution of Macedonian exports confirms the dominance of the EU as a major export destination, which in the period January-September 2017 imported around 81% of the Macedonian exports, which is a significant increase compared to 2008 when nearly 60% of the Macedonian exports was oriented towards the EU. Analyzing the EU, in the last years, the share of exports to Germany has seen a significant growth, with positive trends in the exports to Belgium and Romania (as well as Spain), amid low initial shares, and an ongoing decrease in the share of exports to Greece, Italy and Bulgaria. Total trade between Macedonia and the EU in the period January-September 2017 constitutes about 70% of the total trade of the Republic of Macedonia, and given the faster growth of exports than imports, the deficit with the EU significantly narrowed, by around 57% annually.

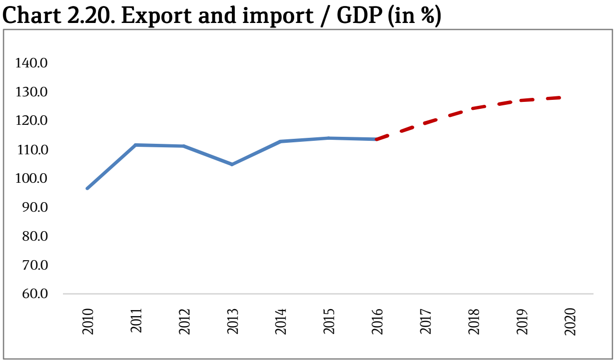
In the period January-September 2017, the real effective exchange rate (REER)[21] of the denar deflated by CPI registered an annual depreciation of 1.1%, while when excluding primary commodities, the denar REER deflated by the same price index registered a minor appreciation (0.1%) compared to the same period last year. Such movements in the two indices reflected the favorable effect of the relative prices and the moderate appreciation of the nominal effective exchange rate of the denar against the currencies of some of the trading partner countries. Nominal unit labor cost registered a growth of 6.5% in the first three quarters of 2017, which amid moderate wage growth, reflects the productivity fall (amid employment growth and fall in economic activity).

Chart 2.19. Export market share
(% of world export of goods and services)



Source: IMF and NBRM, forecast for 2017.

Chart 2.20. Export and import / GDP (in %)



Source: SSO, NBRM forecast for the period 2017-2020.

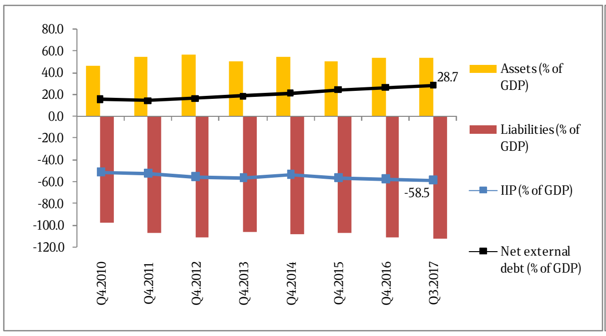
The export market share of the economy in the world exports increased in 2016 as a continuation of the growth in the previous period, from 2013 onwards. In 2017, the export market share in the

[20] The WEF Global Competitiveness Report 2016 ranks Macedonia at the 89th position by FDI and technology transfer (up by 24 positions compared to 2011) and at 47th position by quality of local suppliers (up by 44 positions compared to 2011).
[21] Within the REER, the calculation of the nominal effective exchange rate and relative prices includes 15 major trade partners of the Republic of Macedonia by their share in foreign trade in the period 2010-2012 and the base period 2010.

world export of goods and services is expected to continue moderately accelerating, given the larger acceleration of the Macedonian export of goods and services compared to the growth of the world export of goods and services. The level of trade openness of the Macedonian economy is generally high, and in the period 2014-2016 it was maintained at a relatively stable level of around 110%, and starting from 2017, over the next three years, it is expected to register gradual moderate increase to about 120%. More detailed analysis of external and internal sustainability indicators is presented in Annex 1.

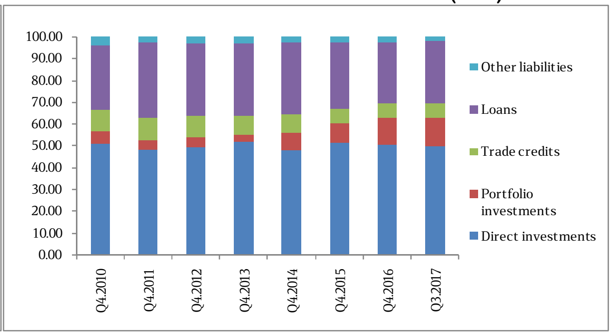
International investment position and external debt. At the end of the third quarter of 2017, the negative international investment position (IIP) increased by 7.1% compared to the end of 2016, amid higher increase in external liabilities compared to the increase of assets. The negative IIP expanded given the lower positive IIP of the monetary authority (reflecting the fall in foreign reserves), and the increased negative net position of the "other sectors" and government[22], while the negative net position of depository institutions reduced. The negative IIP in September was 58.5% of estimated GDP and compared to the end of 2016, it is higher by 1.2 p.p. of GDP.

Chart 2.21. IIP and net external debt



Source: NBRM and SSO.

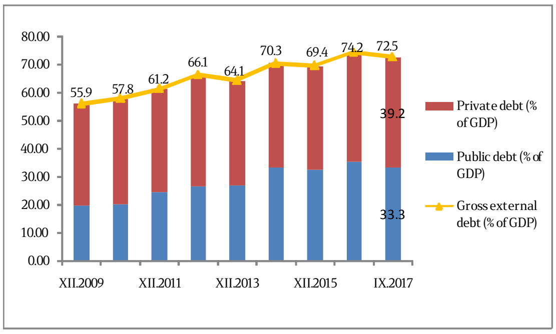
Chart 2.22. Structure of liabilities to abroad (in %)



Source: NBRM.

Given the significant share of foreign direct investment as external liabilities (about 50% in recent years), typical for the converging countries, the analysis of external position also needs to consider other variables, such as net external debt, which includes only net debt instruments. At the end of the third quarter of 2017, the net external debt of the Republic of Macedonia was 28.8% of GDP, or by 1.8 p.p. of GDP more compared to the end of 2016 (amid increased net debt of the public sector by 2.4 p.p. and lower net debt of the private sector by 0.6 p.p. of GDP).

Chart. 2.23. Gross external debt



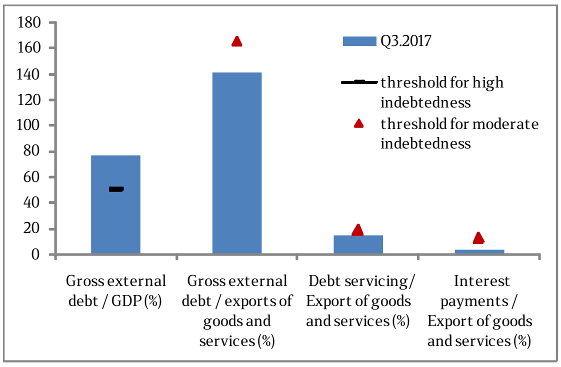
Source: NBRM

At the end of the third quarter of 2017, the gross external debt was EUR 7,406 million (without the NBRM repo transactions, which appear in almost the same amount on both the side of the liabilities to and the claims on non-residents). The gross debt equaled 72.5% of GDP, which is a decrease of 1.7 p.p. of GDP, compared to the end of 2016. This decrease is mainly due to the public sector debt (decline of 2.1 p.p. of GDP), amid higher private sector debt (by 0.4 p.p. of GDP). The long-term debt, occupying approximately 75%, is still predominant in the debt structure. The analysis of the external debt sustainability is presented in Annex 2.

At the end of the third quarter of 2017, the coverage of short-term debt by residual maturity with foreign reserves was 0.9, which indicates a slightly reduced liquidity in terms of external

[22] Government sector includes central government, local government and social security funds.

Chart. 2.24. Indebtedness indicators



Source: NBRM calculations

payments, amid relatively higher short-term debt by residual maturity and simultaneous decline in foreign reserves. The analysis of foreign indebtedness[23] of the Republic of Macedonia indicates a low level of indebtedness based on three indicators (gross external debt, debt servicing and repayment of interest, individually, relative to export of goods and services), whereas only gross debt-to-GDP ratio indicates high debt. According to the financial account forecast for the period 2017-2020, all indebtedness indicators regarding export are expected to improve or remain relatively stable in the next three-year period (amid expected exports growth), with the exception of the debt servicing indicator relative to exports, which would deteriorate in 2020 (repayment of larger amount of external debt). Observing maturity structure, long-term debt is expected to remain prevalent.

Forecasts of the Balance of Payments. Global economic recovery is expected to continue in the next year. In this context, the annual foreign effective demand for Macedonian products[24] in 2017 is estimated to have accelerated, recording a growth of 2.2%, which is more than expected in last year's scenario (1.7%). The economic activity of the trading partners for 2018 is expected to have a similar growth of 2.1%, and for 2019, the growth of foreign demand would slow down to 1.8%.

The latest estimates of the external sector in the next three years suggest retaining a moderate current account deficit at around 2% of GDP. In the next three years, the needs for external funding are expected to be covered by borrowing and direct investments. It is expected that capital inflows will ensure maintenance of adequate level of foreign reserves of about four-month coverage of import of goods and services of the next year.

Along with the gradual stabilization of foreign demand, with further positive effect of the existing companies with foreign capital and larger utilization of their capacities, as well as those pending to be established, in the next three years, the exports of goods and services are expected to continue increasing. In the next three years, imports would be driven by the increased imports for the needs of export production, as well as from imports for the needs of the strengthened investment consumption. For 2017, trade deficit in goods and services is estimated to moderately narrow to 14.1% of GDP (14.8% of GDP in 2016). This assessment is based on the improvement of the trade balance in goods (especially due to the contribution of the new industrial facilities), despite the moderate expansion of the energy trade balance (according to the movement of world prices of fuels) and slightly lower surplus in the trade of services. The estimated trade deficit in goods and services in 2017 is lower than expected in the last year's scenario (15.3% of GDP) given the stronger improvement in non-energy balance relative to the expectations. In the period 2018-2020, the trade deficit in goods and services is expected to follow a slight downward trend, i.e. to reduce to around 13% of GDP in the period 2018-2019, and to about 12% of GDP in 2020. In this light, balance of services is expected to register positive developments due to the strengthened export perspectives of the services sector (especially in the area of processing services, transport services and travel), complemented by a small narrowing of the non-energy balance, and in 2019-

[23] Tailored use of the World Bank method, where calculation of the indicators is based on three-year moving averages of GDP and exports of goods and services, as denominators. The methodology also defines criteria of indebtedness, as reference values for indebtedness level.
[24] The calculation of external demand takes into account the growth rates of GDP (Consensus Forecast) of the ten major trading partners, according to their share in the Macedonian exports in the period 2010-2012.

2020, a moderate narrowing of the energy trade balance is expected in line with the expected trends in world crude oil prices.

Chart. 2.25. Balance of payments (% of GDP)

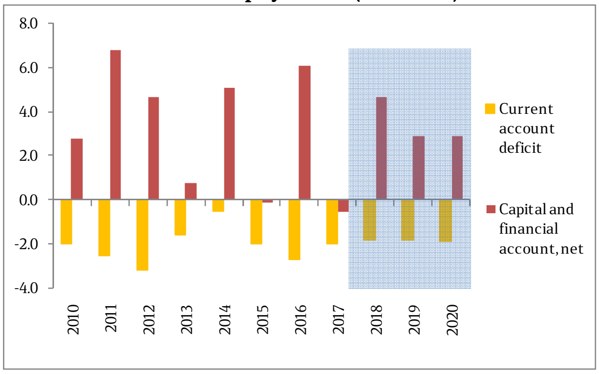
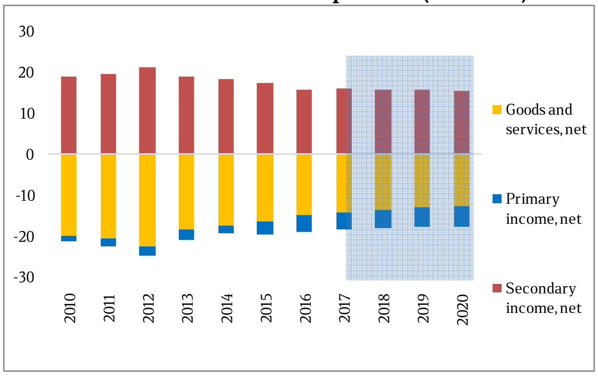


Chart. 2.26. Current account components (% of GDP)



Source: NBRM. Estimate for 2017 and forecast for 2018-2020. Source: NBRM. Estimate for 2017 and forecast for 2018-2020.

A significant part of the trade deficit will continue to be financed by inflows of secondary income (which primarily reflects the net purchase on the currency exchange market as the main component of private transfers). Net inflows of secondary income in 2017 are estimated at 16.2% of GDP, which is slight acceleration compared to 2016 (when they accounted for 16% of GDP and slowed down as a result of the increased demand for foreign currency due to the political uncertainty). In the next three years, net inflows in the secondary income are expected to be relatively stable, with a mild declining tendency (to 15.7% of GDP in 2020). The deficit in the primary income category of the current account for 2017 is estimated at 4.2% of GDP, while in the next three years, it is expected to increase moderately and to be maintained at about 5% of GDP, in line with the forecasts for growth in foreign capital income.

Amid such forecast movements in the current account items, the current account deficit is estimated at 2% of GDP for 2017, and to remain relatively stable at nearly 2% in the next three years (1.8% of GDP in 2018-2019 and 1.9% in 2020). In addition, the gradual moderate narrowing of the trade deficit in goods and services amid improved trade of both components is expected to be partially offset by the moderate expansion of the primary income deficit and the expectations for further slight slowdown in inflows from private transfers. The reduction in deficit in goods and services to around 12-13% of GDP is in line with the expected medium-term effects of FDI inflows in recent years in the tradable sector (as well as expectations for further inflows) that have already changed the structure of the economy, contributed to greater export diversification, and consequently, given the strengthening of their export potential and favorable external environment, stabilized and narrowed the trade deficit (for comparison, the trade deficit in goods and services in 2009 was 22.7% of GDP).

In 2017 and the next three years, capital inflows will mainly result from the expected FDIs and the expected external public and private debt. Foreign direct investment in 2017 has been estimated at 2.5% of GDP, which is a moderate slowdown compared to 2016 (3.2% of GDP), mainly reflecting the decreased investors' confidence given the political instability, as well as the higher amount of paid (accumulated) dividends. The growth of the domestic economy and the easing of the domestic political situation, along with the improved global environment, are expected to create positive perceptions among investors, with FDIs expected to grow gradually in the next three years and reach 3.3% of GDP in 2020. This forecast is similar to last year's scenario and is due to the continuity of FDI inflows (including in 2016 and 2017, which were marked by internal political crisis), expectations for reinvesting part of the earnings of the existing foreign companies, and announcements for further implementation of policies for attracting new FDIs. Amid repayment of the external government debt and lower net FDIs, in 2017, the financial account is expected to register a small net outflow of around 0.5% of GDP, while in the next three years net inflows are expected, which would be higher for 2018 (by 4.7% of GDP) in line with the expected government borrowing, and in the next two years, they would be maintained at a lower level (close to 3% of GDP). Cumulatively, forecast trends in the current and financial account are estimated to provide additional accumulation of foreign reserves in the next three years and further maintenance of relatively stable and adequate coverage of the average imports of each coming year.

Financial sector. Maintenance of financial system stability, its further development, as well as enhancing intermediation remain to be the main priorities in the area of the financial system. Therefore, the following activities will be undertaken:

- In 2018 new Banking Law will be adopted, by which, banking regulations will be further aligned with the Directive 2013/36/EU on access to the activity of credit institutions and the prudential supervision of credit institutions and investment companies and Regulation (EU) No. 575/2013 on prudential requirements for credit institutions and investment companies. The new Law will enable further strengthening of domestic regulation through further harmonization of the requirements of the risk management system established by the banks and its proper monitoring by the competent supervisory authority.

- During the same period, what is also envisaged is adoption of the Law on Bank Recovery and Resolution by implementing 2014/59/EU Bank Recovery and Resolution Directive. The new Law will define the bodies and instruments that will be available for prompt reaction in case of risks and problems in the operation of a particular bank.

- In 2018, Law on Payment Services and Payment Systems will be adopted, transposing provisions of the Payment Services Directive 2 (2015/2366/EC), the Electronic Money Directive (2009/110/EC) and Settlement Finality Directive (98/26/EC), the Payment Accounts Directive (2014/92/EC), as well as the relevant provisions of the Regulation on substitute fees for card-based payment transactions (2015/751 / EC) and the Regulation on the establishment of technical and business requirements for credit transfers and direct debit in euros (260/2012/EC). The initial version of the draft Law on Payment Services and Systems has been prepared through the Project „Further Harmonisation with the EU Acquis in the Field of Movement of Capital and Payments and Financial Services - Securities Markets and Investment Services", financed from IPA 2010, which lasted for 18 months and was completed in August 2016. This version is in the process of upgrading to the new EU directives and regulations that were not covered by the IPA project, but are important for establishing a robust legal framework in the payment sector in the Republic of Macedonia, thus achieving high compliance with the EU regulations. Adoption of the Law on Payment Services and Payment Systems will provide for the following:

- opening the payment services market for payment services providers other than banks, as well as for new issuers of e-money and increasing competition in this segment of the payment system;

- establishing aligned prudent regime for giving authorisations to payment services providers other than banks, as well as for new issuers of e-money, for the purpose of providing adequate level of safety to the users of payment services;

- introducing harmonised operational manuals to be applied on all payment services providers and issuers of e-money for providing equal access to the market of payment services;

- greater degree of protection for payment service users;

- greater degree of payment involvement and

- greater degree of harmonization with the EU in the domain of payment instruments.

- The two new laws in the field of capital market (Law on Financial Instruments and Law on Securities Prospectus and Issuers' Transparency Requirements) will be adopted in the first half of 2018. Laws will be prepared through the Project „Further Harmonisation with the EU Acquis in the Field of Movement of Capital and Payments and Financial Services - Securities Markets and

Investment Services“, financed from IPA 2010.

New legal solutions will be fully aligned with the EU Acquis in the field of capital market, thus providing for greater transparency of the companies, introducing new financial instruments and services, introducing new trading platforms, precisely defining the behavior of participants on the capital market that will be considered as market manipulation, and increasing the authorisations of the Securities and Exchange Commission as supervisory body in the field of capital market.

- New Insurance Law will be adopted in 2018, transposing the Solvency II Directive (2009/138/EC) on the taking-up and pursuit of the business of Insurance and Reinsurance, providing for compatibility and competitiveness of the domestic insurance industry with the one in EU Member States. The Law will contribute to increasing reliability and stability of the insurance sector and strengthening the insurers’ protection. Capital requirements as regards establishment of insurance undertaking will be strengthened and supervisory measures, adequate to the detected irregularities in the undertakings’ operations will be prescribed, and effective mechanisms for protection the rights of consumers of insurance services will be established.

2.3. ALTERNATIVE SCENARIOS AND RISKS

Alternative Scenarios. Two alternative scenarios will be elaborated on below. The first alternative macroeconomic scenario is based on the assumption for lower economic growth in the EU in the forecasting period. According to this scenario, real GDP growth in 2018 is projected at 2.5%, at 2.7% in 2019 and at 3.1% in 2020.

Such scenario implies weaker external demand and lower growth of export activity and, accordingly, of industrial production. According to this scenario, real export growth is projected at 5.7% in average annually in the forecasting period, being lower by 2.2 p.p. compared to the baseline scenario.

Such scenario also assumes unfavourable effects on the inflow of capital in the country in the form of direct investments, implying slower growth of gross investments in the medium term, as a result of the lower growth of investments in the construction sector and of import of investment goods. As a result, real growth of gross investments is lower by 1.2 p.p. compared to the baseline scenario, projected at 3.2% in average annually in the forecasting period. Lower growth of gross investments is mainly due to the slower growth of private investments, and to a lesser extent to the growth of public investments.

Effects on the consumption are expected to be smaller in relation to the other components. Hence, the forecasted real growth of public consumption is around 1%, while real growth of private consumption is 2.4% in average annually in the forecasting period. Lower growth of both export and domestic demand implies slower growth of import which, in the analysed period, is envisaged to increase by 4.7% in average annually, which is by 1.7 p.p. lower growth compared to the baseline scenario.

The second alternative macroeconomic scenario is related to the risk of weaker contribution of domestic demand to economic growth, in terms of lower realization of infrastructure projects and weaker effects from the support of the investment activity of companies. In such conditions, the projected real growth of gross investments is 1.9% in average annually in the forecasting period, which is lower growth by 2.5 p.p. compared to the baseline scenario, where it is estimated that 3/4 of this effect is due to public investment, and the rest is due to private investment. Moreover, the weaker investment growth implies lower real growth of import, which, according to this scenario, is 5.8% in average annually in the forecasting period, which is by 0.6 pp. lower growth compared to the baseline scenario. The effects on exports in this period are expected to be somewhat smaller, with net exports having a mild positive contribution to economic growth, but only partially offset the negative effect of weaker investment growth on the domestic demand and economic growth. Hence, according to this scenario, the projected growth of the economic activity is 2.9% in 2018, 3.1% in 2019 and 3.4% in 2020.

As regards labour market, slower pace of economic growth implies slower growth of the number of employees and slower pace of reduction of unemployment rate compared to the baseline scenario. Hence, according to the first alternative scenario, the average annual increase in the number of employed is expected to be 1.6% in the forecasting period, while the unemployment rate in 2020 is expected to drop to 20.1%. According to the second alternative scenario, growth of employment in 2017 is projected to be 1.8% in average annually, resulting in decline of unemployment rate to 19.8% in 2020.

As regards inflation rate, it is assumed that trends of commodity prices on the global stock markets remain unchanged in relation to the baseline scenario, i.e. we assume similar projections as regards the developments on the supply side and the level of foreign prices. Slower economic growth, according to the first alternative scenario, implies that no inflationary pressures from the demand side are expected, taking into account that output gap is projected to close in 2019, while in 2020 lower positive output gap is estimated.

Effects of the alternative scenarios on the budget deficit are presented in point 3.6. Sensitivity Analysis.

Risks. Risks as regards projected economic growth rates are generally reduced compared to the projections in the previous programme, especially those related to the domestic environment. Risks with respect to the international environment are mainly related to the economic trends and the growth dynamics of the EU economy, as the most important partner of Macedonia. Thus, possible weaker economic performance in the EU and the other trade partners in the country from the projected one in the next medium-term period, may worsen the prospects for growth of the economic activity in Macedonia, through weaker growth of export and industrial production, as well as the reduced inflow of foreign capital. Weaker growth than the expected one or the possible drop in prices of base metals on the global market is an additional risk thereof.

As regards the domestic environment, in conditions of stabilisation of the domestic political situation and prospects for increased growth of the domestic economy, risks have been significantly reduced. In fact, the projected growth of domestic demand, which is expected to have significant contribution to the economic growth, is related to risks which are assessed as balanced in the medium term and are primarily related to the projected growth of gross investments, i.e. with the realisation of infrastructure projects, as well as with the effects from the support of investment activity by domestic and foreign enterprises over the economy.

The main risks to the presented external sector scenario in the next period in part still arise from the global surrounding, particularly the pace of global recovery and its influence on the growth of domestic economy and investor perceptions. Any weaker external demand may have adverse effects on the presence of domestic exporters in foreign markets. Any financial market instability and exacerbation of geopolitical risks could bring about increased investors' risk aversion and consequently, risks of lower capital inflows of non-debt financing or possible capital outflows for funding parent companies. It is estimated that the direct effects of Brexit on the Macedonian economy would be small, while potential risk is the indirect transmission of effects through the EU, as our major trading partner. In addition, the movement of world prices is accompanied by uncertainty, with possible effects on domestic inflation and export prices. Despite the favorable movements in world metal prices in 2017, the expected future developments indicate less favorable and divergent price movements which is relevant for the growth and export outlook of the domestic metal industry as traditional export sector, although with significantly reduced share in recent years (in the context of structural changes in the economy and already dominant share of higher value-added industries).

The assessment and extent of the effects of new export capacities in the economy is crucial for the trade balance forecast. The number of export capacities in the economy has been increasing, and once they establish their production facilities, they start contributing to the country's exports. The trade deficit in the last four years was lower than expected in the scenarios, largely as a result of the new export companies, which points to an upward risk (potential also for the future). In this context, it should be noted that current scenario incorporates an expectation that in the next three years, part of the existing companies will continue increasing their capacity utilization, but upward risk remains, especially with regard to new companies. In the medium term, changes in the production structure are expected to lead to further diversification of exports and to improve export performance, which goes in favor of strengthening the resilience of the economy to external shocks. Given the growing number of new production capacities in the economy, and the expected improvement of the global environment, the expectations in this regard are justified. The forecast of net inflows from secondary income (within them, net purchased currency on the exchange market) envisages for a gradual slowdown in their share in GDP and can generally be regarded as conservative. The forecast of net inflows from FDIs takes into account the past performance, and is assessed as moderate, considering the continuity of these inflows (at a moderate level, even in crisis years), the expectations for reinvestment of some of the earnings of the existing companies with foreign capital, as well as the continuation of the FDI attracting policies.

Risks to the inflation forecast are mainly conditioned upon the assumptions about the movements in prices of primary commodities, potential changes in regulated prices and possible second-round effect on other prices in the economy. Risks to the forecast medium-term inflation path are predominantly related to the external factors on the supply side (the output gap would register slight positive changes).

Observing the expected banks' credit growth, the pace of global recovery, in the context of its influence on the domestic economic growth and the loan portfolio quality, as before, would affect the banks' risk perceptions and consequently, lending. Risks arising from the business strategies of foreign banking groups and changes in the regulatory requirements, could also affect the operations of their subsidiaries in the country.

The aforementioned risks to the macroeconomic scenario for the next three years[25] point to a need for constant monitoring of any changes in the external and domestic economic conditions in the period ahead and timely taking of adequate measures by policy makers. One should note that the expected internal political stabilization, coupled with improved Euro-Atlantic perspectives, points to potential upward risks to the scenario.

3. FISCAL FRAMEWORK

3.1. FISCAL STRATEGY[26] AND MEDIUM-TERM OBJECTIVES

Fiscal policy in the coming medium-term period will be aimed at fiscal sustainability and gradual fiscal consolidation, maintaining macroeconomic stability, boosting competitiveness of the economy and increasing employment. In fact, the focus will be placed on creating favourable

---

[25] It is important to mention that the forecasts for the external and monetary sector are based on the Fiscal strategy for 2017-19, as the only available at the time of closing these forecasts.

[26] The Fiscal strategy 2018-2020 is published on MoF website http://finance.gov.mk/files/u3/Fiskalna%20Strategija%20na%20RM%202018-2020.pdf

business climate, supporting domestic enterprises, above all SMEs, as well as supporting the economy with substantial investments in infrastructure projects.

During the next medium-term, special attention will be put on the commitment to gradual consolidation of public finances, to the end of maintaining the macroeconomic stability and controlling the level of indebtedness.

Projected revenues of the consolidated government budget in the next three-year period decline relatively, as a share of GDP, from 31.1% of GDP in 2018 to 30.5% in 2020. As a result of continuity in implementing disciplined budget policy and strengthened control of public spending, in the period 2018-2020, total expenditures will also decline from 33.8% in 2018 to 32.8% in 2020.

Set basic postulates of the fiscal policy in the coming period provide for gradual reduction of the budget deficit level and its positioning at a level of around 2.5% of the projected GDP in 2019 and 2.3% of GDP in 2020.

Table 3.1. Consolidated general government budget (Denar million)

	2018	2019	2020
Consolidated general government budget - Revenues	206,262	216,040	228,225
% of GDP	31.1	30.7	30.5
Consolidated general government budget - Expenditures	224,495	233,969	245,100
% of GDP	33.8	33.3	32.8
Consolidated general government budget - Deficit	-18,233	-17,929	-16,875
% of GDP	-2.7	-2.5	-2.3
Central Budget - Revenues	**116,545**	**122,616**	**131,125**
% of GDP	**17.6**	**17.4**	**17.5**
Central Budget - Expenditures	**134,778**	**140,545**	**148,000**
% of GDP	**20.3**	**20.0**	**19.8**
Central Budget - Deficit	**-18,233**	**-17,929**	**-16,875**
% of GDP	**-2.7**	**-2.5**	**-2.3**
Budget Funds - Revenues	57,420	60,772	64,323
% of GDP	8.6	8.6	8.6
Budget Funds - Expenditures	57,420	60,772	64,323
% of GDP	8.6	8.6	8.6
Budget Funds - Deficit	0	0	0
% of GDP	0.0	0.0	0.0
Local Government Budget - Revenues	32,297	32,652	32,778
% of GDP	4.9	4.6	4.4
Local Government Budget - Expenditures	32,297	32,652	32,778
% of GDP	4.9	4.6	4.4
Local Government Budget - Deficit	0	0	0
% of GDP	0.0	0.0	0.0

Source: Ministry of Finance

3.2. Budget implementation in 2017

In the period January - September 2017 Budget revenue and inflow performance is within the expectations for this period of the year, while expenditures are executed on regular and timely basis. Total revenues were collected in the amount of Denar 130,972 million (70.9% relative to the plan in the 2017 Supplementary Budget), i.e. collection was higher by 4.1% in relation to the revenue collection in the analysed period last year. Denar 77,821 million out of this amount are tax revenues, being higher by Denar 2,805 million or by 3.7% compared to last year. VAT revenues are collected in the amount of Denar 35,555 million, being higher by 1.7% compared to the same period in 2016, predominating in the structure of tax revenues with 46.3%. Higher revenues compared to last year also include revenues from Profit tax by 11.5%, Personal income tax by 7.9%, Excise by 2.5% and Import duties by 7%.

Revenues on the basis of social contributions were collected in the amount of Denar 38,509 million. This was by Denar 1,639 or 4.4% more compared to the same period in 2016. Denar 25,890 million was collected on the basis of pension insurance, while revenues collected on the basis of health insurance contributions amounted to Denar 10,971 million.

During the first nine months of 2017, non-tax revenues were collected in the amount of Denar 10,009 million, which compared to the same period in 2016, were higher by Denar 480 million, i.e. by 5%. Capital revenues amounted to Denar 1,100 million, being generated from sale of construction land and social flats. Budget users generated Denar 3,366 million on the basis of donations from international multilateral and bilateral cooperation.

Expenditures in the period January-September 2017 were executed in the amount of Denar 142,027 million (69.9% relative to the plan in the 2017 Supplementary Budget), i.e. by Denar 7,127 million or 5.3% higher compared to the same period last year. Within this framework, current expenditures were executed in the amount of Denar 130,501 million or by 5.2% higher than the same period in 2016. During this period, Denar 19,627 million was paid for salaries and allowances to employees in institutions - budget users, while expenditures related to goods and services were executed in the amount of Denar 10,542 million.

Transfers-related expenditures have the highest share in current expenditures, amounting to Denar 93,900 million in this period. Government liabilities on the basis of payments related to exercising the rights to guaranteed social protection of the citizens (pecuniary allowances to vulnerable categories of citizens, as well as child allowance and parenting payments) were settled on regular basis, accounting for Denar 6,143 million. As regards regular payment of pensions, Denar 38,643 million was allocated therefore, with respect to financing health services and benefits, Denar 19,770 million was paid, while Denar 716 million was allocated for payment of unemployment benefits through the Employment Agency. Denar 11,227 million was transferred to the municipalities, as block grants for financing the transferred competences, as well as earmarked grants for financing the operating costs in local public institutions. In addition, Denar 1,572 million was transferred on the basis of VAT revenues. During this period, most of the agricultural subsidies have been paid, i.e. around 85% of the annual plan.

Denar 6,432 million was allocated for regular servicing of liabilities on the basis of interest, according to the repayment schedules on domestic and foreign borrowing. Denar 4,395 million out of this amount was allocated for payment of interest on foreign borrowing.

In the period January - September 2017, capital expenditures were executed in the amount of Denar 11,526 million, being higher by 6% compared to the same period in 2016.

During this period, budget deficit amounted to Denar 11,055 million, or 1.75% of the projected GDP for 2017.

Table 3.2. Budget of the Republic of Macedonia 2017

(Denar million)	**Budget 2017**	**Realisation in the period January-September 2017**
1. Total revenues	**184,745**	**130,972**
1.1. Tax revenues and contributions	159,497	116,330
1.1.1 Tax revenues	106,755	77,821
1.1.2 Contributions	52,742	38,509
1. 2. Non-tax revenues	16,321	10,009
1.3. Capital revenues	1,941	1,100
1.4. Donations and other revenues	6,986	3,533
2. Total expenditures	**203,312**	**142,027**
2.1. Current expenditures	179,915	130,501
2.1.1 Salaries and allowances	26,614	19,627
2.1.2 Goods and services	17,660	10,542
2.1.3 Transfers	127,421	93,900

2.1.4 Interest	8,214	6,432
2.2. Capital expenditures	23,397	11,526
3. Deficit	**-18,567**	**-11,055**
4. Deficit financing	**18,567**	**11,055**
4.1 Inflow	36,920	25,270
4.1.1 Other inflows	0	79
4.1.2 External sources	23,535	2,899
4.1.3 Domestic sources	20,796	13,200
4.1.4 Deposits/Additional sources	-7,421	9,092
4.1.5 Revenues on the basis of sale of shares	10	0
4.2 Outflow	18,353	14,215
4.2.1 Repayment upon foreign borrowing	9,057	6,956
4.2.2 Repayment upon domestic borrowing	9,296	7,259

Source: Ministry of Finance

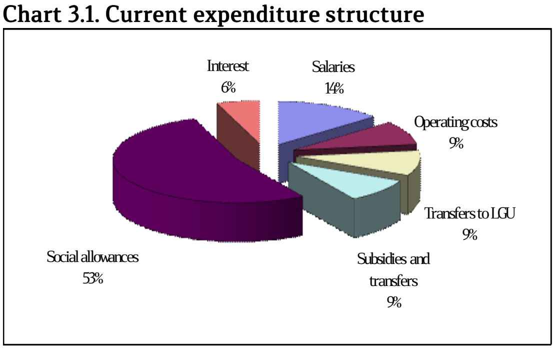
3.3. MEDIUM-TERM BUDGETARY OUTLOOK

Total genuine revenues of the Budget of the Republic of Macedonia (central government) for the period 2018-2020 are projected to around 29% of GDP, whereby their share in GDP by years is reduced. Revenues projections are based upon the existing legal solutions, while they will be subject to revision by adopting the reforms to the end of introducing fair taxation. Thereby, tax revenues account for around 59.5% of the projected revenues, followed by revenues on the basis of social contributions accounting for around 28.8%, non-tax revenues and capital revenues accounting for around 9.4%, while the rest of the revenues are expected to be generated from IPA Funds and other donations. With respect to tax revenues, most revenues will be realised on the basis of VAT, personal income tax and excises.

Projections for social contributions, which are genuine revenues of the Pension and Disability Insurance Fund, Health Insurance Fund and the Employment Agency, are based on keeping the existing mandatory social insurance rates and increasing the maximum base for calculation and payment of the contributions from 12 to 16 average wages for the employed persons, i.e. from 8 to 12 average wages for self-employed persons, as well as the expected positive economic trends, which will accordingly reflect on the growth rates of both employment and wages.

Non-tax revenues in the next medium-term period account for around 8.7% of the total revenues, wherein revenues on the basis of administrative fees and other non-tax revenues the budget users generate on their own accounts account for the most.

Chart 3.1. Current expenditure structure



Source: Ministry of Finance

In the coming period, budget revenue projections with regard to foreign donations include the donations the budget users will realise for specific projects, as well as disbursements from the EU pre-accession funds.

Expenditure side of the Budget of the Republic of Macedonia in the coming medium-term period will be focused on regular and timely fulfillment of all legal obligations, support to the national economy and intensification of infrastructure projects. Average share of expenditures in the Budget in the period 2018-2020 is around 31.5% of GDP.

When projecting the current expenditures for the next period, following assumptions were taken into account:

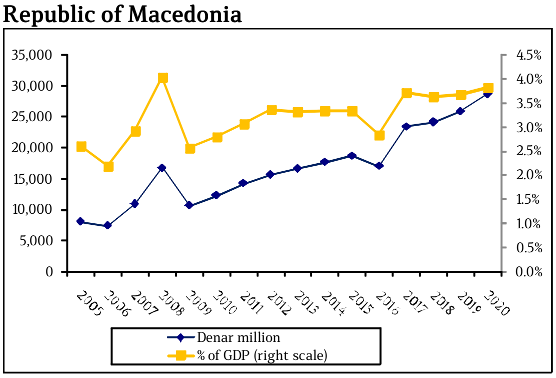
- As regards expenditures related to wages and allowances, continuation of strict control over new employments and gradual wage increase of certain sectors in line with the fiscal opportunities (public defense, health, education);

- Timely payment of pensions and social benefits, for the purpose of ensuring the well being of the beneficiaries of these rights. Medium-term projections also include regular servicing of liabilities on the basis of social benefits for socially most vulnerable families as social assistance, child allowance, allowances on the basis of rights of disabled persons, war invalids and civilian invalids;

- Provision of subsidies and funds under the IPARD Programme to support farmers, to the end of strengthening agricultural production;

- Support for domestic companies, new Greenfield investments and improvement of the innovation capacity of companies will contribute to boosting both the competitiveness of the private sector and the economic growth.

Chart. 3.2. Capital expenditures in the Budget of the Republic of Macedonia



Source: Ministry of Finance

In the 2018 Budget, an amount of Denar 24,144 million capital investments are envisaged, being intended for road, rail, energy and communal infrastructure, as well as capital investments for improving the conditions in the health, educational and social system, agriculture, culture, sports, environment protection and judiciary. Their effective implementation will contribute to growth of the economy and creation of new jobs.

More specifically, investments are envisaged for:

- continuation of rehabilitation of roads on multiple routes;
- continuation of construction of new highway sections;
- improvement of the Corridor X railway line and completion of the Railway Corridor VIII, as well as railway fleet renewal;
- continuation of activities for construction of the national gasification system;
- improvement of municipal services by financing infrastructural investment projects in the field of water supply and waste water treatment, solid waste management and other investments that are a priority for municipalities;
- investments in communal infrastructure in rural areas;
- construction of the Regional Clinical Hospital in Stip will continue and construction of the Clinical Center "Mother Teresa" in Skopje will commence;
- continuation of activities for building physical education facilities and procurement of equipment in primary and secondary schools, as well as rehabilitation of primary and secondary schools;
- realization of the second and the third phases of the “Zletovica Water Basin Utilisation Improvement Project”, whereby the third phase covers construction of small hydro power plants along the river Zletovica;
- second phase of the “Irrigation Program Southern Vardar Valley”, which includes rehabilitation and modernization of irrigation systems in the southeastern region;
- activities for construction, reconstruction, renewal and expansion of 4 penitentiary institutions, thus implementing standards set in international and European prison standards;
- activities for construction of apartments for low-income persons.

Projected Deficit and Its Financing. As for the period 2018-2020, budget deficit is envisaged to gradually reduce, as follows: Denar 18.2 billion in 2018, Denar 17.9 billion in 2019 and Denar 16.9 billion in 2020. This means that gradual fiscal consolidation is envisaged in this medium-term period, i.e. the share of budget deficit in GDP will decrease from 2.7% in 2018 to 2.5% in 2019 and 2.3% in 2020.

Financing of the planned deficit will be provided from foreign and domestic borrowing. Foreign borrowing may be realised through issuance of Eurobond on the international capital market or by disbursing funds from favourable loans from foreign financial institutions and credit lines intended for financing certain projects. Thereby, the choice of certain source of foreign financing will be based upon the ongoing and expected developments on the international capital markets. Furthermore, borrowing on the domestic government securities market will provide for additional financing under favourable terms and conditions, by using the relatively low interest rates and the high level of interest of investors on the domestic government securities market. For the purpose of optimising the payments and reducing the refinancing risk, main commitment of the Ministry of Finance will be to lengthen the maturity of issued securities, by issuing government bonds with longer maturities.

Table 3.3 Projected deficit and sources of its financing

(Denar million)	2018	2019	2020
Budget balance	**-18,233**	**-17,929**	**-16,875**
Deficit financing	**18,233**	**17,929**	**16,875**
Inflows	**40,897**	**32,883**	**53,203**
Domestic sources	17,700	17,374	11,250
External sources	34,839	25,485	24,520
Deposits	-11,642	-9,976	17,433
Outflows	**22,664**	**14,954**	**36,328**
Repayment upon foreign borrowing	12,246	8,755	3,639
Repayment upon domestic borrowing	10,418	6,199	32,689

Source: Ministry of Finance

Local Government Budget. In the course of 2018, as well as in the medium run, it is expected for the municipalities to continue the trend of improved collection of own revenues, strengthening the capacities for development of policies for financing the municipalities and enhancing the capacities for financial management. Revenues are allocated to the municipalities from the state budget on the basis of VAT grant (general grant), in the amount of 4.5% of VAT collected in the previous year.

New revenues are provided by allocating funds from lease of state-owned agricultural land to the municipalities, the proportion of which is 50% for the Budget of the Republic of Macedonia and 50% for the municipalities, to be distributed from 2018. Revenues are allocated from the fee collected by issuing concession for usage of water resources for electricity generation (50% for the central government budget and 50% for the local authorities).

Performance of own revenues of municipalities, in particular revenues collected on the basis of taxes on real estate, as a result of fully including the real estate of natural persons and legal entities and re-assessment of the value of real estate, will continue to increase in the next medium-term period. At the same time, part of the municipalities generate higher revenues on the basis of property taxes as a result of the higher property tax rate, within the set spread pursuant to the Law on Property Taxes. Higher revenues are also expected by applying the improved elements of calculation in the Methodology on Determining Market Value of Real Estate, as well as the improved quality assessment of the value of real estate, thus providing the municipalities the legal possibility to employ an expert – an evaluator or to use the services of licensed evaluators.

In the coming period, higher revenues are expected to be generated by determining the real market value of the real estate after completing the procedure on treatment of illegally built facilities on construction and agricultural land.

Implementation of the 2009 – 2019 Strategy for Equal Regional Development of the Republic of Macedonia in the eight planning regions, by better vertical and horizontal coordination between the national and the local policies and through the integrated development projects adjusted to the local needs, will provide for more balanced local development throughout the country. Special efforts will be put in supporting municipalities by encouraging local development via supporting the local projects and harmonizing them with the national ones.

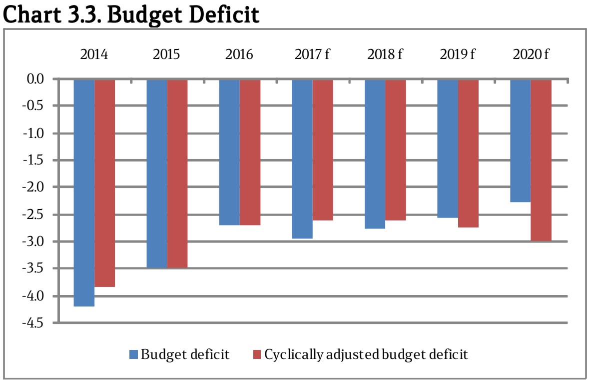
Realisation of series of infrastructure projects related to improvement of the quality of life will accordingly improve the regional development and the active integration of regions in the economy. To that end, series of projects will be undertaken aimed at improving the overall road and communal infrastructure, as well as urbanization of villages to the end of development and support of rural tourism and recreational centers.

Implementation of the “Municipal Services Improvement Project", supported by the World Bank will continue in 2018 as well. The loan proceeds are intended for financing infrastructure investment projects in the field of water supply and wastewater drainage, management of solid waste and other investments in municipal services. In order to improve services and quality of life in rural areas, reduce socio-economic differences and improve competitiveness of these areas, funds are provided under the EU IPA grant for rural infrastructure.

At the same time, pursuant to the legal regulations, municipalities fulfilling the legal criteria to borrow, will be able, in the coming period, to finance their projects by borrowing on the basis of concluding loan agreements with domestic or foreign creditors or on the basis of issuing municipal bonds.

3.4. STRUCTURAL DEFICIT

Chart 3.3. Budget Deficit



Source: Calculations of the Ministry of Finance, f-forecast

Economic activity, over time, tends to grow, but, moving along the trend line, the economy usually fluctuates above and below the long-term trend. Such cyclical developments in the economy are also reflected in the fiscal developments, through automatic stabilisers. In order to exclude the effects from fluctuations of economic activity on the fiscal indicators and to estimate the basic fiscal stance of the country, we calculate and analyse the cyclically adjusted budget balance, which is obtained by adjusting the budget revenues and the budget expenditures by the effect of deviation of the potential from the actual/projected GDP, and the adjustment is made on aggregate level.

Calculations point out that cyclically adjusted budget deficit accounted for 2.6% in 2017, and it is lower than the projected budget deficit in the respective year, taking into account that the cyclical budget component has a negative value, as a result of the estimated negative output gap.

In 2018, taking into account that projected GDP is expected to move towards the potential one, cyclical budgetary component is narrowed, i.e. cyclically adjusted budget deficit is almost equal as the projected one (see chart 3.3). In 2019 and 2020, in conditions of positive output gap, estimated cyclically adjusted budget deficit is higher than the projected budget deficit, i.e. it amounts to 2.7% in 2019 and 3.0% in 2020. During the analysed period, cyclically adjusted primary budget deficit is fairly constant, i.e. it accounts for 1.2% (Table 3.4).

Table 3.4. Aggregate fiscal indicators and production gap

	2017	2018	2019	2020
Total budget balance	**-2.9%**	**-2.7%**	**-2.5%**	**-2.3%**
Primary budget balance	-1.6%	-1.4%	-1.0%	-0.5%
Production gap	-1.1%	-0.5%	0.6%	2.3%
Cyclical component of the budget	-0.3%	-0.1%	0.2%	0.7%
Cyclically adjusted total budget balance	-2.6%	-2.6%	-2.7%	-3.0%
Cyclically adjusted primary budget balance	-1.3%	-1.3%	-1.2%	-1.2%

Source: Calculations of the Ministry of Finance

Note: Data on production gap and cyclically adjusted total/primary budget balance are expressed in relation to the potential GDP.

3.5. Debt levels and developments, analysis of below-the-line operations and stock-flow adjustments

At the end of the third quarter in 2017, government debt of the Republic of Macedonia[27] amounted to EUR 3,875.8 million, i.e. 37.8% of GDP. At the end of the third quarter, total public debt[28], which includes both the government debt and the guaranteed debt, amounted to EUR 4,691.5 million, accounting for 45.8% of GDP. During the analysed period, domestic government debt accounted for 38.7% in the total government debt, while the external government debt accounted for 61.3%. Share of external government debt decreased by 2.2 p.p. compared to the end of 2016, given that in the course of 2017 more emphasis was placed on borrowing on the domestic market, and regarding external debt, the loan from Deutsche Bank was fully paid out in the amount of EUR 75 million. From interest structure point of view, fixed interest rate debt slightly decreased by 0.1 p.p. compared to end-2016, by which the ratio between fixed interest rate debt and variable interest rate debt was 71.8% to 28.2% respectively. As for the currency structure of foreign currency debt, share of euro-denominated debt in the foreign currency debt portfolio accounted for 90.6% and, compared to end-2016, it increased by 1.2 p.p.

Table 3.5. Public debt stock (EUR million)

	2011	2012	2013	2014	2015	2016	30.9.2017
External Public Debt	1,881.9	1,941.2	2,078.7	2,725.1	2,847.5	3,286.0	3,174.0
Government Debt	1,582.1	1,615.9	1,597.5	2,092.2	2,096.7	2,446.6	2376.7
Guaranteed debt	299.9	325.3	481.2	633.0	750.8	839.4	797.3
Domestic Public Debt	532.9	967.6	1,202.7	1,196.2	1,379.7	1,425.4	1,517.5
Government Debt	510.8	938.6	1,174.1	1,170.3	1,356.6	1,404.9	1,499.1
Guaranteed debt	22.1	29.0	28.6	25.9	23.2	20.5	18.4
Total Public Debt according Public Debt Law	2,414.9	2,908.8	3,281.4	3,921.3	4,227.2	4,711.4	4,691.5
Total Public Debt as % GDP	32.0	38.3	40,3	45.8	46.6	48.5	45.8
Total Government Debt	2,092.9	2,554.5	2,771.6	3,262.5	3,453.3	3,851.5	3,875.8
Total Government Debt as % GDP	27.7	33.7	34.0	38.1	38.1	39.6	37.8
Guaranteed Debt	322.0	354.3	509.8	658.9	774.0	859.9	815.7
Guaranteed Debt as % of GDP	4.3	4.7	6.3	7.7	8.5	8.8	8.0

Source: MF and NBRM

Medium-Term Fiscal Strategy, covering 3-year period, is the framework determining the public debt management policy in the Republic of Macedonia.

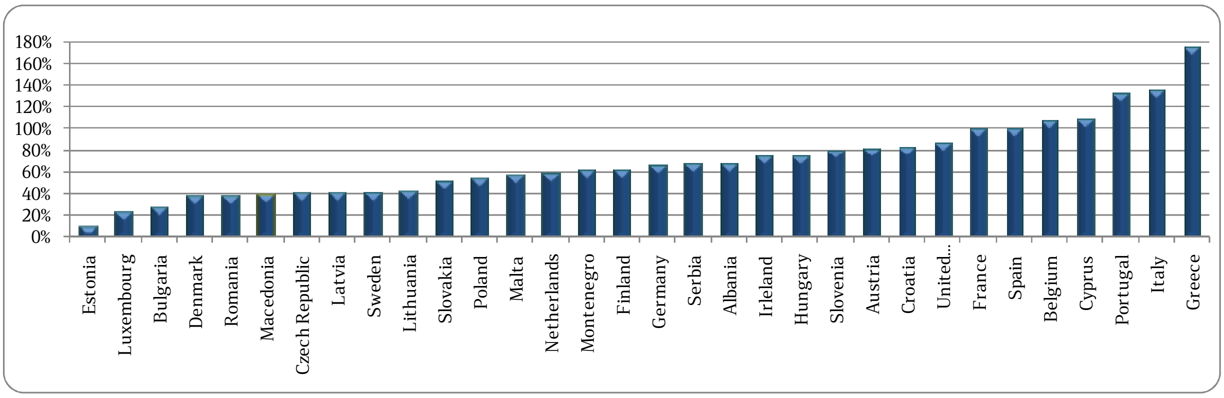
Investments launched in the past period in the field of infrastructure, water supply and sewerage, sports facilities, education, health, energy, construction of the National Gasification System, as well as other projects that are in line with the Government Programme are expected to continue realizing in the period 2018 - 2020. The projects, co-financed with foreign loans, will be implemented by the state administration bodies, strongly committed not to jeopardize the long-

[27] Government debt comprises financial liabilities incurred on the basis of borrowing by the Republic of Macedonia, public institutions established by the Republic of Macedonia and the municipalities, the municipalities within the City of Skopje and the City of Skopje.

[28] Public debt comprises the government debt and the guaranteed debt of public enterprises and state-owned joint stock companies.

term sustainability of the debt level of the country. According to the Fiscal Strategy, moderate and contained increase of government debt up to 42.6% of GDP is expected at the end of 2020, while public debt is expected to account for 53.5% of GDP during the same period. The Fiscal Strategy is submitted to the Parliament of the Republic of Macedonia, whereby the legislative authority has insight in the public debt management policy.

Chart 3.4. Government debt of EU Member States and candidate countries in the second quarter of 2017 (% of GDP)

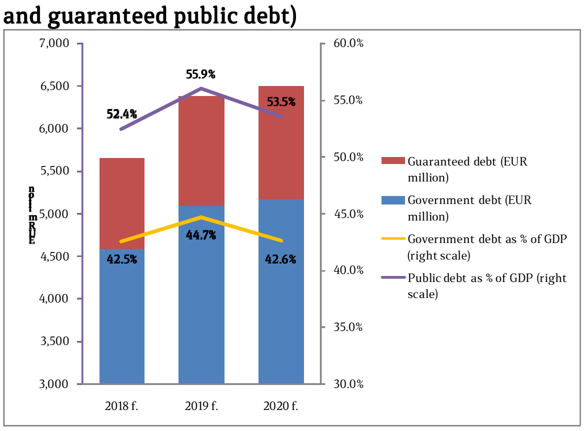


Source: Ministry of Finance, Eurostat, October 2017

In order to reduce the exchange rate risk, currency limits are set in the Fiscal Strategy, whereby the minimal share of euro-denominated debt in the foreign currency debt portfolio should account for 80%. In addition, interest limit on government debt is also set in the Fiscal Strategy, i.e. the fixed interest rate debt should account for at least 50% in the total debt portfolio.

In order to protect central government debt portfolio against the refinancing risk, minimum level of the "average time to maturity" indicator in 2018 should be 3 years. In order to protect central government debt portfolio against the interest rate risk, minimum level of the "average time to refixing" indicator in 2018 should be 2 years.

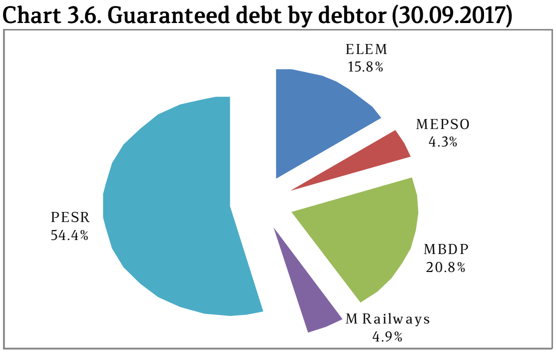
Chart 3.5. Forecast of total public debt (government and guaranteed public debt)



Source: Ministry of Finance

Moderate growth of investment activity is projected in the course of 2018, by using credit support from abroad. In addition, in the period 2018 – 2020, investments are expected to be carried out in infrastructure, water supply and sewage network, construction of social flats, as well as investments in education and health aimed at increasing productivity, i.e. boosting the competitiveness of the economy in the long run. Regarding guaranteed debt, moderate increase is expected until 2019 due to withdrawal of funds from projects mainly in road infrastructure, implemented with state-guaranteed loans. After 2019, these loans enter a repayment period and, accordingly, the guaranteed debt in relation to GDP is expected to decrease.

Chart 3.6. Guaranteed debt by debtor (30.09.2017)

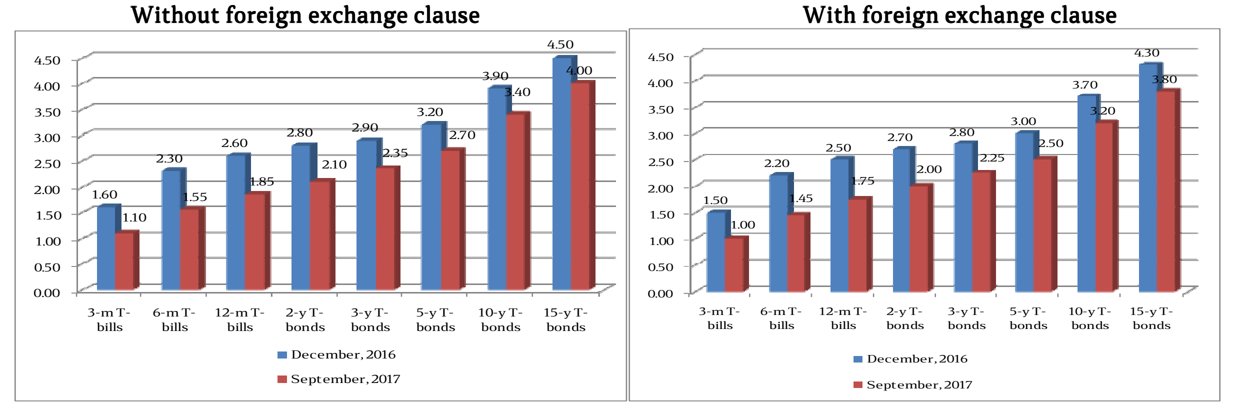


Source: Ministry of Finance

As for the new borrowings, account is taken of the long-term sustainability of debt, whereby the process of issuing new guarantees is strictly regulated and subject to the borrowing procedure prescribed in the Public Debt Law, according to which the public debt issuers should fulfill certain criteria so as for the country to be able to issue guarantee. As of 30th September 2017 inclusive, issued sovereign guarantees amounted to EUR 815.7 million, accounting for 8% of GDP (included in the public debt which accounted for 45.8% of GDP).

Primary Government Securities Market. According to the Calendar for Issuance of Government Securities (GS) on the Domestic Market, in the period January - September 2017, Ministry of Finance issued 6- and 12-month treasury bills on regular basis, as well as 2-, 5- and 15-year government bonds. In this period, total of 54 auctions of GS were carried out, i.e. 26 auctions of treasury bills and 28 auctions of government bonds. Total amount offered for sale at the auctions was Denar 40,295.78 million, demand was Denar 57,584.28 million and amount realised accounted for Denar 38,987.20 million. In order to reduce the frequency of issuance of government securities, the Ministry of Finance has reduced the number of auctions held during one calendar month, and starting from the second semester of 2017, it carries out two auctions per month.

Chart 3.7. Interest rates of Government Securities without and with foreign exchange clause



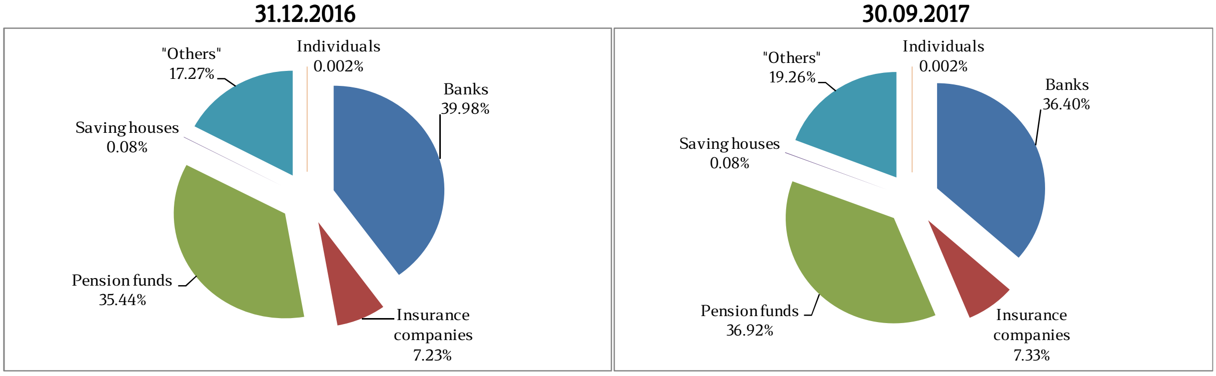
Source: Ministry of Finance

Interest rates on government securities in the period December 2016 – September 2017 are shown in Chart 3.7. In January and March 2017 the Ministry of Finance decreased the interest rates on government securities by around 0.50 p.p. and as of September 2017, interest rates on government securities remained at the same level.

As of September 2017 inclusive, stock of outstanding government securities amounted to Denar 87,847.65 million, Denar 38,327.86 million out of which as treasury bills and Denar 49,519.79 million as government bonds.

Increased share of pension funds, compared to the same period in 2016, can be observed in the ownership structure of the government securities portfolio. As percentage, the share of pension funds equalizes with the one of banks, which were dominant investors in government securities in the past (Chart 3.8).

Chart 3.8. Government securities market ownership structure



Source: Ministry of Finance

In the period January - September 2017, except for the banks, saving houses and individuals, share of other categories of market participants in the ownership structure increased. During the analysed period, share of banks dropped by 3.58 p.p. in relation to the share of other market participants. As of September 2017 inclusive, ratio between banks and other market entities was 36.40% to 63.60% respectively. Such ownership structure changes the nature of the government securities portfolio, increasing its duration and reducing exposure to refinancing risk.

Secondary Government Securities Market. Legal regulations on secondary trading provide for trading in all structural government securities on the Macedonian Stock Exchange AD, as well as trading in continuous government securities on the OTC markets.

In January - September 2017, only trading in government denationalisation bonds was recorded at the Macedonian Stock Exchange. Total volume of trading during this period amounted to Denar 164.00 million, dropping by Denar 485.54 million compared to the same period last year.

During the same period, 5 transactions with government securities, pertaining to treasury bills, and 10 transactions with government securities, pertaining to government bonds, were realised on the OTC market. Total nominal trading amount amounted to Denar 1,589.81 million. Compared to the trading in the same period last year, it can be concluded that lesser number of transactions with government securities were realised in 2017, while total nominal amount of trading was lower by Denar 1,360.19 million.

International Capital Market. In the course of 2017, Eurobonds issued by the Republic of Macedonia, falling due in 2020, 2021 and 2023, were traded on the international capital market. As of September 2017 inclusive, yield to maturity as regards the Eurobond falling due in 2020 is 1.92%, while as regards the Eurobond falling due in 2021 yield to maturity is 2.18%, and yield to maturity regarding the Eurobond falling due in 2023 is 3.40%.

Credit Rating of the Republic of Macedonia. On 4th August 2017, "Fitch" Credit Rating Agency affirmed Macedonia's Long-Term Foreign and Local Currency Issuer Default Ratings at 'BB' with negative outlook. On 15th September 2016, "Standard & Poor's" Credit Rating Agency affirmed the previously awarded 'BB-' long- and short-term foreign and local currency sovereign credit rating of the Republic of Macedonia, at the same time affirming the stable outlook of the country.

3.6. SENSITIVITY ANALYSIS

Sensitivity of Budget Deficit. Medium-term projections are always coupled with certain degree of uncertainty and risks, thus we present below a review of the results from the sensitivity analysis, examining budget deficit sensitivity under three pessimistic scenarios, the conditions being different from the ones taken as basis for medium-term projections.

Taking into account that medium-term fiscal scenario is based on macroeconomic assumptions, we consider them as factor with potential effect on the fiscal trends. Hence, the first scenario assumes lower economic growth, according to the alternative scenarios elaborated on in point 2.3. In fact, the baseline scenario, which budget revenue and expenditure projections are based on, envisages real GDP growth of 3.2% in 2018, 3.5% in 2019 and 4.0% in 2020. According to the first alternative scenario, real GDP growth is projected at 2.5% in 2018, at 2.7% in 2019 and at 3.1% in 2020. Lower economic growth projections imply lower growth of budget revenues, and in terms of unchanged expenditures, also higher budget deficit compared to the baseline scenario, amounting to 3.1% of GDP in 2018, 3.0% in 2019 and 2.8% in 2020. According to the second alternative scenario, real GDP growth is projected at 2.9% in 2018, at 3.1% in 2019 and 3.4% in 2020, implying lower increase of budget revenues and respectively higher budget deficit in relation to the baseline scenario, i.e. unchanged deficit level in 2018 compared to the previous year and a deficit of 2.8% and 2.6% of GDP in 2019 and 2020, respectively.

As a second scenario, we assume for economic agents to restrain from spending, and the result thereof would be reduction of the annual growth rate of total budget revenues by 20% in the analysed period in relation to the initially projected rates, presented in Table 3.6. Hence, by assuming for growth of budget revenues to account for around 3.8% in 2018, 4.0% in 2019 and 4.8% in 2020, budget deficit would amount to around 3.0% in the forecasting period, i.e. the deficit would be higher by 0.6 p.p. in average above the level projected in the baseline scenario. Table 3.6. shows the budget deficit in the analysed period according to both the baseline and the alternative scenarios.

Table 3.6. Sensitivity analysis of budget deficit

	2018	2019	2020
GDP, real growth rate	3.2	3.5	4.0
Budget revenues, growth rate	4.7	5.1	6.0
Budget expenditures, growth rate	4.1	4.5	5.0
Budget deficit (% of GDP)			
Baseline Scenario	-2.7	-2.5	-2.3
Scenario 1a. Lower GDP growth rate in the analysed period according to the first alternative scenario	-3.1	-3.0	-2.8
Scenario 1b. Lower GDP growth rate in the analysed period according to the second alternative scenario	-2.9	-2.8	-2.6
Scenario 2. Lower growth rate of revenues by 1/5 in the analyzed period	-3.0	-3.1	-3.1
Scenario 3. Higher growth rate of expenditures by 1/4 in 2018 and 2019	-3.1	-3.2	-2.9

Source: Calculations of the Ministry of Finance

Under the third scenario, growth rate of budget expenditures is assumed to be higher by 25% in 2018 and 2019 in relation to the projected growth rate in the baseline scenario. As a result thereof, i.e. increase of budget expenditures by 5.2% and 5.6% in 2018 and 2019 respectively, budget deficit accounts for 3.1% of GDP in 2018 and 3.2% of GDP in 2019. Should projections for increase of both budget revenues and expenditures in 2020 remain unchanged, the budget deficit narrows, but is higher than the projection in the baseline scenario, as a result of the spillover effects of the previous two years.

Government of the Republic of Macedonia is prepared, should any of the presented scenarios occur, to respond appropriately, by adjusting the public spending, i.e. the budget expenditures, to a level necessary to retain the projected budget deficit rates.

Public Debt Risks. Uncertainty arising from the future trends of macroeconomic variables on the international capital market significantly affects the decision making for efficient management of debt portfolio of the country. In conditions of large oscillations of economic variables, need arises to actively manage risks which public debt portfolio in the Republic of Macedonia is exposed to. Main risks identified when managing this portfolio are re-financing risk, market risk, including interest rate risk and exchange rate risk, risk associated with contingent liabilities and operational risk.

Public Debt Sensitivity. In order to assess the exposure of the debt portfolio to market risk, i.e. interest rate risk and exchange rate risk, the impact of variation of interest rates and the exchange rate on the costs of servicing the external government debt were analysed. Sensitivity analysis is based upon the following assumptions: by changing one variable, all other variables remain unchanged, i.e. ceteris paribus, in conditions of possible currency movements in relation to the euro, Denar exchange rate in relation to the euro retains the stable value, and non-correlation between interest rate movements and exchange rate movements.

The analysis covers the period 2018-2020, being based upon scenarios of increase of interest rate by 1 p.p. and by 2 p.p. compared to the baseline scenario, as well as increase of euro appreciation and depreciation by 10% compared to the other currencies.

Table 3.7. Sensitivity analysis of servicing-related costs of the external government debt where there is change in the interest rates and the foreign exchange rates

Index figures	2018	2019	2020
Baseline scenario	100.0	100.0	100.0
Scenario 1: increase of respective interest rates by 1 pp.	106.0	106.6	105.8
Scenario 2: increase of respective interest rates by 2 pp.	112.0	113.2	111.5
Scenario 3: appreciation of other currencies of the portfolio in relation to the euro by 10%	101.2	101.6	100.5
Scenario 4: depreciation of other currencies of the portfolio in relation to the euro by 10%	98.8	98.4	99.5

Source: Calculations of the Ministry of Finance

Main conclusions under this analysis are the following:

- servicing-related costs on the basis of interest on external general government debt are sensitive to the interest rate movements. Should the interest rates in 2018 increase by 1 p.p., it would cause increase of the interest-related costs by 6%, or by EUR 5.3 million. Such sensitivity is a result of the exposure of the debt portfolio to the interest rate risk.

- future euro appreciation, i.e. depreciation, in relation to the other currencies in the portfolio (US dollar, Japanese yen and special drawing rights) by 10% will cause an increase, i.e. decrease, of servicing-related costs by 1.2% in 2018, i.e. by EUR 3.0 million. Possible unfavourable movements at exchange rates of other currencies in relation to the euro will not cause any more significant increase of the servicing-related costs, due to the fact that most of the external general government debt is denominated in euros.

3.7. FISCAL GOVERNANCE AND BUDGETARY FRAMEWORKS

In December 2017, the Government adopted the Public Finance Management Reform Program[29], following public consultation with representatives of international community, universities, civil society and other stakeholders. The program identifies key challenges in the management of public finances coupled with measures and activities with a timeframe for strengthening the public finance system and improving the efficiency and effectiveness of public spending. Seven priorities are established for this PFM Reform Programme:

- Priority 1: Improved Fiscal Framework,
- Priority 2: Revenue Mobilization,
- Priority 3: Planning and Budgeting,
- Priority 4: Budget Execution,
- Priority 5: Transparent Government Reporting,
- Priority 6: Internal Control,
- Priority 7: External Control and Parliamentary Oversight.

In order to monitor the implementation of the reforms within the Program, Public Finance Management Council is envisaged to be established, as a coordinating body of the Government of the Republic of Macedonia.

The Public Finance Management Council will be established with a Decision of the Government of the Republic of Macedonia, and will be chaired by the Minister of Finance.

Based on the Program, a Sector Planning Document and a draft Action Document with specific support projects under the IPA 2 instrument were prepared. Within the draft Action Document, which is currently in the phase of approval by the DEU, the following results are foreseen:

1. Improved budget system based on implementation of a new organic budget law,
2. Improved stability, efficiency and quality of revenue collection system (tax system and policy and customs system),

[29] http://finance.gov.mk/files/u3/PFM%20Reform%20Programme__EN%20DEC%202017_final%20Vlada.pdf

3. Improved legal compliance, efficiency and transparency of the public procurement system,
4. Strengthened internal control in line with the new PIFC Policy Paper,
5. Improved external audit efficiency.

In the meantime, Ministry of Finance has started activities to prepare a new organic budget law, which will include all planned reforms regarding medium-term budgeting, as well as setting up fiscal rules.

3.8. SUSTAINABILITY OF PUBLIC FINANCES

Calculations for long-term sustainability of public finances[30] are based upon the following assumptions:

- average labour productivity growth of approximately 1.8%;
- increase of male participation rate from 77.8% in 2016 to 86.3% in 2060;
- more intensive increase of female participation rate (from 50.8% in 2016 to 72% in 2060), by which share of female population in the total active population is expected to reach 45.5% in 2060;
- reduction of unemployment rate with higher intensity by 2030, projected at 12.9% in 2030, and with lower intensity in the remaining 30 years, whereby unemployment rate is projected to account for 5.2% in 2060;
- Gradual increase of the share of population above 65 years of age, reaching around 26% in 2060.

On the basis of the employment and wages growth projections, an average annual growth of 5.1% of revenues on the basis of pension insurance contributions is envisaged in the analysed period, however, their share in GDP is gradually decreasing, amounting to 4.9% of GDP in 2060. As for pension-related expenditures, it is worth mentioning that those of the Pension and Disability Insurance Fund are taken into account, while expenditures of the private pension insurance funds are not taken into account. Thus, share of pension-related expenditures in GDP in the period by 2030 is expected to maintain above the level of 8%, while, in the coming period, the share is envisaged to significantly reduce, if one takes into account that share of pensioners, having been paid their pensions in full from the first pillar, will decline, and share of the pensioners, to be paid part of their pensions from the second pillar, will rise. Public expenditures for health protection as percentage of GDP are projected to gradually increase and reach 6% in 2060. Such projected increase of expenditures is partially a result of the effects of population aging. Education-related expenditures are envisaged to increase by 5.7% on average annually in the next forty years, so their share in GDP is expected to reach 5.4% in 2060. Interest-related costs, as a share of GDP, are expected to gradually decrease and reach a level of slightly below 1% in 2060, in line with the projected trend of budget balance, i.e. government debt.

4. STRUCTURAL REFORMS IN 2018-2020

4.1. IDENTIFICATION OF KEY OBSTACLES TO COMPETITIVENESS AND INCLUSIVE GROWTH

In the first three quarters of 2017, economic activity in the country contracted by 0.4% in real terms, as a result of the prolonged political crisis that affected a significant decline in investments by 5.9%. Consumption registered 2.1% growth in real terms, driven by the increase in private consumption by 2.9%, while public spending decreased by 1.4%. Export of goods and services increased by 8.1% in the first three quarters of 2017, mainly driven by the increased export of machinery and transport equipment by 20.8% and chemical products by 15.7%. Import of goods

[30] See Table 7 in Annex 1.

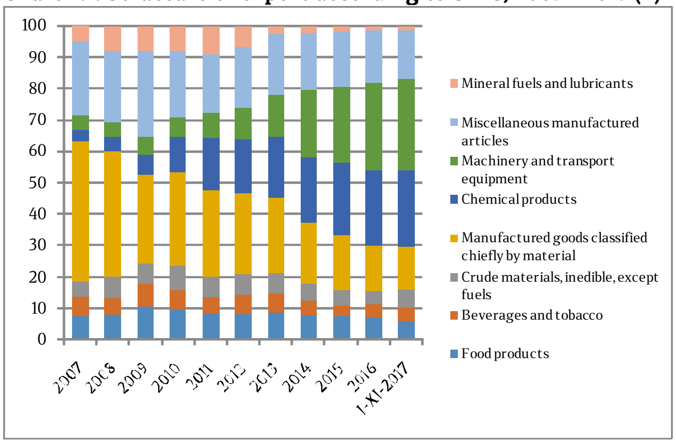
and services increased by 6.7% in the same period, whereby net export had a positive contribution to growth.

Analyzed by sectors, construction activity, being the driving force of economic growth over the past year, dropped by 11.5% in real terms in the first three quarters of 2017. Drop was also registered in industrial sector by 3.9%, while agriculture and services sector grew by 4.2% and 1.1%.

By overcoming the political crisis and establishing a new government in June 2017, already, at the end of the third quarter of the year, investor's sentiment started to improve. In the next period, the economy is expected to revive and intensify economic growth driven by growth of investments, private consumption, and exports.

As a small economy, Macedonia must develop competitive tradable goods with higher value that will drive exports. In the last decade, the structure of Macedonian exports has changed significantly in a positive direction, with more significant participation of products with higher level of finalization and at higher technological level, largely as a result of foreign direct investments. Thus, in the first nine months of 2017, the share of these categories of products in the total export reached almost 53%, compared to 10 years ago when it was 9.1%. In fact, export of traditional goods, such as ores or agricultural products, which are subject to external shocks due to price changes or climate change, is declining.

Chart 4.1. Structure of export according to SITC, 2007 - 2017 (%)



Source: MF calculations based on SSO data

Although the average growth of the Macedonian economy in the period 2009-2016 is 2.2% and is above the regional average of 1.5%[31], the growth rates are relatively low and reflect the low productivity primarily due to low investments of the private sector, low activity of the labor force and insufficient quality of education. In addition, promoting cheap labor does not lead to achieving high results, although the number of 17,000 employment in foreign companies cannot be ignored, bearing in mind that Macedonia still has an unemployment rate of over 20%. The effect of foreign companies is not sufficiently reflected in the domestic economy through transfer of modern technology, employment of highly educated personnel, transfer of knowledge and increased linkages with domestic companies.

Over the past few years, pressures have also been rising due to deteriorating fiscal discipline and rising public debt. Although it has one of the lowest public debt in Europe, which accounted for 39% of GDP in 2015, Macedonia has one of the fastest growing debt, which has doubled since 2008, since fiscal policy in recent years has been used to secure stimulus for short-term growth[32]. In order for the living standard of the Republic of Macedonia to converge with that of the EU Member States, real GDP growth should accelerate to around 4.5%[33] in the next 20 years.

Further improvement of the business environment and the conditions for growth led by the private sector are essential for maintaining growth and job creation. Macedonia has made significant progress in improving the business environment and the country ranks 11th out of 190

[31] World Bank Macedonia Policy Notes 2017
[32] World Bank Macedonia Policy Notes 2017
[33] Ibid.

economies according to the World Bank's Doing Business 2018 report. Despite the improvement of business regulations, domestic firms continue to face difficulties. Domestic firms have difficulty accessing loans and collecting claims, and are also burdened with various forms of unpredictable and ad hoc inspections that impose financial and non-financial costs[34]. Frequent legal changes also pose difficulties for the domestic business sector. The national legislation contains the principle of equal treatment of domestic and foreign investors, but in practice the support was largely provided for FDI. The existence of an informal sector creates unequal conditions for companies paying taxes and social contributions and adhere to the legislation. Bank lending is the main source of funding for companies in the country. Although this has increased in recent years (during the global financial crisis as well), SMEs continue to see access to finance as a major challenge in their operations. Alternative sources of funding are at an early stage of development, they could benefit from strengthening the legal framework, in particular factoring activities, which can be an important alternative to bank financing for SMEs.

The capacity of domestic SMEs to further integrate into the international markets is limited as a result of the relatively low management, financial and technical capacity. Having in mind that the geographical orientation of Macedonian export confirms the EU dominance as the main export destination, it is necessary to take measures that will allow companies to become competitive and take advantage of the Macedonian membership in the World Trade Organization and CEFTA, and in particular from the Stabilization and Association Agreement which allows trade without tariff barriers. Although Macedonia is a regional leader in trade policy and trade facilitation, there is room for improvements in transport and logistics that can improve trade performance by making the delivery of goods easier, faster and safer. Cross-border bottlenecks must be overcome in order to reduce costs and time for transport, which will directly contribute to the competitiveness of companies. Macedonia is a landlocked country and is particularly dependent on a well-developed transport network. One of the main challenges is to reduce the distance to export markets and reduce transport costs arising from the poor condition of transport corridors and large delays at border crossings.

Reduction of costs of energy used for production also has an impact on competitiveness. The electricity supply in Macedonia mainly relies on lignite power plants, which constitute more than 50% in total production. On the demand side, Macedonia ranks among the most energy-intensive economies in the Balkans due to the combination of energy-intensive industries (iron and steel, mining, cement), poorly isolated buildings and inefficient electrical appliances in households. According to the Global Competitiveness Report, although the overall quality of Macedonia's electricity supply is the highest in the SEE6 region (67 out of 168 countries), it still lags behind the EU member states. It is necessary to work on improving the supply side in combination with increasing energy efficiency and reducing distribution losses. Macedonia's integration on the regional energy market is necessary through investments in energy transfer and institutional development that will support market participation, in the direction of providing security in supply, sustainability and competitiveness.

To increase productivity, and hence competitiveness, companies need to focus on larger production with fewer resources, using modern technologies. In this regard, only innovations can provide success in the global market, which is becoming increasingly integrated. The latest indicators of the European Innovation Ranking List (2017) still categorize Macedonia as a "moderate innovator" compared to the other European countries. This ranking stems from the poor performance (below the EU average) in relation to several key indicators, although there is a

[34] Ibid.

steady progress in relative performance, by 10.4% between 2010 and 2016.[35] The Fund for Innovation and Technological Development provides opportunities for innovation and technological development of companies; however, capacities for absorbing grants for research, development and innovation should be developed, increasing cooperation between academic institutions and companies and increasing readiness for investment. Companies are more focused on buying new technology or innovative solutions, but the number and quality of products does not increase significantly.

Highly qualified human capital is a necessary prerequisite for increasing innovations of companies. Limitations related to skills are considered to be the most important challenges related to the labour force in Macedonia. Human capital is low and declines as measured by educational attainment and health indicators. The latest Program for International Student Assessment (PISA) results suggest that the quality of primary education and market relevance of the secondary education has deteriorated. Aligning labor market needs with labor force skills is a result of the ability of the education system to create knowledge that the labor market can absorb, thereby affecting not only to increasing productivity, but also to reducing unemployment.

Active labour market policies in recent years have helped to reduce unemployment. Macedonia is the only country in the region where the employment results are constantly improving from 2009. Employment grew by 2.5% in 2016 and by 2.7% in the first half of 2017. Most of the newly created jobs are linked to government-supported employment programs in trade, transport and manufacturing sectors. The unemployment rate dropped to 22.1% in the third quarter of 2017, which is the historically lowest rate. However, the reduction in unemployment is partly explained by the low participation rate in the workforce, which was around 57% at the beginning of 2017, the lowest rate since 2012. However, youth unemployment and long-term unemployment remain high at 46 and 81%[36], respectively.

Inequality among the citizens based on income is high in Macedonia, is the highest in Europe, and there is a growth tendency. The richest 1% in Macedonia make up 14% of the total income. The average personal income of these richest people is 14 times the average personal income in the country[37].

Growth in recent years has helped to reduce poverty largely due to the fiscal stimulus, which raises concerns about the viability of these gains. As a result of solid growth and improved labour market outcomes, Macedonia experienced a decline in poverty in the post-crisis period (2009-2016). Despite the significant reduction in poverty in recent years, nearly 100,000 people still live in extreme poverty in Macedonia. The current design of the social transfers is quite uneven and inadequate, and, as such, contributes to the deepening of inequality in the society. As regards the social protection services, it has been established that they are not tailored to the individual needs of end users, and that they should be provided in the community through further implementation of the process of deinstitutionalization, decentralization and diversification.

4.2. Summary of reform measures

Public finance management
Measure 1: Harmonization of the Public Procurement Legal framework with the Acquis
Measure 2: Improvement of Internal financial control
Energy and transport market reform
Measure 3: Increasing the competitiveness of the electricity market
Measure 4: Promotion of renewable energy sources and improvement of energy efficiency

[35] European Innovation Scoreboard 2017
[36] Labour force survey, SSO 2016
[37] http://www.finance.gov.mk/mk/neednakvost

Measure 5: Facilitating Macedonia-Serbia cross-border crossing
Agriculture sector development
Measure 6: Improving of irrigation systems
Measure 7: Consolidation and defragmentation of agricultural land
Measure 8: Agricultural cooperatives
Industry sector development
Measure 9: Supporting activities for attracting FDIs and investments by domestic companies
Measure 10: Support for Investments
Measure 11: Improving the competitiveness of domestic companies for new markets
Services sector development
Measure 12: Increasing competitiveness in Tourism & Hospitality Sector
Business environment and reduction of the informal economy
Measure 13: Development of a National E-Services Portal
Research, development and innovation (RDI) and digital economy
Measure 14: Improving infrastructure and access to finance for research, development and innovation
Trade related reforms
Measure 15: Trade facilitation
Education and skills
Measure 16: Further development of the qualification system
Employment and labor markets
Measure 17: Upgrading the active measures included in the Operational Plan for Active Employment Programs and Measures and Labour Market Services
Measure 18: Youth guarantee
Social inclusion, poverty reduction and equal opportunities
Measure 19: Enhancement of financial benefits in the field of social protection

4.3. ANALYSIS BY AREA AND STRUCTURAL REFORM MEASURES

4.3.1. PUBLIC FINANCE MANAGEMENT (PFM)

The Public Finance Management Reform Program 2018 – 2021 (PFMRP) was adopted by the Government on 19 December 2017. It was prepared taking into account the recommendations of the Public Expenditure and Financial Accountability Assessment[38] (PEFA), the SIGMA Report based on the monitoring of the implementation of the public administration principles including public finances[39], the WB Public Expenditure Review[40], the IMF's Mission Report under Article IV[41] and EC Progress Report[42].

The PFMRP envisages improvement in several segments of public finance, such as: strengthening and implementation of a mid-term budget framework including budget planning, introduction of an integrated information system for public finance management, improvement of the compliance, efficiency and effectiveness of the public procurement system, modernization of the tax system and improving tax collection, increasing the quality of customs procedures and services, further improving of public internal financial control and effectiveness of external audit.

Within PFM area we analyze the main obstacles in the public procurement system and the public internal financial control. The envisaged changes in other parts of PFMRP are described in point 3.7 Fiscal governance and budgetary frameworks.

[38] https://pefa.org/sites/default/files/assements/comments/MK-Dec15-PFMPR-Public.pdf
[39]http://www.oecd-ilibrary.org/docserver/download/5jm0xw47v6f7-en.pdf?expires=1482240711&id=id&accname=guest&checksum=1C97E0A6161202E211BFA2CADF076D90
[40]http://documents.worldbank.org/curated/en/895641468269982851/pdf/Macedonia-PER-2015-Revised-for-Submission-Final-clean.pdf
[41]https://www.imf.org/external/pubs/ft/scr/2015/cr15242.pdf
[42]https://ec.europa.eu/neighbourhoodenlargement/sites/near/files/pdf/key_documents/2016/20161109_report_the_former_yugoslav_republic_of_macedonia.pdf

The public procurement system regulates the use of public funds by public (state) authorities, in order to obtain the necessary resources from external, commercial sources. The tendency and purpose of the regulated process of using these funds is to achieve a fair process, fair participation of the business sector and best value for money.

The Law on Public Procurement (PPL) is based on the EU public procurement directives that were in force at the time of its adoption (2007). The EC reports, as well as the SIGMA reports, confirm that "the PPL is generally in line with the EU legislation".[43] However, since the adoption of the PPL, the compliance with EU requirements has not been improved, on the contrary, the level of compliance has been reduced by frequent amendments, in particular, from 2013 onwards. The frequency, nature and the scope of amendments may affect the legal certainty. On the other hand, this trend also reflected a very active interest of national authorities on the importance of public procurement legislation that, if coordinated constructively, could contribute to future strategic reforms.[44]

Another part within PFM area is effective internal financial control in the public sector that is the essence of good governance of public funds, which requires internal control to provide the necessary guarantees for achieving an optimal price and quality ratio in a lawful, financially responsible, ethical and appropriate manner.

Although the regulations in this area are generally good, they must be reassessed in order to increase managerial accountability through the use of modern management methods and measurement of efficiency, effectiveness, cost-effectiveness and transparency in using public funds and increasing the capacity of the administration in risk management.

With adoption of PFMRP the policy guidance 4, set out in the Joint Conclusions of the Economic and Financial Dialogues from 2016 and 2017, has been partially implemented. The envisaged changes related to prioritization of public investments according to clear policy objectives; greater transparency of the criteria for selecting investments and their impact on economic growth and fiscal movements are described in point 1.1. (under Guidance 4) and point 3.7 Fiscal governance and budgetary frameworks.

Measure 1: Harmonization of the Public Procurement Legal framework with the Acquis

Description of the measure

This measure aims to harmonise the PPL with directives 2014/24/EU, 2014/25/EU, EU Directive on Defense and Security Procurement and partially with the Remedies Directive 2007/66/EC. In fact, the existing remedy procedure system prescribed by the PPL is based on certain elements of the Remedies Directive, but several additional elements remain to be implemented, such as alternative penalties.

Two activities are planned: 1. Adoption of new PPL that shall introduce among other an obligation on contracting authorities to publish their annual procurement plans and 2. Professionalization of civil servants working with public procurement.

The publication of annual public procurement plans and their updates will lead to greater transparency of the overall process in the implementation of public procurement procedures.

The professionalization of civil servants working with public procurement will strengthened the capacities of the contracting authorities and economic operators in the implementation of the PPL, by systemic approach in organizing trainings and certification of public procurement entities, especially for the novelties provided in the new PPL.

[43] Report. Review of the Public Procurement System. SIGMA. April 2016.
[44] Final report on performance audit. SAO. 26.04.2017.

Activities planned in 2018

- Adoption of a new PPL along with a package of bylaws harmonized with the new directives and upgrade of public procurement software.

Activities planned in 2019 and 2020

- Professionalization of civil servants working with public procurement.

Responsible institution for implementing of activities is the Public Procurement Bureau.

Activity performance indicators and targets:

- Adopted new PPL with a package of bylaws harmonized with the new directives – 2018,
- Published procurement plans of the Contracting Authorities – 100% in 2020,
- Number of educated public procurement officers for requirements introduced with new legislation – minimum 300 civil servants per year.

Expected impact on the competitiveness/rationale of the measure

The new PPL harmonized with the directives will make it easier and cheaper for SMEs to bid for public contracts, will ensure the best value for money for public purchases and will respect the EU's principles of transparency and competition. It will also allow for environmental and social considerations, as well as innovation aspects to be taken into account when awarding public contracts, so that public procurement encourages progress towards particular public policy objectives. The new rules take a more holistic view of value for money, thus not only raising the question of minimizing cost, but looking at what else can be achieved through procurement.

Creating conditions for fair competition among economic operators in a great manner provides benefits to contracting authorities, as obtaining competitive bids can result in savings and rational utilization of public funds. The savings of public funds leave room for their allocation in other important fields.

Estimated cost of the activities and the budgetary impact

1. Adoption of a new PPL in accordance with EU directives – EUR 50.000 grant for technical assistance and upgrade of public procurement software to allow publishing of procurement plans of the Contracting Authorities – EUR 15 000 PPB Budget.

2. Professionalization of civil servants working with public procurement: 30.000 EUR per year.

Expected impact on employment and gender

With the new Law on Public Procurement, which will be harmonized with the EU Directives from 2014, SMEs access will be facilitated, green procurement, innovations, the principle of obtaining the best value for money spent in public procurement will be promoted, and at the same time ensuring principles of transparency and competition. The gender equality will be respected in the process of implementation of the measure.

Potential risks

Measure 2: Improvement of Internal financial control

Description of the measure

Managers in public sector entities have full responsibility in ensuring transparent and efficient management of public resources, through setting up an effective internal control system. This system will provide sound financial management in the public sector, aimed at directing and controlling the financial effects of working in a way that supports the achievement of goals. Thereby, the funds will be spent in a lawful, correct, cost-effective, economic, effective and efficient manner. In addition, the system should ensure the reliability and comprehensiveness of financial reports and protecting funds from losses caused by poor management, unjustified spending and utilization.

The introduction and implementation of the principles of good governance is a difficult and long-lasting process that not only requires a change to the national legislation on financial management control and internal audit but also the culture, the way of thinking, the mentality of the leaders of the budget users and their employees, while the difficulties that have arisen in the past from implementation of the Law on public internal financial control should be analysed and obtain direction how to improve good governance.

Activities planned in 2018

- Reassessment of policies in the area of public internal financial control.

Preparation of a new strategic document "Public Internal Financial Control Policies for the period 2018-2020" (PIFC Policy Paper 2018-2020) that will ensure sustainability of the strengthened managerial accountability and improve efficiency in public financial management through strengthening internal controls, strengthening internal audit, i.e. raising administrative capacities in the public sector at all levels.

Activities planned in 2019

- Harmonization of the legal framework for internal control in the public sector with the COSO (Committee of Sponsoring Organization of the Treadway) framework for internal control.

Adoption of a new Law on the system of internal controls in the public sector, which will further harmonize the legal framework with the COSO framework.

Activities planned in 2020

- Implementation of the new Law on the system of internal controls in the public sector.

Responsible institution: Ministry of Finance.

Expected impact on competitiveness/rationale of the measure

The planned public sector reforms are expected to affect the economic growth of the country in the longer term, by respecting the principles of "good governance", which basically means efficient management of public funds at all levels and production of visible values, which will contribute to creating better working conditions for the entire economy.

Estimated costs of the activities and budgetary impact

The planned activities will be financed with EUR 1 million grant.

Expected impact on employment and gender

The measure should contribute to an effective use of resources by the public sector and encouraging competition on the market that is crucial for creating better jobs. The gender equality will be respected in the process of implementation of the measure.

Potential risks

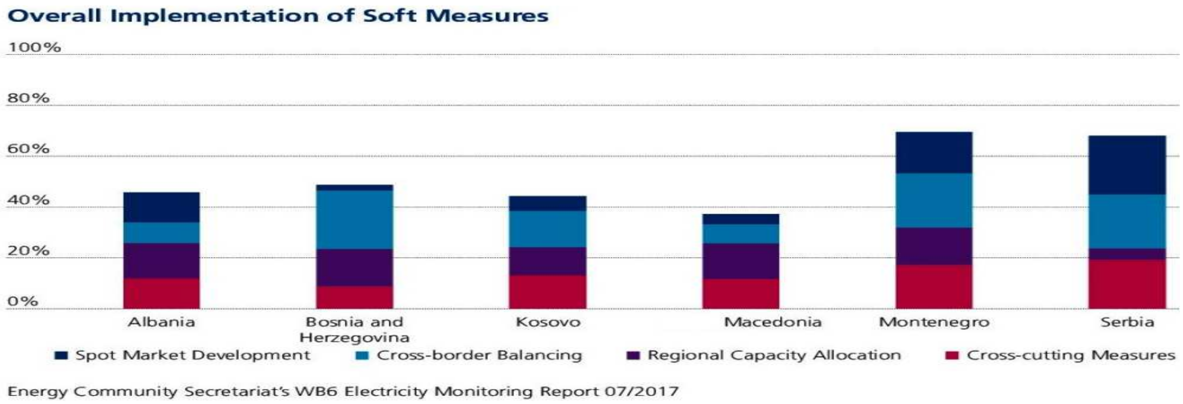
The risk in the implementation of the measures directly dependent on the success of implementation of closely related measures foreseen within the framework of Public Administration Reform Programme, Public Finance Reform Programme and measures related to fight against corruption.

4.3.2. ENERGY AND TRANSPORT MARKET REFORM

Energy market - The Republic of Macedonia has limited range of options for energy supply and is highly dependent on energy imports as demand has outpaced domestic supply. In the total amount of electricity for consumer needs for 2016, domestic generation accounts for 70.77%, while imports account for 29.23%. The total installed capacity of the power plants for generation of electricity for 2016 is 2,057 MW.

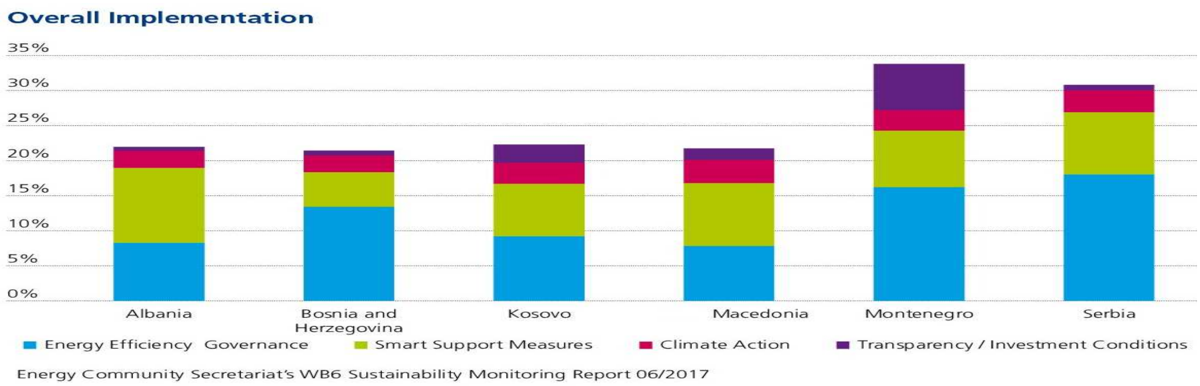
The Republic of Macedonia has high consumption of total energy per GDP compared to the developed countries, although it has low energy consumption per capita. The energy-intensity indicator expressed as the ratio between total energy demand per unit of GDP is worsened by 2% in 2016 (332 kgoe/1,000 euro in 2015, 338 kgoe/1,000 euro in 2016), indicating the energy efficiency as an important contributor to this trend. For comparison only in the EU-28, the total energy required per unit of GDP was 120 kgoe / 1,000 euro in 2015.

At the Summit for the Western Balkan Countries (WB6) in August 2015, the Republic of Macedonia signed a joint declaration on the establishment of the regional office for cooperation of the Western Balkans countries, agreeing to implement the so-called “soft” energy reform measures that are divided in four groups: 1) spot market development, 2) cross-border balancing, 3) regional capacity allocation of capacities and 4) cross-cutting measures. In the Energy Community Secretariat (ECS) Monitoring report Republic of Macedonia is assessed with low level of implementation of the energy reform measures, as shown in the chart.



The low level of implementation stems from the non-adoption of the Energy Law in 2015, which was to transpose the EU Third Energy Package, as well as the unrealized liberalization of the electricity market. According to the Report of the Energy Regulatory Commission for 2016, the percentage of liberalization of the electricity market is approximately 47% in 2016.

On 4th of July 2016 in Paris, within the framework of Summit for the Western Balkan Countries (WB6), the Republic of Macedonia signed the Sustainability Charter, for which the ECS has prepared a detailed Plan for the implementation of measures related to: improving the governance for energy efficiency, implementing the smart support measures that improve the sustainability of energy systems, fostering climate action and fostering transparency of sustainable energy markets. In the ECS Monitoring report Republic of Macedonia is assessed with low level of implementation of the measures deriving from the Sustainability Charter, as shown in the chart.



The preparation of a new Energy Law and the Energy Efficiency Law are underway, in which the provisions and obligations arising from the EU Third Energy Package, the Renewable Energy Sources Directive (new market-oriented support mechanisms) and the Energy Efficiency Directive shall be implemented, and these two laws should be adopted in the first half of 2018.

Transport market - The economic development of the Republic of Macedonia, as a small continental country, depends to a large extent on a well-developed transport network. The most important transport corridors in Macedonia are the Pan-European Corridor X, extending from north to south across the country (from the border with Serbia to the border with Greece) and Pan-European Corridor VIII, extending from east to west and connecting the port of Durres in Albania with the ports Burgas and Varna on the Black Sea in Bulgaria.

Road infrastructure is an important priority, since 85% of passengers and 91% of exported or internationally transported goods are transported by road traffic. Macedonian road network has a total of 14.182 km. Roads are classified as: highways (242 km), national roads (911 km), regional roads (3.771 km) and local roads (approximately 9.258 km). Road traffic is the key way for intercity travel, followed by railway network, which has a total length of 700 km and it is mainly used for travel along Corridor X.

Progress has been made in implementation of construction projects and projects for preparation of documentation for construction in relation to road and railway sections along Corridor VIII and X (Xd), as part of the indicative expansion of TEN-T network of SEE.

The completion of construction works along the section Demir Kapija-Smokvica will complete Corridor X as a motorway in the first half of 2018. The Corridor VIII road network is only 36% highway and requires further upgrading. The western part of Corridor VIII is currently expanding in level of highway. At present, the road connection is the only connection with Bulgaria and Albania. Although railway Corridor X is operational, activities for its rehabilitation are underway.

Road transport domination, especially in the transport of goods, leads to an increase in the delays at the border crossings and a reduction in the rapid flow of goods, which imposes the need for undertaking measures that will contribute to reducing the imbalance in transport by increasing the share of the railway transport.

Facilitating international rail transport by reducing the waiting time at border crossings by shortening border-crossing procedures in accordance with the one stop shop principle and will contribute to increasing the competitiveness of the railway transport.

The development of road and rail infrastructure is complemented with the implementation of horizontal measures, part of the connectivity reform measures.

The preparation of the national strategy for the transport sector to 2030 is underway and is expected to be adopted in the first quarter of 2018. The strategy is aimed at improving the economic efficiency, safety and accessibility of transport, environmental impact management and future transport activities and ensure integration with other sectoral policies.

Liberalization in the railway transport or, the opening of the market for the entry of a new operator has not yet been implemented entirely. For the purpose of harmonization with the EU legislation regarding the liberalization of the railway transport and creating an environment in which the national transport company will be ready for opening the market. The project "Business Segmentation in Macedonian Railways Transport AD-Skopje" is ongoing.

Measure 3: Increasing the competitiveness of the electricity market

Description of the measure

Adoption of the new Energy Law will enable fulfillment of the energy reform measures, removal of the main legal obstacles for the establishment of an organized electricity market, as well as further liberalization of the energy market. The establishment of a power exchange will enable reliable functioning of a liquid electricity market and creation of conditions for greater competition in the supply of energy to consumers in the Republic of Macedonia. The Government adopted an Action Plan for the establishment of a national organized electricity market (power exchange) and obligated JSC MEPSO to implement it, as an electricity market operator. The

Energy Community shall provide technical assistance for finding a viable and compatible solution for organizing a day-ahead electricity market and institutional arrangements suitable for coupling the national day-ahead electricity market with neighboring markets, as well as procedures for designation of Nominated electricity market operators (NEMO) in accordance with the EU CACM (Capacity Allocation and Congestion Management) Regulation. These activities will enable fulfillment of the energy reform measures from group 1.

The amendments to the Electricity Market Rules, which will be implemented from 1st July 2018, establish a national balancing market and non-discriminatory and cross-border market exchange of balancing services, which is fully market-oriented and applies to all market participants, including the regulated market segment. JSC MEPSO (TSO) will procure balancing services from the Balance Service Providers in national and in perspective from a regional balancing market at competitive conditions. The incumbent generation company JSC ELEM signed a Memorandum of Understanding with the ECS, which will provide technical assistance for improving their electricity trading capacities and developing business strategies for managing its electricity production and trading portfolios in order to be competitive on the electricity market, with a gradual deregulation of the generation price. This will enable fulfillment of the energy reform measures from group 2 and 4.

JSC MEPSO (TSO) signed a contract on 31st of May 2016 and became the founder and partner of the Coordinated Auction Office in South East Europe (SEE CAO), hence the process of coordinated distribution of the available cross-border transmission capacities on the Macedonian-Greek border was started. With the other adjacent system operators (Macedonian-Serbian and Macedonian-Bulgarian border) it will be realized when they join the SEE CAO. This meets the energy reform measures of group 3.

The responsible institutions are: Government of the Republic of Macedonia, Ministry of Economy, Energy Regulatory Commission, JSC ELEM and JSC MEPSO.

Activities planned in 2018

- Adoption of the Energy Law and secondary legislation (bylaws);
- Unbundling and certification of the transmission system operator in accordance with the Third Energy Package;
- Establishing a national balancing market and non-discriminatory and cross-border market exchange of balancing services;
- Adoption of Action plan for phasing out price regulation;
- Procurement of technical support and provision of a trading, clearing and settlement platform;
- Corporate plan for the company holding the activity-organized electricity market;
- Establishment of a company (power exchange);
- Designing trading strategies, portfolios and risk management solutions, taking into account the generations in each user;
- Code of conduct (compliance with legal and regulatory requirements).

Activities planned in 2019

- Training and education of staff on the way of working on the trading platform, as well as training of participants on the market;
- Rules for trading, clearing and contracts;
- Implementation of trading and clearing platforms;
- Selection of a settlement bank;
- Promotion of organized market;
- Provision of balancing services at the regional level.

Activities planned in 2020

- Functioning of an organized electricity market;
- Adhering to neighboring power exchange.

Expected impact on competitiveness/rationale of the measure

This measure will enable a liquid electricity market and create conditions for greater competition in the supply of energy, and further liberalization also has indirect effects on other economic sectors, which encourage increased productivity driven by competition in the energy sector and lower electricity prices. Detailed overview of the benefits in millions of Euros with the implementation of soft measures in the short and medium term is given in the OECD Report on soft measure evaluation.[45] In Part 3 Results of the economic analyses Table 1 – Overview of the results. All results are additional benefits in million EUR compared to the baseline scenario today (without the implementation of the respective soft measure). Y+1 is EUR 444,28 million and in Y+5 is EUR 1.903,04 million.

Estimated costs of the activities and budgetary impact

Technical assistance has been provided by donors and ECS for implementation of the new Energy Law and for preparation of the sub legislation.

For establishment of power exchange about EUR 1 million are planned, which would be provided from JSC MEPSO's own funds and donors.

Expected impact on employment and gender

Opening the electricity market positively affects employment, taking into account that the opening of new companies directly affects the opening of new jobs. The gender equality will be respected in the process of implementation of the measure.

Potential risks

Delays of adoption of the new Energy Law can lead to delay in the opening of the market, i.e. liberalization of the electricity market.

Measure 4: Promotion of renewable energy sources and improvement of energy efficiency

Description of the measure

Greater utilization of renewable energy sources (RES) and improvement of energy efficiency (EE) is one of the main strategic goals in the energy sector for the Government of the Republic of Macedonia. Improving energy efficiency and energy savings leads to a reduction in the final energy consumption, which directly affects the increase of RES share in the final energy consumption.

According to the RES Action Plan, the percentage share of RES in 2020 should be 23.9%, and should be achieved through construction of new RES plants, as well as reinforced energy efficiency measures. According to the Second Progress Report on RES, the share of RES in 2014 is 19.7% and in 2015 it is 19.9%. In accordance with the Sustainability Charter signed within the Western Balkans Summit (WB6), the Republic of Macedonia has committed itself to introducing market-oriented support mechanisms for the promotion of RES (auctions and feed-in premiums), which would be acquired in a competitive and transparent manner, and are prescribed in the new Energy Law.

The Government of the Republic of Macedonia will announce a public call for awarding 3-4 locations for the construction of photovoltaic power plants with a capacity of 20-25 MW, which will provide state land with regulated infrastructure and connection to the electricity grid. The

[45] The OECD Report on Soft Measure evaluation regarding the electricity market's reform priorities for the Republic of Macedonia

wind power plant Bogdanci (currently with installed capacity of 36.8 MW) will be completed with the construction of Phase 2 with capacity of 13.2 MW and production of around 35 GWh. Also, the Government of the Republic of Macedonia will announce a public call for construction of wind power plants with a capacity of 50 MW using feed-in premium at locations already determined to have potential for wind energy production.

It is necessary to adopt a Strategy for the renovation of buildings by 2050 and operation of an EE Fund, to support faster implementation of successful energy efficiency programs.

The responsible institutions are: Government of the Republic of Macedonia, Ministry of Economy, Energy Agency, Energy Regulatory Commission and JSC MEPSO.

Activities planned in 2018

- Adoption of the Law on Energy Efficiency;
- Bylaw regulation prescribing procedures for acquiring the right to feed-in premiums;
- Preparation of tender documentation for a public announcement with a model of a Feed-in Premium Agreement;
- Publication of a public announcement for bidding on the amount of the feed-in premium for determined locations;
- Preparation of the Strategy for the renovation of buildings by 2050;
- Further harmonization of the legislation for application of energy services contracts.

Activities planned in 2019

- Realization of a public announcement and concluding contracts;
- Initiation of construction of power plants using RES;
- Decision by the Government to determine which buildings of state bodies will be subject to reconstruction in 2019;
- Initial activities for establishing an EE Fund.

Activities planned in 2020

- Construction of power plants using RES;
- Functional EE Fund.

Expected impact on competitiveness/rationale of the measure

The implementation of the measure will ensure: diversification in supply, increased utilization of RES, reduction of greenhouse gas emissions and improvement of the general state of the environment and will help for the smooth transition of the country to low-emission, competitive economy. There are statistically determined indicators (study of Vivid Economics - Energy Efficiency and Economic Development, June 2013) on EE's positive contribution to economic development.

Estimated costs of the activities and budgetary impact

Technical assistance by donors has been provided for implementation of the Law on Energy and the Law on Energy Efficiency and bylaws for RES. The preparation of the Strategy for Building Renovation by 2050 requires EUR 400,000, expected to be provided by donor assistance. Through the World Bank, in the next period, technical assistance for the establishment of the EE Fund is planned to be provided.

Expected impact on employment and gender

Jobs in RES can be created directly and indirectly in the manufacturing and distribution of equipment, project management, installation, operation, and maintenance. By introducing EE measures, it is expected to engage highly qualified personnel who will be constantly engaged in monitoring consumption and proposing new saving measures. Gender equality will be respected in the process of implementing the measure.

Potential risks

Investors in RES can face the risk of changes in the market price of electricity, which can have a direct impact on their income by using feed-in premiums.

Unless the preparation of the Strategy for the renovation of buildings is started at the beginning of 2018, there is a risk of timely implementation of all other activities.

Measure 5: Facilitating Macedonia-Serbia cross-border crossing

Description of the measure

In order to reduce the crossing time at the Macedonian-Serbian border, the Government of the Republic of Macedonia and the Government of the Republic of Serbia, in February 2015, signed an Agreement on the establishment of border procedures. Protocols between the relevant services from Macedonia and Serbia (police, customs, inspection services etc.) were signed in June 2016, in accordance with the European Parliament and Council Directive 2012/34 of 21 November 2012 for the creation of a single European area.

With the construction of a joint railway border crossing in Tabanovce, an efficient cross border movement of passenger and freight traffic at the border crossing will be achieved by shortening the procedures for controls by the services of both countries by one stop shop principle.

The measure is rolled over from the Economic Reform Program 2017-2019. The envisaged activities for 2016 were fulfilled, i.e. in October 2016, the Steering Committee for monitoring and managing of Project activities, composed of all the involved institutions from the Republic of Macedonia and the Republic of Serbia, approved and accepted the Assessment of Official Staff Needs Report and the concept design.

In February 2017, the kick-off meeting was held for Phase 2 of the project. The development of the physical planning documentation, the Feasibility Study and the Environmental Report are being drafted. The crossing will be put into operation in 2021. By that time, the condition of the railway Corridor 10 on the territories of the Republic of Serbia and the Republic of Macedonia will be improved.

Activities planned in 2018

- Preparation of urban planning documentation, Feasibility Study and preparation of the main designs.

Activities planned in 2019

- Selection of the contractor, Supervision of the construction and signing of the contracts.

Activities planned in 2020

- Implementing the construction activities.

Ministry of Transport and Communications is responsible for implementation of the activities.

Expected impact on competitiveness/rationale of the measure

The greatest impact is expected to be in the time saving. Total travel time saved, as a result of the construction of the JBS Tabanovce may be expected to be 30 minutes out of 60 minutes per passenger train due to the fact that most controls will be done on the moving train, and 90 minutes per freight train out of 180 minutes.

Due to travel time savings as anticipated, the competitiveness of Corridor X will increase, especially for international transportation. As mentioned above more train operations (mainly freight) and more train operators may be expected to be operating on the network.

Companies performing transport activities will experience lower costs and lower transport times, which will create conditions for increased amount of transport by railway.

Estimated cost of the activities and the budgetary impact

Project preparation: EUR 380.000 grant – technical assistance.

Construction: around EUR 3.5 million - the funds are planned to be provided as an investment grant through the WBIF instrument in 2018.

Expected impact on employment and gender

The construction of the JBS will have short-term direct impact on employment by engaging construction workers. The gender equality will be respected in the process of implementation of the measure.

Potential risks

Prolongation of construction activities for completion of the railway border crossing (BC). Mitigation: regular monitoring of the implementation of activities for construction of the BC. The regional dimension of the measure contributes to reduce the risk of untimely implementation of activities.

4.3.3. SECTORAL DEVELOPMENT

4.3.3.1. Agriculture sector development

Agriculture plays an important role in the Macedonian society, with wide regional differences. Its share in the total gross value added (GVA) was 10% in 2015 (SSO) but went as high as 35% in the Southeast region and up to 20% in the Pelagonia, Polog, and Vardar regions. At the same time, its share in employment was 18% in 2015 and has been stagnant over the past years (SSO).

Job creation represents a high priority in Macedonia, and further modernization and development of the agri-food sector can generate a job creation and economic growth. Rural areas in Macedonia face many structural and socio-economic challenges. Huge rural areas remain depopulated and their resources unutilized, with negative economic, social and environmental consequences. The rural population has been stagnant over the last decade as a share in the total population, holding about 42% (SSO). Employment opportunities in rural areas are limited and dominated by agriculture as an economic sector. All these factors limit rural employment and economic growth.

Primary agricultural production remains caught in a low-productivity-low-income trap. Most agricultural producers are engaged in subsistence and semi-subsistence activities, registered as unemployed and have poor labor force mobility. The average physical size of a farm in 2016 was 1.8 ha and 2.1 LSU (livestock size units). The value added per agricultural worker[46], as a measure of productivity in agriculture, amounts to 19,127 in 2016 and is 2/3 of the EU average 29,425.

The arable land cadastre data indicate excessive land fragmentation where the average size of a privately owned parcel is 0.22 ha, while for the state-owned it is 0.56 ha. The consolidation of agricultural land will take place through the processes of exchanging parcels with or without changing their form, until the land borders are completely changed in order to obtain utilized arable land with proper form suitable for agriculture production. Additionally, an audit will be carried out for state agricultural land already granted and categorization of the land by quality, which will depend on the value and duration of the concession.

Widening agri-food trade deficit reflects the sector's competitive weaknesses. The country is a net agri-food importer, having had a negative trade balance for more than a decade. The agri-food trade situation continued to worsen in the last few years, in spite of an improvement in the general trade performance, overall. Only a few agri-food commodities, such as some fruits and

[46] https://data.worldbank.org/indicator/EA.PRD.AGRI.KD?locations=MK&year_high_desc=true

vegetables, wine, tobacco, and lamb, register a trade surplus. Thus, construction of modern storage facilities and distribution centers in the production regions for specific agricultural products with the capacity of over 5,000 tons will be financed, as well as creation and protection of products with a recognizable brand, a quality mark or mark for geographical origin.

Most processed food products are imported. Hence, agricultural policy will also be directed towards increasing the industrial-processing capacities that will be export-oriented and will produce products with higher added value.

Macedonia's increased vulnerability to climate change poses additional challenges to the performance of its farm sector. Climate change is already affecting the country and its adverse impacts are likely to increase over the next decades. Increases in the mean temperatures (by 2.5°C in the summer, by 2050) and water deficits (a decline by 17% in the summer, by 2050) are the risk factors most likely to manifest in the future (World Bank 2010). As reaction to the challenges with climate change, the agriculture will be distribute in regions according to the soil and climatic conditions of the areas for planned plant and animal production and lists of recommended crops and varieties will be made, taking into account the traditional production and the needs for watering. Additionally, arable land will increase by investing in hydro-melioration systems.

In order to provide healthy food to the citizens of the Republic of Macedonia and increasing the export, the VAT rate for veterinary drugs will be reduced, the registration of EU veterinary medical products will be undertaken, new accredited methods and accreditation of the laboratories will be subsidized which are engaged in the control of food safety export and domestic market.

Measure 6: Improving of irrigation systems

Description of the measure

This measure is rolled over from last year, the implementation details are presented in Table 11.

The new capital investments in construction of dams and irrigation systems already started and will proceed in the next period. Overall objective of irrigation investments is increasing of irrigated areas in the country on the level of installed capacity (144.000 ha), and gradual widening of irrigation systems to fulfill the objective irrigated land to be a half of total cultivated land (around 250.000 ha). Those capital investments will have direct impact over increasing of irrigated crop yields and physical agricultural production.

The activities are realized in accordance with the "Investment Plan for Water Management Master Infrastructure 2015-2025", which encompasses the following types of infrastructure works:

- Rehabilitation and reconstruction of installed infrastructure for irrigation and drainage in order to achieve their sustainability and water conservation;
- Upgrading and expansion of the existing hydro-system in order to increase the irrigated area in the country; and
- Construction of new major facilities in the Macedonian hydro-system.

Activities planned in 2018

- Continuing construction works on dam Konsko;
- Starting construction activities on dam Rechani;
- Starting construction activities on irrigation system Raven – Rechica;
- Finishing technical documentation for construction on dam on Slupchanska River, and starting procedure for issuing construction permit;
- Continuation of discussions and acting upon EIB's recommendations for loan approvement for construction of II stage - irrigation and III stage - energy of HS Zletovica;
- Starting construction activities for irrigation system in South Vardar valley project II stage;

- Preparation of technical documentation for construction of small irrigation systems up to 300 ha and construction work should start on three irrigation systems.

Activities planned in 2019

- Continuing construction works on dam Konsko;
- Continuing construction activities on dam Rechani;
- Continuing construction activities on irrigation system Raven – Rechica;
- Starting construction works on dam Slupchanska;
- Starting tendering procedure for construction of II stage - irrigation and III stage - energy of HS Zletovica;
- Continuing construction activities for irrigation system South Vardar valley II stage;
- Finishing technical documentation preparation for construction of small irrigation systems, and finishing construction activities of three irrigation systems.

Activities planned in 2020

- Continuing construction works on dam Konsko;
- Continuing construction activities on dam Rechani;
- Continuing construction activities on irrigation system Raven – Rechica;
- Continuing construction works on dam Slupchanska;
- Starting construction works on HS Zletovica II and III stage;
- Continuing construction activities for irrigation system South Vardar valley II stage;
- Starting new three-year IPA financing period for construction of small irrigation systems up to 300 ha.

Main contractor of this measure is Ministry of agriculture, forestry and water economy (MAWFE).

Expected effects on competitiveness/rationale of the measure

The implementation of the measure will increase the proportion of irrigated agricultural land from the current 4% to approximately 6% (from 20,575 to 32,275 ha) and will also improve the existing irrigation systems. Access to regular irrigation for farmers is expected to contribute for sustainability of the agricultural economy, as well as increased yields, which will also contribute to increasing the competitiveness of agricultural farms. Additionally, the measure will enable production of electricity through construction of hydropower plants, as well as provision of additional quantities of water for the hydro system "Rescue of Dojran Lake".

Estimated cost of the activities and the budgetary impact

The total cost of the measure for the period 2018-2020 is EUR 123 million, of which EUR 119.1 million are from the Budget of the Republic of Macedonia, and EUR 3.9 million are non-budgetary financing.

In million euros	2018	2019	2020
Construction of dam Konsko	10.1	10.1	9.7
Construction of dam Rechani	5.1	7.1	5.0
Construction of irrigation system Raven Rechica	5.2	5.2	2.3
Zletovica second and third stage	7.4	24.8	17.3
South Vardar Valley second stage	6.1	3.0	0.1
Preparation of tender documentation for construction of small irrigation systems up to 300 ha	0.3	0.6	3.0

Expected impact on employment and gender

The construction of hydro systems will have a direct short-term impact on employment, by engaging construction workers. There is currently no estimate for these jobs. Additionally, in the medium and long term, positive impact on employment is expected as a result of increased competitiveness of the agricultural sector.

The gender equality will be respected in the process of implementation of the measure.

Potential risks

Lack of financial resources, as well as a long process of obtaining the necessary permits and construction approvals.

Measure 7: Consolidation and defragmentation of agricultural land

Description of the measure

This measure is rolled over from last year, the implementation details are presented in Table 11.

The ongoing land consolidation activities are taking place within the IPA 2015 project "Implementing the National Land Consolidation Program". Potential land consolidation projects are in the phase of identification, based on a nationwide feasibility study and an assessment of the interest of landowners and other impact factors in micro locations across the country.

During the implementation of two pilot projects for consolidation in certain regions of the country in the period 2014-2016, a number of obstacles and inconsistencies in the existing legislation were found that prevent the implementation of consolidation of agricultural land in the procedures for allocation and exchange of land. For these reasons, amendments to the Law on Consolidation of Agricultural Land are being prepared and are expected to be adopted in 2018.

The expected effects of this process are the reduction of fragmentation of land parcels, their clustering, improved form of parcels for the application of modern techniques and production technologies, increased average size and providing access to new or rehabilitated irrigation systems and upgraded or newly built road infrastructure.

The activities are realized in accordance with the National Strategy for Consolidation of Agricultural Land 2012-2020.

Activities planned in 2018

- Adopt a revised and improved legal framework for the consolidation of agricultural land;
- Strengthening the capacities of the MAFWE, especially the regional units and the Sector for Consolidation of Agricultural Land exchange and identification of land parcels;
- Preparation of 12 feasibility studies (analysis of the current state) of selected micro locations as potential consolidation areas;
- Selection and training of service providers for the preparation of consolidation plans and infrastructure plans;
-Preparation of the procedure and methodology for preparation of consolidation plans and infrastructure plans;
- Preparation of 9 consolidation plans for selected consolidation areas;
- Implementation of the consolidation procedures in the pilot regions KO Konce and KO Egri.

Activities planned in 2019

- Selecting new areas with potential for consolidation of agricultural land;
- Continuation of the capacity building of the Ministry MAFWE, especially the regional units and the Sector for Consolidation of Agricultural Land, exchange and identification of land parcels;
- Preparation of new 3 feasibility studies (analysis of the current state) of selected micro locations as potential consolidation areas;
- Continuing training of service providers for the preparation of consolidation plans and infrastructure plans;
- Finalization of the consolidation in the pilot regions KO Konce and KO Egri;
- Implementation of new 4 consolidation procedures;
- Preparation of 4 infrastructure plans;

- Preparation of the procedure and methodology for analysis of the impact of the consolidation procedure on the environment and implementation of 4 environmental impact analyses;
- Preparation of National Program for Consolidation of Agricultural Land;
- Establishment of a system for monitoring and evaluation of the national program for consolidation of agricultural land.

Activities planned in 2020

- Continuation with the strengthening of the capacities of the MAFWE, especially the regional units and the Sector for Consolidation of Agricultural Land, exchange and identification of land parcels;
- Continuing the training of service providers for the preparation of infrastructure plans;
- Finalization of new 4 consolidation procedures;
- Finalization of 4 infrastructure plans and construction of the same;
- Finalization of 4 analyses of the environmental impacts in the areas where consolidation of agricultural land is carried out;
- Adoption of the National Program for Consolidation of Agricultural Land.

Expected impact on competitiveness/rationale of the measure

Improving the structure of agricultural holdings by consolidation of land parcels and that are larger and better shaped should facilitate the adoption of new agricultural technologies that will lead to an efficient agricultural sector. Benefits of land consolidation in EU countries include increasing farmers' gross income and reducing working time in this area.

Estimated cost of the activities and the budgetary impact

The total costs for implementation of the Strategy for Consolidation of Agricultural Land are provided from IPA II and FAO in the total amount of EUR 2,561,189 for the entire period of implementation, out of which EUR 914,809 in 2018, EUR 835,305 in 2019 and EUR 79,444 in 2020.

Expected impact on employment and gender

The results of various surveys of land consolidation projects show that many communities that have experienced land consolidation show an increase in the number of jobs created.

The new legal framework to support the implementation of the land consolidation procedures for agricultural land, especially emphasizes the gender issue, by providing mechanisms for inclusion of women in the decision making processes by guaranteeing their rights as co-owners (registered or unregistered) of agricultural land.

Potential risks

Long process of implementation of consolidation procedures and institutional and organizational readiness of the other state institutions and respected institutions in charge to accept and support the required procedures for implementation of consolidation of agricultural land. The risk of a lack of trust based on bad experience in the past will be addressed by a transparently driven land consolidation process with the enrollment of all participants in the consolidation area. Committing to the landowners consent for land consolidation output would further assist to overcome the recognized risk. The land consolidation approach that will be deployed is based on the best EU countries practices in implementation of land consolidation.

Measure 8: Agricultural cooperatives

Description of the measure

This measure is rolled over from last year, the implementation details are presented in Table 11.

The activities for support of the association of the farmers in agriculture cooperatives are part of project "Creation and support of agriculture cooperatives" and the measure "Economic association of agricultural holdings for joint agricultural activities" within the "Program for financial support of the rural development".

The establishment of agricultural cooperatives is envisaged in the National Strategy for Agriculture and Rural Development 2014-2020, aimed at improvement of the structure in the agriculture sector, improvement of the market position of farmers, increase of their negotiation power in relation to wholesale buyers, as well as getting lower prices for raw materials, machinery and investment assets.

In the Registry of agriculture cooperatives there are 39 registered agriculture cooperatives, of which 7 are cooperatives of a large size, and the other 32 are cooperatives of a small size, with a total capacity of 1,130 ha agriculture land, 1000 bee families, 450 cattle, 200 goats and 250 sheep.

Activities planned in 2018

- Encouraging the process of market-oriented association of farmers in agricultural cooperatives;

- Providing continued financial support for cooperatives (continuation of the implementation of the previous period);

- Support for investments in processing, finalization and marketing of agricultural products.

Activities planned in 2019

- Providing continued financial support for cooperatives (continuation of the implementation of the previous period);

- Support for investments in processing, finalization and marketing of agricultural products;

Activities planned in 2020

- Support for acquisition of Protected labels of quality of the agriculture and processed products;

- Providing continued financial support for cooperatives (continuation of the implementation of the previous period);

- Support for investments in processing, finalization and marketing of agricultural products.

Expected impact on competitiveness/rationale of the measure

Establishment of agricultural cooperatives is an opportunity for development of farms by promoting economic partnership in form of agriculture cooperatives, that through joint production, sale and marketing of their products, will strengthen their market role, increase competitiveness and efficiency, increase individual income of the farmer, and moreover will provide for qualitative production, assured sale and higher profits. As a result, the objective of horizontal integration of the entities involved in the sector of food production basically is oriented towards agricultural cooperatives as the most suitable way for improvement of supply chain of agricultural products.

Estimated cost of the activities and the budgetary impact

The total cost of the implementation is EUR 6,265,000, out of which EUR 2,645,000 in 2018, EUR 1,060,000 in 2019 and EUR 2,560,000 in 2020.

- Encouraging the process of market-oriented association of farmers in agricultural cooperatives and Providing continued financial support for cooperatives: EUR 845,000 in 2018, EUR 1,060,000 in 2019 and EUR 1,060,000 in 2020 from the state budget.

- Support for investments in processing, finalization and marketing of agricultural products: EUR 1,800,000 in 2018 and EUR 1,500,000 in 2020 from external donor.

Expected impact on employment and gender

Development of agricultural cooperatives will additionally contribute to the community by increasing and retaining jobs in agriculture and processing industry. The gender equality will be respected in the process of implementation of the measure.

Potential risks

The limited capacity of cooperatives can prevent modernization of production practices of members and transfer of new technologies into production.

4.3.3.2. Industry sector development

According to the preliminary data of the SSO for 2016, the industry sector accounts for 17.3% of GDP, with the manufacturing industry accounting for 12.2%. Although in the past years the structure of the industry gradually shifts towards production of products with higher technological value, it continues to rely heavily on production of traditional sectors such as textile, food, mining and metal processing industries. In 2016, the manufacturing industry accounted for 82.9% of the total industrial production, while Mining and Electricity, gas, steam and air conditioning supply accounted for 9.1% and 7.9%, respectively. Within the manufacturing industry, food and beverage production accounted for 15.9%, textile and clothing production for 12.6% and production of metals and fabricated metal products for 8.9% of the total industrial production. As a result of the opening of new capacities, primarily in the technological and industrial development zones, the production of machines and devices reached 10.9%, and together with the production of motor vehicles (6.5%) and the production of electrical equipment (4, 9%) constitute more than a fifth (22.3%) of the total industrial production.

The domestic market is relatively small and does not offer sufficient space for growth of the economy. Therefore, the alternative is seen through expansion of exports of domestic companies and access to foreign markets. In order to promote exports, domestic companies lack support for product innovation and diversification, for finding suitable business partners in other countries, presenting their production on foreign markets.

The UNIDO Competitive Industrial Performance Index (CIP)[47] is a good indicator of the capacity and potential of the industry. Industrial competitiveness is defined as the capacity of states to increase their presence on international and domestic markets while developing industrial sectors and activities with higher added value and technological composition. According to UNIDO, the Macedonian industry index is 0.028 in 2015 (latest available data). For example, Germany has the highest CIP index of 0.541.

The problems facing the industry are the dependence on imports of raw materials and intermediary goods, export of products where the price is the primary driver of competitiveness, insufficient development of clusters, insufficient development of managerial and marketing skills, etc. Significant problem is the lack of cooperation between scientific and educational institutions and industry, as well as poor compliance of educational programs with the needs of the labor market, resulting in a lack of adequately trained workforce.

Although several industrial capacities, mainly FDIs which diversified industrial production, opened up in the country in the past period, the spillover in the domestic economy is limited and the expected multiplier effect of cooperation with domestic companies is still low (less than 1%).

The national regulation contains the principle of equal treatment of domestic and foreign companies, but in practice the support was largely provided for FDIs. In order to ensure the broad benefits and sustainability of the growth strategy, it is necessary to remove barriers that the domestic private sector faces.

At the moment, the existing Industrial Policy of the Republic of Macedonia 2009-2020 is being revised along with an analysis of the achieved effects and improvement/revision of the strategic framework for supporting the industrial development of the country.

[47] United Nations Industrial Development Organization, Industrial Development Report 2018

Measure 9: Supporting activities for attracting FDIs and investments by domestic companies

Description of measure

The national legislation contains the principle of equal treatment of domestic and foreign investment companies, but in practice the support was more extensively ensured for FDIs. Within the Economic growth plan, adopted by the Government in December 2017, the equal treatment of domestic and foreign investors is being reinforced. The priority of this measure is given to increase domestic private investments, efficiency, productivity and competitiveness of the private sector, which is in line with the Government Programme 2017-2021, as well as the national Competitiveness Strategy and its Action Plan 2016-2020.

The activities for implementation of this measure will focus on attracting FDIs, support of investment by domestic companies and support of "brown-field" investments.

Activities planned in 2018

Activity 1: Introduction of legal, financial and organizational framework for implementation of support activities.

Activity 2: Support of new FDIs and domestic companies that will invest in new (green-field[48]) investment in addition to the existing "support package" (ex. tax exemptions) implemented for investments projects in the zones.

The support will be granted as following types of financial support:

Activity 2.1. Support for newly created jobs and newly created jobs with higher salaries, where the amount of financial support will depend on the amount of the salary for the new jobs;

Activity 2.2. Support for establishing and improving the business cooperation of FDIs with Macedonian suppliers, where business cooperation with domestic companies will be measured according to the share (percentage) of the total inputs of products/services supplied from domestic (Macedonian) companies.

Activity 3. Support for purchase of the assets of firms under insolvency or liquidation. The measure envisages providing grant reimbursement of 10% of the amount used for purchasing assets of company under insolvency or liquidation. The funds will be reimbursed after the restarting of a factory.

Activity 4. Support for investment projects with major economic impact of domestic economy. This activity envisage support for investment projects with huge impact upon the development of some industrial branches and/or sectors of Macedonian economy, or which will likely lead towards inclusion of domestic firms in international value chains. For attracting FDIs with total annual revenue higher than billion dollars, additional types of support will be created.

Activities planned in 2019 and 2020

Activities 2, 3 and 4 shall continue in 2019 and 2020.

Expected impact on the competitiveness/rationale of the measure

The measure shall lead to more competitive economy. The expectations will be fulfilled through various activities referring to FDI support and creation of linkages with domestic investment projects and businesses, as well as the investment of effort and finances for creation of high paid jobs. Boosting the cooperation between FDIs and domestic companies, shall also lead to expansion of the supply chain. It is also expected that expansion of the supply chain will lead to internationalization and increased capabilities for export of domestic companies (and capacities

---

[48]"Greenfield investment" includes new facilities on new locations, or new facilities within existing locations (production sites) of companies.

in some cases). Overall, the measure will contribute to the development of the economy by increasing the competitiveness lead by the stable companies with solid balance sheets and positive results.

Estimated cost of the activities and the budgetary impact

The planned amount for the measure is around EUR 20 million per year or around EUR 80 million for 4 years.

Expected impact on employment and gender

This measure is designed to encourage employment of high skilled labour force to high quality and well paid jobs. In the past 10 years via implementation of supporting activities for FDIs around 10.000 jobs were created.

The gender equality will be respected in the process of implementation of the measure.

Potential risks

Coordination between institutions that will implement the measures, the companies' interest in utilizing the measures. Regular communication between the institutions and continuous monitoring of the implementation of the measures.

Measure 10: Support for Investments

Description of measure

One of the main principles of the Economy growth plan is to boost the Macedonian economy and its growth. Support of domestic companies shall be improved in order to make them more competitive in foreign markets, primarily in the Western Balkan region. The rationale of the measure is to support the entities capable to increase private investments, efficiency, productivity and competitiveness of the domestic private sector. The measure is in line with the Government Programme 2017-2021, as well as the national Competitiveness Strategy and its Action Plan 2016-2020.

Activities planned in 2018

The activities focus on support of investments by domestic companies, creation of stronger linkages for technological cooperation between domestic companies and FDIs, as well as with scientific, R&D institutions and universities (clustering), stimulation of innovation and technology modernization. More precisely, the following activities are envisaged:

Activity 1: Introduction or improvement (revision) of the legal, financial and organizational framework for implementation of support activities.

Activity 2: Support for investment for growth. Through this activity the companies increasing the number of employees and total operational revenues above the average number of employees in the previous 3 years will be incentivized.

Activity 3: Support for growth of SMEs. Through this activity SMEs will be incentivized to: obtain quality certificates (HACCP, HALAL, ISO, etc.); purchase equipment and specific software; cover the costs of training and professional development of employees; incentives for initiatives/projects on improving the access to finance for SMEs.

Activity 4: Support for transfer and/or establishment of R&D and innovation departments in companies established in the country. This activity introduces incentives for innovation activities and R&D in Macedonian companies through a range of incentives (reimbursement of 50% of eligible costs of industrial R&D, from which 30% will be reimbursement of the value of the new equipment for the company user).

Activities planned in 2019 and 2020

Activities 2, 3 and 4 shall continue to be implemented.

Expected impact on the competitiveness/rationale of the measure

The measure shall stimulate investment in technological development, which will have effects on companies productivity, profitability and competitiveness at domestic, as well as foreign markets.

Estimated cost of the activities and the budgetary impact

The planned amount for the measure is around EUR 5 million per year or around EUR 20 million for 4 years.

Expected impact on employment and gender

Expected direct impact of this measure is employment of highly skilled labour force, and support of the employers with reimbursement of the cost for R&D, including the salaries of the workers in R&D departments. This measure also contributes to retaining the young highly educated people in the country and lowering the impact of brain drain.

The gender equality will be respected in the process of implementation of the measure.

Potential risks

Companies' readiness to undertake such investments is one of the risks envisaged for the implementation of this measure. Coordination between the institutions that will implement the measures, the companies' interest in utilizing the measures. Regular communication between the institutions and continuous monitoring of the implementation of the measures.

Measure 11: Improving the competitiveness of domestic companies for new markets

Description of measure

The measure covers supporting domestic companies for: product innovation and diversification, finding appropriate business partners in other countries, presenting their production on foreign markets, etc.

Activities planned in 2018

Activity 1: Financial support for companies which will improve their competitiveness on new markets. The eligible companies will be granted financial support in the amount of 10% of the direct investment costs for increasing the competitiveness on new markets. Additionally, if the new markets are within the Western Balkan countries, the financial support will be increased by additional 10%.

Activity 2: Support in finding partners and access to new markets. Under this activity support will be provided for presentations of companies at business fairs in other countries, business and political missions to foreign countries, B2B meetings, analyzes of foreign markets, certification of products in accordance with the needs of foreign markets. The implementation of this activity is in line with the mission of the Enterprise Europe Network that helps businesses to innovate and grow on an international scale, and the efforts do not exclude any support to companies.

Activities planned in 2019 and 2020

Activities 1 and 2 from 2018 will continue in the next two years.

Expected impact on the competitiveness/rationale of the measure

Support activities in this measure are expected to facilitate access to new markets for domestic companies, which is expected to lead to increased production and new investments in production facilities.

Estimated cost of the activities and the budgetary impact

The planned amount for the measure is around EUR 5 million per year or around EUR 20 million for 4 years.

Expected impact on employment and gender

Facilitating access to new markets and expanding production is expected to contribute to job creation and employment growth.

The gender equality will be respected in the process of implementation of the measure.

Potential risks

Coordination between the institutions that will implement the measures, the companies' interest in utilizing the measures. Regular communication between the institutions and continuous monitoring of the implementation of the measures.

4.3.3.3 Services sector development

The services sector of the Macedonian economy has the highest share in GDP with over 50%. The sector registered growth of 3.9% in 2015, whereas the highest contribution to the growth was recorded in the wholesale and retail trade with real growth rate of 7.3%. The services sector also employs the highest number of employees in the economy with a share of over 50% in 2015. Within the service sector the major activities supported are related to digital society and closely related to it – the creative industries[49], as well as tourism.

Tourism and hospitality. Macedonia has good tourism potential, but it lacks an adequate approach towards planning and management of tourism development in the country. A limiting factor is the delay in the adoption of the new tourism development strategy, as well as the low level of realization of activities set in the previous strategy for 2009-2013.

The total contribution of travel and tourism to the country's GDP, employment, and total capital investment in 2014 was relatively small (5.2%, 4.7%, and 2.2%, respectively) in comparison with other countries in the region (WTTC 2015). Capital city Skopje and UNESCO-protected Ohrid ski and resorts such as Mavrovo and Popova Sapka remain the key tourist attractions in the country, complemented by rural, alternative and cultural heritage tourism.

The country needs comprehensive approach and streamlined action in the sector Tourism where several actions are implemented over the past year and will continue in the following one. Increasing the tourism and hospitality capacities as well as improving their quality and efficiency are challenges that are expected to be overcome by the new Tourism Strategy. Moreover, all the analyses shows that tourism sector faces problems when it comes to clear and targeted promotions, capacities to absorb the incoming tourist and needs of better destination management approach.

Number of tourists and nights spent

	Category	2015	2016	2016, August	2017, August
Number of tourists	Domestic	330,537	346,359 (+4.8%)	266,119	283,656 (6.6%)
	Foreign	485,530	510,484 (+5.1%)	351,031	430,818 (22.7%)
	Total	816,067	856,843 (+5.0%)	617,150	714,474 (+15.8%)
Number of night spent	Domestic	1,357,822	1,407,143 (+3.6%)	1,195,597	1,247,627 (+4.4%)
	Foreign	1,036,383	1,054,017 (+1.7%)	733,682	899,588 (+22.6%)
	Total	2,394,205	2,461,160 (+2.8%)	1,929,279	2,147,215 (+11.3%)

Source: State Statistical Office

Measure 12: Increasing competitiveness in Tourism & Hospitality Sector

Description of the measure

This measure is rolled over from last year, the implementation details are presented in Table 11.

[49] The specific measure for creative industries from ERP 2017 – 2019 is not proposed in ERP 2018 – 2020 because there are some delays in the implementation. However, the creative industries are supported by various means in general by the national institutions.

The measure will provide assistance and capacity building to enhance the business environment and skills along with targeted investments in infrastructure, support to tourism activities and promote destinations, and will help foster linkages with related industries and SMEs. The project will support a limited number of potential tourism destinations in the country over a _ four-year period through a combination of infrastructure investments, technical assistance, and capacity building support to public sector and non-state sector entities. This is expected to result in an improved enabling environment for private sector investments, including the establishment of regional tourism destination management structures.

This measure is comprised of the following:

I. **Local and Regional Competitiveness in tourism** is a four-year operation for financing investments in tourism-related infrastructure and services at destinations. Large and small-scale investments will be supported at selected tourism destinations in order to upgrade the product offer in terms of attractions, sites, and general visitor experience. The objective is to enhance the contribution of tourism to local economic development and improve the capacity of the Government and public entities to foster tourism growth and facilitate destination management.

The investments include: 1/Restoration of cultural and natural heritage sites, facades of traditional and historic significance buildings (buildings of historic value and/or traditional architecture); 2/Rehabilitation of municipal infrastructure and utilities in the central historic areas (historic cores) and publicly owned vacation facilities; 3/Improvement of access roads to sites and attractions, landscaping and public parking; 4/Signposting; 4/Upgrading public spaces and cultural buildings, ski and spa resort facilities; 6/Mapping and upgrading of hiking and biking routs and trails; and 7/Construction or rehabilitation of tourist information kiosks and offices, and public toilets.

II. **Programme for increasing market employability** consists of implementing activities for increasing the competitiveness of SMEs in tourism. Three tourism destinations Ohrid, Mavrovo and Krusevo will be assisted to exploit the full potential of their historical, natural and cultural heritage through the University of St. Galen's methodology for collaborative destination management, improved service delivery and enriched touristic offer.

The National Agency for Promotion and Support of Tourism and Macedonian travel agencies will continue to promote and support the tourism sector in Macedonia through targeted promotion on international markets, which should improve the competiveness of the tourism sector on national level.

Introduction of new and upgraded services such as rescue, insurance, parking etc. will add value to Krusevo's tourism offer and will be incorporated in the tourist offer, thus creating the basis for commercially sustainable business model and creating competitive advantage of Krusevo as paragliding destination.

Consolidation and strengthening of the tour guide sector through interactive IT platform that will have wider impact on Macedonian tourism industry. Establishing global standards in the tour guide sector (digital registry of licensed tour guides, criteria of reviewing licenses, rating system, online reviews, etc.) will indirectly help in development and access to new markets and will support the efforts of the country to reveal new destinations for active tourism.

Activities planned in 2018

- Establishing the Destination Management Process

- Implementation of large infrastructure and small-scale investments sub-grants under the Grant Scheme

- Strengthen the implementation capacity of key government entities and the private sector and civil society organizations to play an active role in tourism development in Macedonia.

- Improved access to international markets (Destination Ohrid scaled up to export)

-Improved destination management in order to access international markets for paragliding (Destination Krusevo),

- Improved tour guide services and visibility of tour guides to travel agencies.

Activities planned in 2019:

Activities commenced in 2018 will be completed.

Activities planned in 2020

The second phase of the Increasing market employability project is expected to take over.

Expected impact on competitiveness/rationale of the measure

The expected outcomes are oriented towards the local economic growth, but also towards the improved productivity, service quality, linkages and innovation.

Following the trends from the recent years, the key indicators in tourism sector is envisaged to reach following targets:

- Number of tourists - continued growth by 5% annually, reaching 1.000.000 tourists by the end of 2019 (out of which 50% foreign tourists),
- Overnight stays - continued growth by 3% annually, reaching 2.700.000 by the end of 2019.

Estimated cost of the activities and the budgetary impact

The total funds for implementation of the measure in the next three years amounts to EUR 17,900,000, provided by IPA funds with a national contribution and an external donor. For 2018, the funds amount to EUR 9 million, in 2019 EUR 7.9 million, and EUR 1 million in 2020.

Expected impact on employment and gender

New jobs will be created along the whole tourism value and supply chain and it is expected higher participation of young people and women. It is also expected that actions will produce spillover effect to other industries and sectors in their further growth and development (e.g. education, trade, transport etc.).

Considering that the gender disparities can be found mostly in the rural areas, this measure can potentially have a positive impact on female activity rates.

Potential risks

The overall risk of the measure is moderate. Significant risks that may arise are the following: 1/ risks related to the management of the measure and change in the level, as well as the continuity of support of the implementing agency and the public entities that are beneficiaries of the measure, 2/ low level cooperation between stakeholders and limited capacity to implement the measure, and 3/ potential risks of inappropriately used assets.

Measures to overcome the risks include: strong communication with institutions, private sector, civil society and other relevant stakeholders in order to maintain a broad platform to support reforms that will help overcome the risk of inadequate management of activities; capacity building of public sector agencies and substantial technical assistance for agency coordination and public-private dialogue; direct monitoring of the available and spent resources and linking with relevant decision makers in order to avoid bottlenecks in the implementation of activities.

4.3.4. BUSINESS ENVIRONMENT AND REDUCTION OF THE INFORMAL ECONOMY

Through a series of measures undertaken in the past years, Macedonia has significantly strengthened its business environment, but there is still room for further improvement. In the latest World Bank business report "Doing Business 2018", Macedonia ranks 11th among 190 economies. Macedonia is best ranked in the area of Protecting minority investors (4th place), Getting credit (12th place), Starting business (22nd place), etc. However, areas such as Registering Property and Getting Electricity still have room for improvement.

Despite being a small landlocked economy[50], Macedonia is relatively competitive and dynamic compared to its regional peers. The private sector mainly consists of SMEs accounting for 99.8% of the total number of active enterprises. SMEs are the dominant type of enterprises. Because of their high share in the total number of enterprises they are important source of employment, investment and significant creators of GDP. The growing number of SMEs absorbs the majority of the workforce and contributes to reducing the unemployment. SMEs contribute with 76.6% of the total employment and 66.6% of the value added.

For a business environment that will enable more dynamic growth, it is necessary to pay particular attention to the following:

- Frequent legal and regulatory amendments in the past period has created an unpredictable environment for both domestic and foreign companies.
- Despite the low tax burden, companies complain about the so-called parafiscal charges, especially micro and small enterprises indicate that these payments do not take into account the size of the firm. Often there are overlaps on the same charges at central and local level, and an additional problem is the fact that for some of the charges there is no clear purpose why are they used and what do the finance.
- Opaque interpretation of business regulations, notably by local administrations, uneven enforcement of rules and contracts, as well as corruption and the large informal economy hamper private sector development[51].
- Macedonia’s large informal economy (estimated by SSO at around 17% of total output) creates an unleveled playfield with formal businesses that comply with the taxes, contributions, and regulations. In fact, approximately 30% of companies indicate the informal sector as their primary constraint to growth[52].
- SMEs in the SEE region no longer identify access to finance as the primary limitation for business development, and point to a lack of programmes for strengthen financial literacy and investment readiness, especially for newly established enterprises. [53]

The country lacks a National Strategy for Development of SMEs. The preparation of a new SME Strategy is in its final stage and is expected to be adopted in the first quarter of 2018. A Strategy for Formalizing the Informal Economy 2018-2022 is being prepared, which is expected to also be adopted in 2018.

E-services. There is currently no single central gateway for accessing government e-services with a higher level of sophistication, and users of government e-services access e-services in a non-unified manner. The portal for e-services www.uslugi.gov.mk is outdated and provides only informational services. On the other hand, a significant number of institutions offer their services electronically on their web portals. However, electronic identification and payment of e-services are inconsistent for all services, thus creating confusion and discouraging the use of e-services. According to the recommendations outlined in the SIGMA report for 2015, the Ministry of Information Society and Administration (MISA) should modernize the public services portal.

[50] Assessing the implementation of the European Small Business Act
[51] European Commission Progress Report of the Republic of Macedonia 2016
[52] World bank Policy notes 2017
[53] Assessment framework for research, development and innovation Competitiveness in South East Europe A POLICY OUTLOOK, 2018

One of the main priorities of the Government of the Republic of Macedonia is the increase in the quality of administrative services, and in that direction, amendments to the Law on General Administrative Procedure (Official Gazette of the Republic of Macedonia No. 124/15) have been made in order to improve the provision of public services through fully coordinated and integrated public administration activities.

Since administrative procedures for providing public services are complex processes that involve the exchange of evidence and data between the institutions ex officio, the establishment of the Catalogue of Public Services will help in the implementation of the Law on General Administrative Procedure in the direction of systematic data management for each of the public services, in accordance with the prescribed legal provisions. The Catalogue of Public Services will be used to digitize the services, simplify the processes (administrative guillotine, cutting red tape, etc.), and above all to develop new and improve existing e-services for citizens and businesses.

Measure 13: Development of a National E-Services Portal

Description of the measure

The measure envisages activities for development of a dynamic e-services web portal (National e-services Portal), as a single contact point with state bodies according to the one-stop-shop principle and the use of standardized user interfaces. The visual design of the portal, ease of use, easy navigation and use of W3CG standards are particularly important. The goal of the e-services portal is to increase the efficiency of state institutions and provide faster and simpler services by creating a single contact point between citizens and businesses (e-service users) and service providers and by implementing a solution that will allow electronic data exchange between institutions in order to accelerate the e-services delivery process.

The e-services portal is closely connected with the current activities on interoperability, the National Population Register/Central Electronic Population Register, the Catalogue of Services, as well as establishing Halls for single point of services, and harmonization with EU legislation[54].

The catalogue of services will cover all public services, data and evidence necessary for the realization of these public services, legal deadlines for the provision of services, distinction of data and documents that will be obtained ex officio and those that citizens and legal entities will have to attach to the requests, legal remedies for each of the services, the level of fees and taxes for the service, etc. A software solution for managing the Catalogue has already been developed, and so far it has included data on 199 services from 26 laws. The Catalogue of Public Service will contribute for improved records and overviews of public services provided by state institutions and unification of services.

Activities planned in 2018

- Entering data on services from remaining laws in the Catalogue of services;
- Qualitative analysis on data entered in the catalogue (administrative guillotine),
- Revision and amendments of the Law on electronic management and its bylaws;
- Adoption on the Law on e-services and its bylaws;
- Development of new electronic services;
- Launch and promotion of the National e-services Portal;
- Training for public sector employees - users of the portal.

The activities will be implemented by the MISA in cooperation with other institutions.

[54] Relevant EU acquis (Regulation 910/2015 and its implementing acts, Directive 95/46 and Regulation 2016/679, and Directive 2003/98), as well as policy documents (EU eGovernment Action Plan 2016 – 2020, updated European Interoperability Framework, EU eGovernment Report 2016); Law on Electronic Management and its by-laws, Law on Data in Electronic Form and Electronic Signature, Law on General Administrative Procedure etc.

Activities planned in 2019

- Analysis of the use of the National e-services Portal;
- Promotion of the National e-services Portal;
- Trainings to public sector employees about the amendments in the Law on Electronic Management and Implementation of the Law on Electronic Services;
- Training for public sector employees - users of the portal;
- Qualitative analysis of data in the Catalogue (administrative guillotine).
- Analysis for linking the Catalogue of Public Services with the National e-services Portal for the purpose of automated changes to the processes of the Portal based on changes in the Catalogue and providing recommendations.

The activities will be implemented by the MISA in cooperation with other institutions.

Activities planned in 2020

- Linking the Catalogue of Public Services with the National e-services Portal.

The activities will be implemented by the MISA in cooperation with other institutions.

Expected impact on competitiveness/ rationale of the measure

The National e-services Portal is expected to reduce administrative burden on citizens and businesses and increase the efficiency of businesses. Reducing the time for obtaining the services entails a reduction in costs for businesses, leading to their increased competitiveness.

Estimated cost of the activities and the budgetary impact

The estimated cost for the development of the National Portal is EUR 518,980. The cost of the service catalogue is EUR 200,000 (EUR 100,000 in 2018 and 2019).

Expected impact on employment and gender

By reducing the administrative burden on companies and increasing their competitiveness, they could expand their activities and increase employment.

Electronic services are equally accessible to all citizens and businesses, regardless of location (urban and rural), gender and social background, degree and type of disability, etc.

Potential risks

Insufficient coordination and communication between the institutions that need to be involved with providing e-services on the portal. This risk is mitigated by establishing a working group with stakeholders.

4.3.5 RESEARCH, DEVELOPMENT AND INNOVATION (RDI) AND DIGITAL ECONOMY

The Small Business Act's implementation assessment ranks the Republic of Macedonia as leader among Western Balkan countries in terms of innovation policies for SMEs. However, despite the significant progress made in designing, implementing and monitoring of innovation policies from 2012 to 2015[55], the latest European Innovation Ranking List (2017) still categorizes the Republic of Macedonia as a "moderate innovator" compared to other European countries.[56]

Although the analysis identify enhanced export of medium and high technologies and increased public investment in research and development, the total expenditure for RDI as a percentage of the GDP remains significantly low, which indicates to modest investment contribution from both the public and the private sector.[57]

[55] SME Policy Index: Western Balkans and Turkey 2016

[56] European Innovation Scoreboard 2017

[57] Assessment framework for research, development and innovation Competitiveness in South East Europe A POLICY OUTLOOK,2018

Industry-academia-government partnerships for innovation can accelerate value creation in innovation when the actions of these three stakeholders are coordinated and the main challenge in implementing such partnerships is to ensure effective communication between the three stakeholders, in light of their different priorities, environment and mindsets.

Promoting innovation at firm level (for example, creating new products, processes and services and/or upgrading the quality of existing products, processes and services) is central to Macedonia's competitiveness and enhanced research and innovation capacity will facilitate regional integration, integration into the European Research Area and compliance with EU requirements and standards in key industries.[58] Innovation-driven and export-oriented development in Macedonia requires a policy change and a deepening of public sector support for research and innovation. According to the data from the above analyses, providing systematic and sustainable financial support at all stages of the innovation cycle (from the initial idea to the commercialization in the global market), including mechanisms for supporting the cooperation between the academy and the private sector, as well as strengthening the research base and the private sector capacities for investment absorption are a serious challenge. Addressing those challenges would enable the country to build an innovation ecosystem, which would facilitate transition towards a knowledge-based economy. The key strategic documents that coordinate these challenges are the Innovation Strategy 2012-2020, the Competitiveness Strategy 2016-2020 and the Comprehensive Education Strategy 2018-2025.

Measure 14: Improving infrastructure and access to finance for research, development and innovation

Description of the measure

This measure is rolled over from last year, the implementation details are presented in Table 11.

The current infrastructure for supporting the research, development and innovation is consisted of the following instruments: (1) Co-financing grants for newly established enterprises: start-ups and spin-offs; and (2) Co-financing grants and conditional loans for commercialization of the innovation. In 2017, the Fund for Innovation and Technology Development worked on drafting bylaws for introduction of new instruments that would be piloted in the forthcoming period:

Instrument III – „Co-financing grants for technology extension“

The instrument is intended for conducting needs analysis and introduction of new, advanced technologies that would improve the performance and competitiveness of Macedonian SMEs. The advanced technologies would further enable and enhance innovative activities in the enterprises and consequently increase the absorption capacity for investment capital of the private sector.

Instrument IV - "Co-financed grants for the establishment, operation and investments of business-technology accelerators"

The instrument will support the establishment and operation of business-technology accelerators as entities providing infrastructural and financial support for innovation activity by providing technical and financial resources, as well as strengthening human capacities within start-up companies, thus contributing to increased their readiness for investment and venture capital.

Instrument V – Technical assistance to support innovative business

The instrument is intended for provision of external expert support to innovative enterprises (e.g. innovation potential analysis, innovation management, protection of intellectual property, investment readiness and fundraising for innovative projects, development of innovation

[58] World Bank Policy Notes 2017

projects, technology transfer and strengthening the cooperation between the academia and the private sector.

Instrument VI –Introduction of innovation in the public sector and organization of thematic challenges

Through this instrument, competitions, thematic challenges, prototrons and / or hackathons will be organized for SMEs aimed at finding innovative solutions to problems of public interest. The introduction of the innovative solutions will contribute to increase the quality and efficiency of public services.

Activities planned in 2018

- Adoption of the bylaws for the newly designed instruments,
- Piloting the new support instruments (announcing the first public calls under all of the newly designed instruments).

Activities planned in 2019-2020

- Implementation of the new support instruments (announcing public calls according to annual work plans and monitoring of the granted projects),
- Monitoring and evaluation of the results on programme level.

Responsible institution: Fund for Innovation and Technology Development.

Expected impact on competitiveness/rationale of the measure

The above-mentioned support instruments are expected to enhance public and private investment in RDI, to increase the number of companies that have introduced an innovation, to strengthen the human capacities of SMEs and foster cooperation between academia and the private sector. Increased investment in RDI contributes to increased quality of goods and services and thereof competitiveness of domestic companies.

Estimated cost of the activities and the budgetary impact (in Euros)

Instrument	2018	2019	2020
III.	675.000	400.000	325.000
IV.	542.000	500.000	458.000
V.	250.000	200.000	200.000
VI.	200.000	250.000	300.000

Expected impact on employment and gender

Through investments in research, development and innovation, the competitiveness of domestic companies on the domestic and global markets increases, resulting in economic growth and increased number of jobs, especially of highly skilled workforce.

The gender equality will be respected in the process of implementation of the measure.

Potential risks

Further strengthening of FITD capacities is a prerequisite for successful implementation of the instruments listed under this measure. Improving SME investment readiness in parallel with the increase in financial support is crucial for the absorption of available funds. The insufficient complementarity of the resources and mechanisms poses a significant risk to the further implementation of the existing and the new instruments for support of innovation activity. For this purpose, in the forthcoming period, the Fund will strengthen its human resources with new employments and by providing tailored trainings for its employees. The Fund will also invest additional effort to provide technical assistance for strengthening the capacities of the potential applicants and the grant beneficiaries, especially in regards to elevating their investment readiness in parallel to the implementation of all support instruments.

4.3.6 TRADE RELATED REFORMS

The trade relations with EU of the countries in the region are part of the Stabilization and Association Agreements or processes that requires brining national legislation in line with the EU Acquis for establishing free trade area between each candidate or potential candidate country and EU. Albania, Macedonia and Montenegro are also World Trade Organization (WTO) members. All countries are signatories of the Central European Free Trade Agreement (CEFTA) and for those not yet being part of WTO, this is of great benefit as it prepares them to meet the criteria for WTO membership.

Trade liberalization and facilitation measures, as part of multilateral trade agreements, enable access to bigger markets and global value chains and provide opportunity to companies to increase their competitiveness. When goods and services cross borders many times and are subject to repeated sampling and testing procedures, it impacts both the domestic producers and foreign suppliers by increasing the trade costs.

There is a joint initiative in Western Balkans to accelerate regional economic cooperation and develop a Regional Economic Area, based on CEFTA and EU rules and principles as reflected in Stabilization and Association Agreements (SAAs), which will progressively allow an increased free movement of goods, services, investment and skilled workers, in full coherence with each country's path. This 'Regional Economic Area' will help unleash the vast potential of the region of about 20 million people by creating better and more sustainable economic opportunities for all, and attracting greater volumes of FDIs than the current individual efforts.

The trade policy of the region, in accordance with the CEFTA Agreement, provides for a significant level of openness in the commodity market and the possibility of wider liberalization of trade in services. The economies in the region have made progress in creating policies that facilitate trade, but they still face non-tariff barriers and restrictions on trade in services. Regarding non-tariff barriers, improvement is needed in several categories, such as technical standards, sanitary and phytosanitary measures and administrative obstacles.

In order to strengthen and improve the quality of risk analysis so as to avoid repetition of sampling and testing, as well as to establish regional standards for mutual recognition of programmes, documents and inspection certificates, to facilitate trade in goods, CEFTA countries undertake activities for the application of regional protocols that will be an integral part of the CEFTA Agreement.

Measure 15: Trade facilitation

Description of the measure

By implementing the practice of controls based on risk analysis and by prior submission of information or issued veterinary or phytosanitary certificates through the TRACEE system, the time and cost of import and export will be reduced.

It is closely linked the Additional Protocol 5 (AP5) to 2006 CEFTA Agreement aiming to simplify inspections related to all clearance procedures and reduce formalities to the possible maximum extent by electronic data exchange data between customs authorities. Negotiations on AP5 have started in 2015 and it is expected entering into force in 2018.

Trade policy and facilitation is part of the Integrated Growth Pillar of the SEE Strategy 2020. The main objective of this pillar is to promote regional trade that is non-discriminatory, transparent, and predictable and that enhances flow of goods and services within the region.

Activities planned in 2018

Completion of the ratification procedure of Additional Protocol 5. An effective enforcement of the protocol is expected in late 2018 after all CEFTA countries complete the ratification process.

Activities planned in 2019

Developing transparent tools (expanding the TRACEE certificate for veterinary certification, creating a phytosanitary certificate system) and upgrading customs systems intended for data exchange between customs authorities in the region.

Expected impact on competitiveness/rationale of the measure

By simplifying customs and trade procedures, the measure will contribute for reduction of costs and time needed to export and import goods. It is estimated that trade costs and the average time needed to import and export to other CEFTA countries will be reduced by 47%. It will contribute for an annual increase of exports to other CEFTA countries by 3.5%.

Estimated cost of the activities and the budgetary impact

Planned activities in 2018 will be financed within the regional IPA Project for CEFTA countries. Planned activities in 2019 amount to EUR 55.1 thousand, planned in the 2019 Budget of the Republic of Macedonia.

Expected impact on employment and gender

More open markets for goods and services stimulate job creation.

The gender equality will be respected in the process of implementation of the measure.

Potential risks

In order for the Protocol to come into force, at least three countries need to ratify it.

4.3.7. EDUCATION AND SKILLS

Even though access to education has improved, challenges remain in provision of skills for the „new economies“[59], as well as for linking the educational system with the private sector needs. Vocational education and training (VET) and higher education emphasize traditional cognitive skills, and in the case of vocational education, the focus is on narrowly defined professional profiles, with low vertical and horizontal flexibility. "New economy" skills are lacking, such as capability for completing complex tasks, analytical and organizational capabilities etc., indicating that the education system has to change its role from teaching facts and theory to developing skills which can be applied to different workplaces.

The vocational education and post-secondary education do not attract sufficient number of students due to obsolete and unreformed vocational profiles. Therefore, there is an ongoing reform of the VET curricula with modular approach. Although Macedonia has an index of 2.5[60] for cooperation between the Centre for vocational education and the business community, higher than most SEE countries, there is still room for improvement.

Employers are still not aware of the essential role of the National Occupation Standards (which provide information on the workplace and knowledge, skills and competencies required to perform the tasks and constitute a base for preparing qualifications) and the standards of qualifications in creation of relevance between businesses and VET. VET students need to be prepared to enter a rapidly changing labor market.

In order to optimize (efficiency and effectiveness) of the VET system in terms of expenditures, relevance and labour market needs, an assessment of the VET institutions and schools will be done. The aim is to provide adequate basis for establishing Regional Centers of Excellence. This activity would encompass training of the existing VET staff. Also, focus will be given on further development of the mutual cooperation between VET schools and the business community with

[59] World Bank Country Partnership Strategy for the Republic of Macedonia 2015 – 2018

[60] (Ranging from 1 to 5) OECD Competitiveness in SEE Report

an aim of improving youth employability. The idea is to stimulate work-based learning by encouraging companies to invite and accept students on practical education and training thus equipping them with skills for specific job requirements.

The main challenges in the high education are its insufficient quality along with the not fully functional accreditation and evaluation system of universities, and study programs not adjusted to the labour market needs. Almost one third of recent graduates have a job that is not aligned with their field of study. In addition, more than half of recent graduates are "vertically" mismatched, with one third being overqualified for their job, and one fifth being under qualified for their work. Another challenge is the lack of work experience, sufficient and appropriate skills that many graduates have when entering the labour market, which limits their job opportunities[61]. As a result of these findings, the ministry, in cooperation with higher education institutions, is working on a new Law on Higher Education, as well as on developing a new model for financing universities based on outcomes.

The main challenges of informal education and adult education are the noncompliance between the demand and supply of adult education due to lack of information about the labour market needs, low awareness of population and companies, lack of a system for validation of nonformal and informal learning.

The key strategic documents targeting these challenges in a coordinated manner are: SEE Strategy 2020, Comprehensive education strategy 2018-2025, VET strategy in the context of lifelong learning 2013-2020, Adult education strategy etc.

Measure 16: Further development of the qualification system

Description of the measure

This measure is rolled over from last year, the implementation details are presented in Table 11.

The analyses have shown that there is a huge discrepancy between the skills acquired in the educational process and the employers needs. There are several sectors that are not able to find employees with adequate qualifications and skills. Therefore, the National Qualification Framework (NQF) for lifelong learning was developed as a tool for reforms in the education and training system and as tools for communicating a quick response to the needs of the employers.

National Qualification System will be supported by the Skills Observatory, which will be used to analyze the adequacy of the skills students have in correlation with the labour market needs in order to continuously improve the curriculum in accordance with the requirements of the employers. The Skills Observatory will also support key national stakeholders, including universities, secondary schools, training providers etc. The Objective of the Skills Observatory is to support the development of evidence-based policymaking for development of vocational and professional education, by providing adequate analytical and informational capacity.

VET reforms have already started and according to the labour market analysis, 79 new qualifications for formal education and 5 standards of qualifications for non-formal education have been prepared. Thirty four special programs were developed within adult education, as a possibility to acquire qualifications, pre-qualification or additional qualification, in accordance with the labour market needs.

The cooperation with the employers has strengthened though practical learning with employers, who prepare the students for future work processes during their education and through the preparation of the curricula and syllabi. So far, 737 certified mentors in companies were trained,

[61] European Commission, Report on Higher Education Provision and Labour Market Needs

who lead the students through the learning process in the company. Also, in cooperation with the employers around 200 occupation standards were developed.

Activities planned in 2018

Planned activity	Responsible institution
1. Development of 10 new qualifications according to the requirements of employers and new technologies in companies	National Board for the Macedonian Qualifications Framework; Sectoral committees; Ministry of Education and Science; Centre for Vocational Education and Training; Employers
2. Establishing three sectoral committees for qualifications	National Board for the Macedonian Qualifications Framework
3. Implementation and operationalization of the Skills Observatory. Establishing a connection with the information systems of all involved institutions and collecting data. Conduct training for using the Skills Observatory for MoES staff involved in the process of creating educational policies.	Ministry of Education and Science - Skills Development and Innovation Support Project
4. Development of 5 special programs for adult education and training for additional qualification or pre-qualification for easier mobility and employability in the new companies	The Adult Education Centre; Providers of educational services
5. Strengthening of cooperation between higher education institutions and employers, as well as with the vocational secondary schools in order to provide quality practical work for students in companies and possibility for the workforce to be recognized by the company where the practical work is taking place.	Universities and higher education institutions; Secondary vocational schools; Companies.

Activities planned in 2019

Planned activity	Responsible institution
1. Development of 5 qualifications required by employers and flexible access for their acquisition	National Board for the Macedonian Qualifications Framework; Sectoral committees; Ministry of Education and Science; Centre for Vocational Education and Training; Employers; Providers of educational services
2. Development of programs for training for specific jobs, for additional qualification	Providers of educational services and higher education institutions
3. Strengthening of cooperation between higher education institutions and the private sector, and vocational schools and the private sector to provide quality practical work for students in companies.	Universities and higher education institutions; Secondary vocational schools; Companies

Activities planned in 2020

Planned activity	Responsible institution
1. Training for transversal skills upon request from employers	Employers; Providers of educational services
2. Validation of non-formal education to acquire specific qualifications (establishment of a system for validation and recognition of previous study)	Centre for Vocational Education and Training; Special accredited institutions for validation of non-formal education

Expected impact on competitiveness/rationale of the measure

Employees with higher qualifications will provide higher efficiency and productivity in companies and will reduce the cost of training of employees for additional qualification. The measure will contribute to reducing the inadequacy of education and labor market needs, acquiring skills and competences that will meet labor market needs, recognizing acquired qualifications in the state by foreign investors and recognizing qualifications acquired abroad by domestic employers for easier employability of job seekers.

Estimated cost of the activities and the budgetary impact

	2017	2018	2019	2020
Budget expenditures (in Euros)	1,822,635	1,617,632	263.650	288.750
Non-budget financing (in Euros)	2,043,000	3,000	310.000	310.000

Expected impact on employment and gender

Increasing the quality of the curricula based on learning outcomes will lead to acquiring knowledge, skills and competences that will enable students to easily find a job after finishing education. Additionally, strong transversal skills, acquired due to the new reformed curricula will contribute to better mobility of labour force and career development. Most of the companies in Macedonia are SMEs, which do not have capacity to recognize and develop the potential of their employees; therefore the NQF as a meeting point for all stakeholders will contribute to better recognizing of the needed skills and competences.

Potential risks

Lack an overall framework for the implementation of all activities might contribute to various non-systemic decisions; Insufficient capacities for administering the implementation of activities contributes to delay of activities and discourages all participants in the process; Lack of common approach might make the implementation of certain activities harder; Inefficient leadership of the reform process negatively affects the decision making and the effective flow of activities; and Insufficient interest of the relevant interested parties, particularly employers, whose opinions and suggestions are crucial.

In order to overcome potential risks MoES undertakes the following activities: establishing accompanying bodies for support of NQF (sectoral committees) consisting of employers' organization, trade unions, students, higher education institutions, government institutions, associations etc; Strengthening of the awareness for the role of NQF; Improving forecasts of the labour market needs so as to improve educational programmes, create new qualifications and strengthen quality assurance procedures; and Finding adequate instruments to motivate employers.

4.3.8. EMPLOYMENT AND LABOR MARKETS

The country is still facing high unemployment rate and low rates of employment and activity. The employment rate is low as a result of the low employment of women and young people. The youth employment is about 2.5 times lower than the average in the country. Young people face difficulties in transition from education to the labor market. Youth unemployment is declining with an increase in the level of education, so uneducated or low educated young people face higher unemployment rates than those with completed secondary and tertiary education. In the structure of employment, the most frequent occupations are the ones which require workers with secondary education. Significant share of unemployed persons are long-term unemployed, their knowledge and skills diminishes, their productivity decreases, and thus their chances of finding work. The activity rate is low as a result of the low activity of women and low educated persons.

In August 2017 the Employment and Social Reform Program 2020 - ESRP was adopted, which identifies the following goals: 1/ Improving economic development and creating jobs, 2/ Improving the situation of unemployment, especially for the most vulnerable categories (young, long-term unemployed and others), 3/ Dealing with informal employment, 4/ Improving the quality of work and services of the public employment service, and 5/ Strengthening the social dialogue on a tripartite and bipartite level, at national and local level, promotion of collective bargaining.

In one of the joint conclusions of the Economic and Financial Dialogue of May 2017, the need "to increase the coverage of active measures for long-term unemployed, young and low-skilled persons" is highlighted. Also, the Economic Reform Program Assessment 2017-2019 states that "the administrative division between registered active and other jobseekers (passive) makes an artificial and administrative barrier to the use of active measures".

The reasons for high unemployment are mostly associated with insufficient labor demand, which is largely a consequence of poor economic growth in the past decade. To improve labor market outcomes[62], labor demand needs to be fostered by creating conditions for more productive firms to grow and hire workers, increase the skills levels of the population to help meet demand for modern, workplace-relevant skills, and better assist marginalized groups getting into the labor market.

So far, the measures on the labor supply side were mainly aimed at improving skills of the unemployed, retraining and qualification, supporting young unemployed persons to gain work experience, etc. However, matching the needs of companies and the offered workforce remains a major challenge.

In the past period, the impact of active employment measures was assessed, and they were adjusted in compliance with the recommendations, and quotas of minimum 30% youth participation in active employment measures was determined, method of measuring performances of participants in employment services and measures was developed, information on the labor market was improved and the work and services of EARM were modernized. However, few employers use the services of EARM for hiring employees. In the past two years, EARM performs profiling of unemployed persons and develops individual employment plans, through which the most vulnerable are directed towards active employment measures.

Measure 17: Upgrading the active measures included in the Operational Plan for Active Employment Programs and Measures and Labour Market Services

Description of the measure

Each year, the Government adopts an annual operational plan for active employment programmes and measures and labor market services (OPs), which includes measures for self-employment and starting a business, subsidized employment programs, training for a known employer and for demanding occupations, municipal works, pilot measures, as well as employment services for both employers and job seekers.

In the past years, only active job-seekers (persons who register in EARM each month) were entitled to participate, however from 2018, all job-seekers registered in EARM are able to participate. The profiling of unemployed and the individual employment plans serve to direct the active measures towards the most vulnerable unemployed. Thus, in addition to young, long-term unemployed, low-skilled and unemployed over the age of 50, a focus will also be placed on people who are inactive for more than 5 years on the labor market. Activities for development of social entrepreneurship will be included, as well as measures for early prevention of the loss of knowledge and skills of young people after completing their education until their inclusion in the labor market (youth guarantee).

In the medium term, in order to provide more reliable information on labor demand, an Occupational outlook will be developed, based on statistical data and surveys. Based on the information, more adequate measures (trainings) will be included in future OPs. Dissemination of occupational information will be done through a special website.

This measure is related to the ESRP 2020, the Employment Strategy 2016-2020 and the Government Programme 2017-2019, primarily in the area of decent work.

---

[62] World Bank Policy Notes 2017

Activities planned in 2018

- Detailed analysis of active measures and programmes that have been implemented over the past years in order to detect shortcomings and develop improved active measures.
- Preparation and adoption of the OP for 2018.
- Development and implementation of the Occupational outlook.

Activities planned in 2019 and 2020

- Preparation and adoption of the OP on the basis of the Occupational outlook.

Expected impact on competitiveness/rationale of the measure

The mismatch between supply and demand of workforce is expected to reduce through adequate active measures designed according to employers' needs.

Expected costs of the activities and expected impact on the budget

In the 2018 Budget EUR 16 million are provided.

Expected impact on employment and gender

Considering that 16,000 unemployed persons are planned to be covered with OP 2018, a significant number of those persons are expected to become employed. For illustration, in 2016, 6,551 people were covered by the OP, out of which 3,618 or 55% were employed.

In order to respect the principle of gender equality, women will be encouraged to participate in active measures.

Through profiling and individual plans, the active measures will be directed to the most vulnerable categories on the labor market (people who are unlikely to be employed if they do not participate in these measures). The measure is expected to have a greater impact on activation of inactive on the labor market by enabling participation in active measures of potential 100,000 passive job seekers.

Potential risks

Inadequate design of active policies, lack of information and poor interest of unemployed persons and employers can lead to incomplete realisation of the planned number of applicants. The insufficient number of EARM employees working with the unemployed (1:358) could hamper the successful implementation of active measures.

In order to overcome these potential risks in the preparation of the OP, the employers, local community and other stakeholders will be actively involved. Public debates will also be conducted and the OP will be reviewed by the Economic and Social Council, and OP will be promoted on national media. If there is poor interest, it will be revised in order to redirect resources towards measures of greater interest. Since the number of employees in EARM cannot be increased, capacities will be continuously improved through internal redistribution of work tasks and appropriate trainings of the employees.

Measure 18: Youth guarantee

Description of the measure

With the Youth Guarantee measure, each young person under the age of 29 will be given an adequate job offer, an opportunity to continue education or be included in some of the internship or training measures for preparation for employment. This will be provided within 4 months after completion of education or registration as an unemployed person in EARM.

The Youth Guarantee begins with activation measures for young people. It will initially apply to young people who are active jobseekers and are registered for the first time as unemployed. Once the unemployed persons are registered in the unemployment register, they are immediately referred to their first interview with an expert from EARM, who makes the profiling of their employability using a control questionnaire and develops the individual employment plans (IEP). The IEP defines activities that will enable the young unemployed person in the next 4 months to be included again in the educational process (not in regular education) or to be included in some of the measures and services for employment, which will enable him to increase his opportunities for easier employment, i.e. he will be offered adequate employment which corresponds to his education and skills. These activities include group and individual counseling and information; providing job search assistance services; motivational training; inclusion in one of the labour market integration measures (employment, education and training measures).

Activities planned in 2018

The measure will be piloted in 3 employment centers.

Activities planned in 2019

This measure will be implemented in all 30 employment centers, having in mind the experience of the pilot implementation in the previous year.

Activities planned in 2020

This measure will be implemented as a regular activity of the EARM, having in mind the experience from the previous years.

Expected impact on competitiveness/rationale of the measure

All implementation activities foreseen within this measure are expected to increase the competitiveness of young people and facilitate their inclusion in the labour market. In addition, competitiveness will be assessed through indicators that will be determined before the start of the implementation of the measure.

Estimated cost of the activities and the budgetary impact

In 2018, the planned target in 3 employment centers is 1,200 people, for which EUR 1,595,000 are planned in the 2018 Budget. In 2019 and 2020 the planned target in all employment centers is 9,500 persons annually, for which approximately EUR 12,628,000 will be spent per year.

Expected impact on employment and gender

The measure aims to improve employment opportunities of young people, hence to increase their employment. The employment of young people involved in this measure will be monitored monthly, semi-annually and annually. In addition, gender representation will be also monitored.

Potential risks

The insufficient number of EARM employees working with the unemployed (1:358) can negatively affect the successful implementation of the measure. Due to lack of opportunities for increasing the number of employees in EARM, capacities will be continuously improved through internal reorganization of work tasks and appropriate trainings of the employees.

4.3.9. SOCIAL INCLUSION, POVERTY REDUCTION AND EQUAL OPPORTUNITIES

In Republic of Macedonia there is a trend of continuous reduction in poverty and inequality, however, despite these positive trends, they are still is at a high level. According to the latest published SSO data, the at-risk-of-poverty rate was 21.8% in 2016, while the Gini coefficient (measure of inequality of income distribution) was 33.6%.

Laeken poverty and social exclusion indicators, 2013–2016

	2013	2014	2015	2016
At-risk-of-poverty rate, % of population	24.2	22.1	21.5	21.8
Number of persons below at-risk-of-poverty threshold, in thousand persons	500.4	457.2	445.2	450.5
At-risk-of-poverty threshold of single-person household - annual equivalent income in denars	70,275	71,925	78,362	82,560

At-risk-of-poverty threshold of four-person household (2 adults and 2 children aged less than 14) - annual equivalent income in denars	147,578	151,043	164,560	173,376
At-risk-of-poverty rate before social transfers and before pensions, % of population	41.0	41.7	40.5	41.6
Inequality of income distribution, S80/S20, %	8.4	7.2	6.6	6.6
Inequality of income distribution, Gini coefficient, %	37.0	35.2	33.7	33.6

Source: SSO

However, despite the reduction of the poverty rate of from 27% in 2010 to 21.8% in 2016, poverty and inequality are high when compared with other countries with similar levels of development in the region[63] and there are concerns about the sustainability of the recent gains in poverty reduction.

Significant reforms are necessary, among other things, in redesigning the types and adequacy of social welfare cash benefits as assistance and support to the most vulnerable categories for dealing with poverty, especially having in mind the goal of the Government of the Republic of Macedonia to reduce the poverty rate below 16% by 2020.

Analyses show that the social protection system is in a phase when essential reforms are necessary, primarily in order to improve the effectiveness of financial benefits and the efficiency of benefits and social services that are delivered to end users. The current design of the social transfers is quite uneven and inadequate, and, as such, contributes to the deepening of inequality in the society. As regards the social protection services, it has been established that they are not tailored to the individual needs of end users, and that they should be provided in the community through further implementation of the process of deinstitutionalization, decentralization and pluralization.

Although the Law on Social Protection allows the process of pluralization in the provision of social services, in practice, these are mainly provided by the state. There is a lack of initiative from municipalities to establish institutions for institutional or extra-institutional social protection, as well as greater activity and involvement of the local communities in the implementation of policies in these areas, coordination at the local level between relevant stakeholders and their greater cooperation with institutions at the national level. The private initiative is not sufficiently present in relation to all social protection services; however, what can be highlighted as the reason for this is the non-existence of the amount of the cost of the service defined by the state (per hour and per beneficiary). There is an evident lack of provision of social services by the civil sector, which is usually dependant on funds provided by external donors. Hence, the access to social protection services and the coverage of the beneficiaries of these services within the established forms of social protection do not fully satisfy the needs of the vulnerable categories.

Measure 19: Enhancement of financial benefits in the field of social protection

Description of the measure

The reform of the social protection system will ensure proper targeting and directing of social benefits to persons at social risk of poverty and social exclusion. The introduction of a programme for minimum adequate income will allow families at social risk (the most materially vulnerable families) to receive financial benefits in addition to their income in order to reach the poverty threshold. It is planned to introduce family packages and to group entitlements from social protection and child protection. Part of these transfers will be conditioned with entry into the labour market for work-age beneficiaries and strengthening their work capacities.

[63] World Bank Policy Notes 2017

These planned measures will have direct impact on poverty and social inclusion of the vulnerable categories of citizens.

Activities planned in 2018

- Analysis and preparation of proposals for redefining the social protection system.
- Drafting a new Law on Social Protection, consultative process with stakeholders and preparation of bylaws.
- Start of activities for changing and upgrading the existing software solution for administering financial entitlements, where in addition to entitlements, social services will also be covered.

Activities planned in 2019

- Adoption of a new Law on Social Protection.
- Trainings for persons employed in social protection system, in order to get acquainted with the new solutions and their implementation.
- Public campaign for new legal solutions in order to introduce them to end-users.
- Finalization of the upgrade of the software solution for administering financial entitlements and social services.

Expected impact on competitiveness/rationale of the measure

Better targeting of target groups and increase of effectiveness of cash transfers allows for exiting the poverty circle, economic strengthening and social inclusion. The measure will contribute to optimal utilization of financial resources aimed at providing social services.

Estimated cost of the activities and the budgetary impact

The funds for implementation of planned activities will be secured within a World Bank project, but the exact amounts will be known after completing detailed analyzes and preparation of the legal solution.

Expected impact on employment and gender

Cash transfers for job-seekers will be conditioned by strengthening their work capacity and inclusion in the labor market, which is expected to contribute for employment of some of the beneficiaries. Gender equality will be respected in the implementation of this measure.

Potential risks

The practical application of the Law and payment of financial entitlements is related to timely adoption of new bylaws and upgrading of the system for administering financial entitlements.

5. BUDGETARY IMPLICATIONS OF STRUCTURAL REFORMS

The projected expenditures of the Budget of the Republic of Macedonia also include expenditures for key structural reforms in the following period. Significant funds will be allocated to support domestic companies for investment and improving competitiveness, as well as attracting FDIs as an extremely important factor for achieving higher economic growth rates. Significant funds for active policies and measures are foreseen for improvement of conditions on the labor market. Also, for upgrading of agricultural production, significant funds have been allocated for improvement of irrigation systems, consolidation and defragmentation of agricultural land and support of agricultural cooperatives. The effect on budget revenues is calculated in Measure 1: Harmonization of the Public Procurement Legal framework with the Acquis.

More details on budgetary implications of structural reforms are shown in Table 10 of Annex 3.

6. INSTITUTIONAL ISSUES AND STAKEHOLDER INVOLVEMENT

Economic Reform Programme 2018-2020 is a joint result of the collaboration of many institutions, while the overall preparation is coordinated by the Ministry of Finance. The preparation of this programme as a coherent strategic document is confirmation of the capacity of the administration in terms of coordination and efficiency. The programme was prepared by the Ministry of Finance, coordinated by the Minister of Finance, with the following institutions:

- Cabinet of the Deputy Prime Minister in charge of economic affairs;
- Secretariat for European Affairs of the Republic of Macedonia;
- National Bank of the Republic of Macedonia;
- Ministry of Economy;
- Ministry of Labour and Social Policy;
- Ministry of Education and Science;
- Ministry of Transport and Communication;
- Ministry of Agriculture, Forestry and Water Economy;
- Ministry of Information Society and Administration;
- Ministry of Justice;
- Public Procurement Bureau;
- Fund for Innovation and Technical Development;
- Employment Agency of the Republic of Macedonia;
- Ministry of Finance - Customs Administration.

The program was adopted by the Government of the Republic of Macedonia on January 23, 2018.

Considering the fact that the Programme should be submitted to the European Commission no later than January 31st 2018, upon proposal of the Ministry of Finance, all participants in process adopted a timetable for implementation of activities for the preparation of this document:

- June 9, 2017, an Initial Meeting on ERP was held, attended by about 70 participants, including: the Minister of Finance, the representative from the EC Enlargement Directorate responsible for the Republic of Macedonia, coordinators from line institutions involved in the process, representatives of the EU Delegation, OECD, as well as representatives from stakeholders;
- 9 June - 30 August 2017, the ministries and other institutions performed diagnostics of their sector, using the tools provided by the OECD and formulated proposals for sectoral reform measures and, together with the diagnostics, submitted them to the Ministry of Finance;
- August 30, 2017, a working meeting of ministers and the expert public was held, where the initial versions of diagnostics were reviewed, as well as prioritization of the proposed reform measures;
- By September 11, 2017, the First draft version of the Structural Reform Measures Part was completed and submitted to the OECD;
- September 27-29, 2017, an OECD workshop was held where the draft ERP was discussed (workshop on the updated diagnostics and prioritization of the reforms). Following the workshop, part of the revised draft measures were sent to the OECD on October 10 2017, while the remaining part was submitted on October 19 2017;
- TAIEX expert mission was held from 24 to 27 October 2017 for assessment of the budgetary impact (costs and revenues) of structural reforms and their expected impact on competitiveness, employment and gender;
- October 26, 2017, recommendations and comments from the OECD were received, which were immediately distributed to the institutions;

- October 31, 2017, the Second draft version of the Structural Reform Measures Part was completed, including recommendations from the OECD and TAIEX experts, and was submitted to the EC;
- November 8-9 2017 an EC mission was carried out to support the preparation of ERP;
- November 27, 2017, the Third draft version of the Structural Reform Measures Part was prepared, based on the recommendations received from the EC and OECD;
- November 27 to December 10, 2017, the third version of ERP was posted on MoF's website as part of the public consultation process;
- December 5 2017, a Consultative Meeting with stakeholders was held, where it was agreed that comments and suggestions for ERP should be submitted by December 10 2017;
- By December 25, 2017, the first version of the remainder of the Economic Reform Programme (macroeconomic and fiscal framework) was prepared;
- December 26, 2017, the Program was reviewed at a session of the Economic and Social Council;
- Submission of ERP to the Government – January 5, 2018;
- The Government adopted the Programme on its session held on January 23, 2018;
- Submission of ERP to the European Commission no later than January 31, 2018.

Having in mind that regarding last year's programme, the European Commission acknowledged the efforts that the Government is making in implementing reforms to improve competitiveness, the Ministry of Finance made a significant effort to maintain, but also to improve the quality of this year's document in accordance with the recommendations made by the Commission.

During the preparation, consultation process with stakeholders was conducted: the business community, universities, ZELS, local authorities, social partners, civil society and other stakeholders.

In this regard, from November 27 to December 8, 2017, the draft ERP 2018-2020 was published on the Ministry of Finance's website and at the same time invitations were sent to interested parties for their active contribution to the process of preparation of the document by giving opinions on the content of the document and suggestions for its improvement. The opinions and proposals received were reviewed by the institutions participating in the preparation of ERP 2018-2020.Additionally, on December 5, 2018, a public debate was held in the premises of the Ministry of Finance between the institutions participating in the preparation of the document, representatives of the European Delegation in Skopje and the stakeholders.

For the first time this year, on December 26, 2018, the draft ERP 2018-2020 was also discussed at a session of the Economic and Social Council.

More detailed information on contributions submitted by the stakeholders is presented in Annex 4 of the document.

Annex 1. Indicators for the Macedonian economy in 2016 according to the Macroeconomic Imbalances Procedure of the European Commission

Observing the economy using scoreboard indicators with set of indicative thresholds, under the EC's Macroeconomic Imbalances Procedures[64] - MIP implemented in the EU member states, is useful for monitoring the main areas of vulnerability among candidate countries, and for understanding the extent of their convergence towards the EU. Main indicators within this approach for the Macedonian economy in 2016, according to the given thresholds, are presented below.

	Indicative thresholds		2011	2012	2013	2014	2015	2016
Indicators	**upper**	**lower**						
External imbalances and competitiveness								
Current account balance (% of GDP, 3-year moving average)	-4	6	-3,8	-2,6	-2,4	-1,8	-1,4	-1,9
International Investment position, net (end-year, % of GDP)	-35		-52,6	-55,1	-55,9	-53,1	-56,0	-57,3
Real effective exchange rate (CPI-based, 3-year percent change)	-11	11	-1,4	-2,5	2,1	2,7	2,3	1,9
Share in the world export (at current prices, 5-year percent change)	-6		23	-10,4	-7,7	21,7	25,2	23,1
Nominal unit labour costs (3-year percent change)		12	0,6	1,6	4,2	1,6	2,9	2,4
Internal imbalances	**upper**	**lower**	**2011**	**2012**	**2013**	**2014**	**2015**	**2016**
Real estate prices (annual change in %, deflated)		6	-10,3	-1,1	-6,1	-0,5	0,1	0,8
Credit flows to the private sector (% of GDP)		14	3,5	2,4	2,8	4,4	4,4	3
Private sector debt (% of GDP)		133	81,5	86,4	83,7	85,1	87,2	87,6
Public debt (% of GDP)		60	32,0	38,3	40,3	45,8	46,6	48,5
Liabilities of the financial sector (annual percent change)		16,5	9,6	9,9	4,9	7,9	8,0	3,7
Unemployment rate (3-year moving average)		10	31,9	31,5	30,4	29,3	27,7	25,9
Activity rate (3-year change in percentage points)	-0,2		0,5	-0,2	0,3	1,0	0,8	-1,2
Long term unemployment rate (3-year change in percentage points)		0,5	-2,8	-0,8	-2,8	-2,5	-4,2	-4,7
Youth unemployment (3-year change in percentage points)		2	-1,2	-1,1	-1,7	-2,1	-6,6	-3,6

Source: National institutions, IMF, Eurostat; NBRM calculations using available data. However, some indicators do not correspond fully with the requirements under this approach. Shaded fields point to noncompliance with the threshold. The terms 3-year and 5-year percent change relate to a change relative to the third and the fifth previous year.

The Macedonian current account deficit, as a three-year moving average, in the period 2011-2016, is held below the minimum vulnerability threshold (-4% of GDP), i.e. ranges within the limits. Since 2011, the net international investment position of the country has been enhancing (with certain improvement in 2014) and in 2016, it reached -57.3% of GDP. This level is well below the vulnerability threshold of -35% of GDP. It should be borne in mind that the net international position on the liabilities side also includes foreign direct investments, which makes up nearly half of the increase in total liabilities to abroad in the past years. In this light, when analyzing the converging countries, just because of the effect of foreign direct investment, under the EC's approach, other indicators should also be considered, such as net external debt, which covers only debt instruments, on a net basis. At the end of 2016, the net external debt of the Republic of Macedonia was 27.1% of GDP.

In the period 2013-2016, changes in REER indicated moderate appreciation of about 2% (determined mainly by the NEER), which is within the allowable range. Export market share of the economy in the world exports, as a five-year change, after the fall in 2012-2013, as a consequence of the crisis, registered a rapid annual growth in the period 2014-2016. These developments reflect the improved export performance, determined by structural changes in the economy due to the entrance of new export-oriented foreign companies in recent years. Nominal unit labor costs, as a three-year change, have been in the safe zone, and relatively stable in the last three years, registering modest annual changes. *In general, taking into account the*

[64] Alert Mechanism Report, European Commission, February, 2012.

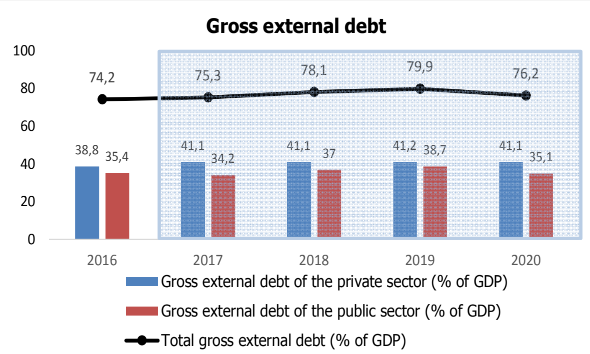
arguments in the area of external liabilities, the analysis indicates solid trends in the external sector.

Analyzing the indicators of internal imbalances, the annual changes in banks' loans to the private sector in the period since 2011 have been moderate and constantly below the vulnerability threshold (14% of GDP). Unlike the period 2014-2015, when the credit growth moderately accelerated (to 4.4% of GDP in both years), in 2016, the indicator slowed down to 3% of GDP (corrected for write-offs), and has still been well below the threshold. In 2016, financial sector liabilities decelerated and recorded an annual growth of 3.7%, which is below the threshold (16.5%). In the period 2011-2014, real estate prices registered negative annual growth, while in the next two years, they slightly increased (0.8% in 2016). The total domestic and foreign debt of the private sector (loans from domestic banks and abroad) was also constantly below the threshold of vulnerability. In 2016, it constituted 87.6% of GDP (corrected for write offs of domestic banks), which is significantly below the threshold of 133% of GDP, but on the other hand, it is worth mentioning that in recent years, the indicators has mostly been increasing. Public debt is also below the threshold (48.5% in 2016, vis-a-vis the threshold of 60% of GDP for the general government), but constantly increasing.

The unemployment rate, as a three-year moving average, although abating in recent years, has constantly been well above the threshold of 10%. Within the labor market, in 2015, the EC also introduced indicators of activity, youth unemployment (aged 15 to 24) and long-term unemployment (unemployed for more than one year). Some of these indicators for the Macedonian economy in 2016 registered favorable changes (reduction of youth unemployment and long-term unemployment), within the safe zone. Only the activity rate reduced, more than the set threshold. *Hence, within the internal imbalances, the Macedonian economy shows vulnerability to the overall unemployment rate and currently to the activity rate, albeit with favorable developments in unemployment rate and in other indicators of this segment.*

Annex 2. External debt sustainability analysis

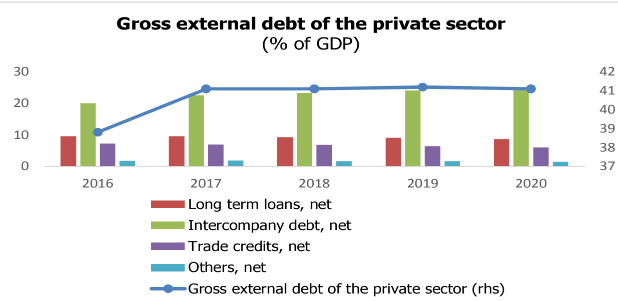
According to the analysis of the external debt sustainability[65], the gross external debt at the end of 2017 is estimated at 75.3% of GDP, which indicates an increase relative to the previous year by 1.1. p.p. of GDP. Considering the decline in the public debt by 1.2 p.p. amid higher amount of repayments, the estimated increase of the external debt mainly reflects the assessment for higher private sector debt by 2.3 p.p. of GDP, due to expected intercompany debt movements in the last quarter of 2017. In the next two years further increase of the external debt is estimated, considering the announcement for new public sector borrowings, while in 2020 it is expected to decrease amid higher amount of repayments (for maturing Eurobonds). Thus, the level of external debt in 2020 would be higher than the actual in 2016 by 2 p.p., due to the increase in private sector debt by 2.3 p.p., while public debt would be lower by 0.3 p.p. of GDP.



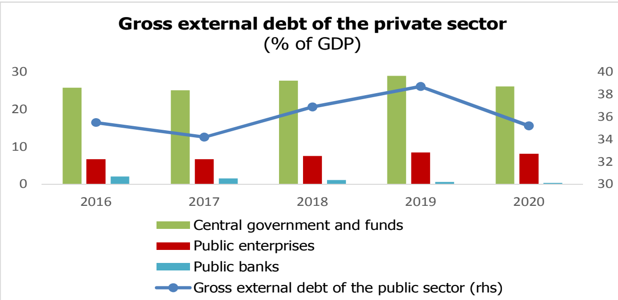
Source: Forecast for the period 2017-2020; External debt sustainability analysis, NBRM.

The primary current account deficit (excluding interest payments) is a flow that creates debt, although it is estimated to maintain at a low level in the next three-year horizon. On the other hand, the automatic debt dynamics (which includes the effects of the real GDP growth and the changes in the prices and nominal effective interest rate) and non-debt capital flows act towards its reduction. It should be noted that in the next three-year period an increase in the foreign exchange reserves is expected as well as their maintenance at the adequate level.

Within the external public debt, in 2020 relative to 2016, the share of the debt of central government and funds is expected to increase (by 0.3 p.p. of GDP) and the share of the debt of the public enterprises is expected to increase (by 1.5 p.p. of GDP) considering the expected borrowings for infrastructure projects, opposite to the expected decline at the other institutional segments (public banks). Within the private sector external debt only the intercompany debt relative to GDP is expected to increase by 2020 compared to 2016, which would be partly offset by decline at the other categories (loans, trade credits).



Source: Forecast for the period 2017-2020; External debt sustainability analysis, NBRM.



Source: Forecast for the period 2017-2020; External debt sustainability analysis, NBRM.

The stress tests indicate that the expected debt dynamics on a medium run, is however, especially sensitive to shocks with the primary current account and the economic growth. However, the structure of the external debt is in favor of lower vulnerability, considering relatively high share of close to 40% in the overall forecasting horizon of intercompany debt and trade credits, as more flexible and less risky types of debt.

[65]Source: Calculations and analysis of NBRM, based on the IMF approach. The basic scenario assumes average GDP growth in the period 2018-2020 of 3.7% and it is based on the Fiscal strategy of the Republic of Macedonia 2018-2020 and the presented balance of payments forecast, thus it is worth to point out that balance of payments statistics does not fully correspond to the external debt statistics.

Annex 3: Summary data

Table 1a. Macroeconomic prospects

	ESA Code	2016	2016	2017	2018	2019	2020
		Level (bn EUR)	Rate of change				
1. Real GDP at market prices	B1*g	9.339	2.9	1.6	3.2	3.5	4.0
2. GDP at market prices	B1*g	9.723	7.1	5.3	5.3	5.9	6.4
Components of real GDP							
3. Private consumption expenditure	P3	6.440	3.1	2.7	2.8	3.0	3.1
4. Government consumption expenditure	P3	1.569	1.9	1.6	1.3	1.3	1.3
5. Gross fixed capital formation[66]	P51	3.125	13.3	-2.7	3.6	4.5	5.0
6. Changes in inventories and net acquisition of valuables (% of GDP)	P52+P53	:	:	:	:	:	:
7. Exports of goods and services	P6	4.781	8.1	7.8	7.5	8.0	8.2
8. Imports of goods and services	P7	6.576	11.6	5.3	6.0	6.7	6.5
Contribution to real GDP growth							
9. Final domestic demand		11.1	6.5	1.2	3.2	3.6	3.8
10. Change in inventories and net acquisition of valuables	P52+P53	:	:	:	:	:	:
11. External balance of goods/services	B11	-1.8	-3.6	0.5	0.0	-0.1	0.2

Source: SSO and calculations of the Ministry of finance

Table 1b. Price developments

		2016	2017	2018	2019	2020
1. GDP deflator	%, yoy	4.1	3.6	2.0	2.3	2.3
2. Private consumption deflator	%, yoy	-0.4	1.6	1.8	2.2	2.3
3. HICP	%, yoy	:	:	:	:	:
4. National CPI	%, yoy	-0.2	1.4	2.0	2.0	2.0
5. Public consumption deflator	%, yoy	0.3	1.1	1.0	1.5	1.5
6. Investment deflator	%, yoy	1.4	5.6	2.6	2.6	2.5
7. Export price deflator (goods & services)	%, yoy	1.6	4.1	1.3	1.6	1.7
8. Import price deflator (goods & services)	%, yoy	-4.3	2.3	1.3	1.6	1.7

Source: Calculations of the Ministry of Finance and NBRM

Table 1c. Labour market developments[67]

	ESA code	2016	2016	2017	2018	2019	2020
		Level	Rate of change				
1. Population (thousands)			2,072.5	2,074.8	2,077.0	2,079.3	2,081.6
2. Population (growth rate in %)			0.1	0.1	0.1	0.1	0.1
3. Working-age population (persons, thousands)			1,678.9	1,678.4	1,678.7	1,679.6	1,680.8
4. Participation rate			56.5	56.8	57.2	57.7	58.2
5. Employment (persons, thousands)			723.6	740.2	754.4	770.2	787.2
6. Employment, hours worked			:	:	:	:	:
7. Employment (growth rate in %)			2.5	2.3	1.9	2.1	2.2
8. Public sector employment (persons)			:	:	:	:	:
9. Public sector employment (growth in %)			:	:	:	:	:
10. Unemployment rate			23.7	22.4	21.5	20.5	19.5
11. Labour productivity, persons		795.0	0.4	-0.6	1.3	1.4	1.8
12. Labour productivity, hours worked			:	:	:	:	:
13. Compensation of employees	D1	:	:	:	:	:	:

Source: SSO and calculations of the Ministry of Finance

[66] Data refers to gross capital formation.
[67] ILO definition (15+) is used for the labour market indicators.

Table 1d. Sectoral balance

% of GDP	ESA	2016	2017	2018	2019	2020
1. Net lending/borrowing vis-à-vis the rest of the world	B9	3.4	-2.6	3.0	1.1	1.1
of which:						
- Balance of goods and services		-14.8	-14.1	-13.4	-12.7	-12.3
- Balance of primary incomes and transfers		12.1	12.0	11.6	11.0	10.5
- Capital account		6.0	-0.5	4.7	2.9	2.9
2. Net lending/borrowing of the private sector	B9/EDP B9	6.1	0.4	5.5	3.7	3.2
3. Net lending/borrowing of general government		-2.7	-2.9	-2.7	-2.5	-2.3
4. Statistical discrepancy		0.0	0.0	0.0	0.0	0.0

Source: NBRM and MoF

Table 1e. GDP, investment and gross value added

	ESA	2016	2017	2018	2019	2020
GDP and investment						
GDP *level* at *current* market prices (in bn Denars)	B1g	598.9	630.9	664.1	703.1	748.1
Investment ratio (% of GDP)		32.6	31.8	32.1	32.5	32.9
Growth of Gross Value Added, percentage changes at constant prices						
1. Agriculture		2.8	:	:	:	:
2. Industry (excluding construction)		1.4	:	:	:	:
3. Construction		11.9	:	:	:	:
4. Services		2.6	:	:	:	:

Source: SSO and calculations of the Ministry of Finance

Table 1f. External sector developments

Euro billion	2016	2017	2018	2019	2020
1. Current account balance (% of GDP)	-2.7	-2.0	-1.8	-1.8	-1.9
2. Export of goods	3.5	3.9	4.3	4.7	5.1
3. Import of goods	5.3	5.7	6.2	6.7	7.2
4. Trade balance	-1.8	-1.8	-1.9	-2.0	-2.1
5. Export of services	1.4	1.4	1.6	1.8	1.9
6. Import of services	1.1	1.1	1.2	1.2	1.3
7. Service balance	0.3	0.3	0.4	0.5	0.6
8. Net interest payments from abroad	:	:	:	:	:
9. Other net factor income from abroad	-0.4	-0.4	-0.5	-0.6	-0.6
10. Current transfers	1.6	1.7	1.7	1.8	1.9
11. Of which from EU	:	:	:	:	:
12. Current account balance	-0.3	-0.2	-0.2	-0.2	-0.2
13. Foreign direct investment	0.3	0.3	0.3	0.3	0.4
14. Foreign reserves*	2.6	2.3	:	:	:
15. Foreign debt*	7.2	7.4	:	:	:
16. Of which: public*	3.4	3.4	:	:	:
17. O/w: foreign currency denominated	:	:	:	:	:
18.O/w: repayments due	:	:	:	:	:
19. Exchange rate vis-à-vis EUR (end-year)	61.5	61.6	61.6	61.6	61.6
20. Exchange rate vis-à-vis EUR (annual average)	61.6	61.6	61.6	61.6	61.6
21. Net foreign saving (lines 21-25: percentages of GDP)	:	:	:	:	:
22. Domestic private saving	:	:	:	:	:
23. Domestic private investment	:	:	:	:	:
24. Domestic public saving	:	:	:	:	:
25. Domestic public investment	:	:	:	:	:

Source: National Bank of the Republic of Macedonia

* Data for 2017 are as of September 2017

Table 1g. Sustainability indicators

	Dimension	2013	2014	2015	2016	2017
1. Current Account Balance*	% of GDP	-1.6	-0.5	-2.0	-2.7	-2.0
2. Net International Investment Position**	% of GDP	-55.9	-53.1	-56.0	-57.3	-58.5
3. Export market share*	% growth	4.8	13.7	2.0	11.6	2.4
4. Real Effective Exchange Rate**	% growth	1.6	1.0	-0.3	1.2	-1.1
5. Nominal Unit Labour Costs**	% growth	1.0	-1.1	0.1	2.0	6.5
6. Private sector credit flow***	% of GDP	2.8	4.4	4.4	3.0	:
7. Private sector debt***	% of GDP	83.7	85.1	87.2	87.6	:
8. General Government Debt	% of GDP	34.0	38.0	38.1	39.5	39.2

Source: National Bank of the Republic of Macedonia and Ministry of Finance

*Forecast for 2017

** Data for 2017 are as of September 2017

*** Data for 2016 is adjusted for write-offs of non-performing loans

Table 2a. General government budgetary prospects

	ESA	2016 Level (bn denars)	2016	2017	2018	2019	2020
			% of GDP				
Net lending (B9) by sub-sectors							
1. General government	S13	-15.912	-2.7	-2.9	-2.7	-2.5	-2.3
2. Central government	S1311	-16.736	-2.8	-3.0	-2.7	-2.5	-2.3
3. State government	S1312	:	:	:	:	:	:
4. Local government	S1313	0.140	0.0	0.0	0.0	0.0	0.0
5. Social security funds	S1314	0.685	0.1	0.0	0.0	0.0	0.0
General government (S13)							
6. Total revenue	TR	181.745	30.3	31.3	31.1	30.7	30.5
7. Total expenditure	TE	197.657	33.0	34.2	33.8	33.3	32.8
8. Net borrowing/lending	EDP,B9	-15.912	-2.7	-2.9	-2.7	-2.5	-2.3
9. Interest expenditure	EDP,D41	6.927	1.2	1.3	1.3	1.5	1.8
10. Primary balance		-8.985	-1.5	-1.6	-1.4	-1.0	-0.5
11. One-off and other temporary measures		:	:	:	:	:	:
Components of revenues							
12. Total taxes (11 = 11a+11b+11c)		107.895	18.0	18.3	18.6	18.5	18.3
12a. Taxes on production and imports	D2	78.327	13.1	13.4	13.5	13.4	13.3
12b. Current taxes on income and wealth	D5	26.744	4.5	4.3	4.6	4.6	4.6
12c. Capital taxes	D91	2.824	0.5	0.5	0.5	0.4	0.4
13. Social contributions	D61	50.300	8.4	8.4	8.3	8.3	8.3
14. Property income	D4	4.757	0.8	0.7	0.6	0.6	0.5
15. Other (15 = 16-(12+13+14))		18.793	3.1	4.0	3.6	3.4	3.4
16 = 6. Total revenue	TR	181.745	30.3	31.3	31.1	30.7	30.5
p.m.: Tax burden (D2+D5+D61+D91-D995)		158.195	26.4	26.6	26.9	26.8	26.6
Selected components of expenditures							
17. Collective consumption	P32	63.753	10.6	10.6	10.3	9.7	9.1
18. Total social transfers	D62 + D63	89.005	14.9	15.0	14.9	14.8	14.6
18a. Social transfers in kind	P31 = D63	:	:	:	:	:	:
18b. Social transfers other than in kind	D62	89.005	14.9	15.0	14.9	14.8	14.6
19 = 9. Interest expenditure (incl. FISIM)	EDP,D41	6.927	1.2	1.3	1.3	1.5	1.8
20. Subsidies	D3	14.530	2.4	2.7	2.8	2.7	2.6
21. Gross fixed capital formation	P51	22.649	3.8	4.6	4.5	4.5	4.7
22. Other (22 = 23-(17+18+19+20+21)		0.793	0.1	:	:	:	:
23.=7. Total expenditures	TE	197.657	33.0	34.2	33.8	33.3	32.8
p.m. compensation of public sector employees	D1	40.598	6.8	6.6	6.4	6.1	5.7

Source: Ministry of Finance

Table 2b. General government budgetary prospects

	ESA	2016	2017	2018	2019	2020
		Level (bn denars)				
Net lending (B9) by sub-sectors						
1. General government	S13	-15.91	-18.57	-18.23	-17.93	-16.88
2. Central government	S1311	-16.74	-18.76	-18.23	-17.93	-16.88
3. State government	S1312	:	:	:	:	:
4. Local government	S1313	0.14	0.0	0.0	0.0	0.0
5. Social security funds	S1314	0.69	0.19	0.0	0.0	0.0
General government (S13)						
6. Total revenue	TR	181.75	197.50	206.26	216.04	228.23
7. Total expenditure	TE	197.66	216.06	224.50	233.97	245.10
8. Net borrowing/lending	EDP,B9	-15.91	-18.57	-18.23	-17.93	-16.88
9. Interest expenditure	EDP,D41	6.93	8.27	8.74	10.84	13.47
10. Primary balance		-8.99	-10.30	-9.49	-7.09	-3.40
11. One-off and other temporary measures		:	:	:	:	:
Components of revenues						
12. Total taxes (11 = 11a+11b+11c)		107.90	115.21	123.25	129.84	136.77
12a. Taxes on production and imports	D2	78.33	84.80	89.86	94.48	99.31
12b. Current taxes on income and wealth	D5	26.74	27.40	30.39	32.36	34.45
12c. Capital taxes	D91	2.82	3.00	3.00	3.00	3.00
13. Social contributions	D61	50.30	52.74	55.40	58.70	62.19
14. Property income	D4	4.76	4.46	3.88	3.88	3.88
15. Other (15 = 16-(12+13+14))		18.79	25.09	23.73	23.62	25.39
16 = 6. Total revenue	TR	181.75	197.50	206.26	216.04	228.23
p.m.: Tax burden (D2+D5+D61+D91-D995)		158.20	167.95	178.65	188.54	198.96
Selected components of expenditures						
17. Collective consumption	P32	63.75	66.88	68.16	68.41	68.41
18. Total social transfers	D62 + D63	89.01	94.83	98.83	103.99	109.26
18a. Social transfers in kind	P31 = D63	:	:	:	:	:
18b. Social transfers other than in kind	D62	89.01	94.83	98.83	103.99	109.26
19 = 9. Interest expenditure (incl. FISIM)	EDP,D41	6.93	8.27	8.74	10.84	13.47
20. Subsidies	D3	14.53	16.97	18.64	18.82	19.12
21. Gross fixed capital formation	P51	22.65	29.14	30.13	31.91	34.84
22. Other (22 = 23-(17+18+19+20+21)		0.79	:	:	:	:
23.=7. Total expenditures	TE	197.66	216.06	224.50	233.97	245.10
p.m. compensation of public sector employees	D1	40.60	41.44	42.40	42.65	42.65

Source: Ministry of Finance

Table 3. General government expenditure by function

Percentage of GDP	COFOG	2016	2017	2018	2019	2020
1. General public services	1	3.7	4.4	3.6	:	:
2. Defence	2	1.0	0.9	1.0	:	:
3. Public order and safety	3	2.4	2.3	2.2	:	:
4. Economic affairs	4	3.2	3.4	3.7	:	:
5. Environmental protection	5	0.1	0.1	0.1	:	:
6. Housing and community amenities	6	2.1	2.3	2.4	:	:
7. Health	7	4.9	4.9	4.9	:	:
8. Recreation, culture and religion	8	0.7	0.8	0.7	:	:
9. Education	9	3.7	3.8	3.9	:	:
10. Social protection	10	11.3	11.4	11.3	:	:
11. Total expenditure (item 7 = 23 in Table 2)	TE	33.0	34.2	33.8	33.3	32.8

Source: Ministry of Finance

Table 4. General government debt developments

Percentage of GDP	ESA	2016	2017	2018	2019	2020
1. Gross debt		39.5	39.2	42.4	44.6	42.5
2. Change in gross debt ratio		:	-0.4	3.3	2.1	-2.1
Contributions to change in gross debt						
3. Primary balance		1.5	1.6	1.4	1.0	0.5
4. Interest expenditure (incl. FISIM)		1.2	1.3	1.3	1.5	1.8
5. Stock-flow adjustment		-2.7	-3.3	0.5	-0.4	-4.3
of which:						
- Differences between cash and accruals		:	:	:	:	:
- Net accumulation of financial assets		:	:	:	:	:
of which:						
- Privatisation proceeds		:	:	:	:	:
- Valuation effects and other		:	:	:	:	:
p.m. implicit interest rate on debt		3.3	3.5	3.5	3.8	4.3
Other relevant variables						
6. Liquid financial assets		:	:	:	:	:
7. Net financial debt (7 = 1 - 6)		:	:	:	:	:

Source: Ministry of Finance

Table 5. Cyclical developments

Percentage of GDP	ESA	2016	2017	2018	2019	2020
1. Real GDP growth (%)	B1g	2.9	1.6	3.2	3.5	4.0
2. Net lending of general government	EDP.B.9	-2.7	-2.9	-2.7	-2.5	-2.3
3. Interest expenditure	EDP.D.41	1.2	1.3	1.3	1.5	1.8
4. One-off and other temporary measures		:	:	:	:	:
5. Potential GDP growth (%)		2.9	2.7	2.6	2.4	2.2
Contributions (percentage points):						
- *labour*		1.4	1.4	1.2	1.0	0.8
- *capital*		1.9	1.7	1.7	1.7	1.7
- *total factor productivity*		-0.4	-0.4	-0.3	-0.3	-0.2
6. Output gap		0.0	-1.1	-0.5	0.6	2.3
7. Cyclical budgetary component		0.0	-0.3	-0.1	0.2	0.7
8. Cyclically-adjusted balance (2-7)		-2.7	-2.6	-2.6	-2.7	-3.0
9. Cyclically-adjusted primary balance (8-3)		-1.5	-1.3	-1.3	-1.2	-1.2
10. Structural balance (8-4)		:	:	:	:	:

Source: Ministry of Finance

Table 6. Divergence from previous programme

	2016	2017	2018	2019	2020
1. GDP growth					
Previous programme	2.3	3.0	3.5	4.0	:
Latest programme	2.9	1.6	3.2	3.5	4.0
Difference (p.p.)	0.6	-1.4	-0.3	-0.5	:
2. General government net lending (% of GDP)					
Previous programme	-4.0	-3.0	-2.6	-2.2	:
Latest programme	-2.7	-2.9	-2.7	-2.5	-2.3
Difference (p.p.)	1.3	0.1	-0.1	-0.3	:
3. General government gross debt (% of GDP)					
Previous programme	41.3	42.7	43.0	43.9	:
Latest programme	39.5	39.2	42.4	44.6	42.5
Difference (p.p.)	-1.8	-3.5	-0.6	0.7	:

Source: Calculations of the Ministry of Finance

Table 7. Long-term sustainability of public finances

Percentage of GDP	2007	2010	2020	2030	2040	2050	2060
Total expenditure	:	34.8	32.8	31.4	30.3	28.7	27.5
of which:	:	:	:	:	:	:	:
- Age-related expenditures	:	:	:	:	:	:	:
- Pension expenditure	:	8.6	8.9	8.3	7.7	7.1	6.6
- Social security pension	:	:	:	:	:	:	:
- Old-age and early pensions	:	:	:	:	:	:	:
- Other pensions (disability, survivors)	:	:	:	:	:	:	:
- Occupational pensions (if in general government)	:	:	:	:	:	:	:
- Health care	:	4.5	4.8	5.0	5.3	5.7	6.0
- Long-term care (this was earlier included in the health care)	:	:	:	:	:	:	:
Education expenditure	:	4.6	4.8	5.1	5.3	5.3	5.4
Other age-related expenditures	:	:	:	:	:	:	:
Interest expenditure	:	0.7	1.8	1.7	1.6	1.1	0.7
Total revenues	:	32.4	30.5	30.3	29.6	28.7	27.7
of which: property income	:	:	:	:	:	:	:
of which: from pensions contributions (or social contributions, if appropriate)	:	6.0	5.6	5.4	5.2	5.1	4.9
Pension reserve fund assets	:	:	:	:	:	:	:
of which: consolidated public pension fund assets (assets other than government liabilities)	:	:	:	:	:	:	:
Assumptions							
Labour productivity growth	:	2.2	1.8	1.8	1.8	1.8	1.8
Real GDP growth	:	3.4	4.0	3.7	3.4	3.2	3.1
Participation rate males (aged 20-64)[68]	:	77.7	78.7	81.2	83.4	85.1	86.3
Participation rate females (aged 20-64)	:	50.4	53.1	57.8	62.6	67.4	72.0
Total participation rate (20-64)	:	64.2	66.1	69.6	73.1	76.3	79.2
Unemployment rate	:	32.2	19.7	12.9	9.2	6.8	5.2
Population aged 65+ over total population	:	11.7	13.5	15.8	18.6	22.1	26.2

Source: Calculations of the Ministry of Finance

Table 7a. Potential liabilities

% of GDP	2017	2018
Public guarantees	10.0	:
Of which: related to the financial sector	1.8	:

Source: Ministry of Finance

Table 8. Basic assumptions on the external economic environment underlying the programme framework

	Dimension	2016	2017	2018	2019	2020
Short-term interest rate	Annual average	-0.3	-0.3	-0.3	-0.1	0.1
Long-term interest rate	Annual average	0.8	1.1	1.1	1.4	1.7
USD/EUR exchange	Annual average	1.1069	1.1295	1.178	1.178	1.178
Nominal effective exchange rate	Annual average	:	:	:	:	:
Exchange rate vis-à-vis the EUR	Annual average	61.60	61.60	61.60	61.60	61.60
Global GDP growth, excluding EU	Annual average	3.4	3.8	4.0	4.0	4.0
EU GDP growth	Annual average	1.9	2.3	2.1	1.9	2.0
Growth of relevant foreign markets	Annual average	:	:	:	:	:
World import volumes, excluding EU (y-o-y)	Annual average	1.3	4.2	4.1	4.1	4.1
Oil prices (Brent, USD/barrel)	Annual average	44.8	54.3	61.6	58.9	57.3

Source: European Commission, Economic Forecast Autumn 2017 and European Central Bank

[68] Labour market calculation refer to the 15-64 age group

Table 9. Selected employment and social indicators

	Data source	2014	2015	2016	2017*	2018*
1. Labour market participation rate (%) total (aged 15+)	SSO	57.3	57.0	56.5	:	:
- male	SSO	69.3	68.9	69.2	:	:
- female	SSO	45.3	44.9	43.8	:	:
2. Employment rate (%) total (aged 15+)	SSO	41.2	42.1	43.1	44.1	44.9
- male	SSO	50.1	50.5	52.3	:	:
- female	SSO	32.4	33.7	33.8	:	:
3. Unemployment rate (%) total (aged 15+)	e	28.0	26.1	23.7	22.4	21.5
- male	e	27.6	26.7	24.4	:	:
- female	e	28.6	25.1	22.7	:	:
4. Long-term unemployment rate (%) of total unemployment	SSO	23.4	21.3	19.2	:	:
- male	SSO	23.1	22.1	20.1	:	:
- female	SSO	23.8	20.1	17.8	:	:
5. Youth unemployment (15-24 yrs) rate (%)	e	53.1	47.3	48.2	:	:
- male	e	52.0	49.7	47.9	:	:
- female	e	55.0	43.3	48.8	:	:
6. Young people (aged 15-24) not in employment, education or training (NEET), in %	e	25.2	24.7	24.3	:	:
7. Early school leavers, in % (aged 18-24)	e	12.5	11.4	9.9	:	:
8. Participation rate in early childhood education and care	e	:	:	:	:	:
9. GINI coefficient	e	35.2	33.7	33.6	:	:
10. Inequality of income distribution S80/S20, %	e	7.2	6.6	6.6	:	:
11. Social protection expenditure in % of GDP	MoF	:	11.3	11.3	11.4	11.3
12. Health expenditure in % of GDP	MoF	:	5.0	4.9	4.9	4.9
13. At-risk-of-poverty before social transfers and pensions, % of the population	e	41.7	40.5	41.6	:	:
14. Poverty rate	e	22.1	21.5	21.9	:	:
15. Poverty gap	e	:	:	:	:	:

*Data for 2017 and 2018 is forecast

Table 10. Matrix of policy commitments

Description of policy	2016	2017	2018	2019
Measure 1: Harmonization of the Public Procurement Legal framework with the Acquis				
A. Duration of the reform*		X	X	X
B. Net direct budgetary impact (if any) (in €)	0	13,000	-5,000	5,000
B.1 Direct impact on budgetary revenue (in €)	0	40,000	50,000	55,000
B.2 Direct impact on budgetary expenditure (in €)	0	27,000	55,000	50,000
B.3 Possible non-budgetary financing (in €)	0	50,000	0	0
- B.3.1 Of which committed IPA funding including WBIF funding (in €)	0	0	0	0
Measure 2: Improvement of Internal financial control				
A. Duration of the reform*				
B. Net direct budgetary impact (if any) (in €)	0	0	0	0
B.1 Direct impact on budgetary revenue (in €)	0	0	0	0
B.2 Direct impact on budgetary expenditure (in €)	0	0	0	0
B.3 Possible non-budgetary financing (in €)	0	333,000	333,000	333,000
- B.3.1 Of which committed IPA funding including WBIF funding (in €)	0	333,000	333,000	333,000
Measure 3: Increasing the competitiveness of the electricity market				
A. Duration of the reform*				
B. Net direct budgetary impact (if any) (in €)	0	0	-400,000	-600,000
B.1 Direct impact on budgetary revenue (in €)	0	0	0	0
B.2 Direct impact on budgetary expenditure (in €)	0	0	400,000	600,000
B.3 Possible non-budgetary financing (in €)	0	0	0	0
- B.3.1 Of which committed IPA funding including WBIF funding (in €)	0	0	0	0
Measure 4: Promotion of renewable energy sources and improvement of energy efficiency				

A. Duration of the reform*				
B. Net direct budgetary impact (if any) (in €)	0	0	0	0
B.1 Direct impact on budgetary revenue (in €)	0	0	0	0
B.2 Direct impact on budgetary expenditure (in €)	0	0	0	0
B.3 Possible non-budgetary financing (in €)	0	400,000	0	0
- B.3.1 Of which committed IPA funding including WBIF funding (in €)	0	0	0	0
Measure 5: Facilitating Macedonia-Serbia cross-border crossing				
A. Duration of the reform*				
B. Net direct budgetary impact (if any) (in €)	0	0	0	0
B.1 Direct impact on budgetary revenue (in €)	0	0	0	0
B.2 Direct impact on budgetary expenditure (in €)	0	0	0	0
B.3 Possible non-budgetary financing (in €)	0	380,000	2,000,000	1,500,000
- B.3.1 Of which committed IPA funding including WBIF funding (in €)	0	380,000	0	0
Measure 6: Improving of irrigation systems				
A. Duration of the reform*				
B. Net direct budgetary impact (if any) (in €)	15,055,216	34,120,521	50,504,886	34,625,407
B.1 Direct impact on budgetary revenue (in €)				
B.2 Direct impact on budgetary expenditure (in €)	15,055,216	34,120,521	50,504,886	34,625,407
B.3 Possible non-budgetary financing (in €)	1,455,111	325,733	651,466	2,996,743
- B.3.1 Of which committed IPA funding including WBIF funding (in €)	652,000	325,733	651,466	2,996,743
Measure 7: Consolidation and defragmentation of agricultural land				
A. Duration of the reform*				X
B. Net direct budgetary impact (if any) (in €)	0	-330,000	-330,000	-340,000
B.1 Direct impact on budgetary revenue (in €)	0	0	0	0
B.2 Direct impact on budgetary expenditure (in €)	0	330,000	330,000	340,000
B.3 Possible non-budgetary financing (in €)	598,500	780,594	780,595	500,000
- B.3.1 Of which committed IPA funding including WBIF funding (in €)	500,000	780,594	780,595	500,000
Measure 8: Agricultural cooperatives				
A. Duration of the reform*				
B. Net direct budgetary impact (if any) (in €)	-47,000	-845,000	-1,060,000	-1,060,000
B.1 Direct impact on budgetary revenue (in €)	0	0	0	0
B.2 Direct impact on budgetary expenditure (in €)	47,000	845,000	1,060,000	1,060,000
B.3 Possible non-budgetary financing (in €)	0	1,800,000	0	1,500,000
- B.3.1 Of which committed IPA funding including WBIF funding (in €)	0	1,800,000	0	1,500,000
Measure 9: Supporting activities for attracting FDIs and investments by domestic companies				
A. Duration of the reform*		x	x	x
B. Net direct budgetary impact (if any) (in €)	0	- 20,000,000	- 20,000,000	- 20,000,000
B.1 Direct impact on budgetary revenue (in €)	0	0	0	0
B.2 Direct impact on budgetary expenditure (in €)	0	20,000,000	20,000,000	20,000,000
B.3 Possible non-budgetary financing (in €)	0	0	0	0
- B.3.1 Of which committed IPA funding including WBIF funding (in €)	0	0	0	0
Measure 10: Support for Investments				
A. Duration of the reform*		x	x	x
B. Net direct budgetary impact (if any) (in €)	0	- 5,000,000	- 5,000,000	- 5,000,000
B.1 Direct impact on budgetary revenue (in €)	0	0	0	0
B.2 Direct impact on budgetary expenditure (in €)	0	5,000,000	5,000,000	5,000,000
B.3 Possible non-budgetary financing (in €)	0	0	0	0
- B.3.1 Of which committed IPA funding including WBIF funding (in €)	0	0	0	0

Measure 11: Improving the competitiveness of domestic companies for new markets				
A. Duration of the reform*		x	x	x
B. Net direct budgetary impact (if any) (in €)	0	- 5,000,000	- 5,000,000	- 5,000,000
B.1 Direct impact on budgetary revenue (in €)	0	0	0	0
B.2 Direct impact on budgetary expenditure (in €)	0	5,000,000	5,000,000	5,000,000
B.3 Possible non-budgetary financing (in €)	0	0	0	0
- B.3.1 Of which committed IPA funding including WBIF funding (in €)	0	0	0	0
Measure 12: Increasing competitiveness in Tourism & Hospitality Sector				
A. Duration of the reform*	X	X	X	X
B. Net direct budgetary impact (if any) (in €)	0	- 1,000,000	- 2,100,000	0
B.1 Direct impact on budgetary revenue (in €)		0	0	0
B.2 Direct impact on budgetary expenditure (in €)	0	1,000,000	2,100,000	0
B.3 Possible non-budgetary financing (in €)	4,300,000	8,000,000	5,800,000	1,000,000
- B.3.1 Of which committed IPA funding including WBIF funding (in €)	4,000,000	7,000,000	4,800,000	0
Measure 13: Development of a National E-Services Portal				
A. Duration of the reform*	X		X	
B. Net direct budgetary impact (if any) (in €)	-30,046	-493,351	0	0
B.1 Direct impact on budgetary revenue (in €)	0	0	0	0
B.2 Direct impact on budgetary expenditure (in €)	30,046	493,351	0	0
B.3 Possible non-budgetary financing (in €)	270,416	296,667	100,000	0
- B.3.1 Of which committed IPA funding including WBIF funding (in €)	270,416	196,667	0	0
Measure 14: Improving infrastructure and access to finance for research, development and innovation				
A. Duration of the reform*		X		
B. Net direct budgetary impact (if any) (in €)	0	-1,667,000	-1,350,000	-1,283,000
B.1 Direct impact on budgetary revenue (in €)	0			
B.2 Direct impact on budgetary expenditure (in €)	0	1,667,000	1,350,000	1,283,000
B.3 Possible non-budgetary financing (in €)	0	40,000	0	0
- B.3.1 Of which committed IPA funding including WBIF funding (in €)	0	40,000	0	0
Measure 15: Trade facilitation				
A. Duration of the reform*				
B. Net direct budgetary impact (if any) (in €)	0	0	-51,500	0
B.1 Direct impact on budgetary revenue (in €)	0	0	0	0
B.2 Direct impact on budgetary expenditure (in €)	0	0	51,500	0
B.3 Possible non-budgetary financing (in €)	0	0	0	0
- B.3.1 Of which committed IPA funding including WBIF funding (in €)	0	0	0	0
Measure 16: Further development of the qualification system				
A. Duration of the reform*				
B. Net direct budgetary impact (if any) (in €)	-1,822,635	-1,617,632	-263,650	-288,750
B.1 Direct impact on budgetary revenue (in €)	0	0	0	0
B.2 Direct impact on budgetary expenditure (in €)	1,822,635	1,617,632	263,650	288,750
B.3 Possible non-budgetary financing (in €)	2,043,000	3,000	310,000	310,000
- B.3.1 Of which committed IPA funding including WBIF funding (in €)	2,043,000	3,000	310,000	310,000
Measure 17: Upgrading the active measures included in the Operational Plan for Active Employment Programs and Measures and Labour Market Services				
A. Duration of the reform*		X	X	X
B. Net direct budgetary impact (if any) (in €)	0	-16,000,000	-16,000,000	-16,000,000
B.1 Direct impact on budgetary revenue (in €)	0			
B.2 Direct impact on budgetary expenditure (in €)	0	16,000,000	16,000,000	16,000,000
B.3 Possible non-budgetary financing (in €)	0	0	0	0
- B.3.1 Of which committed IPA funding including WBIF funding (in €)	0	0	0	0
Measure 18: Youth guarantee				

A. Duration of the reform*				
B. Net direct budgetary impact (if any) (in €)	0	-1,595,000	-12,628,000	-12,628,000
B.1 Direct impact on budgetary revenue (in €)	0	0	0	0
B.2 Direct impact on budgetary expenditure (in €)	0	1,595,000	12,628,000	12,628,000
B.3 Possible non-budgetary financing (in €)	0	0	0	0
- B.3.1 Of which committed IPA funding including WBIF funding (in €)	0	0	0	0
Measure 19: Enhancement of financial benefits in the field of social protection[69]				
A. Duration of the reform*				
B. Net direct budgetary impact (if any) (in €)	0	0	0	0
B.1 Direct impact on budgetary revenue (in €)	0	0	0	0
B.2 Direct impact on budgetary expenditure (in €)	0	0	0	0
B.3 Possible non-budgetary financing (in €)	0	0	0	0
- B.3.1 Of which committed IPA funding including WBIF funding (in €)	0	0	0	0
Total net budgetary impact				
Total impact on budgetary revenues	0	40,000	50,000	55,000
Total impact on budgetary expenditures	16,954,896	87,695,504	114,743,036	96,875,157

* indicate start and, if needed, end with an “X” mark

[69] The funds for implementation of planned activities will be secured within a World Bank project, but the exact amounts will be known after completing detailed analyzes and preparation of the legal solution

Table 11: Reporting on the implementation of the structural reform measures of the ERP 2016-2018 and the ERP 2017-2019

	Measure 1: Public Finance Management Reform Programme
Activities planned for 2016 and 2017	The adoption of the Public Finance Reform Program as an activity was foreseen in the Economic Reform Program 2017-2019. The program addresses priorities, measures and activities for improvement of several segments of public finances: strengthening and implementation of the medium-term budgetary framework and budget planning, introduction of an integrated information system for managing public finances, improvement of the harmonization, efficiency and effectiveness of the public procurement system, modernization of the tax system and improvement of tax collection, increasing the quality of customs procedures and services, improving the public internal financial control and effectiveness of the external audit.
Have the activities planned for 2016 and 2017 been implemented?	Yes, the program was adopted by the Government on December 19, 2017.
If yes/partially, include: -Description of steps taken -Timeline of implemented actions -Difficulties and delays in implementation -Whether the reform will continue in 2018	In 2017, the draft program was finalized; The Ministry of Finance, as coordinator and institution in charge of some of the activities, organized a public event for consultation with all stakeholders on the proposed measures; A Sectoral Planning Document was prepared containing the measures and activities of the Program proposed to be financed under EU IPA 2 Instrument; Subsequently to the Sectoral Planning Document, an Action Document is currently under preparation, containing specific project proposals for the proposed measures, which are expected to be implemented from 2018 onwards, depending on each individual project cycle.
If no, explain why not	/
Actual cost of implementation and impact on the annual budget (indicate deviation from estimated costs if any)	The estimated total indicative cost for implementation of the Public Finance Management Reform Program is around EUR 40 million, of which approximately EUR 8 million are national co-financing, and the rest is envisaged to be provided with donor support. Indicative value of the Action document with specific project proposals for the proposed measures is around EUR 18 million.
	Measure 2: System (IT platform) for co-ordination, management, monitoring and evaluation of funds on regional and local level (SiReRa)
Activities planned for 2016 and 2017	Establishment of a System (IT Platform) with several components (human resources, projects, programs and finances) will provide information and support to the process of planning and implementation of regional and local development activities in order to improve the socio-economic conditions and quality of life. The system will monitor the implementation and allocation of funds from the Budget of the Republic of Macedonia and various donors and will provide information for adoption of future strategic decisions. For 2016 and 2017, development of documentation in terms of the IT system, establishment of a legal and organizational framework for the functioning of the system, provision of funds for implementation of the activities and start of implementation was planned
Have the activities planned for 2016 and 2017 been implemented?	Partially.
If yes/partially, include: -Description of steps taken -Timeline of implemented actions -Difficulties and delays in implementation -Whether the reform will continue in 2018	The activities for 2016 were realized, i.e. detailed concepts were developed for the operations of the subsystems of the System, that is, human resources (including training), programs and projects (including monitoring budgets and monitoring the development of the planning regions). The activities for 2017 have been partially implemented, i.e. an agreement has been signed with a donor, which provides 50% of the funds for realization, while 50% is provided by the Government. However, due to the electoral process in 2017, the Agreement for the implementation of the activities and the start of the implementation has not yet been realized. Activities started in January 2018. According to the European Commission's Assessment of the Economic Reform Program 2017-2019, the measure was assessed to be more appropriate to be included in public administration reform and is therefore not part of ERP 2018-2020.
If no, explain why not	/

Actual cost of implementation and impact on the annual budget (indicate deviation from estimated costs if any)	There is no deviation. Funds are provided within the 2018 Budget of RM in the amount of EUR 150,000 euros per year in the next three years.
	Measure 3: Joint border railway station Macedonia - Serbia
Activities planned for 2016 and 2017	In 2016 - Starting the Consultant's engagement (IPF4 / COWI) - Realization of Phase 1 of the Project, which includes preparation of a Report on estimated needs of the official staff from the Republic of Macedonia and the Republic of Serbia, as well as preparation of the Concept design of the joint border station with accompanying contents - Adoption of documents from Phase 1 In 2017 - Starting Phase 2 of the engagement of consultants, which includes preparation of a Feasibility Study, urban plans, Environmental Impact Assessment, investment and technical documentation, tender documentation for selection of contractor and project task for selection of consultants who will perform expert supervision over the construction, preparation of an Investment grant application for the WBIF instrument.
Have the activities planned for 2016 and 2017 been implemented?	Partially
If yes/partially, include: -Description of steps taken -Timeline of implemented actions -Difficulties and delays in implementation -Whether the reform will continue in 2018	The foreseen activities for 2016 were fully completed, that is, in October 2016, the Steering Committee for monitoring and managing all activities of the Project set up for this Project, in which there are members of all the involved institutions from the Republic of Macedonia and the Republic of Serbia, approved and accepted the Report on the estimated needs the official staff of the Republic of Macedonia and the Republic of Serbia and the concept design, thus completing Phase 1 of the Consultants Engagement. By the end of 2016 and early 2017, the Consultants worked on the need for budget increase, ie in January 2017 additional funds were located in the Budget and they were approved by the WBIF. In February 2017, the first kick-off meeting was held for Phase 2 of the consultant's engagement. The consultant started with the development of the urban planning documentation and in parallel will work on the preparation of the Feasibility Study and the Environmental Report. The reform will continue in 2018 and beyond.
If no, explain why not	/
Actual cost of implementation and impact on the annual budget (indicate deviation from estimated costs if any)	/
	Measure 4: Upgrading and rehabilitation of transport Corridor X
Activities planned for 2016 and 2017	The upgrading and rehabilitation of the Transport Corridor X will enable the entire road Corridor X to be completed at the level of a highway, and together with the rehabilitation of the sections along the Corridor X, the capacity and the overall efficiency of the E-75 North-South route will be improved. Also, an extension and modernization of the railway Corridor X is envisaged. 2016 - Rehabilitation of the railway station Skopje - Rehabilitation of bridges along Corridor 10 with a grant from NATO 2017 - Construction of the road section Demir Kapija - Smokvica in the length of 28.3 km - Rehabilitation and upgrading of the section Smokvica - Gevgelija in the length of 10.15 km. - Rehabilitation and upgrading of the left section of the highway section Kumanovo-Miladinovci in the length of about 22.5 km

	- Rehabilitation of the section Negotino-Demir Kapija - Reconstruction of the railway section Negotino - Nogaevci in a length of 30 km - Modernization of 10 railway stations along Corridor X.
Have the activities planned for 2016 and 2017 been implemented?	Yes/Partially
If yes/partially, include: -Description of steps taken -Timeline of implemented actions -Difficulties and delays in implementation -Whether the reform will continue in 2018	Due to the poor financial condition of the Contractor, the realization of the construction activities for the repair of the section from Nogaevtsi to Negotino is taking place at a slower pace. The activities will continue in 2018. The contract for construction works concluded between Macedonian Railways and the Contractor was extended by Annexes on six occasions, ie the Contractor should complete the construction activities as of 31.12.2017. Due to poor progress, it is more than certain that the deadline for performance will continue in 2018. In parallel with the extension of the deadline for the completion of construction works, so far, the last date of availability of the loan is also extended, so until 31.12.2017 all funds from the loan should be withdrawn. Due to the poor progress of the works and the need to extend the deadline for the construction activities for 2018, the last date of availability of the loan should be re-extended.
If no, explain why not	/
Actual cost of implementation and impact on the annual budget (indicate deviation from estimated costs if any)	There is no deviation from the estimated costs.
	Measure 5: Upgrading and rehabilitation of transport Corridor VIII
Activities planned for 2016 and 2017	2017 - Construction of the highway A2, section Kicevo - Ohrid (57 km) - The construction of Kumanovo-Beljakovce, according to the Building Agreement concluded between the Macedonian Railways and the Contractor, was to be completed in September 2016. However, due to numerous problems, the project is not completed within the deadline, i.e. as of September 2016, the financial progress is 18.99%. The unit is no longer operational, leading to a standstill in operation. - Beljakovce-Kriva Palanka, the elaboration of the basic projects is in the final phase. A tender has been launched for the selection of a contractor in May 2016. By the deadline - 22.07.2016, 17 applications submitted pre-qualification documentation. Applications evaluation is ongoing. At the Summit in Trieste (July 12, 2017), an investment grant in the amount of EUR 70,000,000 was granted for this section, with which the loan debt of 145,000,000 euros will be reduced for the awarded grant. The unit is no longer operational, leading to a standstill in operation. - Preparation of a basic project with tender documentation for construction of the railway section Kriva Palanka - Deve Bair, border with the Republic of Bulgaria: in December 2017 the engagement of the consultants who prepared the basic documentation was completed. - Preparation of a basic project with tender documentation for the construction of a new railway section from Kicevo to Lin, border with Albania: in December 2017 the engagement of the consultants who prepared the basic documentation was completed.
Have the activities planned for 2016 and 2017 been implemented?	1. For the section Kumanovo-Beljakovce: Partially 2. For the Beljakovce-Kriva Palanka section: Partially 3. For the section from Kriva Palanka - Deve Bair, the border with the Republic of Bulgaria: Yes, activities are completed by end-2017.
If yes/partially, include: -Description of steps taken -Timeline of implemented actions -Difficulties and delays in implementation -Whether the reform will continue in 2018	1. For the section Kumanovo-Beljakovce, a draft text of the Annex to the Construction Contract has been submitted with the aim of continuing the deadline until May 2019. EBRD does not approve the Annex because, with the Annex, besides the extension of the deadline for execution, the Contractor also requires additional financial resources that are not quantified, ie the Bank requires that the financial implications of the Project need to be presented. In the first half of 2017, the Bank appointed its consultants who made an assessment of the progress achieved in terms of ecology and physical realization of the Project. Upon receiving the reports from these two missions, the Bank will come out with its position regarding the delays of the Project. The Project Implementation Unit is required to resume operation. 2. For the Beljakovce-Kriva Palanka section, the Project Implementation Unit is required to resume work, so that the assessment of the

	applications for prequalification can continue. The engagement of the consultant who prepares the basic projects and should provide technical assistance with regard to the contractor's choice, should be continued until the conclusion of an agreement with the contractor. 3. For the section of Kriva Palanka-Deve Bair, the border with the Republic of Bulgaria: the activities for preparation of a basic project with tender documentation were completed in 2017.
If no, explain why not	/
Actual cost of implementation and impact on the annual budget (indicate deviation from estimated costs if any)	There is no deviation from the estimated costs.
	Measure 6: Construction of 400kV Overhead Transmission Line SS Bitola 2 to Macedonia-Albania border and SS 400/110 kV Ohrid
Activities planned for 2016 and 2017	1. Macedonia - Albania Interconnection phase 1 This project contains several parts: GRANT Designing: Macedonia - Albania interconnection phase 1 - main project for 400 kV transmission line Bitola-Ohrid and 400 / 110kV substation in Ohrid While the proceeds of the loan are intended for: 1. Construction of 400 kV transmission line TS Bitola 2-MK-AL border 2. Construction of a new 400/110 kV SS near Ohrid 3. New 400 kV field in S / S Bitola 2 4. Improvement of Smart Grid - Smart Network in AD MEPSO Funds are provided by: EBRD Loan for realization of projects of importance for AD MEPSO 37 million Euros Grant 12 million Euros, signed on 22.02.2016, received from IPA II and Luxembourg The main activity is the preparation of Macedonia - Albania interconnection phase 1 - main project for 400 kV transmission line Bitola-Ohrid and 400 / 110kV substation in Ohrid - GRANT
Have the activities planned for 2016 and 2017 been implemented?	1. Partially
If yes/partially, include: -Description of steps taken -Timeline of implemented actions -Difficulties and delays in implementation -Whether the reform will continue in 2018	Tender documentation is prepared for a certain number of sub-projects. Tenders are published and for some of them the evaluation processes are ongoing. - the activities have been started will be carried out over a period of 18 months. - long-term tender procedures with an overview of the evaluations. -Yes, the reforms will continue in 2018
If no, explain why not	/
Actual cost of implementation and impact on the annual budget (indicate deviation from estimated costs if any)	/
	Measure 7: Revitalisation and modernization of the transmission network and power system management
Activities planned for 2016 and 2017	The project itself is supported by the EBRD Loan, the Loan Agreement was signed on December 18, 2013. This ensures uninterrupted conditions for performing the projects.

	The structure of the loan and the sources of funding are listed in the table below
	
	Sources of financing — EUR
	Own funds
	  MEPSO — 15,500,000
	Loan
	  EBRD — 25,000,000
	Total — 40,500,000
	
	This type of loan that AD MEPSO has taken from the EBRD is without state guarantee, which confirms the capacity of the company to deliver timely payment of the arrears.
	The Loan funds are intended for realization of the following activities:
	1. Procurement of high voltage and protection equipment for sub-stations
	2. Remote monitoring, video supervision, controlling and adjustment of substations
	3. Telecommunication equipment for closing of optical network in the transmission grid and preparation of a model for maximum utilization)
	4. Rehabilitation of the 110kV transmission line
	5. Consulting services to the Project Implementation Unit)
	These projects are performed recognizing/observing:
	• the need to improve the stability and reliability of the power system, increase the efficiency of the company
	• the existing condition of the old equipment in the substations and the problems that exist in its manipulation
	• technical inability to remotely manipulate existing equipment through SCADA systems
	• the difficulties and risks of exploitation due to equipment obsolescence
	• Inability for regular maintenance due to lack of spare parts that are not produced for years
	• Improvement of the environment
	• savings in maintenance costs of equipment
	• Increasing the security factor in the supply of electricity to the transmission system in all substations where new equipment is planned
	• improving the reliability of the power supply, for the regions listed, covered by these transmission lines

Have the activities planned for 2016 and 2017 been implemented?	1. Partially
If yes/partially, include: -Description of steps taken -Timeline of implemented actions -Difficulties and delays in implementation -Whether the reform will continue in 2018	-Prepared tender documentation for a number of sub-projects. Published tenders and for some of them the evaluation processes are ongoing. - the started activities are carried out over a period of 18 months. - long-term tender procedures with an overview of the evaluations. - Yes, the reforms will continue in 2018
If no, explain why not	/
Actual cost of implementation and	/

impact on the annual budget (indicate deviation from estimated costs if any)	
	Measure 8: Improvement of Irrigation Systems
Activities planned for 2016 and 2017	For continuous and long-term investments in irrigation and drainage infrastructure, a ten-year planning document was prepared "Investment Plan for Water Management Infrastructure for the period 2015-2025". This plan includes: Rehabilitation and reconstruction of the existing irrigation and drainage infrastructure in order to achieve sustainability in water use; Upgrading and expanding the existing hydro systems in order to increase irrigated area in the country; and Construction of new large facilities in the Macedonian hydrosystem. 1. Finishing construction of road to location where Orizarska dam will be constructed and obtaining of construction license. 2. Construction works of dam going on for building of dam Konsko 3. Obtaining construction license for building of irrigation system Raven Rechica 4. Finishing technical and planning documentation for construction of dam on Slupchanska river and applying for construction license 5. Finishing tender documents for second stage – irrigation and third stage – hidro power plants of hydro system Zletovica 6. Starting construction works on irrigation system South Vardar – second stage 7. Tender dosier preparation for construction of 8-10 small irrigation systems under 300 ha (IPA).
Have the activities planned for 2016 and 2017 been implemented?	1. Partially 2. Yes 3. Partially 4. Yes 5. Yes 6. Partially 7. Yes
If yes/partially, include: -Description of steps taken -Timeline of implemented actions -Difficulties and delays in implementation -Whether the reform will continue in 2018	**Construction of the dam Konsko** According to the terms of the contract, the preparatory works at the construction site are completed and construction works are underway. **Construction of a dam on the river Orizarska** The construction of the access road is in the final stage. The works for the construction of the dam have not been started, because a procedure for obtaining a building permit is underway. **Construction of HS Raven – Rechitsa** Performance and performance oversight agreements have been concluded. Construction works have not started because the building permit has not yet been provided. **Construction of a dam on the river Slupchanska** A preliminary design and technical solution for the optimal type of dam and associated facilities were developed. According to the dynamics, it is envisaged that the realization of these two contracts (design and revision) will end in 2017. **Hydro system Zletovica** By the end of 2017, the preparation of the technical documentation for Phase II - Irrigation and Phase III – Energy should be completed. **Hydrosystem Lisice** Regular activities for managing the hydro system. **Irrigation of the South Vardar Valley** Currently, the procedure for selecting a contractor for the Irrigation System South Vardar Valley second phase is underway. **Construction of small irrigation systems up to 300 ha funded through IPA** An agreement was signed for the preparation of tender documentation for the construction of 6-8 small irrigation systems.

	The realization of all listed projects will continue in the course of 2018
If no, explain why not	Activities will continue during 2018 according to signed agreements with contractors.
Actual cost of implementation and impact on the annual budget (indicate deviation from estimated costs if any)	Actual budget cost for these projects in 2017 is EUR 1.211.911 (up to October 2017), expected payment until end of 2017 is EUR 11.307.197. Total estimated cost for those projects in 2017 was EUR 12.050.330.
	Measure 9: Consolidation and defragmentation of agricultural land
Activities planned for 2016 and 2017	1. Continuation of the project activities (2 pilot projects for land consolidation) with the project supported by FAO "Support to implement a national land consolidation program". 2. Signing of the project "Introduction of the national land consolidation program" (MAINLAND). 3. Raising awareness of the consolidation procedures and identification of new consolidation regions; Initiative of the process of capacity building of MAFWE and other stakeholders for successful implementation of the projects for consolidation of agricultural land; Initiative of the process of development of tools and procedures for implementation of consolidation projects; Establish a monitoring and evaluation system.
Have the activities planned for 2016 and 2017 been implemented?	1. 2016 -yes, 2017 -no 2. yes 3. partly
If yes/partially, include: -Description of steps taken -Timeline of implemented actions -Difficulties and delays in implementation -Whether the reform will continue in 2018	- Initiative of the process of capacity building of MAFWE and other stakeholders for successful implementation of the projects for consolidation of agricultural land; Initiative of the process of development of tools and procedures for implementation of consolidation projects; Improving the legal framework and the law on consolidation of agricultural land. - End of 2017 - Delay in the procedure of amending the Law on Consolidation of Agricultural Land. -yes
If no, explain why not	/
Actual cost of implementation and impact on the annual budget (indicate deviation from estimated costs if any)	/
	Measure 10: Agricultural cooperatives
Activities planned for 2016 and 2017	1. Encouraging the process of market-oriented association of farmers in agricultural cooperatives; 2. Providing continuous financial support for cooperatives (continuous implementation of measures from the previous period) and 3. Support for investments in processing, finalization and marketing of agricultural products.
Have the activities planned for 2016 and 2017 been implemented?	1. No 2. Partially 3. No
If yes/partially, include: -Description of steps taken -Timeline of implemented actions -Difficulties and delays in	2. Public call for applications for using of funds from the 2017 Program for Financial Support of the Rural Development for measure "Economic Association of Agricultural Holdings for the Joint Agriculturalal Activities" and submeasure "Establishment and functioning of agricultural cooperatives registered in the Register of agricultural cooperatives " Calls are published quarterly, in accordance with the agreement with the Macedonian Association of Agricultural Cooperatives (MAZZ), as

implementation -Whether the reform will continue in 2018	follows: • for the first quarter no later than 15 April 2017; • for the second quarter no later than 15 July 2017; • for the third quarter no later than October 15, 2017 and • for the fourth quarter no later than December 31, 2017. - The measure will continue in 2018
If no, explain why not	/
Actual cost of implementation and impact on the annual budget (indicate deviation from estimated costs if any)	The budget for measure 131 "Economic association of agricultural holdings for common agricultural activities" for 2017 is planned in the amount of EUR 975.000 and after the payment of the obligations from the budget from the previous year remained EUR 47.000.
	Measure 11: Increasing competitiveness in Tourism & Hospitality Sector
Activities planned for 2016 and 2017	The activities planned for 2016 and 2017 were aimed at improving access to foreign markets, for which activities were carried out with entities in Ohrid. Activities were also directed towards managing destinations in tourism, with paragliding covered as part of the market. In order to improve the tourist service, activities were also undertaken to improve the work of the tourist guides within the travel agencies.
Have the activities planned for 2016 and 2017 been implemented?	Yes
If yes/partially, include: -Description of steps taken -Timeline of implemented actions -Difficulties and delays in implementation -Whether the reform will continue in 2018	In the period 2016-2017, the following interventions were carried out: – Learning best practices for students in tourism and hospitality in Macedonia – Improving the standards for operation of tourist guides – Improving the experience of paragliders in Krushevo – Training for professionals in tourism through sharing experience and knowledge exchange – Measures for energy efficiency in hotels – Master training in revenue and expenditure management, distribution and sales techniques for management and quality of customer-oriented services and customer communication. – Organization of the first regional conference on active tourism – Support and development of a Model for Successful Tourism for Winter Sports in Mavrovo. – Sharing knowledge and skills for improving mountain tourism in Mavrovo Support interventions will continue in 2018, depending on the needs of the market.
If no, explain why not	/
Actual cost of implementation and impact on the annual budget (indicate deviation from estimated costs if any)	There are no costs envisaged in the Budget of the Republic of Macedonia. The activities are planned and implemented with donor funds in the amount of 6.25 million Swiss franks for the entire duration of the project (from 1 April 2015 to 30 March 2019).
	Measure 12: Increasing competitiveness in Creative Industries Sector
Activities planned for 2016 and 2017	Activities for 2016 and 2017 include support for access to the market for designers, designing with social impact, increasing the export of IT companies and support services for IT companies.
Have the activities planned for 2016 and 2017 been implemented?	Partially

If yes/partially, include: -Description of steps taken -Timeline of implemented actions -Difficulties and delays in implementation -Whether the reform will continue in 2018	In the period 2016-2017, the following interventions have been implemented/ supported: – Mentorship for better success of companies owned by women – Providing consultancy assistance for women entrepreneurs – Measures to support youth employment – Support the design of creative solutions in the fields of economy, culture and social innovation – "Hobbies that will turn into Profession" - support the opportunities for employment of young people and women. The measure will continue to be implemented, only delayed for the deployment of an adequate local implementer. This is why it is not proposed as a measure in the ERP 2018-2020.
If no, explain why not	/
Actual cost of implementation and impact on the annual budget (indicate deviation from estimated costs if any)	There are no costs envisaged in the Budget of the Republic of Macedonia. The activities are planned and implemented with donor funds in the amount of 6.25 million Swiss franks for the entire duration of the project (from 1 April 2015 to 30 March 2019).
	Measure 13: Development of National Portal for e-services
Activities planned for 2016 and 2017	This project is implemented through a concluded service contract that is funded under IPA 2012 and contains two components and several measures and activities, including: **Component 1:** MISA assistance in the implementation of eGovernment policies **Operation 1.1.** Improving the legal framework for electronic governance **Operation 1.2.** Implementation of e-services (Solution for Population Register and national e-services portal) Activity: Development of a population register solution Activity: Development of a national e-services portal that uses the system for interoperability, which will function as: - Register of e-services - System for development and management of e-services - System for authentication and user management At the same time, the integration of existing e-services will be carried out and the system will offer an option for e-payment of all costs. Activity: Increased use of e-services by end-users Activity: Plan for communication and promotion of the population register Activity: Strengthening the capacities of Internet clubs as support centers for the use of electronic administrative services **Operation 1.3.** Improve the measurement of service quality Activity: Upgrading of the one-stop mechanism in terms of technical, organizational and legal aspect Activity: Development of an integrated background system for "evaluating administration" Activity: Strengthening the capacities for providing administrative services Activity: Improving the process of bringing administrative services **Component 2:** Strengthening the capacity of MISA to coordinate horizontal policies Operation 2.1. Improve coordination of horizontal policies in relation to PAR Operation 2.2. Improve the coordination of horizontal policies regarding the development of the information society
Have the activities planned for 2016 and 2017 been implemented?	Partially
If yes/partially, include: -Description of steps taken -Timeline of implemented actions	The activity related to the national e-services portal started with the selection and analysis of the relevant EU regulations (Directive 95/46 and Regulation 2016/679 and Directive 2003/98) as well as the relevant documents (Action Plan 2016-2020 for eGovernment, the updated European Interoperability Framework and eGovernment Report 2016). An analysis of the Law on Electronic Management and its bylaws and the first

-Difficulties and delays in implementation -Whether the reform will continue in 2018	draft guidelines for its audit and guidelines for meeting the EU requirements regarding electronic identification has been initiated. At the same time, steps were taken to design and establish the functional architecture of the solution. This includes the decomposition of the general components and the definition of their functionalities as an integral part of the National e-Portal. The implementation of all activities is in accordance with the work plan defined at the initial stage of the project. The activities will continue in 2018 (July).
If no, explain why not	The implementation of all activities is in accordance with the work plan defined at the initial stage of the project (July 2018).
Actual cost of implementation and impact on the annual budget (indicate deviation from estimated costs if any)	There is no deviation (the project is funded under the IPA framework).
	Measure 14: Adoption of a National Strategy for SMEs (2017-2022) with an Action plan (2018-2020)
Activities planned for 2016 and 2017	In 2017 the adoption of the National SME Strategy (2017-2023) was envisaged, aimed at supporting the development of SMEs and entrepreneurship in order to increase the productivity and innovativity of SMEs and improve their competitiveness on national and international markets.
Have the activities planned for 2016 and 2017 been implemented?	No
If yes/partially, include: -Description of steps taken -Timeline of implemented actions -Difficulties and delays in implementation -Whether the reform will continue in 2018	The National SME Strategy has been developed by experts from the International Labor Organization in cooperation with the Ministry of Economy and other competent institutions. The adoption of the strategy was envisaged for the first half of 2017, but it was delayed due to the election process in the country. In January 2018, the Strategy will be submitted to the Government for adoption.
If no, explain why not	/
Actual cost of implementation and impact on the annual budget (indicate deviation from estimated costs if any)	The preparation of the Strategy was financed by the International Labor Organization. There is no deviation from the planned costs.
	Measure 15: Improvement of the infrastructure and the access to funding for research, development, and innovations
Activities planned for 2016 and 2017	Instrument III – „Co-financing grants for technology extension“ Instrument IV – "Co-financing grants for the establishment, operation and investment of business-technology accelerators" Instrument V – Technical assistance to support innovative businesses Instrument VI – Application of innovative solutions in the public sector and organize thematic challenges
Have the activities planned for 2016 and 2017 been implemented?	3. Partially 4. Partially 5. Partially 6. N/A
If yes/partially, include: -Description of steps taken -Timeline of implemented actions -Difficulties and delays in implementation	The following by-laws have been developed: - Rulebook for the support instrument "Co-financing grants for technology extension" - Rulebook for the support instrument "Co-financing grants for establishment, operation and investment of business-technology accelerators" Because the funds for financing these two instruments are provided by the Loan Agreement with the World Bank, the Rulebooks for these two

-Whether the reform will continue in 2018	instruments have been developed in cooperation with World Bank's experts. In the first quarter of 2018 it is expected that these Rulebooks are adopted. The procedure for awarding funds under the two new instruments, i.e. the piloting of the two new instruments would be conducted in 2018. In regards to the introduction of the support instrument– Technical assistance to support innovative businesses, under the European Union Integration Facility, a project for needs assessment and design of this instrument has been approved for financing. The technical specification for procurement of services for the implementation of the project has been developed. In December 2017 service provider was selected and the implementation of the project will begin in January 2018. In December 2017 the Instrument VI – "Application of innovative solutions in the public sector and organize thematic challenges" was piloted through the publication of "O2 - Challenge to Reduce Air Pollution in Urban Areas in the Republic of Macedonia" and "Challenges for Young Researchers and Researchers".
If no, explain why not	The proposed measure will continue with implementation in 2018.
Actual cost of implementation and impact on the annual budget (indicate deviation from estimated costs if any)	In 2017, the aforementioned activities for implementation of the proposed measure have been financed under the operational budget of the Fund. Because the financial support under the newly developed instrument has not yet been granted, i.e. the instruments have not yet been piloted, no expenses earmarked for the measure have been made.
	Measure 16: Triple Helix Partnership
Activities planned for 2016 and 2017	1. Proposal for amendments and modifications to the Law on Innovation Activity with the aim of providing a legal framework for the NTTO, as well as for inclusion of the Fund for Innovation and Technological Development as one of the founders of the NTTO. 2. Operationalization of NTTO (staffing team, equipping NTTO, organizing trainings for employees, establishing processes and developing strategy for protection of intellectual property, development of marketing strategy, development of strategy for financing and strategy for securing financing sources, establishment financial reporting and control system.
Have the activities planned for 2016 and 2017 been implemented?	1. Yes 2. No
If yes/partially, include: -Description of steps taken -Timeline of implemented actions -Difficulties and delays in implementation -Whether the reform will continue in 2018	- Drafting amendments to the Law on Innovation Activity and submitting them to the Government of the Republic of Macedonia for adoption. The draft amendments were adopted by the Government of the Republic of Macedonia and submitted to the parliamentary procedure for adoption. In October, 2016, the draft amendments to the Law on Innovation Activity were adopted by the Assembly of the Republic of Macedonia. - the holding of the founding assembly for the establishment of NTTO and announcing a competition for the election of a director were postponed due to the parliamentary elections in the Republic of Macedonia. - the measure will continue to be implemented, however it is not part of ERP 2018-2020 because there is delay in activities, but it is expected to continue in 2019
If no, explain why not	/
Actual cost of implementation and impact on the annual budget (indicate deviation from estimated costs if any)	/
	Measure 17: Upgrading the customs clearance facilities of road border crossings Tabanovce (IPA 2012) and Kafasan (IPA 2013)
Activities planned for 2016 and 2017	2017 1. Continuation of the construction of GP Tabanovce. The planned period of operation was 12 months. At the end of 2017 the construction works at the GP Tabanovce were completed. 2. GP Kjafasan - the tender procedure was successfully completed in the third quarter of 2017. The project implementation started in the fourth quarter of 2017.

Have the activities planned for 2016 and 2017 been implemented?	2017 1. Yes 2. Yes
If yes/partially, include: -Description of steps taken -Timeline of implemented actions -Difficulties and delays in implementation -Whether the reform will continue in 2018	2018: 1. Administrative procedures (handover and use permit) 2.Continuation of construction work. In the fourth quarter of 2018, it is planned to complete the upgrade, the construction works and the upgraded facilities of GP Kjafasan to be operational in 2019. The measure will continue in 2018.
If no, explain why not	
Actual cost of implementation and impact on the annual budget (indicate deviation from estimated costs if any)	Activity 1 - There are no deviations. Activity 2 - In 2017 there are no real costs.
	Measure 18: Further development of the qualification system
Activities planned for 2016 and 2017	**2016** 1. Analyzed and redefined existing qualifications and developed new qualifications according to the needs of the labor market 2. Establish Sectorial Qualifications Committees 3. Harmonization of the labor market with technical vocational education through the development of curricula based on occupational standards and promotion of school-industry cooperation through grants for schools 4. Reforming the curriculum, practical work, the cooperation of students and teachers in the two-year and three-year vocational education and training, development of new standards of occupations and standards of qualifications. 5. Strengthening the cooperation between higher education institutions and the private sector, vocational schools and the private sector for providing quality practical work for students in companies **2017** 1. Development of qualifications for two priority sectors 2. Development of new occupational standards - 60 standards according to the needs of the labor market 3. Development of special programs for adult education and redesign of old qualifications
Have the activities planned for 2016 and 2017 been implemented?	**2016** **2017** 2016: 1. **Yes**/No/Partially 2. Yes/No/**Partially** 3. Yes/No/**Partially** **4.** Yes/No/**Partially** 5. Yes/No/**Partially** 2017: 1. **Yes**/No/Partially 2. **Yes**/No/Partially 3. **Yes**/No/Partially
If yes/partially, include: -Description of steps taken -Timeline of implemented actions -Difficulties and delays in implementation -Whether the reform will continue in	**2016** 1. Analysis and redefinition of existing qualifications and development of new qualifications according to the needs of the labor market (mid June 2016) - Analysis of the survey and the labor market assessment prepared for the process of reforming the VET curriculum and adult education 2. Establishing sectoral committees for qualifications (to be continued in 2018) - The criteria for selection of members for such committees have been established. This activity is not fully realized due to the Parliamentary

2018	elections in our country. However, persons that work in various institutions and are involved and know the NQF process have already been identified. 3. Harmonization of the labor market and technical vocational education through the development of curricula based on occupational standards and the promotion of school-industry cooperation through grants for schools (continued in 2017). - An analysis was prepared for the needs of the labor market - A model for technical vocational education was prepared - Concept for modernization of technical education was prepared - 10 pilot schools and companies that will cooperate were selected - The cooperation between schools and companies was strengthen by establishing real companies and practical training in a company (work-based learning) - Trainings and courses for students and teachers (improving the qualifications of teachers) - Beginning of designing standards of qualifications and curricula / modules 4. Reforming the curriculum, the practical work, the cooperation between the students and the teachers in the two-year and three-year vocational education and training, the development of new standards for occupations and standards for qualifications (continued in 2017) - The field analysis of the necessary skills and qualifications was finished: "Analysis of the survey and the labor market assessment prepared for the reform process of the VET curriculum and adult education" - Defined priority sectors for development of qualifications based on the analysis - Documents are prepared (Methodology for ensuring permanent harmonization and harmonization of vocational education and training with the labor market, methodology for development of special programs for adults based on the needs of the labor market and a guide for the development and recording of learning outcomes and their assessment). - 60 occupational standards have been developed - Start of development of standards for qualifications and curricula according to the analysis 5. Strengthening the cooperation between the higher education institutions and the private sector, the vocational schools and the private sector for providing quality practical work for students in companies (continued in 2017). - Developed methodology for evaluation of study programs regarding the requirements of the labor market and direct involvement of the employers - 7 Career Centers of Universities developed as a link between students and employers for practical teaching - Established cooperation between the vocational school and the company where students go to practical training in companies and are directly introduced to the entire work process. - Verification of employers for conducting practical training is carried out in accordance with the Law on Vocational Education and Training - 379 and 358 certified mentors have been trained in companies that will guide students through the learning process in the company **2017** 1. Development of qualifications for two priority sectors (continues in 2018). Although two sectors were planned, within these activities, several sectors were covered and a total of 79 qualifications in formal education and 5 standards of qualifications in non-formal education were designed. - Draft documents have been prepared in order to improve the quality of the qualification system ➢ Rulebook on the work of the National Board for the Macedonian Qualifications Framework; ➢ Manual on the format, content and work of the Register of the National Qualifications Framework; ➢ Manual for the work of the NQF unit;

	➢ Cooperation protocol between Sectoral Qualifications Committees; ➢ Protocol for cooperation between the Bureau for Development of Education, the Center for Vocational Education and Training and the Center for Adult Education in the preparation of the standards for qualifications; ➢ Protocol for cooperation between the National Board of the Macedonian Qualifications Framework and the Board for Accreditation and Evaluation of Higher Education; ➢ Protocol for cooperation of all stakeholders in the process of the NQF; ➢ A manual for adjusting the existing qualifications to the requirements of the NQF and the EQF; ➢ Quality Assurance Manual for the development of new professional qualifications in the Macedonian Qualifications System; ➢ Quality assurance procedure: Evaluation of a newly developed qualification; ➢ A manual for developing new qualifications - A process of modular approach to acquiring qualifications and achieving learning outcomes has begun, which facilitates the mobility in vocational education and training. - -76 educational qualifications have been developed (standard of qualification and curriculum programs) (47 standards of qualifications in vocational education and training with a duration of three years of which 13 qualifications standards have been redesigned, and 34 are new and 29 in vocational training with duration up to two years); curricula and programs are redesigned (40% general subjects, 20% vocational courses and 40% practical work, of which 30% are in a company) - 3 occupational standards have been developed and 3 curricula for vocational education and training with a duration of four years have been redesigned based on the modular approach and emphasis on practical classes (4 hours per week in III year and 6 hours per week in IV year) in the formal education. (This academic year students will study 3 redefined qualifications - hotel-tourist technician, construction technician and electrical technician for computer technology.) - At the request of the Chamber of Trades and the Hairdressers Section, the existing standard of qualification - master hairdresser and one module of the curriculum (post-education) were redesigned - Four new qualifications were developed at the request of the employers from the Sector for Tourism and Catering and the Electrical Engineering Sector, IT subsector (barista, airline ticket vendor, softver tester-beginner and softver tester-advisor). - -Six standards of qualifications were developed for post-secondary specialist education (Controller for technical inspection of vehicles, Forestry Specialist, Winery specialist, Specialist for electrical measuring instruments and measuring devices, Chef Specialist and Driving Instructor) on the basis of which curricula and programs will be developed. - -Possibility of vertical advancement (from lower to higher level of education) with previous fulfillment of certain criteria - passing of five differential exams. Students who have completed 3-year vocational education have the right, by passing these exams, to continue their education in the four-year vocational education, and then take a state graduation exam, or a final exam, which enables them to enroll in higher education. - Enhanced cooperation with the business sector through the participation of employers in the development of occupational standards, standards of qualifications and curricula as members of working groups. - Realization of practical training with employers verified for conducting practical training of students. An integrated analysis of work-based learning conditions has been prepared, and a Work-Based Learning Concept is in the process of preparation (Before a practical training in a company, an agreement is signed between the student, ie the parent / guardian, the institution for vocational education and training and the employer). - Training for mentors that will guide students through the learning process in the company continues. - Teacher training for teaching by achieving learning outcomes and modular approach have been conducted 2. Development of new occupational standards - 60 standards according to needs of the labor market (continues in 2018). Occupational

	standards are the basis for the development of full or partial qualifications according to the needs of the labor market. - 90 new occupational standards have been developed (in the procedure of approval are 35 new occupational standards) 3. Development of special programs for adult education and redesign of old qualifications (continues in 2018) - 34 special programs for adult education have been developed as an opportunity for acquiring qualification, re-qualification and further training according to the needs of the labor market, through the system of lifelong learning for faster employability.
If no, explain why not	/
Actual cost of implementation and impact on the annual budget (indicate deviation from estimated costs if any)	There is no deviation from actual costs
	Measure 19. Profiling of unemployed persons and designing an Individual Employment Plan 2
Activities planned for 2016 and 2017	The measure is applied to the registered unemployed persons who are registered with EARM as active jobseekers. Once the unemployed persons are registered in the unemployment register, they are directed to their first interview with an expert from EARM. In the first interview, the person from EARM collects all personal information about the individual and uses the employability checklist, classifies it into one of the three profiles (makes profiling of the unemployed person) as directly employable, facing moderate obstacles, or facing significant obstacles. If the unemployed person is classified as directly employable or with moderate employment barriers, the advisory session continues with the development of an Individual Employment Plan, in accordance with the existing practice in the local employment centers of EARM (IEP version 1). If it is determined that the unemployed person faces significant employment barriers, the first session ends with the filing of information about the individual and scheduling a second (longer) meeting for formulating an individual employment strategy (IEP version 2).
Have the activities planned for 2016 and 2017 been implemented?	Yes
If yes/partially, include: -Description of steps taken -Timeline of implemented actions -Difficulties and delays in implementation -Whether the reform will continue in 2018	In 2016, the process of profiling the unemployed was particularly developed. As of December 31, 2016, profiling of 7,665 persons (3,449 women) was made, and 3,094 (40.36%) were young to 29 years old. In order to continuously develop and improve this service with the unemployed persons, additional training was organized for the employees of the employment centers within the EU Twinning Project "Support to the Employment Agency for the implementation of active labor market measures and services". Also, in organization of EARM, trainings were held through workshops on the topic: "Profiling and Individual plan for employment of hardly employable persons (IEP 2)". These trainings were realized through 6 workshops (6 groups of employment centers) in which a total of 87 employees from all employment centers participated. The trainings were realized in the period September - October 2016. Starting from 2016, this measure is a regular activity of the employment centers.
If no, explain why not	/
Actual cost of implementation and impact on the annual budget (indicate deviation from estimated costs if any)	The cost for profiling and making an individual plan for employment 2 is 336,00 denars per person. There is no deviation from the predicted costs.

Annex 4: Contribution from consultations with stakeholders ERP 2018-2020

The Economic reform program 2018 represents a joint result from the collaboration among several institutions, and the overall preparation is coordinated by the Ministry of Finance.

Content of the Economic Reform Programme	Institution	Person in charge
1. Overall Policy Framework and Objectives	Ministry of finance	Andrija Aleksoski Vesna Cvetanova Bojana Ilievska
1.1. Measures taken to implement the targeted policy guidelines adopted at the Economic and Financial Dialogue between the EU and the Western Balkans and Turkey in May 23 2017	All institutions in charge	
2. Macroeconomic framework		
2.1. Recent economic developments	Ministry of finance National Bank of the Republic of Macedonia	Nedzati Kurtishi Aneta Krstevska Natasha Andreeva
2.2. Medium-term macroeconomic scenario	Ministry of finance National Bank of the Republic of Macedonia	Nedzati Kurtishi Lenche Tagasovska Violeta S. Petreska Aneta Krstevska
2.3. Alternative scenario and risks	Ministry of finance National Bank of the Republic of Macedonia	Nedzati Kurtishi Aneta Krstevska
3. Fiscal framework		
3.1. Fiscal strategy and medium-term objectives	Ministry of finance	Maja Argirovska Verica Prokovikj
3.2. Budget implementation in 2017	Ministry of finance	Biljana Minoska Mara Srezovska Liljana Gjurovska
3.3. Medium-term budgetary outlook	Ministry of finance	Maja Argirovska Verica Prokovikj
3.4. Structural deficit	Ministry of finance	Nedzati Kurtishi
3.5. Debt levels and developments, analysis of below-the-line operations and stock-flow adjustments	Ministry of finance	Sanja M. Mancheva Dejan Nikolovski
3.6. Sensitivity analysis	Ministry of finance	Nedzati Kurtishi Dejan Nikolovski Sanja M. Mancheva
3.7. Fiscal governance and budgetary frameworks	Ministry of finance	Maja Argirovska Verica Prokovikj
3.8. Sustainability of public finances	Ministry of finance	Nedzati Kurtishi
4. Structural reform priorities in 2018-2020		
4.1. Identification of key obstacles to growth and competitiveness	Ministry of finance	Andrija Aleksoski Vesna Cvetanova Bojana Ilievska
4.2. Summary of reform priorities	Ministry of finance	Andrija Aleksoski Vesna Cvetanova Bojana Ilievska
4.3. Structural reform priorities by area		
4.3.1. Public Finance Management (PFM)	Ministry of finance Public Procurement Bureau	Trajko Spasovski Frosina Doninovska Susinov
4.3.2. Energy and transport market reform	Cabinet of the DPM in charge of economic affairs Ministry of Economy Ministry of Transport and Communication	Natasha Veljanovska Milica Karafiloska Andonov Goran Temovski Biljana Zdraveva Jasminka Kirkova

4.3.3. Sectoral development		
4.3.3.1. Agricultural sector development	Ministry of Agriculture, Forestry and Water Economy	Maja Lazareska Kiril Georgievski Aleksandar Mitrevski Lile Simonovska
4.3.3.2. Industry sector development	Ministry of finance Cabinet of the DPM in charge of economic affairs	Gjoko Gjorgjeski Dane Josifovski
4.3.3.3. Services sector development	Cabinet of the DPM in charge of economic affairs	Maja Barikj
4.3.4. Business environment and reduction of the informal economy	Ministry of finance Ministry for information society and administration	Andrija Aleksoski Vesna Cvetanova Bojana Ilievska Rozalinda Stojova
4.3.5. Research, development and innovation and Digital economy	Fund for Innovation and Technical Development	Katarina Krecheva
4.3.6. Trade-related reforms	Ministry of finance Ministry of Economy	Vesna Cvetanova Ilir Shabani
4.3.7. Education and skills	Ministry of Education and Science	Biljana Trajkovska
4.3.8. Employment and labour markets	Ministry of labour and social policy Employment Agency of RM	Goran Veleski Biljana Zivkovska
4.3.9. Social inclusion, poverty reduction and equal opportunities	Ministry of labour and social policy	Sofija Spasevska
5. Budgetary implications of structural reforms	All institutions in charge	
6. Institutional issues and stakeholder involvement	Ministry of finance	Andrija Aleksoski Vesna Cvetanova Bojana Ilievska
7. Annexes	All institutions in charge	

Having in mind that for the last year's programme the European Commission acknowledged the efforts the Government is making in implementing reforms to improve competitiveness, the Ministry of Finance made additional effort to maintain and improve the quality of this year's document in accordance with the recommendations made by the Commission.

During the preparation of this program a consultation process with stakeholders was conducted at national level: the business community, the universities, ZELS, local authorities, social partners, civil society and other stakeholders. The consultation process was conducted in accordance with the ERP 2018 Guidelines.

An initial meeting with stakeholders was held on June 9, 2017 with the following agenda:

РЕПУБЛИКА МАКЕДОНИЈА МИНИСТЕРСТВО ЗА ФИНАНСИИ — REPUBLIC OF MACEDONIA MINISTRY OF FINANCE

In-country Kick-off Meeting of the Economic Reform Programme

AGENDA

9 June 2017

VENUE: Holiday Inn Skopje hotel
Filip Vtori Makedonski No. 5
1000 Skopje
Republic of Macedonia

9 June 2017

10:45 – 11:00	Registration
11:00 – 11:30	**Welcome and Opening Remarks**
	Mr. **Dragan Tevdovski,** Minister of Finance Mr. **Willem Noe,** DG NEAR, European Commission Ms. **Marzena Kisielewska,** Head of the OECD South East Europe Division moderator **Mr. Andrija Aleksoski**, National ERP Coordinator
11:30 – 12:00	**Lessons learned from the 2017 ERP Process followed by a roundtable discussion**
	Ms. Vesna Cvetanova, Assistant Head of Macroeconomic Department, Ministry of Finance *Presentation of the Commission Assessment of ERP 2017 and Joint Conclusions of the Economic and Financial Dialogue followed by a roundtable discussion.*
12:00 – 12:30	**The 2018 ERP Guidance Note followed by a roundtable discussion**
	Ms. Bojana Ilievska, Head of Unit, Macroeconomic Department, Ministry of Finance *Presentation of the new version of the ERP Guidance note supporting the ERP 2018-2020 preparation process followed by a roundtable discussion.*
12:30-13:00	**OECD support for ERP preparation**
	Ms. Anita Richter, OECD, Project Manager, South East Europe, Global Relations *OECD support to Western Balkan and Turkey for ERP preparation, OECD monitoring tool for reform measures.*
13:00-13:30	**2018 ERP preparation process and Work Plan followed by a roundtable discussion**
	Mr. Andrija Aleksoski, National ERP Coordinator, Ministry of Finance *Main milestones and key dates with a focus on the government internal coordination process, the consultation of stakeholders and options for additional technical support.* *Presentation of the Work Plan to prepare the ERP 2018-2020 followed by a roundtable discussion.*
13:30-14:30	**Lunch**

In the period from November 27 to December 8, 2017, the draft ERP 2018 was published on the Ministry of Finance's website and at the same time, a public announcement and invitation were posted for the stakeholders to actively contribute to the process of the document preparation by providing opinions on the document content and proposals for its improvement http://finance.gov.mk/en/node/6844.

On December 5, 2017 a public debate among the institutions participating in the preparation of the document, representatives of the European Delegation in Skopje and the stakeholders was held in the Ministry of Finance.

Public consultation for draft Economic Reform Program 2018 – 2020

INVITATION FOR PUBLIC CONSULTATION FOR DRAFT ECONOMIC REFORM PROGRAM 2018 – 2020

We are glad to present you the Structural Reform Priorities from the draft Economic Reform Program 2018 – 2020 (ERP 2018), which the Government of the Republic of Macedonia would submit to the European Commission at 31 Jan. 2018, the latest. Here you can find the text of the draft ERP 2018 Reform Priorities.

By regular preparation of the ERP, the Government of The Republic of Macedonia joined the EC approach for supporting the growth and competitiveness through economic governess as a key pillar in accession process, in order to provide better reporting for national economic policy plans, including the needs for structural reforms.

The draft ERP 2018 is prepared through established national consultation process, centrally coordinated by the Ministry of Finance and supported by OECD expert assistance. The document closely follows the instructions of the Guidance for Economic Reform Programs issued by EC in April 2017.

Having in mind the significance of the document and the need for high quality preparation, we undertake the public consultation process with broad involvement of the stakeholders. Therefore, we invite the business community, universities, local authorities, social partners, civil society and all other stakeholders for active contribution in document preparation process.

Please submit your comments and proposals in written at 8 Dec. 2017 the latest, at the following e-mail addresses:

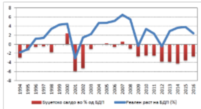
Andrija.Aleksoski@finance.gov.mk National ERP Coordinator, and

Bojana.Ilievska@finance.gov.mk

We would like to invite you for consultation meeting on 5 Dec. 2017 beginning at 12:00, in the premises of Ministry of Finance. For logistical purposes please confirm your participation on 1 Dec. 2017 the latest, at the above mentioned e-mail addresses.

- PDF Draft ERP 2018-2020 Chapter 4_27112017
- PDF ERP 2018-2020 Guidance note

ECONOMIC GROWTH AND BUDGET DEFICIT



MINISTRY

e-services

Projects

Links

ISO 9001:2008

During the consultations with stakeholders, the following opinions and suggestions were received:

December 11, 2017

Dear Mr. Aleksoski,

Please find the attached AmCham Macedonia response to the draft 2018-2020 National Economic Reform Program released for public comment on 28.11.2017. Please note that we have included both a Macedonian and English version to be used, as required.

I'd like to thank the Ministry of Finance for including the American Chamber of Commerce in Macedonia in the process of reviewing and commenting on the 2018-2020 National Economic Reform Program. I'd also like to mention that to have greater inclusion of all relevant stakeholders toward creating a quality program that will address the current situation, it would be advisable to publish draft Programs on the National Electronic Register of Regulations (ENER), allowing them to be reviewed and commented on for at least 15 working days.

Given the limited time we had to comment on the Program, we have limited our feedback to just two subsections of the document (4.3.1 Public Finance Management and 4.3.4: Business Environment). For the same reason, we look forward to a continued dialogue with respect to the Program's implementation details.

Our general impression is that the measures included in the draft fail to address important challenges and therefore are unlikely to help the country meet its reform and growth goals. Specifically, we believe that the Program should include measures in the following reform areas:

- Ensuring all budget users increase the transparency and timeliness of payments owed the private sector;
- Fostering real, open and systemic dialogue with company representatives;
- Reducing the grey economy;
- Reducing regulatory confusion;
- Increasing the predictability, consistency and fairness of inspections;
- Increasing transparency and oversight of company appeal and complaint mechanisms;
- Ensuring para-fiscal charges, taxation and penalty policies are rational and fair;

- Making strategic investments in educational quality; and
- Encouraging internships in companies.

We hope you will receive these comments as constructive criticism aimed at producing a higher quality reform program. Please feel free to contact me directly, if you have any questions or concerns.

Sincerely,

Dijana Despodov
Executive Director

AmCham Macedonia
Vasil Gjorgov 20A, 3rd floor
1000 Skopje, Macedonia
Tel: +389 (0)2 3216 714
www.amcham.com.mk

American Chamber of Commerce in Macedonia response to the draft 2018-2020 National Economic Reform Program released for public comment on 28.11.2017

Comments on Subsection 4.3.1: Public Finance Management

Though not explicitly stated as a desired goal of neither proposed reform Measure 1 nor 2, we would welcome any and all reforms aimed at **increasing the transparency of the payment practices of budget users toward its private sector contractors, as well as their timeliness**. Late payment by budget users toward companies here contributes significantly to liquidity problems in the country. The Law on Financial Discipline applies fully to all budget users, however there is no evidence that institutional payment practices have improved. Given the State's obligation to monitor itself in this process (up to and including fines issued to the Minister of Finance itself), transparency of public payment practices is a key missing element that needs to be addressed.

Another important reform along this line would be to define a standardized methodology in the Enforcement Law by which municipalities' reserved "operational funds" are to be calculated in enforcement proceedings and introduce other measures that prevent blatant and long-term abuse of private contractors who have delivered public works in good faith. The current Enforcement Law lacks a methodology by which judges determine the minimum level of "operational funds" necessary for municipalities to continue normal operations (Article 218). In practice, this means that private contractors who have delivered public works and proven their right in court to be compensated for their work, sometimes cannot realize this right. In essence, this exception allows municipalities to operate above the law, avoid settling past debts and continue normal operations, including issuing new tenders.

Comments on Subsection 4.3.4: Business Environment and Reduction of the Informal Economy

We agree that Government efforts to reform various aspects of Macedonia's business environment in line with assessments of the *Doing Business* Report and, to a lesser degree, the *Global Competitiveness Report* have raised the country's visibility as an FDI destination in the region. This is proven by an increase in Brownfield and Greenfield foreign direct investment and increased employment in such newly established operations. A limited number of bureaucratic processes have been tangibly improved, which has helped the businesses that utilize them.

Unfortunately, the measures included in the draft 2018-2020 Program are limited to very small investment in a long talked-about e-government services portal. (. While we would echo the need for continued investment in e-government systems these measures are insufficient and cannot be considered fundamental reforms.

Instead, concrete and tangible reform is needed in a number of fundamental areas that would create positive change in the business environment overall. These reforms should include measures to:

- Foster real, open and systemic dialogue with industry via proper use of the National Electronic Register of Regulations (ENER), placing a moratorium on the use of the "short procedure" in Parliament and extending the standard public comment period.
- Reduce the grey economy by ensuring enforcement institutions' responsibilities are properly set, do not generally overlap with one another and that they are properly trained, equipped and motivated to tackle this problem systematically, throughout the territory of the entire country.
- Reduce regulatory confusion by ensuring official, consolidated legal texts are published more regularly, reducing conflicts between new laws and existing legislation, and requiring enforcement institutions to publish official, legally-binding guidance on the application of laws in concrete cases;
- General alignment of the tax (Corporate Income Tax and Value Added Tax) legislation with the requirements of the global digital transformation and alignment with the global taxation. This would contribute to the ease of providing electronic services and doing e-commerce in Macedonia, as well as to the overall transparency and revenue collection
- Increase the predictability, consistency, fairness of inspections by increasing the scope of the Inspections Council's work, increasing the transparency of all State institutions that carry out inspections; increasing the transparency of fine issuance as well as instructional material to help companies increase their compliance, and eliminating incentives for inspectors to increase collections;
- Increase transparency and oversight of company appeal mechanisms; and
- Ensure para-fiscal charges, taxation and penalty policies are rational and fair

Fostering Real, Open and Systemic Dialogue with Company Representatives

Real, open and systemic dialogue with company representatives must be a cornerstone of future Government efforts to improve the business environment.

The Government's introduction of ENER was a commendable move toward increasing public comment on proposed legislation that has been recognized by many. Unfortunately, the platform is only sporadically used by ministries to notify citizens of planned legislative changes and it will require further development and a systematic use of the tool to encourage open, two-way communication.

While selected companies and business associations are occasionally invited to action-oriented meetings with the highest government officials, the vast majority of companies operating in the country are systematically excluded from legislative and regulatory dialogue. This is because too many laws are being passed without any public comment period whatsoever. The so-called "short procedure" is meant to be used only when proposed changes are not "complex and large". Given the vagueness of this definition, this procedure is being used for all kinds of changes, reducing the effectiveness of parallel efforts that government bodies make to conduct dialogue with select representatives of the business community. Meaningful public-private dialogue reform should begin with a moratorium on the use of the "short procedure" by Parliament.

Finally, even when it is respected, the minimum period of 10 calendar days for public comment confirmed by the government is simply too short to allow for thoughtful and constructive responses from company representatives. Thus, an impactful reform would be to set a minimum *15 working day* public comment period for all proposed legislation and a 20 working day public comment period minimum for public comment on legislation proposed in the summer and year-end periods.

Reducing the Grey Economy

We recognize significant government efforts since 2012 to decrease the operations of unregistered companies and particularly to punish those that fail to handle cash transactions and pay taxes in accordance with the law. However, we were surprised to see that the draft 2018-2020 Program did not include any reforms necessary to further reduce the grey/informal economy. We believe that reform is needed to ensure enforcement institutions' responsibilities are properly set, do not generally overlap with one another and that they are properly trained, equipped and motivated to tackle this problem systematically, throughout the territory of the entire country.

The State Market Inspectorate (SMI) should be one of the country's most important enforcement institutions when it comes to tackling the grey economy. However, SMI has virtually no budgetary resources for computers, software, vehicles, storage of seized items or other fundamental tools that would enable it to properly carry out its mission. Also, the law requires an in-person response to every citizen complaint, regardless of the issue in question or transaction size. Further, due to a Government order, an average of 70% of inspections SMI carries out are to enforce non-smoking legislation and closing times. All of these factors severely limit the SMI's ability to tackle the grey economy.

Similarly, while proposed Program measures outline Government programs to support private sector innovation, research and development and similar, the current State Office of Industrial Property struggles to perform even its most basic function of processing patent and trademark applications. In their 2015 annual report, SOIP reports receiving 5,357 applications for recognition and protection of trademarks in Macedonia, but issuing a total of just 614 decisions to recognize their rights (11%). In fact, this ratio has averaged about 20% in the 2003-2014 period. This means that a backlog of thousands of existing trademarks (many of them globally-recognized) have yet to receive basic recognition of their rights in Macedonia. We believe Government efforts to encourage innovation among local companies must begin by efficiently recognizing and protecting those that are already here.

Reducing Regulatory Confusion

In addition to a rapidly changing legislative and regulatory environment where companies are rarely involved in the policy-making process, companies working in Macedonia face a great degree of regulatory confusion caused by:

- The lack of Regulatory Impact Assessments (RIA) that consider impacts on the private sector as well as sufficient time for companies to adjust to new legislation;
- The lack of official, consolidated texts of all laws in force;
- Passage of laws that conflict with measures in existing legislation; and
- The lack of official information published by enforcement institutions on how laws are to be applied in specific cases.

Thus, we believe that reform targeting the reduction of regulatory confusion should include measures to address each of these issues.

It is common practice in Macedonia for Parliament to adopt laws that enter immediately into force upon being published in the Official Gazette. This means companies have virtually no time to adjust their systems, deliver training to their employees or take other measures to comply with the law before it officially enters into force. We believe this is at least partly due to the fact that government RIAs do not take impact on the private sector into account (only State budget impact). The "grey zone" regularly created by this practice is further compounded by implementing legislation that is delayed by several months. Thus, reform targeting the reduction of regulatory confusion should include measures that ensure companies are not held liable for complying with a new Law until its sub-laws have been duly published and a reasonable amount of time has passed, allowing companies to take measures to comply with those sub-laws.

Too often, companies are forced to work from unofficial versions of laws that are manually pieced together with amendments either by private service providers or company employees. This practice exposes companies to unnecessary legal risk and favors large organizations that have the resources to manage this difficult process. For example, the Law on VAT was not officially consolidated between the years 1999-2013, despite many amendments to it during that time. Thus, reform aimed at reducing regulatory confusion in Macedonia's business environment should include the creation of a process that ensures that the responsible Parliamentary Commission publishes official, consolidated legal texts for general public use within 1 month of any and all amendments.

While the Secretariat of Legislation is tasked with ensuring new laws do not conflict with existing measures, this is happening on a regular basis. Reform is necessary to ensure the Secretariat has the appropriate resources, authority and influence needed to reduce the confusion created when laws conflict with one another.

Finally, companies are often in need of reliable official guidance on the application of laws to their concrete situation. Today, institutions with the authority to decide how a given regulation applies to a concrete company situation do not publish these opinions in that official capacity. This encourages uneven application and means that companies are not aware how the law is applied to similar cases, except in rare cases when companies seek an "authentic interpretation" from Parliament. Given the slowness of response and privacy concerns, this measure is rarely used. Companies are also discouraged from going this route by Parliament's practice of rejecting such requests on the basis that the adopted laws are clear. Thus, reform should be made to require enforcement institutions to publish official, legally-binding guidance on the application of laws in concrete cases (excepting private entity data). This is particularly critical when companies have been punished for interpreting the application of the Law differently than enforcement institutions.

Increasing the Predictability, Consistency, Fairness of Inspections

Reforms targeting greater predictability, consistency and fairness of inspections would have a great impact on the local business environment. Such reforms would reduce unnecessary compliance risk for companies and increase their rate of proactive compliance. Specifically, reform is needed to:

- Increasing the scope of the Inspections Council to all government entities that carry out inspections;
- Requiring State institutions that carry out inspections to publish materials online relevant for companies to understand their role and how to contact them with questions;
- Increase the transparency of fine issuance as well as instructional material for companies to increase their proactive compliance; and
- Eliminating all incentives for inspectors to increase collections from companies.

The creation of an Inspections Council with the goal of standardizing the work of all inspectorates was an important step in the right direction. However, the Council should include all State institutions that carry out inspections (e.g., Public Revenue Office, Customs Administration). Also, it is critical that the Council work to identify and reduce overlap in the responsibilities of State institutions that carry out inspections.

Toward increasing general awareness of the number, type and responsibilities of the country's 28 State institutions that carry out inspections, each one must have a functional web site, where they will publish all relevant laws, sub-laws and internal procedures that are necessary for companies to understand their work and to be able to contact them with open questions. For example, today, the State Inspectorate for Agriculture doesn't have a single piece of information available online.

Another important reform would be toward increasing the transparency of the issuance of fines. If fines are to serve an instructive role to other companies, more data must be made available publically on which types of entities are being fined (e.g., size, sector, region) and for which types of offenses. Ideally, inspectorates would regularly publish case studies and other instructional materials on issues for which companies are commonly being fined, to help increase compliance.

Finally, inspectors must not be incentivized in any way to increase collections from companies. For example, UJP annual reports from at least 2007 mention “25% of revenues from discovered and paid taxes and interest” as a source of financing of the institution itself. We believe this constitutes a formal incentive for inspectors to find ways to increase collections, rather than simply ensuring the law is consistently applied as it was intended.

Increase Transparency and Oversight of Company Appeal and Complaint Mechanisms

To avoid creating a business environment where companies are considered guilty before being proven innocent, complaint and appeal mechanisms must be consistent, transparent and efficient. Thus, reform is needed to prevent abuse of companies by individual inspectors by increasing the transparency of institutional handling of company complaints and ensuring best practices are being applied. Such measures would provide internal and independent oversight of appeal mechanisms and publishing of detailed data on complaints received from companies. Important questions to be answered include:

- What portion of appeals to institutional decisions are fully or partially accepted or rejected?
- How often does the Administrative Court overturn a decision by a State institution?
- What steps are taken to ensure decisions of the Administrative Court are respected? and
- Are the disciplinary actions taken for abuse of public positions consistent?

As part of this reform, it’s critical to increase the transparency of the work of the Administrative Inspectorate. In the absence of concrete information about the workings of this institution, companies doubt that it is carrying out its intended function.

Ensure Para-fiscal Charges, Taxation and Penalty Policies are Rational and Fair

A pillar of Macedonia’s strategy to attract FDI has included maintaining comparatively low tax rates and a simple taxation system. However, no measures have been taken to prevent a corresponding rise in the myriad para-fiscal charges companies must pay. At least anecdotally, they seem to be on the rise. Thus, an important reform would involve first assessing then rationalizing para-fiscal charges levied at the national and municipal level. We believe this reform would allow companies to make much more accurate investment and operational cost estimations and enable policy makers to view future cost increases in a holistic context.

Currently, a tiny portion of the business community bears an extremely high portion of the tax burden. The economy’s tax burden should be shared across all sectors in a more even fashion, to prevent reducing the competitiveness of certain sectors. Thus, AmCham recommends that the country’s tax structure be reviewed and reformed with the aim of spreading the country’s tax burden as evenly as possible.

The recent amendment to Misdemeanour Law that reduced fines across a great number of laws was a step in the right direction, since fines had been consistently raised over the past several years without regard to their impact on companies of all sizes. However, penalty policies must be reformed more fundamentally with the goal of ensuring they serve the function of encouraging compliance. Specifically, the severity of misdemeanour fines must correspond to the severity of the offense; human/machine error must not be punished; companies that voluntarily identify and correct errors should not be punished; and enforcement officials must offer warnings and education to companies and allow time for corrective action before punishment is levied.

СОЈУЗ НА СТОПАНСКИ КОМОРИ НА МАКЕДОНИЈА
ВОДЕЧКА МАКЕДОНСКА ДЕЛОВНА МРЕЖА

0302-195-1/17
Скопје, 07.12.2017

До: Министерство за финансии на Република Македонија
Ул. Даме Груев, бр.12
1000 Скопје, Република Македонија

За: г. Андрија Алексоски, координатор на Програмата на економски реформи

Предмет: Мислење на Сојуз на стопански комори на Македонија по нацрт Програма на економски реформи 2018 – 2020 година

Почитуван г. Алексоски,

Би сакале да искажеме благодарност за досегашната соработка и изразиме надеж за продлабочување на истата во иднина.

Во оваа насока, и согласно нашето учество на јавната расправа по предлог Програмата на економски реформи 2018 – 2020 година, која се одржа на 05.12.2017 година во Министерството за финансии истакнуваме благодарност за можноста за достава на коментари по нацрт Програмата.

Сојуз на стопански комори на Македонија како најголема деловна македонска мрежа која ги застапува бизнис интересите на македонските компании континуирано ја следи економската состојба и предлага мерки и активности за унапредување и понатамошен развој. Во оваа насока, а согласно утврденото мислење на бизнис заедницата сметаме дека во идните економски реформи приоритети треба да се дадат на намалувањето на неформалната економија како и реформи и унапредување на инспекцискиот систем. За таа цел, предлагаме точка 4.3.4 Деловно опкружување и намалување на неформалната економија да се дополни со конкретни мерки и/или механизми за намалување на неформалната економија кои ќе бидат во насока на заштита на регистрираните македонски компании кои работат сериозно и професионално и поради тоа се во можност да допринесат за развој на економијата. Исто така, сметаме дека неопходно е спроведување на реформи на инспекцискиот систем во смисла на ревидирање на законската регулатива, унифицирано толкување на истата од страна на сите инспекторати, доквалификација на кадрите кои вршат надзор, како и правилно и професионално утврдување на фактичката состојба.

Секторскиот развој на земјоделството, индустријата и туризмот, реформите во енергетиката и транспортот, како и поддршка на иновациите, мерки за развој на пазарот на трудот и унапредувањето на образованието се активности кои како бизнис заедницат ги поддржувани, а се опфатени во Програмата.

За сите дополнителни информации, Ве молиме да нè контактирате на тел: 076 455 045 или на е-маил: info@chamber.mk.

Срдечно Ве поздравуваме.

Со почит,

Маја Савеска, советник
Сојуз на стопански комори на Македонија

International Chamber of Commerce
The world business organization

ICC World Chambers Federation

Сојуз на стопански комори на Македонија | Ул. Црвена Скопска Општина бр.10, Скопје, Македонија|
www.chamber.mk тел: 02 3091 440 | факс: 02 3090 595 | info@chamber.mk

КОМЕНТАР

COMMENT

Бр. 19

On the Draft Economic Reform Program (2018 – 2020)

05 December 2017

The Ministry of Finance announced the draft Economic Reform Program (2018-2020). Finance Think considers that the document is made up on **clear and sound economic bases** and offers a comprehensive analysis of the priority structural reforms needed by the Macedonian economy. Finance Think believes the program is fully committed to reform and it is encouraging that the program is in line with the recommendations of the domestic expert public and international institutions. **The program clearly incorporates measures from several other programs from national and international institutions, which is a good step towards institutionally harmonizing the measures that are priority for the Macedonian economy.**

Finance Think has few comments and suggestions for the program in order to improve it. More details in the following points:

- **Presenting the expected impact on competitiveness/justification for all measures is correct and in a positive direction, but the explanations are not clear and complete.** First, there is no meticulousness in presenting the justification for each of the measures. The explanations tend to be generalized and lacking data on which it would be determined. Secondly, in the measures themselves, there are no analyzes on the basis of which it is established that each of the measures is justified, or on which their influence on competitiveness has been determined. If such analyzes are implemented, **Finance Think proposes for the expert public to have an insight into the method and assumptions through which the conclusions about the justification and the expected impact of each measure have been determined.**

- Finance Think welcomes the presentation of the expected impact on employment and the gender of each of the measures. Namely, as an organization that monitors gender and income inequalities, we consider that this presentation of the measures is in the right direction towards greater inclusiveness of the various stakeholders. In order to improve them, Finance Think proposes **a clearer and detailed presentation of their impacts.** In the present form, **the results of the impact of the measures on employment and gender, as well as the methods used to determine such impact, are missing.**

- The measure for increasing the competitiveness of the electricity market **is welcomed**. Last year, Finance Think developed a Cost-Benefit Analysis of the Liberalization of the Electricity Market in Macedonia, where it was concluded that households and national institutions would have created more savings and part of the electricity costs would have been intended for other purposes. Finance Think proposes to **conduct a**

national level cost-benefit analysis, as well as a price analysis of the effects of market liberalization.

- The proposed measures for the development of the agricultural sector are appropriate and correct. Agriculture, as part of the key sectors in Macedonia, needs improvement and technological development that would be comparable and competitive with the SEE and EU countries. Finance Think suggests a cautious approach to the financial support of agriculture, given that the Cost Benefit Analysis of Agricultural Subsidies has shown that agricultural subsidies have been **inappropriately used to improve the agricultural sector but have been used mainly as a social measure.** Finance Think proposes to train the Agency for Financial Support of Agriculture and Rural Development in **implementation of monitoring and evaluation methods on subsidies in order to ensure that they are appropriately used in improving the competitiveness of this sector.**
- Finance Think considers that the measures for development of the industry are appropriate and are interconnected with the measures proposed in the government's Plan for Economic Growth. Such a connection is of key importance and indicates that governmental institutions have mutual communication **in finding common measures that would contribute to the improvement of the economy.** We believe that the measures would give a **positive financial impulse to the companies in the short term and provide long-term stability of the business sector**. For more detail, see FT Comment no. 16.
- The measures targeting the business environment and the reduction of the informal economy **indicate that the program appropriately targets and recognizes the problems of the Macedonian economy.** The weak point of this segment of the draft Program is that there are no measures for addressing the problems of the inspection bodies that perform inspection and supervision over the application of the laws, other regulations and acts by the business sector in the Republic of Macedonia. The Policy Brief no. 20 indicated that in the previous years many of the small and medium-sized enterprises in the Republic of Macedonia were victims of bias, favoritism and abuse by the inspection services. **This tendency increases corruption in the private sector and creates inequality in the economy.** Additionally, the presence of the informal economy is confirmed by the analysis "Envelope Salary", which found that 17.8% of the workers who have a formal employment contract, also received cash in hand in 2017. Such results are due to the inadequate work of the inspection bodies. **Finance Think proposes a clear and concise creation of additional policies/measures that would address the problems of the inspection bodies in Macedonia.**
- **Finance Think welcomes the proposed research, development and innovation measures, and digital economy.** Namely, we believe that the measure of triple helix partnership would contribute in **increasing the innovation potentials of Macedonia, and thus the general economic growth of the country.** In order to improve the envisioned measures, Finance Think also proposes **measures that would encourage the construction of technology parks and entrepreneurship centres** that will enable networking of innovative start-ups with investment firms of domestic and foreign origin.
- The special emphasis on vocational secondary education in the proposed measures for education reforms is **in the positive direction and in line with the opinions of the domestic expert public and the international financial institutions**. Finance Think proposes to consider ways and measures that would encourage **greater participation of women in vocational secondary education**, given that women are underrepresented in vocational professions. This would provide an increased range of educational choices for women and remove the barriers to participation in vocational professions. For more, see Finance Think's publications on Gender and Income Inequalities.
- The increase of finances for the employment and labor market measures, as well as more appropriate targeting of the most vulnerable unemployed, are also appropriate and in line with the recommendations from Finance Think's Policy Brief no. 14. **We point to precaution to Measure 19: Youth guarantee** where it has not been determined how a suitable job offer, internship or training for the young unemployed person will be guaranteed

in a market where there is insufficient demand for jobs with no work experience and a major discrepancy between the offered and demanding skills.

- Finance Think believes that the measure for enhancement of financial benefits in the field of social protection is adequate, but recommends that such a measure should be implemented **after revising the number (targeting) of monetary compensation users.** We also propose to conduct a **suitable analysis of the effects that will have on the budget** of the Republic of Macedonia, as well as to **define from where this increase will be financed**. These proposals are aimed at increasing budget transparency as well as determining the overall implementation of policies. Finance Think recommends introduction of a Guaranteed Minimum Income Scheme (GMD), according to our study on this topic, the three separate GMD designs help significantly in reducing poverty and inequality.

MAKAM-TRANS

Economic Reform Program 2018 – 2020

Respected,

Association Makam-trans is an association of employers in the area of road transport with close to 2000 members transport companies, the main activity of which is transport of goods in road transport.

With special attention we considered the Draft Economic Reform Program (2018-2020), which in fully has a positive trend for enabling conditions for securing sustainable growth and development of the economy as a whole if it is implemented in accordance with the set priorities and transparency of the state institutions in order to include all interested stakeholders from the real sector.

We would like to point out a fact that has been omitted in this program and is not sufficiently analyzed to find the reasons for the stalled border crossings.

In point 4.3.2. REFERENCES ON THE ENERGY AND TRANSPORT MARKET is indicated:

"The domination of road transport, especially in the transport of goods, leads to an increase in the delays at the border crossings and a reduction in the rapid flow of goods, which imposes the need to take measures that will contribute to reducing the imbalance in transport by increasing the share of rail transport. "

According to all the surveys conducted in the past period, the reasons for stalling at the border crossings it's not the "domination of road transport" but the bottlenecks existing at the border crossings, the lack of a large number of lanes for exit from the country, too many procedures such as the inspection bodies located at the border lines and the customs authorities.

Overcoming this problem will not be solved by increasing the share of rail transport, because both transports have always been complementary, especially since rail transport is not always available to the initial or final destination, and without road transport it would be inflexible and difficult to access. According to this Program, a lot of support and development of the agricultural sector is foreseen, whose products cannot and must not be transported by rail to a greater extent when it comes to products that are easily perishable and require speed in delivery to the end user. A large part of products from the zones that have high value must not be transported by rail, which is evident from the ban on the carriage of freight motor vehicles together with the goods by train through Austria.

The fastest way that does not require large funds is the construction / addition of two lanes for exit the country in the length of 1.5 km at the Tabanovce border crossing point, which is an infrastructure solution, especially since there is a ready-made project of 600 m which was not made and it is an integral part of the project for construction of the Tabanovce highway. Such similar activities by conducting an appropriate analysis should be done at all border crossings from "A" category in order to extend the crossings, to correct approaches to customs terminals and roads. It is also necessary to apply in the road transport the rule for the establishment of facilitation of international road transport of goods by reducing the waiting time at the border crossings by shortening border crossing procedures in accordance with the principle of one stop shop system "one-stop shop" "As implemented in other countries in our environment

(Kosovo - Albania, Albania - Montenegro, etc.). All these activities must be implemented in parallel with the implementation of the provisions of the CEFTA agreement.

In the greater part of the Program, stimulating measures for the development of the agricultural sector, the industry sector, the service sector, which means an increase in export products from our country, are also determined, but import of products that will be used as raw materials or finished products will be inevitable, unfortunately there is no single element for securing sustainable growth and development of transport companies from the private sector. We remain in the hope that after our previous intervention, to the Ministry of Transport and Communications will provide appropriate measures for assistance and support of this service sector with the National Transport Strategy 2017-2030, which is a strategic document for the development of the overall transport policy in the Republic of Macedonia after the example of the states of the European Union, whether it is a public or private sector.

We particularly welcome part 4.3.7 EDUCATION AND SKILLS that refers to the establishment of measures to increase active measures for long-term unemployed, young and low-skilled.

For several years now, transportation companies face a lack of professional drivers (most of them have gone to the EU countries), we understand that for 20 years the "driver" in the secondary technical school ASUC has been abolished, the requirements that we had for retraining and re-qualification of the unemployed persons in 2016 (60 people) have not been conducted even to this day.

We remain in the hope that these suggestions will be taken into account when implementing the Economic Reform Program 2018-2020.

With all due respect,

Biljana Muratovska
Secretary General

THE ASSOCIATION OF EMPLOYERS ASSOCIATIONS OF TRANSPORT COMPANIES OF REPUBLIC OF MACEDONIA
"MAKAM-TRANS"
www.makamtrans.org.mk street: Pero Nakov no.1 1000, Skopje; tel. 02/ 2551 057