

# *U.S. Embassy - Skopje*

## **ECON NEWSLETTER 03/2004**

### **GOVERNMENT ADOPTS PROGRAM FOR INVESTMENTS IN RAILWAY INFRASTRUCTURE**

The GOM adopted the annual Program for investments in railway infrastructure, which was prepared by the Ministry of Transport and Communication and the management of "Macedonian Railways". It allocated Denar 300 million in the 2004 budget for railways Tabanovce-Gevgelija (Denar 237 million), Veles-Bitola (Denar 53 million) and Skopje-General Jankovik (Denar 10 million).

### **RISING YIELDS, LOW DEMAND FOR TREASURY BILLS**

Banking sources said that the domestic currency liquidity in March has weakened, which affected almost all domestic banks. This is in contrast with the beginning of this year when the banks reportedly had excess domestic currency liquidity. The lack of domestic currency liquidity is supported by the recent performance at the treasury bills auctions, which evidenced falling demand for T-bills and rising yield rates. The rising yields on the bills issued both by the Central bank and the Ministry of Finance are already causing concern among the financial community.

At the fourth auction of treasury bills held on March 9, the banks showed the least interest so far. They purchased only Denar 104.4 million worth bills of the total of Denar 200 million offered by the GOM. As a consequence, the bills yield rate went up hitting the highest so far, which is totally opposite from the Ministry of Finance's expectations that it will come down to 7 percent. The average interest rate was 8.63 percent, with a maximum rate of 9.29 percent and a minimum of 7.53 percent.

The fifth auction held on March 23 also witnessed weak demand and a further increase of the average yield rate. The amount on offer was Denar 300 million, but bills worth only Denar 121 million were purchased at an average yield rate of 8.99 percent. According to analysts the recent weak demand is due to the higher yield offered on the Central Bank bills. The inability to sell the offered treasury bills during the last three auctions

raises the question how the GOM will meet its funding needs.

Treasury bills auction results

Date of auction	Maturity (days)	Supply (MKDmn)	Demand (MKDmn)	Sold (MKDmn)	Yield, %
January 20	91	100	175.4	100	7.53
February 3	91	100	168.2	100	7.35
February 17	91	150	108.7	108.7	7.49
March 9	91	200	104.4	104.4	8.63
March 23	91	300	121	121	8.99

Source: Central Bank

**INDUSTRIAL OUTPUT'S DRASTIC FALL RAISES CONCERNS ABOUT REALIZATION OF GDP GROWTH TARGET**

The drastic fall of industrial output in January reported by the State Statistical Office has raised great concerns whether the set target of GDP growth of 4 percent this year would be achieved. Industrial production registered a sharp decline by nearly 45 percent on a year-to-year basis and 42 percent drop in January. Industry's share of GDP is about 25 percent.

Local analysts noted that although it is too early to predict pessimistic scenarios, the slowdown may seriously question the realization of the target for GDP growth agreed with the IMF, as well as the planned reduction of the unemployment rate.

According to officials from the Ministry of Economy quoted by the press, the deceleration of industrial output in the first month of 2004 was caused by the inactivity of many companies from the heavy industry in the reporting period. In the mining and extracting sector, the drop was by 83.4 percent. The key mining enterprises - the three lead and zinc mines Sasa, Toranica and Zletovo, the copper mine Bucim as well as the Veles-based smelter Topilnica and the steel mill Balkan Steel - are not working.

**NBM CLAIMS IT DOES NOT COMPETE WITH THE GOM**

"We are not competing with the state", NBM claims in regards to the increase of the Central bank (CB) bills' interest rates. The treasury bills' price is created by the market and it cannot be limited as in the case of CB

bills, thus making them attractive to the investors, Central Banking Operations Department indicates.

The decision to intervene by increasing the CB bills rates was made by carefully following the fiscal policy, the cash flow and the foreign exchange transactions. The Central Bank informed that all this was agreed in coordination with the Ministry of Finance (a coordination body was created for the purposes).

#### **55 MILLION EURO REMAIN UNALLOCATED**

The European Agency for Reconstruction (EAR) in Macedonia has failed to disburse 55 million euro allocated by the European Union in the past year, because all projects need time for realization. "We initiated a total of 38 new projects in the course of last year, which should be finalized in the upcoming years. The money allocated in 2003 should not necessarily be disbursed in the current year. Instead, they will be used until we don't close all projects foreseen", Daniel Julgaris, Head of the EAR in Skopje, informed the journalists on March 11.

#### **FIRMS OWE 7 BILLION DENARS IN VAT**

The Public Revenue Office (PRO) reported its satisfaction on the collection of taxes in the first two months of 2004, estimated at 99.97 percent of the plan for that period.

"VAT collection was the most successful, while there was 4 percent deficiency in the profit tax", Petra Miteva, the Public Revenue Office Director informed on March 15. The revenues collected by March 7, amounted to 4.2 billion denars of VAT (73 percent of the quarterly plan), 1.2 billion denars of personal income tax (70 percent), 1.5 billion of excises (66 percent) and 521 million denars of profit tax (60 per cent). She also informed that so far this year 1.5 million denars have been reimbursed in VAT refunds.

The GOM owes 1.2 billion denars to the taxpayers for VAT refunds, but at the same time claims total of 7 billion denars. This sum includes the debts incurred by bankrupted or liquidated firms, Miteva said.

According to daily "Vest", a number of judges were included in the abuses of VAT refunds. The information was confirmed by Miteva, who also stated that criminal charges would be brought against the individuals involved in the illegal processing of VAT refunds.

## **ROUNDTABLE "ECONOMIST": ATTRACTION OF INVESTMENT THROUGH PROMOTION OF MACEDONIA**

Macedonia's promotion for attraction of foreign investments should be the focus of attention of the Macedonian Government, which has achieved significant progress since the last roundtable, said Delia Met Cohn, Chairperson of the Third Roundtable organized by "Economist" on March 16 - 17. Investors need to be shown that the country is not a risk for investments, but she added that there are other problems such as gray economy, great unemployment and low level of export.

PM Branko Crvenkovski attended the conference and addressed domestic and foreign businessmen and experts. He mentioned that some of the Government's goals this year are the maintenance of relatively low and stable inflation, tight control of public expenses, liberalization of the economy and an increase of the export potential. "The communication between the GOM and the businessmen is not at a satisfactory level, and the GOM and its institutions have a share in the blame. Another problem can be detected from the failed functioning of the Economic Chamber, in a situation where there is a lack of an alternative association that could unite various business interests", Crvenkovski stated.

According to him, the real promotion of Macedonia would become possible through the investment of foreign companies in the country. The owner of Jet Oil, Kiriakos Mamidakis, believes that Macedonia is a fertile ground for speculative investors, pushed by their interest of fast profit. According to him, the foreign investors still lack the necessary confidence for investing in the Macedonian economy.

On the businessmen's remark that the Government is too lenient in the negotiations with IMF and the World Bank, the Prime Minister pointed out that "there are special rules in the game with these financial institutions". He announced that this year Macedonia will initiate negotiations for a three-year assistance and development arrangement with the IMF.

According to Crvenkovski, the privatization is a concluded process, adding that the privatization of the Electrical Power Company of Macedonia will be a long and multi-phased process.

## **ESM CUT OFF IN TWO**

"The electricity sector in the country has been constructed as a sole integrative enterprise for production, transfer and distribution of electricity, whereby the Electric Power Company (ESM) possesses the entire infrastructure for fulfilling these functions. The Minister of Economy Stevco Jakimovski explained that the amendments to the Energy Law would establish a new structure in the enterprise from a functional, legal and financial point of view.

According to the model proposed, ESM will be divided in two separate firms, i.e. AD MEPSO, which will remain permanently in public ownership and espouse the functions and infrastructure appertaining to the transfer of electricity and the management of the electrical energy system through the existing dispatching centre, and AD ESM, which is set to integrate production function and infrastructure.

According to Jakimovski, the whole company will be subjected to a full or partial privatization by the strategic investor, selected in a tendering procedure, on a pre-qualification stage. According to the members of the opposition parties, the draft-law on ESM is a political deceit. The opposition believes that the law is "poor in quality" and suggested the GOM to hire experts who will prepare a feasibility study for a sustainable project and then proceed with privatization of ESM.

## **MACEDONIA REFUSES TO INVEST IN LJUBLJANSKA BANKA INDEMNITY FUND**

The GOM does not intend to invest in the Fund that Slovenia, Croatia, Bosnia and Herzegovina, and Macedonia were recommended to create in order to pay off the foreign exchange deposits to the clients of the former Ljubljanska Banka. This is the first, unofficial, information issued by the GOM's Cabinet with regards to the recommendation issued by the Legal Affairs and Human Rights Board within the parliamentary assembly of the Council of Europe.

"Macedonia fully took on Ljubljanska Banka's debt towards the Macedonian clients of this bank. At the moment, the obligations are paid off by issuing national securities. The State spends about 50 million euros every year from the Central budget in its efforts to regularly service the debt towards the former foreign exchange savings.

This is the main argument against investment in the Fund, because in that case there would be double payment", sources from the GOM explained.

The Ministry of Finance has already sent a recommendation to the Parliament against investment in the Fund. According to the experts, Macedonia should insist on a favourable return of funds in the succession process, since it already pays off the obligations towards former clients of Ljubljanska Banka.

#### **WELSH COMPANY REPORTEDLY CHOSEN TO DEVELOP BUNARDZIK FREE ECONOMIC ZONE**

The Welsh company Glendor Estate said that it is the winner of the international tender for a founder (site developer) of the Bunardzik free economic zone, Macedonian media reported. It said that over the first 12 months the amount of the investments would exceed 1 million euros. At least six international companies will invest in Bunardzik. The term of the contract will be 50 years with a possibility for extension of another 25 years. The GOM has not officially announced the founder of the Bunardzik free economic zone.

#### **PRIVATIZATION AGENCY ACTIVE UNTIL THE END OF 2004**

On March 29, the GOM decided to prolong the activities of the Privatization Agency to the end of 2004, instead of March 31. The main reason is that there is still state capital in 137 companies. The changes in the Law of the Agency will be at the agenda of the following Parliament session.

#### **ANNUAL REPORT ON STABILIZATION AND ASSOCIATION PROCESS FOR MACEDONIA**

On March 30 the Chief of European Commission delegation to Macedonia, Donato Chiarini handed over the Annual Report on the Stabilization and Association Process for Republic of Macedonia and the European Partnership to the Vice Prime Minister Radmila Sekerinska. "Macedonia receives the Report for the third time, which refers to the progress in the stabilization and association process, but we received the European partnerships for the first time, which are one of the concrete consequences, i.e. steps after the Thessalonica Summit", Sekerinska stated after the meeting with Chiarini.

"The submitting of the application for EU membership, the effectiveness of the Stabilization and Association

Agreement from April 1, the Report and implementation of the European partnerships show that the space is narrowed, while the obligations are being increased. The Government will treat them seriously and priorities will be set, while results will be closely followed", Sekerinska added, not stating which are the critics and remarks of the Report for the Republic of Macedonia.

The Chief of European Commission delegation Chiarini stated that "there is great progress, there are results, but the task is huge and very complex. We encourage the PM and the GOM to continue the work they are doing", Chiarini said in a response to a journalist question for comparison of the 2004 Report with the one of 2003.

#### **STABILIZATION AND ASSOCIATION AGREEMENT GOES INTO EFFECT ON APRIL 1**

The Stabilization and Association Agreement (SAA) between the European Union and the Republic of Macedonia goes into effect on April 1, which is another step forward of Macedonia towards European integration, the European Commission stated. This Agreement is the first Stabilization and Association Agreement that goes into effect. For that purpose, a Ministers' Council will be established, along with a Commission and sub-Commissions, which will encompass all issues of the Agreement, and which will convene annually.

The SAA was signed on April 9, 2001. It regulates the ambitious goals, and is a framework for leading of an intensive dialogue at a political and technical level. The agreement obliges the parties to continue to work on the political, economic and institutional stabilization of the country, strengthening of institutions and reform of the public administration, strengthening of the commercial and economic cooperation, coordination of the Macedonian legislation with the European one, as well as in the field of justice and internal affairs. The full realization of the agreement will also create a new climate for development of trade and investments, which are key factors for the economic restructuring and modernization of the country.