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**INTERNATIONAL BANK FOR RECONSTRUCTION AND DEVELOPMENT**

**INTERNATIONAL FINANCE CORPORATION**

**MULTIlLATERAL INVESTMENT GUARANTEE AGENCY**

# COUNTRY PARTNERSHIP STRATEGY

# FOR THE FORMER YUGOSLAV REPUBLIC OF MACEDONIA

# FOR THE PERIOD OF FY2015 – FY2018

**August 25, 2014**

**South East Europe Country Unit**
**Europe and Central Asia**

**International Finance Corporation**
**Europe and Central Asia Department**

**Multilateral Investment Guarantee Agency**
**Economics and Sustainability Group**

The last Country Partnership Strategy (CPS) for the Former Yugoslav Republic of Macedonia Report No. 54928-MK was discussed by the Board of Executive Directors on September 20, 2010. The last CPS Progress Report was dated November 1, 2012.

**GOVERNMENT FISCAL YEAR**
January 1 – December 31

**CURRENCY EQUIVALENTS**
(Exchange Rate Effective as of June 6, 2014)
Currency Unit = FYR Macedonian Denar (MKD)
US$ 1.00 = MKD 45.26

**WEIGHTS AND MEASURES**
Metric System

| | World Bank | IFC | MIGA |
|---|---|---|---|
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## ABBREVIATIONS AND ACRONYMS

| | |
|---|---|
| AAA | Analytical and Advisory Activities |
| APL | Adaptable Program Loan |
| ARD | Agriculture and Rural Development |
| ASAP | Agriculture Strengthening and Accession Project |
| BERIS | Business Environment Reform and Institutional Strengthening Project |
| BEEPS | Business Environment and Enterprise Performance |
| BREP | Balkan Renewable Energy Program |
| CCT | Conditional Cash Transfers |
| CHU | Central Harmonization Unit |
| CEFTA | Central European Free Trade Agreement |
| CPS | Country Partnership Strategy |
| CPSPR | Country Partnership Strategy Progress Report |
| CPPR | Country Performance Portfolio Review |
| CRIF | Catastrophic Risk Insurance Facility |
| DB | Doing Business |
| DPL | Development Policy Loan |
| DUI | Democratic Union for Integration |
| EBRD | European Bank for Reconstruction and Development |
| EC | European Commission |
| ECA | Europe and Central Asia |
| ECSEE | Energy Community of Southeast Europe |
| EIB | European Investment Bank |
| ESW | Economic and Sector Work |
| EU | European Union |
| EVN | Electricity Distribution and Supply Company |
| FDI | Foreign Direct Investment |
| FY | Fiscal Year |
| FYR | Former Yugoslav Republic |
| GCR | Global Competitiveness Report |
| GDP | Gross Domestic Product |
| GEF | Global Environment Facility |
| HBS | Household Budget Survey |
| HIF | Health Insurance Fund |
| IBRD | International Bank for Reconstruction and Development |
| ICT | Information and Communications Technology |
| IDA | International Development Association |
| IDF | Institutional Development Fund |
| IFC | International Finance Corporation |
| IMF | International Monetary Fund |
| INSPIRE | Infrastructure for Spatial Information in EC |
| IPA | Instrument for Pre-Accession Assistance |
| IPARD | Instrument for Pre-accession Assistance for Rural Development |
| LFS | Labor Force Survey |
| MAFWE | Ministry of Agriculture, Forestry & Water Economy |
| MCIIP | Macedonia Competitive Industries and Innovation Support Program |
| MEPSO | Public Electric Power Transmission Company |
| MIGA | Multilateral Investment Guarantee Agency |
| MOE | Ministry of Economy |
| MOEPP | Ministry of Environment and Physical Planning |
| MSIP | Municipal Services Improvement Project |
| MOF | Ministry of Finance |
| NATO | North Atlantic Treaty Organization |

| | |
|---|---|
| NBG | National Bank of Greece |
| NCSD | National Council for Sustainable Development |
| NGO | Non-Governmental Organization |
| NPL | Non-performing Loans |
| OECD | Organization for Economic Cooperation and Development |
| PE PBG | Public Expenditure Policy Based Guarantee |
| PESR | Public Enterprise for State Roads |
| PFR | Public Finance Review |
| PIFC | Public Internal Financial Control |
| PPP | Public Private Partnership |
| R&D | Research and Development |
| REBIS | Regional Balkans Transport Infrastructure Study |
| REPARIS | Road to Europe: Program of Accounting Reform and Institutional Strengthening |
| SDSM | Social Democratic Union of Macedonia |
| SEE | South East Europe |
| SEZ | Special Economic Zones |
| SFA | Social Financial Assistance |
| SHPP | Small Hydro Power Plants |
| SIC | Social Insurance Contributions |
| SILC | Survey of Income and Living Conditions |
| SME | Small and Medium Enterprise |
| SOE | State-Owned Enterprise |
| SWC | Social Welfare Center |
| TF | Trust Fund |
| TFP | Total Factor Productivity |
| TIDZ | Technological and Industrial Development Zones |
| UNDP | United Nations Development Program |
| UNHCR | United Nations Commissioner for Refugees |
| USAID | United States Agency for International Development |
| VET | Vocational Education and Training |
| VMRO DPMNE | Internal Macedonian Revolutionary Organization – Democratic Party for Macedonian National Unity |
| WBG | World Bank Group |
| WDI | World Development Indicators |
| WGI | World Governance Indicators |

# Country Partnership Strategy FY 2015 - 2018

# FYR Macedonia

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## EXECUTIVE SUMMARY

i. **FYR Macedonia has come a long way in economic and social development since its independence in 1991, yet challenges remain.** The country's early diplomatic recognition was hampered by a dispute with Greece over the name of the country, and this continues to thwart FYR Macedonia's European Union (EU) accession prospects. The country stood out among its Balkan neighbors by avoiding the inter-ethnic violence following the break-up of Yugoslavia in the early 1990s, yet it experienced inter-ethnic unrest a decade after independence. The Ohrid agreement of 2001 and subsequent amendments to the Constitution confirmed the rights of all ethnic groups. Parties organized along ethnic lines define the political landscape.

ii. **The presidential and parliamentary elections of April 2014 confirmed the mandate of the Macedonian-Albanian coalition government that has been in power since 2008, but political divisions remain**. The ruling coalition of the largest ethnic Macedonian and Albanian parties (VMRO DPMNE and the Democratic Union for Integration (DUI)) received its widest margin yet – 80 out of 123 seats, providing the foundation for a continued reform agenda. At the same time, the main Macedonian opposition party (SDSM) refused to take the 34 seats won in the election. Since then, progress has been made in terms of participation by opposition parties in the work of the Parliament. If the country is to advance on an inclusive growth agenda, all parties have to engage constructively in the political process, to benefit all segments of society.

iii. **The new World Bank Group Country Partnership Strategy (CPS) is based on the World Bank's twin goals, the Government's vision of development and the country's progress towards EU accession.**

iv. ***The World Bank's twin goals – to eliminate extreme poverty and promote shared prosperity - are very relevant in fYR Macedonia*** because economic growth has not yet translated into significant poverty reduction or improved welfare of the poorest 40 percent of the population. Between 2002 and 2009, the economy grew at 3.9 percent per annum in real terms. While average consumption growth (used as a proxy for measuring shared prosperity) increased by 1.1 percent between 2003 and 2008, consumption growth of the bottom 40 percent decreased by 1.5 percent annually in the same period. Although not comparable to the consumption-based data prior to 2008, most recent income-based data for 2010 and 2011 shows a similar pattern: a slight decline in overall income, more pronounced for the bottom 40 percent. High unemployment is a critical feature of the story, with poor labor market outcomes disproportionally affecting the bottom 40 percent, many of whom also have less education and lower quality housing. FYR Macedonia stands out in the region for its recent progress in decreasing unemployment,[1] albeit from very high levels. Unemployment remains high at around 28 percent of the labor force, and productivity and wages are low. Sustaining the recent employment creation momentum and translating economic growth into jobs and income will help reduce poverty and improve the standard of living of all Macedonians. Therefore, helping

[1] Since the outbreak of the crisis fYR Macedonia managed to decrease unemployment from 32.4 percent in 2009 to 28.6 percent in 2013.

the authorities to tackle these important challenges is a crucial reason for continued World Bank Group (WBG) engagement.

v. **The Government of fYR Macedonia has a clear vision of development, which is consistent with the Bank's twin goals.** This vision seeks to improve the welfare of all citizens in fYR Macedonia, including those in the bottom 40 percent of the income distribution, based on economic growth through competitiveness, which is to be achieved through improvements in business climate, infrastructure and human capital. FYR Macedonia's key strategies of development, including the National Strategy for Reduction of Poverty and Social Exclusion in the Republic of Macedonia for 2010-2020 and the recently adopted South East Europe 2020 Strategy, set out specific targets in these thematic areas, to which Bank assistance can contribute.

vi. **EU accession is the main anchor of the reform agenda.** All major political parties and over 80 percent of the people continue to support EU membership. FYR Macedonia became an EU Candidate country in 2005 and since 2009 the European Commission (EC) has been recommending opening accession negotiations with fYR Macedonia, but the decision continues to be postponed in part due to the name dispute with Greece. The Government of fYR Macedonia is committed to the accession agenda, and the country has recently confirmed its participation in the *South East Europe 2020 Strategy*, which sets out specific goals for growth that is integrated, smart, sustainable, inclusive, and pursued with good governance. The EC has an active program of assistance to fYR Macedonia, which includes financing through the Instrument for Pre-Accession Assistance (IPA), the largest source of concessional funds in the country.

vii. **During the CPS period, in-depth analytical work will be undertaken to reduce the current knowledge gaps around poverty.** Knowledge gaps remain due to a lack of reliable poverty data that reduce the reliability to identify the most critical drivers of poverty reduction and the transmission channels for increased shared prosperity. Thus in defining the two pillars of the CPS with the authorities, the Bank used growth and competitiveness, and skills and inclusion, as the main proxies based on our current understanding of the economic and social context in fYR Macedonia as well as our experience from the portfolio we are supporting. The Bank has also embarked on the preparation of an in-depth poverty and drivers of growth analysis, the findings of which will be used to refine the proposed program, as needed, together with the authorities and make adjustments as appropriate at mid-term. The Bank will also apply a social filter for every operation to inform project design in order to maximize their social impact. Finally, during the latter part of the CPS implementation period, the Bank will launch the Systematic Country Diagnostic for fYR Macedonia to inform the next strategy which will be a Country Partnership Framework[2].

viii. **The CPS will focus on two interrelated themes: i) Growth and Competitiveness; and ii) Skills and Inclusion**. Both are crucial for eliminating extreme poverty and boosting shared prosperity in fYR Macedonia. For ***Growth and Competitiveness***, successful poverty reduction would need sustained private sector led growth, making fYR Macedonia more attractive as a destination for investments and as a country whose private companies can compete at the

[2] All country strategies with a concept review meeting held before July 1, 2014 prepare CPS.

regional and global level. Key outcomes targeted under this pillar are improved fiscal and public financial management for better use of public resources to support growth, further increase of private investment and export capacity, strengthened road infrastructure management and better provision of clean energy through public and private investments - crucial for the country's further regional integration. The Government has already achieved impressive results in this area which is one of its key strategic objectives, including as part of the Innovation Strategy 2013-2015 and the "Europe 2020" Strategy. For ***Skills and Inclusion***, the fruits of growth can be shared broadly if more Macedonians have access to better jobs and if public services are of good quality and delivered efficiently. Key outcomes to which this pillar will contribute are skills better adapted to the labor market, more opportunities for disadvantaged groups and better access to basic services. In addition, a focus on improved governance and transparency is essential both for a predictable and stable investment climate and as a foundation of an inclusive multi-ethnic society with broad economic participation. To promote productivity through new skills and competitive technologies, IFC will continue its efforts to assist in attracting and supporting foreign investment. More broadly, the WBG will offer a full range of financial, knowledge and convening services in support of these goals, providing assistance in selected sectors to catalyze a significant impact by leveraging competitive advantages of the International Bank for Reconstruction and Development (IBRD), the International Finance Corporation (IFC) and the Multilateral Investment Guarantee Agency (MIGA) resources.

ix. **Since fYR Macedonia's future is clearly linked to European integration, the CPS will actively promote the EU accession agenda and this will represent a cross- cutting theme.** The strategy is consistent with the new EU Assistance Country Strategy Paper for 2014-2020. In particular, the Bank will contribute to the accession agenda by supporting investments for fYR Macedonia's income convergence with the EU, promoting better economic governance, helping the development of institutions and changes in the legal framework, as well as improving the efficiency of the use of EU's instrument of pre-accession (IPA) assistance. At the project level, the Bank will coordinate project design and implementation with the EU in order to maximize synergies and use the capacity building opportunities of Bank financed operations to support fYR Macedonia's ability to absorb IPA funds. The WBG will also explore opportunities for joint projects with the EU and other development partners in order to minimize transaction costs and increase the impact of resources available to fYR Macedonia for the country's inclusive and sustainable development.

# I. COUNTRY CONTEXT AND DEVELOPMENT AGENDA

## A. Political Context

1. **FYR Macedonia has come a long way since its independence in 1991 yet political challenges remain, impacting the country's growth and development.** The country's early diplomatic recognition was hampered by a dispute with Greece over the name of the country, and this continues to thwart fYR Macedonia's EU accession prospects. The country stood out among its Balkan neighbors by avoiding the inter-ethnic violence following the break-up of Yugoslavia in the early 1990s, yet it experienced inter-ethnic unrest a decade after independence. The Ohrid agreement of 2001 and subsequent amendments to the Constitution confirmed the rights of all ethnic groups[3]. Parties organized along ethnic lines define the political landscape.

2. **The presidential and parliamentary elections of April 2014 confirmed the mandate of the government coalition that has been in power since 2008, although political divisions remain.** The ruling coalition of the largest ethnic Macedonian and Albanian parties (VMRO DPMNE and DUI) received its widest margin yet – 80 out of 123 seats, providing foundation for continued reform agenda. At the same time, the main Macedonian opposition party (SDSM) refused to take the 34 seats won in the election. Since then, some progress has been made in terms of participation by opposition parties in the work of the Parliament. If the country is to advance on the inclusive growth agenda, all parties have to engage constructively in the political process, to benefit all segments of society, drawing on the country's strong track record of peace and stability.

3. **EU accession remains the main anchor of the reform agenda.** All major political parties and over 80 percent of the people continue to support EU membership. The country gained EU candidate status in 2005, and since 2009 the EC has been recommending opening accession negotiations with fYR Macedonia, but the decision continues to be postponed in large part due to the name dispute with Greece. Since March 2012 the Commission has been conducting the High Level Accession Dialogue with the Government of fYR Macedonia. In December 2013, the EU General Affairs Council issued a resolution confirming the EC's recommendation to open accession negotiations, noting that the political criteria continue to be sufficiently met and proposing to "revert to the issue in 2014, on the basis of an update by the EC on further implementation of reforms in the context of the High Level Accession Dialogue, including the implementation of the 1 March political agreement and on tangible steps taken to promote good neighborly relations and to reach a negotiated and mutually accepted solution to the name issue."

[3] According to the last official census of 2002 fYR Macedonia is an ethnically diverse country, with 64.2 percent of the population made up of ethnic Macedonians, 25.2 percent ethnic Albanians, 3.9 percent ethnic Turks, 2.7 percent Roma, 0.5 percent Vlachs, 1.8 percent Serbs, 0.8 percent Bosnians, and 1.0 percent others.

## B. Growth and Inclusion Diagnostic

### Sources of Growth

4. **FYR Macedonia is a small, landlocked and open economy with a sound track record of macro-fiscal stability.** With an openness indicator[4] of 126.3 percent in 2013, it is the most open among the countries of South East Europe (SEE)[5]. FYR Macedonia has been able to preserve macroeconomic stability in the presence of adverse shocks. Its exchange rate peg to the Euro, introduced in 1995, has successfully supported price stability, with inflation averaging 2.4 percent over the last 10 years. Macroeconomic policies have been geared towards keeping the external balance manageable, and monetary policy has responded quickly to any possible threats to the peg. General government debt, which reached 35.8 percent of Gross Domestic Product (GDP) at the end of 2013, is the fifth lowest among the EU and SEE countries[6], and public sector debt at 43.2 percent of GDP at end 2013 is the second lowest among the SEE countries. Growth volatility has been low by regional standards.

5. **Growth would need to accelerate for fYR Macedonia to close its income gap with the new EU member states.** Between 2002 and 2009, fYR Macedonia grew at 3.9 percent annually in real terms, which enabled the country to reduce its income gap with the EU. Between 2002 and 2009, fYR Macedonia's income per capita grew from 25 percent of the EU's GDP per capita to 36 percent in 2009. Since then, average GDP growth has declined to 2.1 percent per year and convergence to the EU has stalled. Real GDP growth would need to accelerate to around 4.5 percent – significantly above the ten-year average of 3.2 percent – for fYR Macedonia to converge to the living standards of the new EU member states within the next 20 years.

6. **FYR Macedonia's sectoral drivers of growth have changed noticeably over the past 15 years, with trade and commerce declining and construction taking over as the fastest growing sector.** Prior to 2002, over 80 percent of growth came from trade and commerce, industry and wholesale and retail. Since 2002, growth in trade and commerce has dropped while industrial growth remained stable. Since 2009, the construction sector has become the predominant driver of growth as the public sector scaled up capital spending to counterbalance the decline in external demand due to the Euro zone crisis. This seems to have come at the expense of quality of public investment: the share of investment in administrative buildings increased while investment in infrastructure and maintenance dropped[7].

7. **FYR Macedonia's growth was driven by both employment and productivity gains before the crisis, but most job creation occurred in low-productivity sectors or in the public sector.** The country made impressive gains by reducing the unemployment rate from 38 percent in 2004 to around 28 percent in 2013, yet the rate remains high in comparison to the recent EU entrants such as Croatia (17 percent in 2013), Bulgaria (13 percent) and Romania (7 percent).

[4] The openness indicator is defined as the sum of imports and exports relative to GDP.
[5] SEE countries include Albania, Bosnia and Herzegovina, Kosovo, Macedonia fYR, Montenegro and Serbia.
[6] Gross public sector debt, which includes the debt of municipalities and public enterprises, but not the debt of the Central Bank, stood at 43.2 percent of the GDP in 2013.
[7] In 2008, 85 percent of all public investment was destined to infrastructure while only 15 percent went to non-residential and residetial buildings. By 2012, investments in non-residential and residential buildings doubled as a share of total public investment, reaching 33 percent.

Despite a relatively large and rising capital share of income from 2001-2008 (between 40 and 50 percent), physical capital accumulation accounted for only 0.3 percentage points of the average annual 4.3 percent GDP growth between 2002 and 2008, whereas employment growth contributed 1 percentage point, and Total Factor Productivity (TFP) growth roughly 3 percentage points. After the 2008 crisis, productivity growth decelerated significantly while employment continued to grow. In fact, fYR Macedonia is the only SEE country where employment increased in the post-crisis period. Agriculture, construction and public administration have been the main drivers of employment growth over the last decade. However, the jobs created in the past years have been either informal, in low-productivity sectors or in the public sector: 27.1 percent of net jobs created between 2007 and 2011 have been in agriculture, 13 percent in retail trade (predominantly informal) and 19.7 percent in the public sector[8]. The share of net jobs created in agriculture is high when considering that agricultural growth has been weak throughout the last decade and averaged zero since 2009.

8. **Growth in the pre-crisis years was powered by domestic demand, engendering relatively large and persistent trade deficits and increasing household indebtedness.** In the years leading up to the 2009 crisis, real GDP growth was underpinned by strong private consumption and rapidly increasing investment, both of which had a large import content and pushed the trade deficit from an already-large 17.8 percent of GDP in 2005 to around 26 percent by 2008. The trade deficit was largely financed by remittances which in turn fueled private consumption. Household debt rose rapidly, albeit from low levels by regional standards.[9] Since the crisis, disposable incomes made a modest recovery thanks to wage and employment growth, increased social transfers as part of the crisis response, and an easing of the tax burden on personal income. At the same time, household consumption declined, bringing it closer in line with disposable income. This renewed savings impetus has helped to stabilize the household debt ratio, which stood at 25.8 percent of disposable income at end-2012.

9. **Expansionary fiscal policy in the aftermath of the crisis led to a widening of the fiscal deficit and a rapid build-up in central government debt.** Revenues fell by over 3 percent of GDP between 2008 and 2011, as economic activity weakened and the Government reduced tax rates and social security contributions to boost competitiveness. Consequently, the fiscal deficit widened consecutively from 0.9 percent of GDP in 2008 to 2.5 percent in 2011, 3.9 percent in 2012 and 4.1 percent in 2013 and central government debt surged from 20.7 percent in 2008 to 35.6 percent by the end of 2013 (see Table 1 in Annex 3). At the same time, the Government shifted a part of capital expenditure off-budget by transforming the former Road Fund into the Public Enterprise for State Roads (PESR). At inception, the PESR carried EUR 82 million in debt (1.1 percent of GDP), but this is set to rise in the near term as the PESR executes strategic priorities of the central government's investment agenda. Based on planned borrowings by the PESR and other State Owned Enterprises (SOEs) to finance an ambitious agenda of infrastructure and other investments, total public sector debt under the baseline scenario is projected to reach 44.3 percent of GDP in 2014 and increase up to 54.1 percent of GDP in 2018, around 15 percentage points higher than the debt of the central government alone.[10]

[8] According to the World Bank report "Employment and Job creation in fYR Macedonia, Labor Market Assessment 2007-2011", from August 2013

[9] Household debt climbed from a mere 10.4 percent of disposable income in 2005 to 27 percent by 2008.

[10] IMF estimates, July 2014 (Article IV consultation report).

10. **As a small, open economy fYR Macedonia will have to rely on exports and increased competitiveness to sustain long-term growth.** Supported by an active strategy to promote Foreign Direct Investment (FDI), fYR Macedonia is shifting gradually to a more export-led growth model. In recent years, fYR Macedonia has diversified its exports both in terms of products and destinations and increased the technological intensity of its export basket due to FDI. On the other hand, small and medium Macedonian companies face challenges of integration into international markets due to lack of managerial, financial and technical capacity, which limits their competitiveness. While multinational firms have made an impact on employment and growth of new industries with better long-term prospects, their limited backward linkages to domestic companies prevent a broader impact on the economy. FYR Macedonia will need to boost and upgrade its exports further to improve its competitiveness by investing in infrastructure, stronger investment climate, facilitating business growth and trade linkages, and supporting innovation. This will help the country to attract additional investments for sustained private sector-led growth. Continued efforts to improve competitiveness are particularly important for Macedonia given its exchange rate peg to the Euro.

**Poverty and Shared Prosperity**

11. **Economic growth and increases in employment in fYR Macedonia have not yet translated into tangible poverty reduction according to available data.** Despite data challenges in monitoring recent poverty trends in fYR Macedonia[11], the existing evidence shows that consumption-based absolute poverty between 2003 and 2008 (from the Household Budget Survey (HBS)) increased from 8 to 9 percent using a regional poverty line of US$2.5 a day, and from 33 percent to 37 percent, using a regional poverty line of US$5 a day. During the same period, official relative poverty statistics[12] remained largely unchanged at around 30 percent. FYR Macedonia has recently adopted a new way of measuring poverty through the income-based Survey of Income and Living Conditions (SILC). Under this new relative measure available for 2010 and 2011, poverty has also remained unchanged (27.3 in 2010 and 27.1 in 2011).[13] Inequality, as measured by the Gini coefficient, increased between 2003 and 2008 in fYR Macedonia from 37 to 40 using consumption data.[14] Income-based data for the years 2010 and 2011 suggests a modest decrease in inequality with a Gini coefficient of 40.8 and 39.2, respectively.

12. **The welfare of the poorest 40 percent of the population has not improved either.** Consumption growth of the bottom 40 percent – the World Bank indicator for the new institutional goal of promoting shared prosperity - decreased by 1.5 percent annually between 2003 and 2008, as average consumption grew by 1.1 percent. The difference between annual growth in average consumption and consumption of the bottom 40 percent was particularly

[11] Monitoring the evolution of poverty in fYR Macedonia has become challenging in recent years due to concerns over data quality of the HBS, particularly from 2009 onwards. Therefore, the HBS series is used until 2008 until further diagnostics are carried out. The Survey of Income and Living Conditions (SILC) started in 2010 in fYR Macedonia, and data available thus far is limited to 2010 and 2011. Recently, official poverty rates in fYR Macedonia started to be reported with income-based data from the SILC.

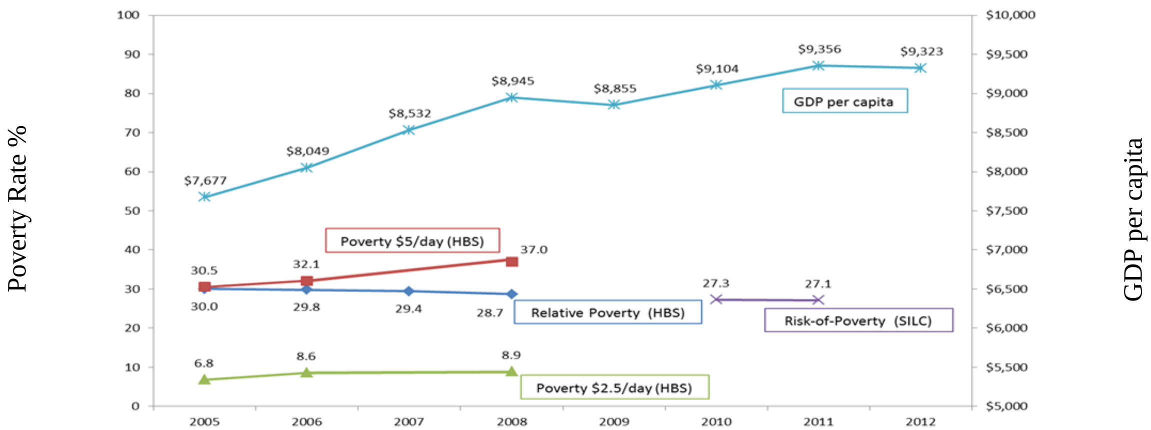
[12] Measured at 70 percent of median consumption.

[13] This indicator, called population at-risk-of–poverty, is measured at 60 percent of median equalized income, same as in countries in the European Union.

[14] Other measures of inequality follow a similar trend. For instance, between 2003 and 2008 the ratio of the $90^{th}/10^{th}$ percentiles increased from 5.7 to 6.4, and the ratio of the $75^{th}/25^{th}$ increased from 2.4 to 2.7.

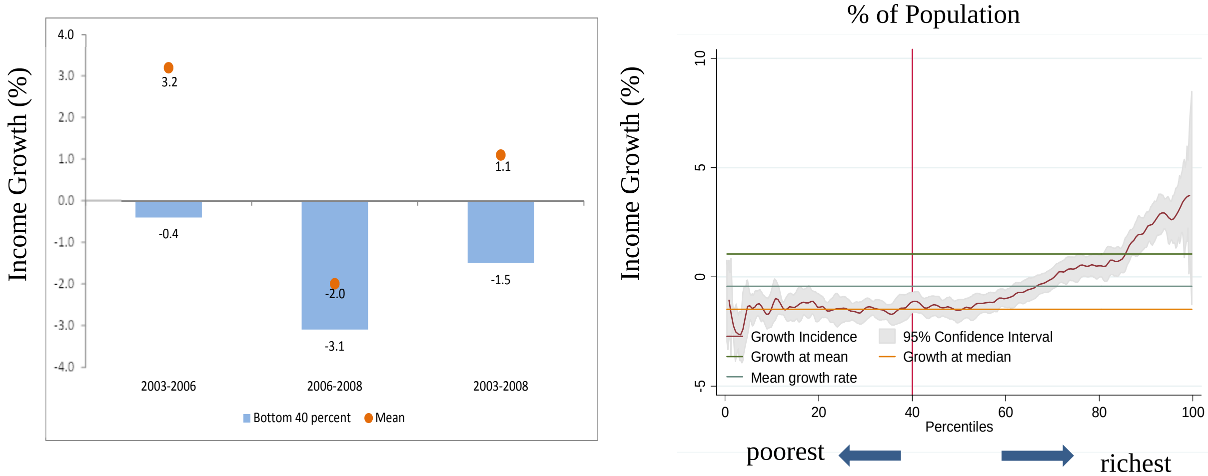
striking in 2003 and 2006, when the mean grew at 3.2 percent, while consumption of the bottom 40 percent fell by 0.4 percent. Growth incidence curves show that those in the top two quintiles of the distribution had higher than average welfare gains while those in the bottom three quintiles were below average. Although not comparable, recent income-based data for 2010 and 2011 shows a slight decline in overall income, more pronounced for the bottom 40 percent.

**Figure 1: GDP per capita, PPP (constant 2005 international $) and Poverty Rates**




*Sources*: GDP per capita: WDI. Poverty $5 and $2.5 a day: HBS. Relative Poverty: HBS (70 percent of median consumption) Risk-of-Poverty: SILC (Laeken poverty estimates).

*Figure 2: Shared Prosperity and Growth Incidence Curves in fYR Macedonia (2003-2008)*




*Source:* World Bank Staff estimates based on the harmonized ECAPOV dataset.

13. **The probability of being poor or among the bottom 40 percent is strongly associated with labor market status, gender and limited access to economic opportunities.** According to a recent study on shared prosperity in the region of SEE[15], the poor and those in the bottom 40 percent in fYR Macedonia are more likely to:

[15] World Bank. 2013. "First Insights into Promoting Shared Prosperity in South East Europe", part of the 5th edition of the *South East Europe Regular Economic Report 2013*.

- **Live in larger households and have more dependents**, especially children, which contrasts with that of the well-off, who have smaller households, fewer children and a relatively higher share of members over 65 years old. In fYR Macedonia 49 percent of the bottom 40 percent of the population live in households with five or more members, significantly higher than the 21 percent mark for the top 60 percent of the population.
- **Have lower levels of educational achievement**: people aged 15 and older in the bottom 40 percent are more likely to have no education or incomplete primary education, and are less likely to have attained tertiary education. The share of adults (15 +) with at most primary education in the bottom 40 percent is around 55 percent, while for the top 60 percent this number is 37 percent. Returns from tertiary education – although high in fYR Macedonia – are out of reach for the bottom 40 percent: the average wage of this group only reaches 62 percent of the average wage of the top 60 percent.
- **Not have accumulated other assets**: e.g., in terms of financial assets, a lower share of individuals in the bottom 40 percent (16 percent of the group) saved money in the past year, compared to those in the top 60 percent (25 percent).

14. **While women are equally represented among the poor, women likely have fewer opportunities to escape poverty** than men given that they are less educated and are significantly more likely to be jobless, particularly given the very high inactivity rates (see Figure 3). Although gender gaps are seen across the population, they can be particularly limiting for women, as both education and access to jobs are key factors of upward economic mobility.

15. **The share of employed adults among those of working age is lower for the less well-off in fYR** Macedonia. For instance, the share of employees in the working age population (age 15-64) is only 35 percent for the bottom 40 percent, while it increases to around 42 percent for the rest of the population. This gap between socio-economic groups is mostly driven by higher inactivity rates among the less well-off, given that unemployment rates are high across the board.

16. **The rural population is overrepresented in the bottom 40 percent,** suggesting differences in economic opportunities in rural areas. Rural population accounts for 36 percent of the total population of the country, yet half of the bottom 40 percent live in rural areas.

17. **The Roma[16] are a particularly vulnerable group in fYR Macedonia**. According to a 2011 World Bank/EU/United Nations Development Program (UNDP) survey, the absolute poverty rate for Roma (PPP US$4.30 income based) is 41 percent, as compared to 14 percent for the non-Roma population. The average Roma adult (age 25-64) has completed 6 years of education, compared to 10.5 years for the rest of the population. While unemployment rates are high in fYR Macedonia as a whole despite recent progress with its reduction, 53 percent of Roma adults (ages 15-64) are unemployed, as compared to 28 percent of the whole population. Roma are also among the group of workers that are likely to receive less than the minimum wage from their employers. Differences exist also in health and housing conditions, and Roma women lag behind men on most counts.

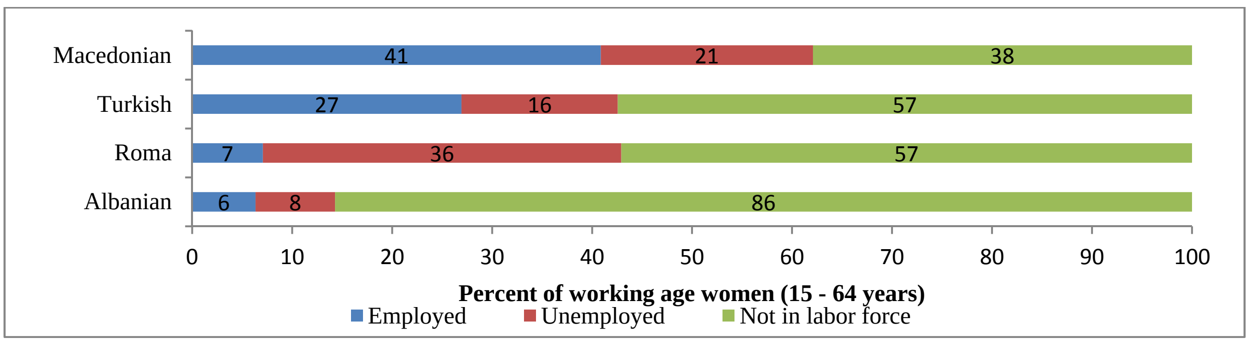
[16] The most recent official census data of Roma living in fYR Macedonia are from the 2002 Population Census, which registered 53.879 Roma citizens - approximately 2.7percent of the total population.

*Gender*

18. **FYR Macedonia has largely closed average gender gaps in education and health; however, gender disparities persist for certain population subgroups[17].** Gender gaps in enrollment rates still exist among ethnic Albanians, and secondary enrollment rates remain low for ethnic Roma men and women. Average learning outcomes are better for women than for men in fYR Macedonia, as in most countries in the region. Men and women, however, tend to choose different fields of study: women are more likely to choose general programs and subjects related to the social sciences, while men often study engineering, production, or construction. There is no evidence of gender-based differences in access to health services, and the country performs well when it comes to births attended by skilled health staff and adolescent fertility.

19. **Gender inequalities remain in access to economic opportunities in fYR Macedonia.** In 2012, female labor force participation (for women aged 15-65) in fYR Macedonia was 51 percent, below the regional average of 62 percent. Moreover, between 2004 and 2012, male labor force participation increased by 6 percentage points while female labor force participation increased by 4 percentage points, bringing gender gap in participation to 26 percentage points in 2012. For those in the labor market, unemployment rates for men and women are similar. Gender wage gap persists, even after controlling for other characteristics, with men receiving higher wages. The World Bank Enterprise Survey (2013) shows that women own 29.4 percent and manage 26.3 percent of the businesses interviewed.

**Figure 3: Female Labor Force Statistics (LFS) by Ethnic Group**




*Source: Labor Market Inequalities in fYR Macedonia: New Evidence and Perspectives on Gender and Ethnicity*, based on LFS (2006).

*Note*: 2006 is the last year when data is publicly available on ethnicity in the LFS. The data in this figure may not be representative at the population level.

20. **Gender gaps in accessing economic opportunities are tightly linked to differences across ethnic groups.** Available data indicate that labor force participation among ethnic minorities is often significantly lower than among ethnic Macedonians, especially among women (Figure 3). Whereas ethnic Macedonian women have an employment rate of 41 percent, only 10 percentage points lower than their male counterparts, women who are ethnically Turkish have an employment rate of 27 percent - a 32 percentage point gap with men of the same ethnic background. Roma and ethnic Albanian women lag even further behind in terms of employment,

[17] Data for the entire population, not for the bottom 40 percent.

with employment rates of only 7 and 6 percent, respectively. Activity rates among ethnic minorities are two or three times lower among women than among men.

21. **FYR Macedonia has made continuing progress in advancing gender relations**. The legal framework for gender equality is comprehensive and provides for equal treatment of both genders. The 2005 Labor Code endorses the definition of gender-based discrimination and provides a framework for anti-discrimination measures. According to the Law on Family all forms of abuse are prohibited, while the Law on Inheritance gives equal rights to men and women. The Criminal Code punishes gender-based discrimination and all forms of domestic abuse and violence. The Law on Equal Opportunities was adopted in May 2006 and amended in 2012. A new Strategy for Gender Equality (2013-2020) was adopted in 2013 and accompanied by a National Action Plan (2013-2016).

### C. Medium-Term Prospects and Risks

22. **In the medium term fYR Macedonia's growth is expected to accelerate, supported by a recovery of domestic demand, growth-friendly public investments and exports.** Under the baseline projections, real GDP growth is expected to reach 3.0 percent in 2014 and accelerate to 3.5 and 3.7 percent in 2015 and 2016, respectively. Domestic private demand is expected to recover on the back of recent increases in public wages and pensions and a continued decline in unemployment. Externally financed public investment in key transport corridors will increase. Export growth will be driven by a rebound of external demand as the Eurozone recovers and by new FDI related exports coming on line. There are several risks to this medium-term outlook.

23. **Macroeconomic risks stem from a potential deterioration of the Euro area economic outlook and an increase in oil prices.** A slower than projected pace of recovery in the Euro area could lead to lower than expected growth, exports and FDI. FYR Macedonia has a relatively high exposure to neighboring countries, especially Greece and Italy, through remittances and exports. Its large trade deficit (21 percent of GDP in 2013) is financed mostly through private transfers. About 50 percent of fYR Macedonia's current account deficit is oil-related, making it very sensitive to oil price changes. Increasing FDI, enhancing linkages between foreign firms and local suppliers, reducing energy imports, and strengthening competitiveness will be critical for reducing fYR Macedonia's reliance on private transfers and its exposure to external risks.

24. **External financing needs are expected to rise in the medium term, but reserve adequacy should remain robust and external debt is projected to decline.** External financing needs will reach around 15 percent of GDP in 2015 as payments on the 2009 Eurobond fall due and the current account widens as domestic demand recovers and FDI-related imports increase. Still, capacity to service existing external obligations is set to remain strong, with gross international reserves projected to average around 4.5 months of imports, covering roughly 150 percent of short-term external debt. Strong FDI inflows and a favorable growth-interest rate differential on external borrowing are expected to place external debt on a gradual downward path from its peak of 67.7 percent of GDP at end-2013 to 62.4 percent by 2018.

25. **FYR Macedonia's ambitious public investment program, while important for competitiveness and growth, is likely to lead to an increase in public debt**. Even under the assumption that gross central government debt stabilizes over the medium term, public sector debt is set to rise rapidly, as SOEs take over much of the investment spending. Stabilizing gross

central government debt will require a strong political commitment to implement the 2013 medium-term fiscal framework, which foresees a reduction in central government deficit from a 4.1 percent of GDP in 2013 to 2.6 percent in 2016[18]. This will also require Government commitment to open up private sector investments in the infrastructure and services sectors through PPPs.

26. **FYR Macedonia is vulnerable to climate change and is at a high risk of natural disasters, such as floods, droughts and earthquakes**. As discussed in the recent Green Growth report[19], a whole range of "no regrets" measures exist that could put the country on a greener and more sustainable growth path. For instance, energy efficiency could reduce demand and so put the country on a more sustainable and green development path, while helping to reduce fiscal pressure through energy cost reduction. Upgrading infrastructure services (water supply and sanitation, wastewater treatment, and solid waste collection) would help improve social, economic, and environmental quality of human settlements and living and working environment and put them on a more sustainable path. Continued development of the insurance mechanisms can help limit the financial damage of natural disasters to which fYR Macedonia is prone.

27. **Finally, one cannot rule out the risk of political instability.** FYR Macedonia has thus far managed to avoid the worst outcomes of a political system drawn along ethnic lines, with coalition governments crossing the ethnic divide and considerable efforts made to enshrine non-discrimination in the legal and regulatory framework. Nonetheless, frustrations over the slow pace of EU accession coupled with a slow decline in unemployment pose an underlying threat of instability and unrest that cannot be ignored in the quest for higher growth and better jobs.

### D. Challenges and Opportunities for Shared Prosperity

28. **To reduce poverty and promote shared prosperity, fYR Macedonia needs to increase private sector-led job creation, improve access to economic opportunities and basic services for the less well-off, and remove structural barriers that prevent certain social groups from progressing**. Recent growth rates, while encouraging in the local context, are not sufficient for meaningful convergence with the EU. Moreover, growth so far has not translated into sufficient job creation or improvement in the welfare of the bottom 40 percent. In addition to spurring growth, the Government needs to prioritize social and economic inclusion.

#### Challenge: Job creation through faster growth and better competitiveness

#### *Fiscal and public financial management*

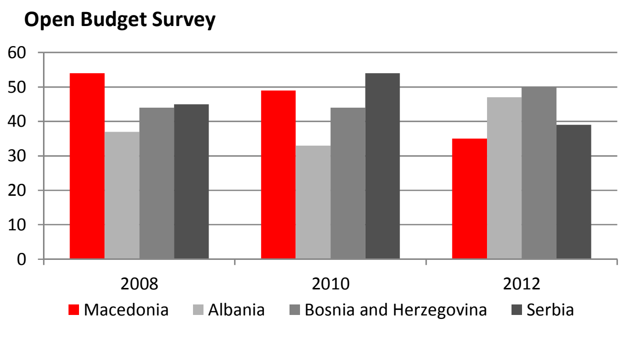
29. **Continued macroeconomic stability and improved public financial management are the foundation of future growth in fYR Macedonia.** Fiscal policies have in the past supported growth through increases in public employment and investment. Going forward, a more growth-friendly expenditure mix and improvements in fiscal management will be important to improve the efficiency and efficacy of public spending and support growth in the context of fiscal tightening at the central government level. It will be particularly important that public investment focuses on sectors that have a higher multiplier effect on the economy, including

[18] The Government has submitted to the Parliament a constitutional amendment, expected to come into force in 2014, which would limit budget deficit to 3 percent and public debt to 60 percent of the GDP.
[19] World Bank. 2014. *FYR Macedonia: Green Growth and Climate Change Technical Assistance Advisory Services*

those providing the necessary infrastructure (such as energy and transport infrastructure) to promote private investments and job creation and country's further regional integration.

**Box 1: Transparency, Accountability and Public Financial Management**

**FYR Macedonia has a mixed track record with respect to fiscal transparency.** While the governance index of the World Bank's World Governance Indicators and the score of the World Economic Forum's transparency of *government policy making* index have improved since 2011, the index of transparency of budget and accountability as measured by the Open Budget Survey has significantly deteriorated between 2008 and 2012[20] as scores on reporting and publication of audit reports, mid-year budget updates, extra budgetary funds and debt reporting declined and – contrary to other countries - progress in other areas stalled.




*Source: Open Budget Survey*

**The authorities have taken steps to improve budget transparency and accountability in 2013.** The Organic Budget Law was amended in December 2012 to improve strategic planning of public expenditures. Amendments to the Manual of Treasury Operations included compulsory recording of multi-year liabilities. In addition, the Ministry of Finance updated the Treasury Information System in 2013 to incorporate entry and monitoring of multi-year liabilities. A medium-term fiscal strategy has been published in 2013. The Government also adopted the Law on Financial Discipline in December 2013, which requires the Government to pay incurred obligations within 60 days, thus limiting the scope for future run-ups in arrears. On the other hand, public debt statistics are fragmented and the preparation and implementation of the medium-term fiscal framework could be improved. The Government is working with the World Bank on a comprehensive Public Finance Review (PFR), which will help identify the scope for further reforms in this area.

**FYR Macedonia's performance on key governance indicators could also be improved.** The country ranks in the middle of SEE countries, but significantly below the new EU member states with respect to the World Governance Indicators (WGI). It performs best on Control of Corruption, outpacing all other SEE countries and some new EU member states. Transparency International's Corruption Index confirms that fYR Macedonia ranks highest (together with Montenegro) among the SEE countries and has managed to improve its rank significantly in recent years. At the same time, fYR Macedonia's WGI ranking on voice and accountability deteriorated in recent years and it scores lowest in the region on political stability indicator, reflecting weak political dialogue and frequent elections. Other transparency concerns include a sharply deteriorating Press Freedom Index.

30. **FYR Macedonia has made improvements in the control framework over the use of public funds**, such as internal audit and external audit, which are among the priority areas for the EU accession. The Public Internal Financial Control (PIFC) framework was established by the Law on PIFC in 2009, followed by establishing the Central Harmonization Unit (CHU) and internal audit and financial management and control in public sector entities. The Law on the State Audit Office was passed in 2010, and its implementation led to an increased coverage of audited public funds as well as strengthened capacity to perform audits. Despite these positive developments, in order to prevent recurrence of public sector arrears further steps are needed to control and record commitments. Other priorities in the public financial management system include (i) improving budget revenue forecasts and adopting a more conservative approach to setting expenditure ceilings, (ii) capacity building to strengthen the system of reporting on SOEs

[20] FYR Macedonia ranked 28 (out of 85 countries) in 2008 and 68 (out of 98 countries) in 2012.

and public debt, and (c) capacity building to strengthen the country's system of public internal financial control.

31. **Strengthening public sector transparency is crucial for the environment of trust that is a prerequisite for increased private investment**. While fYR Macedonia has made strides in some areas of public financial management, significant scope for improvements remains in medium-term fiscal planning and publication of government statistics. As the Government plans to implement a large part of its investment program through SOEs, transparency and public disclosure of fiscal data become increasingly important.

32. **Availability of reliable data and its use for evidence-based policy-making could significantly increase the efficiency of public investment and services.** More analysis needs to be done to understand the relationship between economic growth and job creation, and suggest ways to improve both, yet such analysis for fYR Macedonia is constrained by the scarcity of reliable data, in particular due to an out-of-date census that complicates defining sampling frames for surveys.

***Export, competitiveness and private investment***

33. **Moving to a higher growth trajectory requires continued macroeconomic stability and the development of a competitive export sector in fYR Macedonia.** The country has done well in maintaining macroeconomic stability through a time of global and European crisis, creating a stable environment for investment with low inflation and manageable external balances (see Table 1 in Annex 3). An exchange rate pegged to the Euro has been an important anchor for this stability, but also places the burden of competitiveness on local wages and productivity improvements. In a small open economy like fYR Macedonia, firms must look to export markets for growth. Today, only 5 percent of manufacturing firms in fYR Macedonia export, but this group of firms generates 55 percent of the total sales revenue in the manufacturing sector[21]. The key to accessing export markets is to boost firm productivity in the conditions of a pegged exchange rate as there is a strong relationship between exporting and productivity: exporting firms have six times more revenue per employee than the average firm in fYR Macedonia. Moreover, international evidence suggests that participation in export markets helps to improve firm-level productivity, so that a competitive export sector will translate into a more competitive and dynamic economy.

34. **The Government scaled up export promotion through the adoption of the Export Promotion Strategy and implementation of exporter support programs.** The strategy aims to ensure that appropriate institutional mechanisms are operating at the ministerial and agency levels, and that programs with high potential impact are put in place. The exporter support programs help build the capabilities of those exporters aiming to increase the quality of their products or reach new markets, which could progressively increase fYR Macedonia's share of medium and high-tech exports.

35. **Recent and ongoing analytic work confirms the need to continue and deepen reforms in the area of competitiveness.** In the past several years fYR Macedonia has made

[21] World Bank. 2012. Modular Competitiveness Assessment Making Exports a Catalyst for Economic Growth: An Assessment of fYR Macedonia's Trade Competitiveness. The exporter analysis is based on firm level datasets from the Customs Administration and the Central Registry up to 2010.

significant progress in improving the business climate beyond the "first generation" of reforms often related to the methodology of the Doing Business (DB) Report. The reforms supported by the Business Environment Reform and Institutional Strengthening (BERIS) Project in regulatory impact assessment and regulatory "guillotine" of existing cumbersome and outdated regulations, improved quality infrastructure, competition and innovation policies, among others, are important achievements in improving the business environment. Further, reforms in the governance and efficiency of public spending for private sector and foreign investment were supported by the Competitiveness Development Policy Loans (DPL)[22].

**Box 2: Global Competitiveness Report 2013-2014: The most problematic factors for doing business in fYR Macedonia** (percent of respondents)

| | |
|---|---|
| **Access to financing**…………………………….. | 17.4 |
| **Inadequate supply of infrastructure**…………. | 15.2 |
| **Inadequately educated workforce**……………. | 11.9 |
| Poor work ethic in national labor force……….. | 11.6 |
| Inefficient government bureaucracy……………. | 10.6 |
| Corruption………………………………………. | 8.7 |
| Insufficient capacity to innovate………………... | 5.7 |
| Tax rates………………………………………… | 3.6 |
| Policy instability………………………………... | 3.3 |
| Poor public health………………………………. | 3.2 |
| Tax regulations…………………………………. | 3.1 |
| Restrictive labor regulations……………………. | 1.8 |
| Crime and theft…………………………………. | 1.7 |
| Government instability/coups…………………... | 1.4 |
| Inflation…………………………………………. | 0.4 |
| Foreign currency regulations…………………… | 0.4 |

36. **The Global Competitiveness Report (GCR) 2013-14 ranks fYR Macedonia in the middle of the range (73 out of 148).** The country ranks highest for goods markets efficiency (44) and macroeconomic environment (59), and lowest for market size (109) and business sophistication (100). The report identifies the top three obstacles for doing business in fYR Macedonia as access to financing, infrastructure and skills of the labor force. The Business Environment and Enterprise Performance (BEEPS) 2013 also identifies access to finance among the top three obstacles in the business environment. Closer examination reveals that access to finance and slow credit growth, in particular, are a challenge both on the supply and demand side. Some of the reasons behind this are risk aversion of the banks and firms (particularly micro and small, which are the majority), high and restrictive collateral requirements, lack of bankable projects, and increasing non-performing loans of firms.

37. **Many challenges remain with implementation of business regulations for investment at the municipal and regional levels, due to uneven capacity at lower levels of administration and lack of experience in dealing with foreign companies.** While fYR Macedonia has achieved significant progress in the business environment as measured by Doing Business 2014 (ranked 25 out of 189 countries), it is important to ensure that an efficient environment conducive to investment is in place throughout the country. Recent efforts at decentralization, particularly of the land administration process, create opportunities for local authorities to improve the efficiency of the investment process (land privatization, construction permits and business licenses).

38. **A key part of the Government's competitiveness strategy has been attracting foreign direct investment (FDI) through a package of proactive promotion in key markets, incentives and special economic zones (SEZ) around Skopje, Stip, Tetovo and other cities.** These measures and SEZ infrastructure, which receive high ratings in global comparisons[23],

[22] Competitiveness DPL 1 closed in 2013; Competitiveness DPL2 is active.

[23] Financial Times study *European Cities and Regions for the Future 2014/15* rates several regions in fYR Macedonia among the top ten in nine out of ten categories. Ratings for price efficiency, business cooperation and FDI strategy were particularly favorable.

resulted in increased FDI inflows, especially in medium- and high-tech manufacturing industries. These investments jumped to EUR 78 million in 2013, accounting for net exports of EUR 87 million in 2013 and are expected to be up to EUR 190 million in 2014, with total exports of EUR 1.2 billion. The new FDIs located in and outside the SEZs employed around 5,000 workers in 2013, and this is expected to increase to 9,000 by end 2014. Companies received state aid packages, which include tax incentives and skills training for the employees. They are also developing cooperation with local universities and some of the companies have developed supply linkages with domestic producers of plastic and metal products.

39. **Constraints to linkages with FDI and export competitiveness of domestic firms are related to firm-level productivity, skills, business sophistication, and some aspects of the business environment at the local level.** Business sophistication includes two elements: the quality of a country's overall business networks as measured by the quantity and quality of local suppliers and the extent of their interaction, and the quality of individual firms' operations and strategies. By end 2013, supply linkages between Macedonian companies and foreign investors was estimated at EUR50 million in goods and services (including construction), with potential for increase in the medium and long term. The Government seeks to stimulate partnerships among foreign manufacturing companies operating in fYR Macedonia, local Small and Medium Enterprises (SMEs) and financial institutions by providing assistance to upgrade product quality, quantity and reliability through technical and managerial skills, business planning and access to capital. The increased technological and business sophistication of local suppliers will, in turn, facilitate backward linkages with FDI and stimulate exports. One important element of this support is the Fund for Innovation and Technological Development (Innovation Fund) that was established in 2014 and is receiving funding support from the World Bank.

***Infrastructure - Roads***

40. **Investments in transport infrastructure are crucial for fYR Macedonia's competitiveness and growth.** Inadequate supply of infrastructure is the second most problematic factor for doing business according to GCR 2013. The landlocked country needs investment in transport infrastructure to ensure connection to regional markets, with roads presenting a particular priority since most of the goods in fYR Macedonia, including exports, are transported by road (in the first two quarters of 2013, 93 percent of freight). Roads are also crucial for local competitiveness and development of tourism.

41. **Road construction, rehabilitation and upgrading is the single largest public investment program.** Of the EUR3.5 billion in currently planned public investments, roads account for around EUR1.47 billion, or 42 percent. The World Bank is working with the Ministry of Transport and Communications, and PESR on a new transport sector strategy focused on evidence-based policy-making and investment decision-making, and has a large ongoing and planned program of investment in the sector. Leveraging private sector participation through PPPs, where feasible, could provide additional resources to the sector, including in road management which can also be effected through concessions to the private sector.

42. **The quality of the country's roads has been deteriorating relative to other countries.** According to the GCR fYR Macedonia's road quality ranked 69th world-wide in 2006. By 2013, it ranked only 111th. Key challenge in the road sector relates to the establishing of a road asset management system, which would help PESR plan a financially sustainable road investment program (to complete the main corridor sections and improve overall road condition

worsened due to maintenance backlog), while safeguarding its financial sustainability. Additional efforts are also required to improve the quality and timeliness of maintenance in order to ensure longevity of investments carried out.

43. **Road safety remains a concern despite recent efforts to address it.** The National Council for Road Safety, which brings together all national authorities related to road safety, has provided greater visibility to the issue of road safety. There are over 4,000 car crashes per year in fYR Macedonia resulting in injuries or deaths of around 7,000 people. While the leading reported cause of these is driver behavior, international experience suggests that accidents could be significantly reduced through improvements in road infrastructure, better traffic signs and road markings and features such as crash barriers.

44. **FYR Macedonia's transport infrastructure is highly vulnerable to climate change.** With investments whose life span often exceeds 20 years, a failure to consider climate proofing could lead to costly repairs and rehabilitation. Through its extensive investments in the sector, fYR Macedonia has a unique opportunity to ensure that investments made today are not adversely affected ten years down the line, due to the failure to consider factors such as increased flooding or increased precipitation. At the same time, making transport infrastructure resilient requires assessing the need to incorporate adaptation measures, whether they be for infrastructure design or maintenance, where warranted.

***Infrastructure - Energy***

45. **Availability of adequate energy supply is a major constraint to fYR Macedonia's growth**. Although overall energy consumption remains low by European standards, energy intensity is high and presents opportunities for increased energy efficiency measures. FYR Macedonia's main primary energy resource is lignite, but the available lignite deposits will be fully exploited within the next 30-45 years. Thermal power plants, mostly lignite-burning, generate most (79.7 percent) of the country's electricity. Hydropower is the second largest energy source, accounting for 17.2 percent of electricity generation, with the remaining 3.2 percent supplied by imports[24].

46. **With about half of fYR Macedonia's generation capacity scheduled to close in the next 15 years, combined with an increasing electricity demand, the country is facing the issue of security of supply**. Electricity demand has exceeded supply for a decade and the gap has been filled with power imports at a price well above domestic costs. Investments in energy efficiency and loss reduction, as well as development of new clean energy sources (particularly hydro power) and improved connectivity with the regional energy grid are essential to ensure adequate energy supply for future growth. A review of investment options carried out by the World Bank at the request of the Government of fYR Macedonia has demonstrated that energy efficiency measures provide the least cost option to bridging the supply/ demand gap. Specific energy efficiency measures focused on lighting and electric appliances in households and non-residential buildings, and aggressive reduction of distribution losses, could each deliver an impact similar to half of all existing hydropower, at a cost much lower than any power plant.

[24] 2010 data

*Agriculture*

47. **Agriculture in fYR Macedonia is not only a significant contributor to GDP, but also a major employer and contributor to foreign trade and public and private consumption.** In economic terms, it is the third largest sector after services and industry. Agricultural contribution to GDP was 11.1 percent in 2011, which is significantly higher than the ECA average. When agro-processing is included, contribution to GDP increases to 16 percent. Exports of agricultural products, in particular high value-added products such as wine, lamb, fruits and vegetables, constitute 15-17 percent of the country's total exports. In social terms, the share of employment in agriculture is 20 percent, which is twice the ECA average. With respect to the environment, agriculture uses around 43 percent of total freshwater withdrawals, which is less than the average use in the ECA region. Official statistics, however, capture only a portion of the role of agriculture, as informal and traditional transactions are rarely recorded. For example, almost half of all agricultural workers are unpaid as they are members of agricultural households. In addition, products are often sold at traditional markets, and water withdrawals for irrigation are often unrecorded.

48. **Despite its overall importance for fYR Macedonia's economy, the sector is fragmented, poorly equipped and with obsolete technology with negative implications not only for growth but also for shared prosperity,** since rural population is overrepresented in the bottom 40 percent. The fragmented production and lack of mechanization makes it difficult for farmers to achieve economies of scale in production and produce the quantities required for certain markets, constraining agricultural growth. A more efficient allocation of agricultural subsidies, which account for 2.1 percent of GDP and predominantly support recurrent output, could be a powerful tool for the sector's greater competitiveness. For example, spending more resources on irrigation will be critical to increase production of high-value added crops. Progress on land consolidation and development of a functioning land market would also be important to make the sector more productive. Institutional bottlenecks inhibit the functioning of the agricultural land market and refusal of banks to accept agricultural land as collateral have significantly constrained productivity.

49. **FYR Macedonia is making progress on addressing some of the sector's challenges**. The Bank has been supporting reforms in the agriculture sector through analytic and advisory activities as well as through lending, such as the recently closed Agriculture Strengthening and Accession Project and the Competitiveness DPL series. In particular, the Government is advancing on creating conditions for more efficient land use with the enactment of the Law for the Sale of State-Owned Agriculture Land in mid-2013 and subsequent implementation of the first Annual Program for the Sale of State-Owned Agricultural Land. The sale of state-owned agricultural land could have a major impact on agricultural productivity and generate up to EUR 500 million in fiscal revenues over the coming years. The Government has asked the Bank to target this crucial issue through its program and it has chosen to work with other development partners, in particular the EU on other challenges in agriculture.

50. **Agriculture is also the economic sector most directly harmed by a changing climate.** Both water scarcity and water demand for irrigation are predicted to rise. Irrigation is already insufficient and poorly designed for today's small farms. Many farms depend on local wells and unsustainable extracted groundwater, which is neither regulated nor priced. Soil fertility problems will worsen with a changing climate, especially erosion.

*Water*

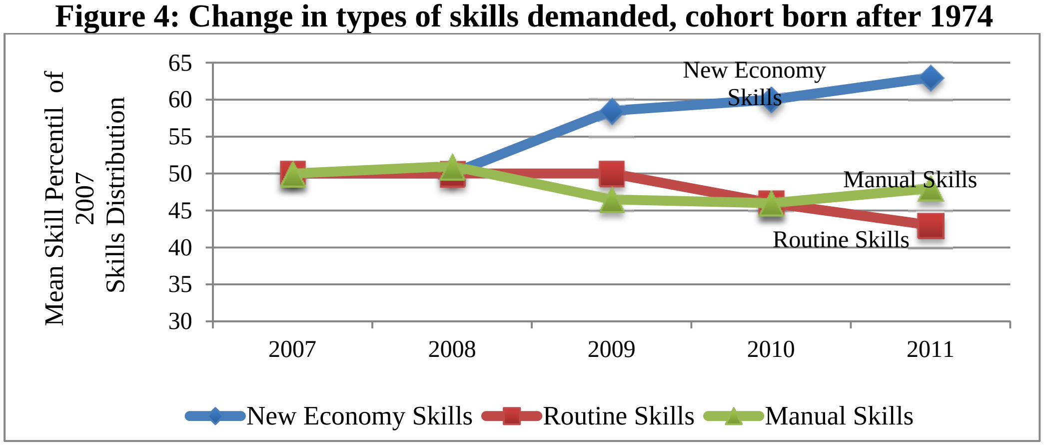
51. **FYR Macedonia's surface and groundwater resources support municipal, industrial, power sector, and agricultural uses, with the agricultural irrigation sector accounting for 43 percent of annual withdrawals**. In addition to these water-using sectors of the economy, fYR Macedonia's mountainous landscape has long supported hydropower generation, which remains an important though not the dominant source for electric power. Most of the country's water resources are generated internally, through rainfall, and are somewhat more heavily concentrated in the western portion of the country – most of the hydropower infrastructure is also located in western Macedonia.

52. **The water sector is already experiencing the effects of climate change, and these are likely to increase in the future.** As the climate warms and dries, competition for water between agriculture, the power sector (for hydropower, a critical element in a lower emissions electricity system, and for thermal cooling), and industrial and municipal uses will pose difficult tradeoffs for Macedonian policymakers by 2020 unless efficiency in both demand and supply is bolstered. The growing scarcity of water can be addressed, first of all, by reducing inefficiencies through pricing and regulation of groundwater and through rehabilitation and maintenance of existing infrastructure. Growing seasonal scarcity can be managed through investment in more storage (for irrigation and for hydropower), while overall shortages in future decades can be addressed through encouragement of water conservation.

**Challenge: Opportunities for all through modern skills and better public services**

***Employment access and skills***

**Figure 4: Change in types of skills demanded, cohort born after 1974**




*Source*: World Bank "Back to Work: Growing with Jobs in Europe and Central Asia", based on LFS.
*Note*: The y-axis plots the percentile of each skill distribution for each year and cohort with respect to the respective median in the initial year.

53. **Improving the country's labor market performance and economic competitiveness – key paths to reducing poverty and promoting shared prosperity - will require a more skilled and better educated labor force and a reduction in barriers to employment.** Lack of skills has been identified as a critical constraint to fYR Macedonia's competitiveness[25], and it is

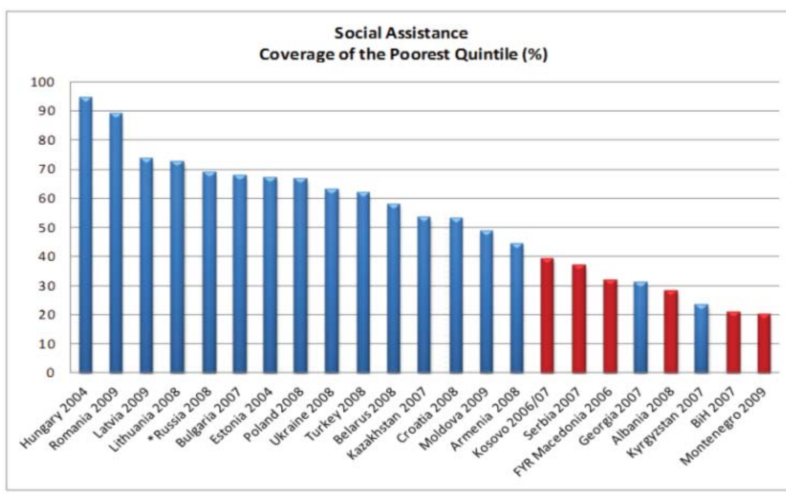
[25] World Bank. May 2012. *Unlocking Macedonia's Competitiveness Potential: A Sectoral Assessment of the Constraints and Opportunities in Automotive, Apparel, Agribusiness, and Logistic Services.*

also consistently mentioned as a key constraint in GCR and BEEPS. While access to education has improved, challenges remain in the provision of integrative "new economy" skills, and in better linking the products of the education system to private sector needs, as companies complain about the quality and availability of skills despite high unemployment. The secondary Vocational Education and Training (VET) and higher education systems emphasize traditional cognitive skills, and in the case of secondary VET, focus is on narrowly-defined occupational profiles with low vertical and horizontal flexibility[26]. Yet, as Figure 4 shows, the demand for skills has been moving away from routine, cognitive activities towards "new economy" skills that include non-routine cognitive (critical thinking and problem-solving) and non-cognitive skills (interpersonal skills, team work, work ethic, grit). Firm surveys in fYR Macedonia also show that firms place equal value on cognitive and non-cognitive skills, and that the latter are particularly lacking[27]. Additional barriers to employment exist for young workers and for women, including access to productive inputs.

***Protecting the vulnerable***

54. **Providing better protection to vulnerable households and enhanced access to public services for the less well-off are necessary for achieving the twin goals in fYR Macedonia**. The social assistance system is complex and performs reasonably well by regional standards, but suffers from both inclusion and exclusion errors. The coverage of social assistance in fYR Macedonia is low at 5.7 percent of the total population, and only 31 percent of the poorest consumption quintile receive any social assistance benefit. The last-resort Social Assistance Program (SFA) also covers around 30 percent of the bottom quintile. The level of benefit may be insufficient to help the vulnerable escape poverty. The World Bank report on the Social Safety Nets in Western Balkans (2011) finds that the generosity[28] of fYR Macedonia's social assistance is low compared to other Western Balkan countries:

**Figure 5: Coverage of Social Assistance in the Western Balkans**




*Source:* Europe and Central Asia Social Protection Database, World Bank

[26] *FYR Macedonia SABER Workforce Development analysis* (forthcoming).
[27] World Bank. 2010. *FYR Macedonia Skills Demand Survey*, Washington, DC.

social assistance transfers account for only about 24 percent of total consumption. The last resort social assistance programs are modest and the share of the transfer in post-transfer consumption of the poorest quintile is around 25 percent.

55. **The Ministry of Labor and Social Policy is working on reforms to improve the system's efficiency and effectiveness**. A new Law on Social Protection was introduced in 2009 streamlining the procedures regulating the social protection system, and allowed for a rapid response of the system to emerging priorities. This allowed the authorities to increase targeted support in the form of energy poverty programs and conditional cash transfers in education. An important next step was achieved with the adoption of the bylaws which introduced a comprehensive definition of countable income for social assistance purposes.

56. **While the system could help mitigate adverse social impacts during an economic downturn, further improvements are needed**. The efforts now should be directed at improvements of benefits targeting as well as coverage of the poorest quintile, changes of the equivalence scales and consolidation of social assistance benefits. Possible reform options will be underpinned by findings and recommendations of the ongoing functional analysis of the Social Welfare Centers (SWCs) and upcoming assessment of targeting, eligibility and registry systems, financed by the Conditional Cash Transfers (CCT) Project. The CCT Project also helps to reduce the inter-generational transmission of poverty by linking benefits to the fulfillment of standards for secondary school enrollment and attendance and by activating youth in families benefiting from the SFA in order to help them make the transition into the labor market.

### *Closing the gap on basic services*

57. **Access to basic infrastructure services, in particular in rural areas of fYR Macedonia, is uneven, and serious gaps persist**. This has a negative impact on the competitiveness and economic growth as well as on the welfare of the bottom 40 percent, who predominantly live in rural areas. The main problems are related to water supply and sewerage, electricity networks, and access roads. The local road network is underdeveloped and of low quality. Around 50 percent of local roads are dirt roads, and their maintenance is a problem. Only 72 percent of rural population have access to a public water pipeline, compared to 88 percent for the whole population, and 9 percent of rural residents have no water access. Most villages do not have sewerage systems and use septic tanks; uncontrolled wastewater discharge into rivers is common. Finding appropriate and innovative low cost solutions for rural areas for the collection and treatment of sewage (and whenever possible the reuse of the treated effluent) is needed. In addition, only 10 percent of the rural population is covered by public municipal collection of solid waste. Development of infrastructure for waste collection in rural areas is also important for preservation of the environment.

## II. GOVERNMENT'S VISION

58. **The Government of fYR Macedonia has a clear vision of development, which is based on the goal of economic growth through increased competitiveness, to be achieved through improvements in business climate, infrastructure and human capital.** This vision

[28] The generosity (or adequacy) of social assistance is the share of benefits in total post-transfer consumption.

is presented in the Pre-Accession Economic Program 2014-2016 and is consistent with the regional SEE 2020 Strategy[29], which fYR Macedonia officially adopted.

59. **The Government's economic program for the period of 2014 to 2018 has a strong focus on growth, competitiveness and human capital development as the basis for improving the welfare of the citizens.** This program was part of the election platform of the recently reelected Government and is summarized in Box 3.

| **Box 3: Government Strategic Priorities, 2014-2018** |
| --- |
| • Faster economic growth and employment, better living standard for the citizens<br>• EU and North Atlantic Treaty Organization (NATO) integration<br>• Fight against corruption and efficient law enforcement<br>• Maintaining good inter-ethnic relations based on the principles of mutual tolerance and respect and equal treatment in accordance with the law<br>• Investment in education, innovation and information technology as key elements for creating knowledge-based society |
| *Pillar 1.* ***Improving the living standards of the citizens through:*** new private sector jobs through further improvement of doing business conditions for domestic and foreign investors; opening new markets and increasing trade; supporting SMEs through further reduction of administrative procedures and facilitating access to credits; supporting tourism development; active labor market policies with special emphasis on youth; improving the road and utility infrastructure; better health and education services; supporting companies' capacity to invest in new technologies, innovation and research; environmental protection. |
| *Pillar 2.* ***Infrastructure development through:*** construction of new national, regional and local roads and their rehabilitation; construction and modernization of railway corridors and strengthening transport capacity; construction of energy capacity, including renewable energy; construction of water supply and wastewater systems; investment in ICT to increase the quality of public services, improving digital literacy, access and inclusiveness. |
| *Pillar 3.* ***Protection of the most vulnerable through:*** employment promotion programs and stimulations for private sector; better social assistance; better access to health and education services; protection from energy poverty. |
| *Pillar 4.* ***Development of agricultural production and improving farmers' quality of life through:*** subsidies in agriculture; policies on efficient allocation of agricultural land and privatization of state agricultural land; better access to financing for primary production and processing of agricultural products; assistance in promotion of agricultural products; new investments in agro-processing; rural development. |
| *Pillar 5.* ***Improving education through:*** investment in education infrastructure; investment in science and connecting universities with private business for developing and commercializing innovation; improving the quality of educational programs and their relevance for private sector needs; teacher training. |
| *Pillar 6.* ***Improving the quality of health services:*** construction of new hospitals and investment in equipment and training for its use; continued education of health workers; improving service quality. |
| *Pillar 7.* ***Reform in public administration***: transparent and efficient work of the Government and public administration, strengthening the capacities and promotion of human resources management system. |
| *Pillar 8.* ***EU and NATO integration***: continuing judiciary and public administration reforms; fulfilling the European Union political criteria; further economic reforms according to the EU standards on functioning market economy; further reforms on competitiveness; maintaining full compliance with Stabilization and Association Agreement. |

[29] EU project. August 2013. *South East Europe 2020: Jobs and Prosperity in a European Perspective.*

## III. WORLD BANK GROUP PARTNERSHIP STRATEGY

### A. World Bank Group Country Engagement Model

60. **The WBG country engagement model in fYR Macedonia is determined by selectivity based on alignment with client priorities, coordination with other development partners, extensive analytic work and careful evaluation of areas where the Bank can bring most value added**. The Government has expressed a clear preference for WBG involvement in three areas: competitiveness, infrastructure investments (particularly energy and transport), and support for EU integration. Engagement in these areas is consistent with the views and programs of other development partners, and opportunities exist for greater coordination and mutual leveraging of support efforts. Selectivity also means that there are important development challenges where the WBG does not foresee an active engagement, most notably in agriculture, where the Government is working closely with the EC, although the Bank will continue providing analytic and advisory support in the area of agricultural land market development as part of competitiveness work. IFC will seek opportunities to support private investments in the agribusiness sector through banking sector as well as advisory services.

61. **The Bank's engagement is guided by the WBG's twin goals of reducing poverty and boosting shared prosperity in a sustainable manner.** Poverty and shared prosperity analysis informs both the choice of specific operations and their design and implementation. The country team is also implementing a social filter, a tool for project teams to maximize the social impact of Bank finance operations, to further strengthen the alignment of the World Bank portfolio with the twin goals.

***Lessons from the previous CPS***

62. **As described in the attached fYR Macedonia FY11-14 Country Partnership Strategy Completion Report (see Annex 2), the previous CPS was largely successful**. The objective of the FY11-14 CPS was to support faster, more inclusive and greener growth while helping the country to prepare for EU accession. The CPS focused Bank Group support in three areas of engagement: (i) faster growth – competitiveness; (ii) more inclusive growth – employability and social protection and (iii) greener growth – environmental sustainability and climate action. During the CPS period the World Bank committed US$534.4 million, of which US$98 million was Investment Project Financing, US$100 million Development Policy Lending and US$336.4 million Policy Based Guarantees. IFC invested US$63.3 million: US$23.7 million in the financial sector, US$35 million in manufacturing and US$4.6 million in energy. In addition, IFC facilitated MIGA to issue a guarantee of US$143.9 million to the National Bank of Greece (NBG) for covering the risk of expropriation of funds for mandatory reserves held by Stopanska Banka, the NBG's subsidiary in the fYR Macedonia.

63. **The strategy was well aligned with client priorities and most operations achieved their intended development objectives, but the focus on inclusion could have been strengthened**. The CPS was weighed towards Competitiveness and Greener Growth Pillars (13 and 10 outcome clusters respectively) and had fewer outcomes under the Inclusiveness Pillar (2 outcome clusters). Out of 29 CPS outcomes, 20 were Achieved, further seven were Mostly Achieved, one Not Achieved and one Not Verified. The Inclusiveness Pillar had a relatively lower percentage of fully achieved outcomes than the Competitiveness and Greener Growth

Pillars. The Bank program was appropriately selective, but the CPS results framework was deemed too complex and not used by the Bank as a practical monitoring tool.

64. **The CPS was based on a partnership between the World Bank and IFC, which resulted in a joint Business Plan for fYR Macedonia**. IFC has worked with the private sector supporting the Government's growth and competitiveness agenda. In the future, greater effort needs to be made to involve MIGA in the WBG program in fYR Macedonia. The WBG tailored its support in response to changing circumstances. Just-in-time aid was effective in dealing with the new challenges and provided timely support to the Government while also ensuring that most outcomes were achieved. The Bank has been able to offer high-quality development solutions to the Government while preparing new lending operations in response to changed circumstances within 6 to 12 months. The Government's commitment is crucial for IFC's success with public-private partnership transactions.

***Lessons from the Country Portfolio Performance Review***

65. **The portfolio of World Bank financed operations in fYR Macedonia[30] consists of six investment projects, with total commitment of US$299.4 million, out of which 44 percent (US$132.5 million) remains undisbursed**. The latest Country Portfolio Performance Review (CPPR) held in November, 2013 concluded that project objectives and associated results frameworks remain relevant, and projects are making good progress towards these objectives. Other key messages coming out of the CPPR were as follows:

- **Working relationship between the Government and the Bank is strong**. All implementing agencies are willing to continue with new operations.
- **Implementing agencies have sufficient capacity to implement the projects successfully**. Although a small number of implementation bottlenecks have been identified, by and large project implementation mechanisms are working. All Bank financed operations include capacity building to further improve implementation.
- **Focusing on a smaller number of operations makes sense given a constrained lending envelope.** Over the last few years the Bank has reduced the number of active projects, from 15 in 2009 to six in 2014. Focusing on a small number of operations allows the Government to use Bank resources more strategically. Selectivity should continue to guide Bank engagement in fYR Macedonia.
- **Investment needs in fYR Macedonia remain large.** To meet these needs, the WBG should work with other development partners, through coordinating strategies and joining efforts where appropriate, as well as through using capacity building activities under Bank financed operations to improve fYR Macedonia's access to other funds, most notably IPA.

***Results of the consultations process and client survey***

66. **Public consultations across a broad spectrum of stakeholders in fYR Macedonia demonstrated strong support for the objectives and scope of the proposed strategy.** As described in Box 4, there is consensus that CPS areas of focus fit well with the country's central goals of reducing poverty and unemployment. Key recommendations emerging from the

[30] Country Portfolio Performance Review covered only IBRD-financed operations. In addition, IFC has disbursed outstanding loans for US$59.7 million and equity for US$7.42 million. MIGA has two active guarantees in fYR Macedonia for the total amount of US$143.9 million.

consultation process and reflected in the proposed strategy were that a stronger emphasis should be put on the most vulnerable groups – women, long-term unemployed and youth, and that the Bank should play a more active role in building in-country capacity for a more efficient use of EU's pre-accession financing, particularly in the area of environment.

**Box 4: CPS Consultations**

The World Bank and IFC Country Offices held joint public consultations on the new Country Partnership Strategy (CPS) with the following groups: government officials in key sectors, donors and development partners, representatives of Parliamentary Commissions across the political spectrum, academia and Non-Government Organizations (NGOs), and representatives of the private sector. Consultations took place in the World Bank Office and in the Macedonian Parliament between December 17, 2013 and February 20, 2014. All groups of stakeholders expressed strong support to the objectives and scope of the proposed new Strategy, and welcomed the opportunity to be involved in its discussion. There was general consensus that the Strategy's main themes of growth and competitiveness, and skills and inclusion are central to fYR Macedonia's objectives of reducing poverty and unemployment. In this respect the focus on jobs, employability and inclusion found a particularly enthusiastic support, and several discussants asked that special emphasis be put on the most vulnerable groups – women, long-term unemployed and youth. The new Government's Jobs Strategy being prepared with support from the World Bank Group will address this concern, as will the Skills Development and Innovation Support Project.

World Bank's activities in fYR Macedonia are seen as both pertinent and successful, and participants in the consultations expressed their appreciation of the knowledge and implementation support provided as part of World Bank operations, as well as financing. Participants made suggestions for sectors that could be added to the future World Bank program, such as agriculture. The insufficient use of the IPA funds across all sectors has been repeatedly underlined by participants, lending support to the Strategy's cross-cutting theme of EU accession. The situation is especially serious in the environment sector. Private sector participants identified several areas where they would welcome greater WBG involvement, including: (1) export promotion, including practical advice to companies wishing to access export markets; (2) education and skills, including through a stronger link between the education system and private sector employers; (3) infrastructure, in particular investment in new and better roads; (4) innovation and quality improvement for better export opportunities; (5) access to finance for SMEs; (6) strengthening backward linkages/supplier development for FDI; and (7) deeper reforms in business environment, including a focus on predictable enforcement and implementation of the laws and rules and creating a level playing field between domestic and foreign investors, and more business-friendly and flexible labor regulations (e.g. part-time and home based work).

67. **A Client Survey, conducted as part of CPS preparation, finds that the WBG has a positive image in fYR Macedonia.** Respondents praised the pragmatic in-country engagement in several sectors as well as the relevance of the Bank's program and its alignment with country needs. The Bank engagement is seen as particularly relevant in areas such as economic growth, agriculture and climate change. In contrast, Bank's achievements in the area of job creation/employment received one of the lowest scores. With regard to the operations of the Bank on the ground, opinions are very positive in regards to disbursement and speed of decision-making. The Bank is perceived as 'being a long term partner' to fYR Macedonia, its responsiveness and collaboration with the Government and other development partners are highly valued. Views about Bank's collaboration with groups outside the government are also positive but significantly lower than other ratings.

68. **The survey recommends that the Bank should reach out to broader groups outside main government counterparts**, and to make a greater effort to publicize the information that the Bank produces. Recommendations for future WBG activities focus on growth (with jobs and broad inclusion) and EU accession, which are seen as top development priorities. Respondents

have a positive view of the quality and relevance of the WBG knowledge work, but translation, dissemination and stakeholder involvement could be improved.

***Lessons from recent diagnostic* work**

69. **The WBG's strategy in fYR Macedonia is shaped by regular analytic reports as well as just-in-time analysis and advisory activities**. *South East Europe Regular Economic Reports* provide a vehicle through which the Bank engages with the authorities and the public on key economic issues in the country. Dialogue and lending in the area of competitiveness draw on *Making Exports a Catalyst for Economic Growth: An Assessment of fYR Macedonia's Trade Competitiveness (2012)* and *Unlocking Macedonia's Competitiveness Potential: A Sectoral Assessment of the Constraints and Opportunities in Automotive, Apparel, Agribusiness, and Logistic Services (2012),* which focused on export sectors and sectors with strong employment and growth potential, such as agribusiness, automotive, apparel, trade logistics, and tourism. Binding constraints were identified in the low-value content of the export basket and in inefficiencies of the factor markets: skills mismatch, labor market flexibility issues, and access to land for productive investment. The studies informed the choice and design of ongoing and planned operations on competitiveness, skills and innovation. As part of the Modular Competitiveness Assessment, the assessment of tourism competitiveness (*From World Heritage to World Destination: Policy Options to Increase the Competitiveness of the Tourism Sector in fYR Macedonia, 2012*) identified the challenges, priorities and strategic directions for Macedonia's tourism sector as a key contributor to local economic development. *Analysis of the Agricultural Support Programs* (2013) explored options for better allocation of agricultural subsidies and improved functioning of the agricultural land markets. These topics will inform further work under the ongoing Public Financial Management Review and Competitiveness DPL series. *Green Growth* reports (2013-14) propose "no regret" measures to shift fYR Macedonia's growth model onto a greener trajectory, most notably greater energy efficiency and use of renewable energy, more water storage and efficient use of water, improving climate resilience of infrastructure and encouraging the use of public transport. These findings underpin recent and planned WBG operations in energy and transport sectors. Analysis of poverty and inclusion was carried out as part of the ongoing *Western Balkans Programmatic Poverty Assessment* technical assistance as well as the recently completed Special Topic Regular Economic Report *First Insights into Promoting Shared Prosperity in South East Europe* (2014). Results of this work are presented in the analytical part of this Strategy and are informing the country dialogue on inclusion and skills. The recent *Labor Market Assessment* (2013), which was carried out as part the *Western Balkan Programmatic Jobs and Labor Market*s work in support of a new jobs strategy for fYR Macedonia, has informed the ongoing country dialogue as well as the design of the Skills and Innovation Project. Finally, the gender assessment carried out under the *Western Balkans Programmatic Gender Task* has contributed to highlighting remaining gender-related challenges in the country.

## B. Translating Country Challenges into World Bank Group Partnership Strategy

70. **The overarching country-level goals of the proposed CPS are reducing poverty and providing more and better jobs for the people of fYR Macedonia for boosting shared prosperity.** Based on our current understanding of the drivers of shared prosperity in fYR Macedonia, a tangible shift in this agenda will require faster growth with more job creation. Two pillars will support these goals: **(1) Growth and Competitiveness, and (2) Skills and**

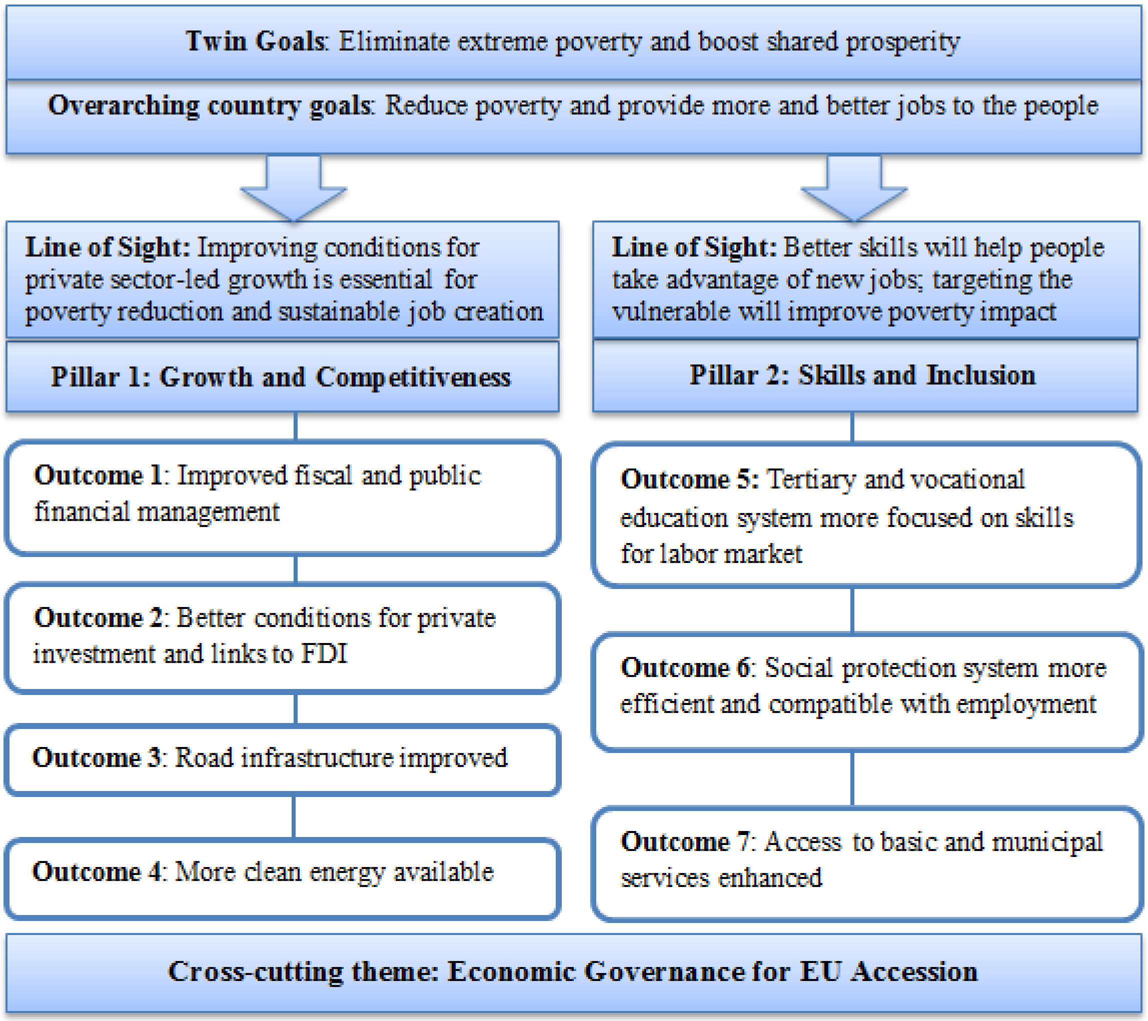
**Inclusion**. Competitiveness through investment in crucial infrastructure while generating an environment that attracts FDI and enables local businesses to thrive will be necessary for putting fYR Macedonia on a sustainable growth path, creating more and better jobs, and promoting shared prosperity. It is however unlikely to be sufficient. Policies to improve educational outcomes and other public services and to remove labor market constraints will be needed to make sure that a large part of the population reaps the benefits of sustained growth. The WBG will offer a full range of financial, knowledge and convening services in support of these goals, providing assistance in several sectors and leveraging Group-wide resources to catalyze impact. Since fYR Macedonia's long-term future is clearly linked to European integration, the strategy will also have a **cross-cutting theme of supporting EU accession**. No separate operation is planned in this area; instead, all Bank Group activities will be aligned with the accession agenda and seek to support it.

71. **The two pillars fit well with the World Bank Group's strategic goals**. Successful poverty reduction and increased shared prosperity would be hard to achieve without sustained private sector led growth, and this in turn implies the need to make fYR Macedonia more attractive as a destination for investment and as a country whose companies can compete regionally and globally, creating jobs for the people. On the other hand, investment in skills and ensuring that vulnerable groups have the necessary protection and equal access to economic opportunities is necessary in order to improve the welfare of the bottom 40 percent of the income distribution. Strengthening of governance, transparency and accountability across the board will be needed both to enhance the investment climate and ensure that all citizens can take advantage of economic opportunities.

72. **Growth with competitiveness, skills and inclusion are also key priorities of the Government's vision of development**. FYR Macedonia's key development strategies, including the *Pre-Accession Economic Programme 2014-2016*, *Government Strategic Priorities 2014-2018*, the *National Strategy for Reduction of Poverty and Social Exclusion in the Republic of Macedonia for 2010-2020* and *South East Europe 2020 Strategy* set out specific targets in these thematic areas. Bank Group assistance will contribute to attaining these objectives.

73. **The theme of economic governance for EU accession will cut across all World Bank Group activities in fYR Macedonia**. ***At the strategy level, the proposed CPS is consistent with the new EU Assistance Country Strategy Paper for 2014-2020***, which proposes assistance in eight areas: governance and public administration reform; justice, home affairs and fundamental rights; environment; transport; competitiveness and innovation; employment, social policies and human resources development; agriculture and rural development; and cross-border and regional cooperation. Competitiveness, jobs and inclusion are therefore also seen as important for EU accession. The specific targets related to closing the gap with the EU as defined in the SEE 2020 Strategy will inform the results framework of the CPS and, where appropriate, of specific operations. ***At the project level***, the WBG will coordinate project design and implementation with the EU in order to maximize synergies and use the capacity building opportunities of World Bank-financed operations to support fYR Macedonia's ability to use IPA funds more efficiently. Finally, the Bank will explore ***opportunities for joint projects with the EU*** and other development partners in order to minimize transaction costs and increase the impact of combined resources available to fYR Macedonia.

**Figure 6: FYR Macedonia CPS FY2015-18: Results Framework**




**Pillar 1: Growth and Competitiveness**

**Challenge: Job creation through faster growth and better competitiveness**

***Fiscal and public financial management***

74. **As described in the diagnostic section of this document, reliance on public investment to drive growth in fYR Macedonia puts special emphasis on the quality and efficiency of public financial management.** FYR Macedonia has both the capacity and track record of prudent macroeconomic management, which has been a key ingredient in the country's past growth. Continued macro sustainability will require continuous ***improvements in fiscal and public financial management***. The Government has announced a program of fiscal consolidation and plans to stabilize central government debt, which are essential for the medium-term stability and which imply a gradual ***reduction in the level of fiscal deficit***. Fulfilling these plans will be challenging in light of the large ongoing and planned public investment program. Greater public transparency, and in particular ***publication of quarterly reports on public and publicly guaranteed debt*** can help maintain the resolve behind fiscal consolidation effort as well

as build trust for new private investment. Strengthening governance and transparency will also be critical for fYR Macedonia's EU accession dialogue. The Bank will contribute to this agenda through the ongoing PFR as well as through Development Policy Lending based on the findings and recommendations of that review. Through its engagement with the Public Enterprise for State Roads, the Bank will also continue to support ***capacity for evidence-based investment decisions*** in the largest public investment program. The WBG will also encourage and support the Government in attracting more private sector investments in infrastructure sectors, as a way of reducing the burden on the budget.

**Outcome 1: Improved fiscal and public financial management**

**Proposed WBG program**: Public Finance Review; Regional and Local Roads Project (ongoing); Public Finance DPL; National and Regional Road Rehabilitation Project; Road Upgrading Project; Growth and Shared Prosperity Diagnostic (planned).

***Export, competitiveness and private investment***

75. **Further improvements in the business climate, attracting private investment and improved export potential are essential in order to achieve sustained private sector led growth and job creation.** As described in the diagnostic section, fYR Macedonia has made important strides in this area already – the country has been recognized as one of the top ten reformers globally in the latest Doing Business Report – but many challenges remain, especially in terms of effective implementation of reforms and further capacity building that would be translated into higher investment and more and better jobs for the Macedonian population. Access to finance for SMEs and implementation of local business-related regulation (for example, issuing construction permits) are among key doing business concerns that companies cite. IFC and the World Bank will continue supporting this agenda through a series of knowledge and financing activities, including just-in-time advisory and technical assistance and lending. IFC will focus on making more financing available to SMEs through credit lines with commercial banks. It is important to note that access to finance is as much a question of effective demand by SMEs as it is a question of liquidity, and the Bank will help address this demand-side challenge through its work on local business sophistication and skills as part of the ongoing fYR Macedonia Competitive Industries and Innovation Support Program and Development Policy Lending. In the short run however this means that IFC's financing may be limited by lack of viable credit demand, excess liquidity in commercial banks and often their cheap parent funding, as well as the availability of subsidized funding and grants provided by other IFIs especially on renewable energy, energy efficiency and SME segments, which further distorts the market. IFC is also considering engagement with non-performing loans (NPL) workouts by helping banks to strengthen capital and offload NPLs, depending on the country's appetite for these market solutions. MIGA will provide guarantees to foreign parent banks to increase the availability of resources to their Macedonian subsidiaries[31]. There are also promising trends in FDI flows to fYR Macedonia, yet the country's ability to extract full growth

[31] MIGA has two active guarantees aimed to improve the capacity of Macedonian subsidiaries of foreign banks to provide credits to local businesses. The first of these is the guarantee to ProCredit Holding (Germany) in the amount of US$12.5 million approved in December 2010 and valid for ten years. The second was approved in March 2014 and covers €104.5 million (US$143.9 million equivalent) of investments by the National Bank of Greece into its Macedonian subsidiary, Stopanska Banka.

and employment potential of these is limited by the level of local business sophistication and innovation, which reduces backward linkages between FDI and the local economy. IFC will look for opportunities to attract and support FDIs and through them to help the country become more competitive and increase the technological intensity of its exports. IFC will also continue to support business environment in fYR Macedonia through the Westerns Balkans regional advisory services platforms in the areas of trade logistics, corporate governance and food safety. The recently approved Skills and Innovation Project will provide incentives for commercial innovation activities through the Innovation Fund, which is starting operations in 2014.

**Outcome 2: Better conditions for private investment and links to FDI**

**Proposed WBG program:** IFC investments (ongoing and planned); MIGA guarantees (ongoing and planned); TA on competitiveness (ongoing); Competitiveness DPL3; Growth and Shared Prosperity Diagnostic (planned).

### *Infrastructure - Roads*

76. **Better road infrastructure is key to overcoming the disadvantages of a small landlocked economy and is the Government's top priority.** As discussed above, the quality of fYR Macedonia's roads has been deteriorating relative to its neighbors: once a regional leader with respect to road quality, it now has the second lowest road quality among the South East Europe (SEE) countries. The Government has an ambitious program of investments in the sector, and World Bank involvement in the design and implementation of this program can not only bring the needed financial resources but ***also strengthen its quality***, including in areas such as road safety, climate resilience and improved capacity for evidence-based investment choices. In the transport sector, the World Bank will provide implementation support to the Local and Regional Roads Project and prepare two further operations to support road rehabilitation and upgrading. A key component of this work will be continued improvement of the financial viability and public resource management in the transport sector. Depending on the level of the Government's interest and commitment, IFC will provide advisory services to the Public Enterprise for State Roads, possibly supporting ***Public-Private Partnerships (PPPs)*** in the sector. If conditions allow for other PPPs in the infrastructure sectors, IFC stands ready to support the country with advisory and financing of high-impact projects that can make significant contributions to growth and employment.

77. **Through its engagement in the road sector of fYR Macedonia, the Bank is helping the Government to integrate road safety considerations into the entire program** through binding infrastructure safety management measures for contractors and road authorities in all stages of planning and execution; improving security standards on road-railways crossings; eliminating black spots; efficient road maintenance; and ensuring visibility on the roads by eliminating physical obstacles. Additionally, to ensure a focus on road safety in the management of the road network the Bank is working with PESR on introducing road safety impact assessments, road safety audits, network safety management and safety inspections by competent authorities. The Bank will also work with the Government on a Road Safety Management Capacity Review to identify recommendations for all institutions to improve the discharge of their responsibilities in road safety.

78. **Gender and inclusion aspects will be mainstreamed into transport investment** through a focus on: (1) ensuring equal participation of men and women in decision-making process, (2) providing equal access to economic opportunities, and (3) measuring impact on specific groups. Poverty and Social Impact Analysis will be conducted to assess the poverty and inclusion impact of road rehabilitation activities and to build government capacity to streamline poverty reduction consideration into investment planning. This analysis will assess the distributional effect of improved road connectivity on the affected population with a particular focus on women as one of the vulnerable groups. Equal employment opportunities in road construction will be promoted by raising gender awareness of construction companies. Improvement of the condition of the selected regional roads will improve public transport service and increase connectivity between urban and rural areas, thus improving access to jobs and markets for the less well-off. As women typically use public transport to a greater extent than men, it is expected that road rehabilitation activities are especially beneficial to women.

**Outcome 3: Road infrastructure management improved**

**Proposed WBG program:** Regional and Local Roads (ongoing), Regional Roads Rehabilitation (planned), Road Upgrading (planned); Upgrade to Regional Balkans Transport Infrastructure Study (REBIS) (planned); IFC advisory on PPP (planned)**.**

***Infrastructure – Energy***

79. **FYR Macedonia is facing a challenge of ensuring adequate energy supply for growth**. The country ranks among the most energy-intensive economies in the Balkans due to a combination of energy-intensive local industries (iron and steel, ore extraction, cement), poorly insulated buildings, inefficient electrical appliances in households and large distribution losses. The entire supply of oil, petroleum products and natural gas is imported. Analytic work carried out by the World Bank in close collaboration with the Government has demonstrated that ***investments in energy efficiency*** are the most cost-effective way towards energy security. In addition, as lignite deposits are being exhausted, the country should capitalize on its ***hydro potential***, which should also help with the need ***to increase water storage capacity*** in the face of the growing drought risk. The ongoing Energy Adaptable Program Loan (APL) 3 Project will improve fYR Macedonia's connection to the regional network while new lending will focus on enhancing new renewable energy capacity (possible investment in small hydropower station) and improving energy efficiency (Energy Efficiency Fund Project). IFC will continue the implementation of its regional Balkans Renewable Energy Program (BREP) in fYR Macedonia[32], supporting the country at regulatory, firm and financial institution level, to increase its renewable energy production. BREP will be implemented through joint Bank and IFC

[32] BREP advisory program, active in Macedonia since 2011, aims to develop renewable energy market with a special emphasis on small hydropower plants (SHPP) in Western Balkan countries with the highest impact potential. The Program, supported by the Ministry of Finance of Austria, provides advisory services to regulatory authorities, renewable energy sponsors and local financial institutions. BREP's key objectives are (i) to improve the existing framework related to renewable energy (RE); (ii) support individual RE investors and (iii) support local banks to improve capacity in project finance and RE technologies. More specifically, BREP is providing technical assistance to the Macedonian Ministry of Economy and Ministry of Environment and Physical Planning on regulation and investment promotion in the RE sector. As a result, the Government is in the process of bundling of SHPP sites to make them more attractive to investors, revising the FiT price for SHPPs (incentivizing smaller sites), and revising the Grid Distribution Code (to enhance SHPP's connection to the distribution grid).

interventions as well as in strong coordination with other stakeholders in the country. IFC is planning through its advisory and financial services to the private sector to stimulate the creation of additional 100MW of renewable energy capacity by the end of the CPS period. MIGA will also explore possibilities of support to public energy enterprises in attracting additional external investments.

**<u>Outcome 4: More clean energy available</u>**

**Proposed WBG program:** Energy APL3 (ongoing); Energy Efficiency Fund, Small hydropower station, Biomass-based Heating Study, Municipal Energy Efficiency Promotion (planned); IFC advisory (ongoing and planned), possible MIGA guarantee.

**Pillar 2: Skills and Inclusion**

**Challenge: Opportunities for all through modern skills and better public services**

80. **This pillar is focused on interventions that would help broader sections of society to participate in the fruits of economic growth** through better employability and more efficient public and municipal services.

***Employment access and skills***

81. **Education and skills** have been identified among critical constraints to employability. While access to education has improved, there is a challenging disconnect between education system outcomes and the private sector needs, as companies complain about the quality and availability of skills despite high unemployment. Lack of a ***clear accreditation mechanism*** means that employers do not know which skills a university graduate should possess, making hiring harder. Graduates of secondary vocational schools often have had no ***practical exposure to the job*** for which they are trained. Providing workers with the skills demanded in the labor market is central to inclusive growth since skills are the main asset workers have to improve their productivity, earn higher wages and lift their households out of poverty and into the middle class. While the skills agenda is broad and involves all levels of education, the Government has asked the Bank to focus on adapting the post-primary education system to the needs of the labor market. The World Bank will support this crucial agenda through the recently approved Skills and Innovation Project, which aims to improve the links between tertiary and secondary VET education institutions and potential employers for its graduates, enforce the focus on competencies and skills relevant for job market.

**<u>Outcome 5: Tertiary and VET education system more focused on skills for labor market</u>**

**Proposed WBG program**: Skills and Innovation Project (ongoing).

***Protecting the vulnerable***

82. **Improving the efficiency and coverage of the social protection system while providing more opportunities to the vulnerable groups** is an important part of the inclusion agenda. ***Targeting and efficiency*** of the social safety net can be strengthened, making it faster and cheaper to administer and at the same time ***ensuring that more people eligible for support receive it***. In particular, as discussed in the diagnostic section of the strategy, there is room to

focus assistance on the poorest quintile, as well as to ensure that more of those who are eligible for programs such as CCT are registered for the benefit. Another challenge is to make ***social assistance compatible with incentives to seek a job***, which could help people exit from the system and improve their welfare in a sustained way. The WBG will support this agenda through ongoing and new operations and knowledge work. The Conditional Cash Transfer (CCT) Project supports employment opportunities for the families in the bottom 40 percent of the population, and helps improve the coverage and targeting of social assistance to the bottom income quintile. Special emphasis is made on the empowerment of women: impact evaluation of the CCT secondary education program reveals that nominating women as the recipients of public transfers can improve the pattern of expenditures in the household. As of 2014/15 school year the transfers will be paid to the mothers in all beneficiary households. The new ICT-based Jobs Project will pilot mechanisms of employment for different population groups through ICT platforms, focusing on women, youth, disabled and other groups that are facing particular challenges in finding regular employment. The project will also improve inter-connectivity among government agencies, raising the efficiency of social assistance administration and other public services. Lessons learned from the pilot may be scaled up in a future operation. Resources available under the new CPS leave room for additional operations in this area, e.g. focused on a more comprehensive reform of the social protection system, subject to discussions with the Government during CPS implementation.

**Outcome 6: Social protection system more efficient and compatible with employment**

**Proposed WBG program**: CCT Project, Employment and Job Creation in fYR Macedonia (ongoing); ICT-based Jobs, Meeting the Jobs Challenges in the Western Balkans (planned); Social Protection operation (possible[33]).

*Closing the gap on basic services*

83. **Improved access to basic and municipal services** is an important part of the inclusion agenda in fYR Macedonia, particularly in the rural areas where the poor and bottom 40 percent are overrepresented. The Bank with support from the European Commission will scale up the geographic coverage of the ongoing Municipal Services Project, reaching poorer rural municipalities and providing not only crucial local infrastructure investment, such as ***piped water*** connections and ***solid waste services***, but also strengthening the capacity of municipalities to prioritize, plan and implement such investments. IFC will support PPP investments in local infrastructure.

**Outcome 7: Access to basic and municipal services enhanced**

**Proposed WBG program**: Municipal Services Project (ongoing).

[33] This operation has not been officially requested by the Government.

**Table 1: Current and planned projects and Analytical and Advisory Activities (AAA) by pillar**

| **Growth and Competitiveness** | | **Skills and Inclusion** | |
|---|---|---|---|
| **Ongoing projects and *AAA***: | US$ million | **Ongoing projects and *AAA***: | US$ million |
| Competitiveness DPL2 | 50 | Conditional Cash Transfers | |
| Real Estate Cadaster | 26 | Skills and Innovation | 25 |
| Regional and Local Roads | 105 | Municipal Services | 24 |
| Energy APL3 | 44 | *IFC advisory on jobs* | 75 |
| IFC support to SMEs | 25.2 | *Employment and Job Creation in fYR Macedonia* | |
| MIGA guarantee to National Bank of Greece for investment in Stopanska Bank | 143.9 | *Mainstreaming Social Accountability in portfolio* | |
| *Accounting and Auditing ROSC* | | | |
| *IFC infrastructure support through PPPs* | | | |
| *IFC advisory "Renewable Energy-Small Hydro Power Plants"* | | | |
| *Public Finance Review* | | | |
| *Macedonia Competitive Industries and Innovation Support Program* | | | |
| *Growth and Shared Prosperity Economic and Sector Work (ESW)* | | | |
| **New projects and *AAA***: | | **New projects and *AAA***: | |
| **FY15** | | **FY15** | |
| Road Rehabilitation (FY15) | 70 | ICT-based Jobs | 10 |
| Small hydro/ water storage | 60 | Solid Waste/ Wastewater | 20 |
| Public Finance DPL | 70 | **FY17** | |
| **FY16** | | Social Protection reform | TBD |
| Energy Efficiency Fund | 20 | IFC investment + *advisory* | |
| Competitiveness DPL3 | 70 | *Gender Diagnostic and Monitoring* | |
| **FY17** | | *PSIA Roads* | |
| Road Upgrading | 80 | *Poverty Assessment* | |
| MIGA guarantee in Energy | | *Meeting the Jobs Challenges in the Western Balkans* | |
| IFC operation + *advisory* for renewable energy and energy efficiency projects | | | |
| IFC support for SMEs through credit lines with commercial banks | | | |
| *Biomass-based Heating Study* | | | |
| *REBIS Upgrade* | | | |
| *Municipal Energy Efficiency Promotion* | | | |
| *IFC support for FDIs* | | | |
| *IFC engagement on NPL* | | | |
| *IFC engagement with regional Advisory Service platforms (trade logistics, corporate governance, food safety and PPPs)* | | | |
| **Economic Governance for EU Accession A cross-cutting theme** | | | |

*Note:* Loan amount for planned operations is indicative. Decision on the choice among new operations will be made during CPS implementation.

## C. Implementing the FY15-18 Country Partnership Strategy

84. **The strategy will be implemented in close collaboration across the WBG and with development partners**. After two years of implementation, a midterm review will be held to assess progress and make necessary course corrections.

85. **The Bank will apply a social filter to its entire pipeline** to help task teams in the country address obstacles that limit poverty reduction and shared prosperity for specific groups (women, minorities, in particular Roma, etc.) and to design activities and policy reforms that promote a more inclusive and cohesive society. Social filter activity will include (a) a rapid analysis of social issues in fYR Macedonia, (b) a practical tool that can help task teams identify how their projects address key social issues, and (c) support to project teams in the design and implementation of activities that can promote greater social inclusion and sustainability.

### Financing and instruments

86. **The new CPS will make available to fYR Macedonia up to US$400 million in new lending for the four years of strategy implementation,** subject to IBRD lending capacity, demand from other borrowers, country performance and priorities, and global economic developments. Depending on the market conditions, this could be supplemented by IFC financing of US$80-100 million for four years and possibly also MIGA guarantees.

87. **Leveraging all parts of the WBG balance sheet (IBRD, IFC and MIGA) could help maximize the amount of financial resources available to the country**. It is important to note however that as a middle income country fYR Macedonia has access to a variety of concessional and commercial funding options, and the decision on how much to borrow will also need to be balanced with the strategy of fiscal consolidation that the Government is pursuing. As such, the actual lending volume may be considerably lower than US$400 million depending on the client's needs and availability of viable projects that fit within the parameters of the strategy.

### Partnerships and Donor Coordination

88. **The World Bank continues to play an active role in donor coordination to improve complementarity and impact of its assistance.** In recent years donor engagement in fYR Macedonia and the amount of grant assistance available to the country have decreased. This trend is partially a result of the increased EU grant financing through the Instrument for Pre-Accession Assistance (IPA). Aside from the EU, other donors include the United States Agency for International Development (USAID), Germany, the Netherlands, the United Kingdom and the United Nations. On the lending side, the country has intensified cooperation with the European Bank for Reconstruction and Development (EBRD), the European Investment Bank (EIB), and the Council of Europe Development Bank (CEB). The World Bank has a close working relationship with all donors and lending partners to ensure complementarity of projects and advisory services to jointly reinforce the EU accession process.

89. **Partnership with donors established during the previous CPS period will be maintained in the future.** Cooperation with EBRD will continue in the new CPS with parallel financing discussed for the national roads rehabilitation program. Close cooperation with UN agencies, namely UNDP and the United Nations High Commissioner for Refugees (UNHCR),

will focus on the green growth and human resources agenda. Cooperation with USAID will focus on energy efficiency and on implementing selected recommendations from the green growth advisory services provided to the Government.

90. **Considering the country's goal to accede to the EU, Bank projects will continue to emphasize EU *acquis* requirements in policy dialogue and operations.** EU accession guides legislative and policy developments, as reform of legislation in line with the *acquis* is the country's priority. The Bank will continue to take the *acquis* requirements into consideration in its policy dialogue with the Government and to provide technical assistance in the reform process.

91. **The Bank will continue working with the Government and the EC to identify appropriate modalities of cooperation between the EU and the Bank and help the Government improve IPA absorption**. Pre-accession assistance is the largest financial assistance to the country, with an annual envelope of approximately EUR100 million in IPA grants available to all levels of government, private sector and civil society, to finance legislation modernization, capacity building and infrastructure investments under the 2007-2013 programing period. However absorption of the EU funds is slow: only about 35 percent of IPA resources available for 2007-2013 have been committed as of May 2014.

92. **Recently the partnership between the EU and the Bank has evolved, moving from regular coordination on strategic issues and parallel financing to joint financing of investment projects and advisory services.** The first such operation, which is at an advanced stage of discussion, involves the additional grant financing provided to the Municipal Services Improvement Project (MSIP) in the amount of EUR15.5 million from IPA, expected to be approved in 2014. Discussions are ongoing about collaboration in other areas, such as local competitiveness and tourism. The World Bank will continue to support the Government in the strategic planning and project preparations for IPA2 financing and to work toward establishing co-financing arrangements under IPA2.

### Monitoring and Evaluation

93. **The results framework for the new strategy is focused on 7 CPS outcomes that the program seeks to influence**. Progress towards these outcomes will be monitored through the specific outcome indicators that include both final and intermediate targets. An annual Country Performance and Results Review (CPRR) will be held to monitor progress on the results framework, and a midterm review exercise will also be held with the client.

94. **Monitoring of the following indicators will be disaggregated by gender**: share of Social Financial Assistance beneficiaries with children ages 15-18 registered for conditional cash transfers; and share of recipients of social assistance who work formally.

## IV. MANAGING RISKS TO BANK PROGRAM

95. **At the country level, the new CPS faces several important risks** that were described in the Medium-Term Outlook and Risks section above. The Bank will adjust its program should any of them materialize. In particular, in the case of an external shock or a major natural disaster

the WBG may change the volume or composition of financial support in response to changing financing needs, for example increase the volume of resources made available as DPLs, subject to available financial capacity, debt sustainability and policy reform requirements. If the Government's fiscal consolidation efforts are unsuccessful and fYR Macedonia's public debt, moderate at present, reaches unsustainable levels, the Bank may reduce the volume of new lending and refrain from offering DPLs. The Bank will also remain vigilant to the risk of civil and ethnic unrest and move to adjust its program as appropriate.

96. **With respect to the proposed program of WBG operations and their expected results,** based on the experience to date the main risk is that of implementation delay, for reasons of budget constraints and capacity limitations. Overall the risk of not achieving the planned results during the timeframe of the new strategy is assessed as low to moderate. Some of the specific risks include:

- **Change in political priorities:** While the current strategy is based on a clear request from the client and has been shaped in the process of extensive consultations, it is possible that priorities may change during the four years of the new CPS implementation. The Bank team will use the strategy as a living document and engage in regular progress and results reviews so as to adjust the course as needed.
- **Resistance to high profile operations:** High profile infrastructure operations, even if impeccable from a technical and economic perspective, may meet with resistance from some groups. The World Bank's policies, such as social and environmental safeguards, the social filter and proactive public communication campaigns will be used to mitigate these risks.
- **Capacity constraints delay or complicate implementation:** While fYR Macedonia has a strong track record of project implementation in many sectors, some capacity constraints remain. World Bank will continue to provide technical assistance and implementation support to all implementing agencies.
- **Data constraints:** Reliable data are scarce on many aspects of poverty and shared prosperity. In particular, fYR Macedonia has not had a census since 2002 and a declining response rate on the HSB makes it difficult to monitor long-term changes in poverty and shared prosperity indicators and reduces the availability of data for evidence-based policy-making. The Bank will use the Survey on Income and Living Conditions, initiated in 2010 by the State Statistical Office for monitoring welfare, to inform the engagement through poverty and shared prosperity analyses. In addition, the Bank will continue providing technical assistance to the State Statistical Office and look for opportunities to strengthen data collection and analysis.

# Annex 1: Results Framework for FYR Macedonia CPS 2014-2018*

| Country Development Goals | Issues and Obstacles | Outcomes directly influenced by CPS interventions<br>Indicators and targets | WBG program |
|---|---|---|---|
| **Pillar 1: Growth and Competitiveness** | | | |
| **Macroeconomic and fiscal stability maintained** | Public debt, while moderate at present, may be driven to unsustainable levels unless fiscal deficits decline.<br><br>Improving transparency to strengthen trust in public financial management.<br><br>Quality of public investment has been declining, putting pressure on long term fiscal sustainability. | **Outcome 1: Improved fiscal and public financial management**<br>• Fiscal deficit declines in line with medium-term budget framework<br>*Baseline*: 4.1 percent of GDP<br>*Target*: below 3 percent of GDP<br>• Quarterly reports on consolidated public and publicly guaranteed debt published on the MOF website<br>*Baseline*: No<br>*Target*: Yes<br>• Road Enterprise makes investments using Road Asset Management System<br>*Baseline*: No<br>*Target*: Yes | **<u>Ongoing:</u>**<br>Public Finance Review<br>Regional and Local Roads Project<br><br>**<u>Planned:</u>**<br>Public Finance DPL<br>National and Regional Road Rehabilitation Project<br>Road Upgrading Project<br>Growth and Shared Prosperity ESW |
| **More private investment to drive economic growth** | Access to finance and implementation of business-related regulations at the local level named among top obstacles for doing business in recent surveys.<br><br>Low level of business sophistication prevents foreign investors from establishing local supply links, reducing growth and employment effects of FDI. | **Outcome 2: Better conditions for private investment and links to FDI**<br>• Private investment facilitated in the real sector through IFC interventions<br>*Baseline:*EUR80 million<br>*Target:* EUR180 million<br>• Number of days to obtain construction permit<br>*Baseline:* Average 181.1; Manufacturing 43; Services 243.1(BEEPS)<br>*Target:* Average 83; Manufacturing 25; Services 100<br>• Improved local business sophistication<br>*Baseline:* Sophistication 3.65; Innovation 3.2 (Global Competitiveness Report 2013, pillars 11 &12)<br>*Target:* Sophistication 4.0; Innovation 4.0 | **<u>Ongoing:</u>**<br>BREP; IFC Advisory on Infrastructure PPP; IFC investment and mobilization in the real sector; Competitiveness DPL2; MCIISP; Skills and Innovation Project<br>WBG Just-in-time advice/AAA<br><br>**<u>Planned:</u>**<br>Competitiveness DPL3<br>Growth and Shared Prosperity ESW<br>IFC investment and advisory |
| **Better transport links within and outside the country** | As a small landlocked country, fYR Macedonia relies on road transport for export and access to foreign markets. The quality of road network has been deteriorating. | **Outcome 3: Road infrastructure improved**<br>• Percentage of national and regional roads network in good and fair condition increased<br>*Baseline:*79 percent<br>*Target:* 81 percent<br>• Number of people with better access to transportation through new PPPs<br>*Baseline:* 0<br>*Target:* 300,000 | **<u>Ongoing:</u>**<br>Regional and Local Roads Project; IFC Advisory on Infrastructure PPP<br><br>**<u>Planned:</u>**<br>National and Regional Road Rehabilitation Project<br>Road Upgrading Project<br>Upgrade to REBIS |

| Country Development Goals | Issues and Obstacles | Outcomes directly influenced by CPS interventions<br>Indicators and targets | WBG program |
|---|---|---|---|
| **Improved energy security in a sustainable manner** | Dependence on coal and imports puts the country's energy security in question and undermines future growth. Analysis shows that energy efficiency and development of new hydro capacity are best ways towards energy security. | **Outcome 4: More clean energy available**<br>• Additional annual renewable clean energy generation<br>*Baseline:* 0 GWh<br>*Target:* 105 GWh (Bank) + 100 GWh (IFC)<br>• Total projected lifetime energy savings of new EE measures implemented under Bank-supported programs<br>*Baseline:* 0<br>*Target:* 600 GWh | **Ongoing:**<br>Energy APL3; IFC infrastructure support through PPPs; Renewable Energy Macedonia Small Hydro Power project<br><br>**Planned:**<br>Small hydro project; Energy Efficiency TA; Energy Efficiency Fund Project; Biomass-based Heating Study; Municipal Energy Efficiency Promotion<br>IFC investments and advisory; possible MIGA guarantee |
| **Pillar 2: Skills and Inclusion** | | | |
| **Labor force skilled in areas that are demanded by the market** | Although unemployment is high, companies report difficulties in filling skilled jobs. Variability in the quality of education programs makes it difficult for employers to interpret applicants' diplomas. Graduates often lack practical skills for the job. | **Outcome 5: Tertiary and vocational education system more focused on skills for labor market.**<br>• Share of public universities accredited with new quality assurance measures consistent with EU norms<br>*Baseline:* 0<br>*Target:* 60 percent<br>• Share of secondary TVET students receiving practical training in firms<br>*Baseline:* 28 percent<br>*Target:* 48 percent | **Ongoing:**<br>Skills and Innovation Project |
| **Social protection system more efficient and promoting household independence** | Social protection system suffers from both inclusion and exclusion errors.<br><br>Although social assistance is not generous, fear of losing it prevents beneficiaries from seeking formal employment. | **Outcome 6: Social protection system more efficient and compatible with employment**<br>• Share of the poorest quintile receiving social assistance<br>*Baseline:* 65.8 percent (SILC 2011)<br>*Target:* over 70 percent<br>• Share of Social Financial Assistance beneficiaries with children ages 15-18 registered for conditional cash transfers<br>*Baseline:* 76 percent (women: 73 percent)<br>*Target:* over 80 percent (women: 75 percent)<br>• Share of recipients of social assistance who work formally<br>*Baseline:* 1.46 percent (women: 0.99 percent)<br>*Target:* 5 percent (women: 3 percent) | **Ongoing**:<br>Conditional Cash Transfers Project<br><br>**Planned:**<br>ICT-based Jobs Project; Social Protection Project; Employment and Job Creation in fYR Macedonia; Meeting the Challenges in the Western Balkans |
| **Close the gap on basic services** | Key infrastructure gaps remain in areas such as water, sewage and solid waste collection. Rural communities are particularly | **Outcome 7: Access to basic and municipal services enhanced.**<br>• Additional households with improved piped water connections<br>*Baseline:* 0<br>*Target:* 30,000 | **Ongoing:**<br>Municipal Services Project |

| Country Development Goals | Issues and Obstacles | Outcomes directly influenced by CPS interventions<br>Indicators and targets | WBG program |
|---|---|---|---|
| | vulnerable. | • Additional households with improved solid waste services<br>*Baseline:* 0<br>*Target:* 60,000 | **<u>Planned:</u>**<br>EU Additional Financing to Municipal Services Project; Solid Waste/Waste Water Project |

*Baseline refers to current FY.  Target refers to end of CPS period (FY18).

## Annex 2: FY11-FY14 CPS Completion Report

| | |
|---|---|
| **CPS Board Discussion:** | September 20, 2010 |
| **CPS Progress Report (Board Presentation)** | November 1, 2012 |
| **Period Covered by CPS Completion Report:** | September 2010 – June 2014 |

## FORMER YUGOSLAV REPUBLIC OF MACEDONIA

## COUNTRY PARTNERSHIP STRATEGY FY11–14 COMPLETION REPORT

## INTRODUCTION

1. This Country Partnership Strategy Completion Report (CPSCR) reviews the experience of implementing the FY11–14 World Bank Group Country Partnership Strategy (CPS) for the Former Yugoslav Republic (fYR) of Macedonia (Report No. 54928-MK, September 20, 2010). The document assesses the effectiveness of the Bank Group's strategy in: (i) aligning its objectives with fYR Macedonia's long term strategic goals; (ii) setting relevant, measurable and realistic CPS outcomes; and (iii) achieving its expected outcomes in an efficient and sustainable way. In addition to discussions with the country team and Government counterparts, this assessment is based on reference documents such as the CPS, Project Appraisal Documents, Implementation Status Reports, supervision reports, and reports related to Economic and Sector Work. The findings of the assessment have informed the preparation of the FY15-FY18 CPS.

2. During the period of the strategy the Government of fYR Macedonia has been pursuing a development strategy focused on the following five objectives: (i) economic growth and private sector development; (ii) integration into the EU; (iii) fight against corruption and economic crime; (iv) good interethnic relations; and (v) investments in education, science and knowledge-based society. The CPS was well aligned with and has contributed to the progress towards objectives one, two and five.

3. During the CPS period the World Bank delivered US$534.4 million in new loans, of which US$98 million was Investment Project Financing, US$100 million budget support and US$336.4 million Policy Based Guarantees. IFC invested US$63.3 million: US$23.7 million in the financial sector, US$35 million in manufacturing and US$4.6 million in energy.

## I. SUMMARY OF FINDINGS AND RATINGS

4. **The objective of the FY11-14 CPS was to support faster, more inclusive and greener growth while helping to prepare for EU accession.** The CPS focused Bank Group support in three areas of engagement: (i) *faster growth* – competitiveness; (ii) *more inclusive growth* – employability and social protection; and (iii) *greener growth* - environmental sustainability and climate action. In these three areas of engagement, the CPS contributed to specific development outcomes which are summarized in Table 1.

During the first half of the CPS, contributions to these outcomes came mainly from interventions carried forward from the FY07-10 CPS. Tables 2, 2a and 3 provide a breakdown of planned and actual operations and knowledge and advisory activities for the FY11-14 CPS respectively.

5. **The Competitiveness Pillar is rated Satisfactory. The program has made outstanding development contributions, particularly in Competitiveness.** The WBG has accomplished highly successful interventions in maintaining macroeconomic and fiscal stability and strengthening municipal services and infrastructure. Some fiscal issues remain, but the Bank's timely intervention was vital to maintaining macroeconomic stability.

6. **The Inclusiveness Pillar that embodied the WBG's strategic goals of fighting poverty and achieving more inclusive growth is rated Moderately Unsatisfactory.** The lack of reliable data on incomes and household budgets made it impossible to monitor the targeting of the social safety net and to properly evaluate some program outcomes. The conditions for employment of vulnerable groups were improved, but on the whole the WB team did not sufficiently mitigate the difficulties of achieving program goals and measuring program impact in this area. On the other hand, the Conditional Cash Transfer project, aimed at improving the efficiency of social safety nets, was the first of its kind to be implemented in the region.

7. **The Greener Growth Pillar is rated Satisfactory.** For the first time in fYR Macedonia, the World Bank successfully engaged with the Government in the area of energy efficiency. Completed activities have demonstrated to the Government the potential of investments in this area, leading to the formulation of the first National Program of Energy Efficiency in Public Buildings and a decision to establish a revolving Energy Efficiency Fund to implement this program. The Bank and Government underestimated the complexity of some infrastructure projects involving land acquisition, and there have been implementation delays, despite which the projects are on track to achieve expected outcomes. High-level policy dialogue on the use of state-owned agricultural lands has led to commitment to land privatization embodied in law.

8. The CPS was weighed towards the Competitiveness and Greener Growth Pillars (13 and 10 outcome clusters respectively) and had fewer outcomes under the Inclusiveness Pillar (2 outcome clusters). Out of 25 outcome clusters 16 were **Achieved**, a further eight were **Mostly Achieved**, and one **Partially Achieved**. **Overall FY11-14 CPS performance is rated Moderately Satisfactory**. This rating reflects the strategic importance of the Inclusiveness Pillar which had a relatively lower percentage of fully achieved outcomes than the others.

## II. PROGRESS TOWARD ACHIEVING COUNTRY-LEVEL GOALS

9. The CPS was aligned with and contributed to the progress toward three objectives of the Government of fYR Macedonia: economic growth and private sector development, integration into the EU, and investments in education, science and knowledge-based society.

### Economic Growth and Private Sector Development

10. **Macroeconomic and financial stability was preserved in the face of significant negative shocks.** fYR Macedonia achieved moderate growth during the ongoing Eurozone crisis, to which as a land-locked and trade-dependent economy it was particularly vulnerable. Average GDP growth between 2009 and 2013 was 2.1 percent per year, slightly better than its South East European neighbors' 1.7 percent. Central Government debt was maintained below 40 percent of GDP through 2013, and spending on pensions below 9 percent of GDP up to 2012. In 2013 the World Bank supported the Government with the second Public Expenditure Policy Based Guarantee (PEPBG) thus helping it obtain a large

commercial loan, which allowed for the fast repayment of arrears and implementation of measures to prevent their reoccurrence. The level of public health arrears was successfully controlled for part of the period, but the goal to maintain them at or below 0.2 percent of GDP was not achieved. Successful PFM reforms supported under PBG2 were key for maintaining macroeconomic stability.

11. **The PBG allowed the country to obtain access to the international bank loan market on improved terms.** The Government used the PEPBG to borrow €250 million in January 2013, covering 46 percent of the total 2013 financing requirement at a reasonable cost (3.915 percent interest rate) in two tranches of 5 and 7 years maturity. The PEPBG also helped leverage the Bank's capital by allowing fYR Macedonia to contract a commercial loan of €250 million out of which IBRD guaranteed 62 percent, or €155 million (US$201.5 million equivalent).

12. **The business climate in fYR Macedonia has consistently improved.** Reforms to registration and permitting processes, property registration procedures, investor protection, and tax collection were carried out. In 2013, *Doing Business* ranked fYR Macedonia the fifth most improved country among the top 50 economies in the world; it had jumped from 92nd position in 2006 to 25th in 2013, outstripping peer countries in the region. The efficiency of judiciary services has improved considerably, with the number of days required to enforce a contract down from 370 to 60. Further, SMEs' access to financing in key growth sectors was enhanced.

13. **The DPL actions supported FDI inflows into medium- and high-tech manufacturing industries, generating significant new employment, however challenges remain.** FYR Macedonia has the potential for a diversified economy and for significant investments and exports, including, *inter alia*, automotive components, healthcare products and pharmaceuticals, agribusiness and food processing, and metals and metal products. The Government's FDI attraction strategy, based on promotion, special economic zones (SEZ) and investor incentives packages, has resulted in inflows of high value added FDI and significant new employment. These investments jumped to €78 million in 2013, accounting for net exports of €87 million in 2013, and are expected to be up to €190 million in 2014, with total exports of €1.2 billion. The companies employed around 5,000 workers in 2013, a figure expected to increase to 9,000 by the end of 2014. The authority of the institutions and the monitoring and audit system for fiscal incentives have been strengthened through the Competitiveness DPL, and support has been extended to exporter support programs and investment programs in new zones based on market demand. Nonetheless, and though it has supported a specialized agency entitled *Invest in Macedonia* to attract FDI to these and other sectors, capital inflows remain below expectations.

16. **While efficiency and transparency of land administration have improved, unleashing long-term agricultural growth and thereby reducing rural poverty requires further reforms.** Real estate transactions grew 29 percent on 2009 and registered mortgages using property as collateral between 2009 and 2012 jumped by 64 percent. The agribusiness sector has seen a large increase in public spending, from €10 million in 2005 to €130 million in 2013. Most of this increase was allocated to direct farm subsidies. While these subsidies can help spur short-term growth, they do not address structural inefficiencies dragging down agricultural profitability and make it even more difficult to pursue reforms necessary to unleash long-term agricultural growth. Rural poverty remains rooted in low agricultural productivity. The sector remains penalized by the absence of a fluid land rental market, high farm fragmentation, inadequate financing for applied agricultural research and farm advisory services, and the slow resolution of institutional problems around water use associations.

19. **In trade logistics, the Government is modernizing transport infrastructure to speed the flow of passenger and cargo traffic, while simultaneously introducing trade facilitation measures.** The largest airports were recently upgraded through a concession with a private operator from Turkey, and the Government has initiated investments to upgrade Corridor X, its main road and rail corridor to EU

markets and ports. Investment plans to upgrade Corridor VIII and local roads are also underway. Facilitation measures include simplified customs procedures and strengthened coordination with inspection agencies; introduction of a single-window system for processing export/import and transport licenses; introduction of a risk-based approach to customs controls and technical inspections, combined with more inspectors at major border crossings, to speed processing; and systematizing professional standards and internal controls to mitigate corruption among customs officers.

20. **To boost competitiveness and reduce unemployment – while on a downward trend, at 28.7 percent in the third quarter of 2013, it remains one of the highest in Europe – the Government has lowered the cost to businesses of employing workers by reducing the tax burden.** Legal reforms supported under the DPLs were enacted to address rigidity in labor market regulations, facilitate seasonal employment and improve public sector capacity and the regulatory framework to nurture private sector innovation.

**Integration into the EU**

21. **EU standards have informed the reforms, consistent with Government's priority.** For example, according to the EC Progress Report 2014, progress in the area of corporate and financial reporting, with Bank support through financial sector TA and regional REPARIS, was satisfactory. Going beyond set country-level goals, the cadastre agency adopted a National Spatial Data Infrastructure Strategy in line with EU requirements. The IPARD-accredited Paying Agency is fully functional. Farm registry and land parcel identification systems are established, and quarterly reports on key agricultural data are published.

**Investments in Education, Science and Knowledge-Based Society**

22. **Increasing innovation capacity is a priority for Government, and a central part of the strategy to accelerate productivity growth and diversify exports.** The Government has taken important steps towards strengthening the innovation policy framework by adopting an Innovation Strategy in October 2012 and enacting a Law on Innovation Activity in May 2013. The Law enabled the establishment of a Fund for Innovation and Technological Development that will introduce competitive financial instruments to stimulate commercial R&D, support new start-ups and spin-offs, and scale up technology commercialization and transfer activities, thus connecting the research sector to private sector and market needs.

23. **Higher education reform has commenced, aimed at bringing it in line with EU standards and making graduates' skills more market-relevant.** The legislative framework on quality assurance in higher education system was amended to align it with EU standards, and a higher education funding model has been defined.

## III. EVALUATION OF PROGRAM PERFORMANCE

**Pillar I. Faster Growth by Improving Competitiveness**

24. **Adverse economic conditions notwithstanding, key macroeconomic stability outcomes were achieved.** FYR Macedonia, like many countries in ECA, confronts an economic and financial environment far more challenging than existed prior to the 2008-2009 crisis. With ECA the worst hit of all developing and transition regions, fYR Macedonia's primary trade and financial partners showed tepid

growth over the short-term. Capital was scarce and imports sluggish. The WBG engaged closely with the authorities to identify where it could provide support to improve macroeconomic stability. The PBGs helped consolidate macroeconomic stability by supporting measures to maintain sustainable debt levels, furthering reforms to the pension system, and strengthening the health financing system through implementing centralized international procurement and adoption of the bylaw establishing the Medical Network. The PBGs strengthened the resilience of the financial sector by supporting adoption of a new law to strengthen the independence and accountability of the Central Bank, while at the same time improving coordination between the Central Bank and the Ministry of Finance and establishing a Supervisory Committee to increase the supervisory capacity of relevant bodies. The second PBG allowed the Government to obtain, on favorable terms, a large commercial loan for the repayment of arrears and implement measures to prevent their reoccurrence. Although health sector reforms rationalized spending by healthcare institutions and PBG health sector outcomes were achieved, public health arrears have remained above the projected level.

25. **The CPS contributed to strengthening competitiveness and improving the business environment, through investment in enterprise development, FDI and exports, land administration, judicial services, access to finance, land, and skills development.** The FY05 Business Environment Reform and Institutional Strengthening (BERIS) Project, completed in FY11, contributed to improving the regulatory regime and institutional framework for business entry and activity. It strengthened capacity in a number of key areas including improving access to information on credit through a credit registry and business entry through a one-stop shop for company registration. The results contributed to fYR Macedonia's meeting EU criteria on the Free Movement of Goods, Company Law, and Industrial and Enterprise Policy.

26. **Policy shifts created or strengthened the enabling environment for innovation and R&D support.** The 2013 establishment of the Fund for Innovation and Technological Development, supported by the FY14 Skills and Innovation Project, evolved from the Innovation Strategy (2012) and Law on Innovation Activity (2013) and development of financing instruments to stimulate private sector innovation through the Fund. The State Statistical Office introduced a new survey instrument measuring innovative activity of enterprises based on international methodology, which was first supported by the BERIS Project in 2010.

27. **The FY05 Real Estate Cadastre project has been supporting the development of an efficient and effective real estate cadastre and registration system, with a view to developing land and real estate markets.** With the exception of the slight fall in customer satisfaction with cadastre services, all land administration outcomes were achieved. Additional financing for the Real Estate Cadastre project approved in FY10 supported the digitization and vectorization of cadastre maps that facilitated data sharing among public, private, and Government institutions, upgraded the national geodetic reference infrastructure, and supported the development of national spatial data infrastructure in line with the EU's INSPIRE Directive. The project also built the capacity of the Authority of Legal and Property Affairs, which oversees property and legal issues involving public authorities and agencies.

28. **The improvement of judiciary services outcome was achieved, with the efficiency and effectiveness of judicial services improved and access to justice strengthened.** The FY06 Legal and Judicial Implementation project, which closed in 2011, strengthened judicial institutions; supported implementation of new bankruptcy legislation; developed a framework for administrative disputes by improving judicial management; and invested in court infrastructure, such as constructing and rehabilitating courthouses and enhancing judicial information technology systems. IFC contributed through its Alternative Dispute Resolution Project, which promoted the use of mediation as an alternative to court proceedings.

29. **The strengthening of higher education outcome was mostly achieved.** World Bank TA supported the Ministry of Education and Science in making informed policy choices about financing higher education, including establishing bodies for external quality assurance in accordance with good practice and European agreements and guidelines. This project demonstrated how investment lending in can support implementation of agreed policy changes.

30. **FDI attraction and SME development outcomes were achieved.** The WBG devoted considerable attention to the competitiveness agenda through the DPO series, underpinned by the Modular Competitiveness Assessment AAA, supporting the Government's program to improve competitiveness of the economy. Reforms created incentives for investment and technology upgrading in manufacturing, agribusiness and trade logistics. In parallel, policy actions laid the groundwork for increasing labor market flexibility and developing job-relevant skills.

31. **IFC continued to assist private companies to improve their access to finance and increase their exports, and to offer to the central and local Governments its PPP advisory services in different areas.** In coordination with the Bank, through its ongoing Trade Logistic advisory program, IFC helped the country to reduce trade constraints, harmonize border clearance through regional cooperation, and facilitate further liberalization of trade and alignment of rules on EU practices linked to the CEFTA regional trade agenda. Through its International Standards and Technical Regulations advisory program, IFC has contributed to increased corporate sales revenues by $15 million and exports by over US$3.5 million. IFC contributed to a better corporate governance culture working with key regulatory and market institutions. As a result, 23 companies improved their performance and 4 companies reported an increase of $30 million in investments as a result of improved corporate governance practices.

32. **Under the Global Trade Finance Program, IFC extended $10.3 million in trade credit lines to three banks in fYR Macedonia.** IFC's financing helped these banks to provide additional financing to small and medium enterprises operating in key import and export sectors such as energy, metallurgy, mining, textile, food processing, and transport. When international financing was becoming harder to obtain due to the European economic crisis, IFC financed a subsidiary of a European bank with $13.4 million to support expansion of lending to SMEs, agribusiness, infrastructure, and climate change. In addition, IFC invested $70 million in a cement group, of which half is expected to be invested in the group's Macedonian subsidiary.

33. **The** r**oads rehabilitation outcome has been mostly achieved.** The FY08 Regional and Local Roads Program Support Project, due to close in 2015, built the capacity of the Public Enterprise for State Roads (PESR) and invested in the rehabilitation of the regional and local road network, with a view to improving the access of isolated communities to markets. To date, all planned regional roads (284 km) have been rehabilitated, and work on local roads continues as planned; it should result in the rehabilitation of a further 420 km of roads and lead to vehicle operation costs reduction. IFC has been assisting the Government to structure a PPP transaction and attract a private concessionaire for expansion, operation and maintenance of the motorway between Skopje and Kicevo. A Road Asset Management System enabling evidence-based planning of further infrastructure development is being put in place.

34. **The facilitation of regional trade outcome has been achieved.** The FY07 Second Trade and Transport Facilitation project (closed in FY11), lowered transport and freight costs, particularly by improving border crossing facilities, upgrading a road corridor section to motorway standards, and harmonizing and improving telecommunications and cargo data exchange between railways and customs. Freight processing times have been reduced and non-tariff trade obstacles removed between fYR Macedonia and its neighbors.

35. **All annual targets for municipal services have been achieved and are ahead of schedule to achieve outcomes planned for 2017.** The Municipal Services Improvement Project (MSIP) helped selected municipalities to improve the financial performance of specific investments, and build the capacity of municipalities and their communal service enterprises, particularly by undertaking financial reforms, enhancing communication with residents, and increasing transparency. To date, sub-loans have been made to 30 of 83 municipalities through the project. At Government's request, the project received additional financing in FY12, tripling the original loan amount to US$75 million. MSIP is also used as a vehicle to increase the absorption of EU Instrument for Pre-Accession (IPA) funds. IFC assisted the GoM in improving the regulatory framework for waste management as well as building municipalities' capacity, including through a specialized certified Waste Management course.

**Pillar II. More Inclusive Growth by Strengthening Employability and Social Protection**

37. **The FY09 Conditional Cash Transfer (CCT) Project contributed to the efficiency and effectiveness of social protection and human capital.** The CCT Program has an enrolment rate of 86 percent of households receiving Social Financial Assistance and with children ages 15-18 or older in full-time secondary education. The program, the first of its kind in the region, conditions cash benefits on secondary school enrollment and attendance, and has been expanded to include active employment programs. In addition, through the establishment of the Cash Benefits Management Information System, the CCT project improved the targeting and administration of services under the social safety net, including oversight mechanisms, service delivery, and monitoring and evaluation. However, due to the lack of data, the targeting accuracy indicator for this project in relation to the poorest quintile is unobservable.

38. **The goal of increasing employment by decreasing labor costs to employers was mostly achieved.** Key reforms supported by the FY11 PBG included reducing Social Insurance Contributions to 27 percent of the gross wages, restraining growth in public sector wages, and improving public sector wage-setting. These contributed to improving employability by reducing impediments to hiring. The Government has started to implement employment subsidy programs that lower employment costs, especially of youth. During CPS implementation, unemployment has fallen modestly and labor force participation has increased.

**Pillar III. Greener Growth: Environmental Sustainability and Climate Action**

39. **The World Bank, with significant financial support from Sweden and Norway, undertook a flagship program of analytic work to help fYR Macedonia better understand the macroeconomic case for investing in green sectors and "greening" brown sectors as a stimulus for stronger growth.** This work focused on energy, water, transport, agriculture, urban development, and environment, and helped promote adaptation to climate change and lower-carbon growth options in policy and investment planning decisions.

40. **The goal to improve the efficiency and environmental sustainability of the energy sector, particularly by exploiting renewable energy and energy efficiency sources, was achieved, with the upgrading of energy transmission infrastructure mostly achieved.** Additional financing for the Energy Community of South East Europe (ECSEE) APL 3 reduced the operating and maintenance cost of selected substations by 25 percent. After delays due to land acquisition, the project is now on track to

reduce the number and duration of power supply interruptions by 80 percent. At Government's request, the Bank provided a Project Preparation Advance (PPA) to support possible development of a water storage project at Lukovo Pole in the northwestern part of the country that would allow more efficient use of existing hydropower plants. The PPA has supported preparation of the detailed design, Environmental and Social Impact Assessment, and a legal review. The GEF Sustainable Energy Project supported setting up a large-scale national program to retrofit public buildings in order to increase their energy efficiency, providing capacity building for this national program while at the same time financing energy efficiency measures in 40 schools and kindergartens, and leading to Government commitment to improving energy efficiency across all sectors.

41. **IFC has invested in energy efficiency and supported renewable energy legislation. In 2012 IFC invested $4.6 million in EVN, the sole electricity supply and distribution company serving 640,000 customers, to support its need for additional working capital.** Through its PPP transaction advisory, IFC has been helping the Government to create a new, more attractive, tender for financing Cebren Hydropower Project, intended to contribute to reducing electricity imports and GHG emissions. To contribute to private sector participation in "greener" energy, in February 2012 IFC launched in fYR Macedonia the advisory services program "Renewable Energy in the Western Balkans with a Focus on Small Hydro Power Plants." Through this program IFC has assisted the Government in adopting key renewable energy legislation, estimated to have contributed to $48 million in private sector financing for small power plants.

42. **The CPS supported the strengthening of the management of water resources in line with EU directives; all water management objectives were achieved.** The FY11 Water Sector Capacity Building TA helped the Government to identify critical infrastructure needed to address water scarcity in the southeast, most affected by climate fluctuations and changes. The Water Economies were restructured to form river basin management bodies in line with the EU water directive. The Agriculture Strengthening and Accession Project (ASAP) also contributed to improving the management of water resources.

43. **The CPS achieved agriculture strengthening objectives, supporting strengthened competitiveness of the agriculture sector, via improvements in the agricultural subsidy system, opening of the land market, and adapting practices to climate change and EU requirements.** Agriculture accounts for 18 percent of GDP and substantial employment in rural areas, where 21 percent of the population live in poverty. The FY07 ASAP enabled the accreditation of the Ministry of Agriculture to distribute EU Rural Development funds, although it did not address the parallel subsidy system the Government created. The project also helped complete the restructuring of the irrigation delivery system and develop veterinary capacity for an EU-compliant food safety system. In addition, it is supporting the development and dissemination among farmers of a Code of Good Agricultural Practices integrating biodiversity and agriculture, and promoting sustainable soil and water management. High-level policy dialogue led to the government's commitment to privatization of agricultural land and enactment of the Law on the Sale of Agricultural Land in State Ownership. Privatization of public lands has started. This achievement has effectively superseded the mostly achieved outcome of increasing the rate of lease collection for state-owned agricultural lands.

44. **The World Bank financed fYR Macedonia's participation in the Southeastern Europe and Caucasus Catastrophe Risk Insurance Facility (SEEC CRIF).** The overall objective of the SEEC CRIF is to increase access to financial protection for the Government as well as homeowners, farmers and SMEs from losses due to weather extremes and geo-hazards. Although the international insurance facility has taken more time to establish than expected, the targeted insurance penetration is likely to be achieved in 2014, as anticipated.

## IV. WORLD BANK GROUP PERFORMANCE

45. **The overall rating of WBG performance is Good.** The WBG successfully contributed to the pursuit of CPS objectives, 96 percent of which were achieved or mostly achieved. The WBG has mostly timely adapted to changing circumstances and priorities, responding to challenges ranging from the economic crisis to client capacity limitations. The program of activities provides a sound platform for the next strategy.

46. **The CPS quality at entry was Good.** The CPS was designed in partnership with the Government of fYR Macedonia, and its objectives were well aligned with the country's development priorities, with about half of the monitored outcomes falling under the Government's promoting growth and competitiveness objective.

- **The CPS design was characterized by continuity, flexibility, complementarity and synergy within the lending program and between its lending and non-lending elements**. The WBG coordinated planned interventions with development partners, the EU in particular. The CPS was structured to be particularly flexible over FY13-14 given uncertainty on the pace of economic recovery and the rapidity of evolving development challenges.

- **The program continued to move toward greater selectivity and portfolio consolidation, while using a broad spectrum of instruments**. Selectivity was driven largely by client demand, the WBG's comparative advantage, and exposure limits. While traditional investment lending accompanied by hands-on implementation support and informed by related knowledge products remained the instrument of choice, the Bank used the PBG instrument to great advantage, leveraging limited exposure space to facilitate fYR Macedonia's access to private financial markets. Further, the Bank used grants, analytic work and small pilot interventions to build momentum in areas where consensus or capacity was insufficient. For example, successful implementation of the GEF Energy Efficiency project provided practical experience that shifted the understanding of energy efficiency. Bolstered by technical assistance and recommendations of the Green Growth analytic work, it has led to Government's adoption of the National Program of Energy Efficiency in Public Buildings and decision to establish a revolving Energy Efficiency Fund to implement it.

- **The CPS results framework was Fair**. While it captured the gist of the Bank's program, the results framework contained too many indicators and outcomes, not all observable. Data shortages were not considered as potential risks. Some indicators were difficult to monitor, because the client did not have the capacity to provide the data.

- **While important country-level risks were identified and addressed, the CPS did not discuss risks to the WBG program**. The strategy document noted risks such as the Eurozone crisis, delay in EU accession, continued high unemployment and natural disasters, all of which continue to be relevant. CPS interventions successfully mitigated the risk of financial instability exacerbated by the Eurozone crisis and contributed to efforts to reduce unemployment. The WBG has provided a substantial amount of information to the Government on climate change and the green agenda, and support to the Europa Re project has led to introduction of new catastrophe insurance mechanisms. However, the CPS did not identify risks to the WBG program. In retrospect, the main challenges to the program were: (a) the introduction of budget ceilings, which affected the speed of project implementation and disbursements; (b) implementing agencies' capacity constraints, which led to slower than expected start up and implementation of some projects; and (c) in the case of infrastructure projects, issues such as land acquisition and availability of qualified contractors. While these challenges caused implementation delays, all projects achieved their development objectives or are on track to do so. The WBG program was concentrated in areas of strong client commitment well aligned with Government priorities, which helped mitigate the risks to WBG-supported operations.

47. **Quality of implementation was Good.** Implementation accommodated changing circumstances such as the Eurozone crisis and internal financing needs. The CPS Implementation Management Tool was used for monitoring operations and identifying implementation bottlenecks. The Bank team provided strong and consistent implementation support, adjusting to evolving circumstances and client needs. At the same time, it did not take full advantage of the Progress Report to revamp the results framework. While there was good focus on successful implementation of specific operations, it was not complemented by regular strategic review of results and priorities, which could have improved performance under the Inclusive Growth Pillar. A more consistent strategic focus on inclusion was needed, as were observable progress indicators and a reliable system for monitoring them.

- **Strong involvement of the local team ensured timely exchange of information and improved Bank's responsiveness to client requests.** All projects were assigned a contact person in the local office, and some projects had field based Task Team Leaders. This close and continuous portfolio management resulted in continuous adjustments to lessons of experience and evolving needs; except for the most recent approvals, every project in the Bank's portfolio was restructured at least once.

- **According to the Client Survey results and consultations carried out in the course of the preparation of the new CPS, knowledge services provided by the WBG during the CPS period were of good quality and well aligned with the country program**. The WBG team used a broad spectrum of knowledge products depending on needs. Most of the analytic work was closely related to lending. For example, Competitiveness Assessments provided the analytical foundation of the Competitiveness DPL series, and all lending operations were accompanied by implementation support and often technical assistance, such as in the case of the Higher Education TA or advice on the preparation of the National Program of Energy Efficiency of Public Buildings. The Land Registration and Cadastre project participated in a South-South exchange with Honduras, sharing project results and lessons with a peer agency. The Labor Market Assessment was complemented by continuing TA for the Government's Jobs Strategy. Recommendations of the Green Growth report were discussed with respective sector authorities and are likely to inform future Government policy and investment choices.

- **The CPS reflected a partnership between the World Bank and IFC,** set out in a Joint Business Plan for fYR Macedonia.

- **The Bank tailored its support in response to changing circumstances**. Just-in-time support was effective in dealing with new challenges and provided timely assistance to the Government while also contributing to achievement of most outcomes. The Bank has been able to offer the Government high-quality development solutions while rapidly preparing new lending operations in response to changed circumstances.

- **While the WBG has in general adequately responded to changing circumstances during the CPS, the WBG did not avail itself of the opportunity to revise CPS goals midstream**. In particular, the Bank team could have used the Progress Report more effectively to adjust the cumbersome results framework. That did not happen in part because of unexpected personnel shifts during Progress Report preparation.

- **Coordination with development partners was continuous and effective**. As a middle income EU candidate country, fYR Macedonia has a relatively small number of active development partners, with most bilateral donors cutting back on their presence over time. Donor coordination is managed by the Government through the Ministry of Finance and Secretariat for European Integration. The World Bank team maintained regular contact with these coordinating bodies and actively participated in development partner coordination/information sharing events, including as part of the new CPS preparation.

## V. LESSONS AND SUGGESTIONS FOR FY15-18 CPS

48. **The Bank is the partner of choice for the Government in carrying out complex reforms, as shown by the World Bank Client Survey 2014 and analysis of the implementation of the FY11-14 CPS.** The Bank must build on the experience of this partnership while continuing to engage with the Government focusing on the areas where it can have the greatest leverage pursuing its goals of reducing poverty and sharing prosperity. The Client Survey also points to the need to broaden the engagement with stakeholders outside the Government and to put more emphasis on promoting openness and availability of information. The following key lessons should be taken into account in the design of the FY15-18 CPS.

- **Close alignment with Government objectives, and those of key partners, was important to the success of the WBG program.** Alignment of CPS strategic goals with the EU regional strategy provided a basis for successful WBG interaction with the EU, particularly on the improvement of IPA funds absorption, as well as with other development partners.

- **The WBG should maintain its strategic focus on inclusion and sharing the fruits of economic growth.** Despite a number of encouraging results in the First Pillar, it is not known whether economic growth has resulted in improvements in living conditions, and if it has, how these improvements were distributed. Reliable data on the living conditions of the poorer segments of society and the structure and dynamics of poverty is largely unavailable. As a result, the Inclusiveness Pillar has been the most challenging both for the Government and the WBG in terms of achieving results and assessing the effectiveness of interventions.

- **The next CPS should focus on fewer outcomes, monitored by observable indicators.** The large number of outcomes in the CPS results framework made it hard to use as a practical tool for dynamic monitoring and adjustment, and complicated focusing on key priorities.

- **High-level policy dialogue was crucial for achieving a number of outcomes,** particularly in the area of improving the land market and agricultural subsidies.

- **The Bank should continue to factor the goals of EU integration and more effective use of IPA funds into operational design and implementation support.** As MSIP demonstrated, Bank projects can facilitate access to and help channel substantial EU funds for which the country is eligible.

- **The Government's commitment and flexibility proved crucial to the success of the IFC PPP mandates.**

- **IFC experience in the energy sector suggests that new projects in the renewable energy sector should continue to be implemented through strong intra-WBG coordination and, where appropriate, joint WBG engagement.**

**Table 1. Summary of CAS Program Self-evaluation**

| CPS Outcomes/Cluster of Outcomes and Outcome Indicators | Status and Evaluation Summary | Lending and Non-lending Activities that contributed to the Outcome | Lessons and suggestions for the new CPS |
|---|---|---|---|
| ***Pillar I. Faster Growth: Competitiveness*** | | | |
| **Promote fiscal, macroeconomic and financial sector stability** | | | |
| Maintain macroeconomic stability through sound management of fiscal conditions, as indicated by:<br>- general Government debt maintained below roughly 40 percent of GDP (baseline: 23.8 percent in 2009)<br><br><br><br><br><br>- arrears in the public health sector maintained at or below 0.2 percent of GDP (baseline: 0.3 percent in 2009) | **Achieved.** According to the Government data, central Government debt as percent of GDP was:<br>2010: 24.6<br>2011: 28.2<br>2012: 34.3<br>2013: 35.5 (estimate)<br>(Note: general Government debt includes central and municipal Government debts. According to GoM, municipal Government debt is about 0.2 percent of GDP)<br>**Not Achieved.** According to information from the Health Insurance Fund (HIF) Arrears in public health (HIF and health care institutions) have grown:<br>2010: 1.3 bill. (or 0.3 percent of GDP)<br>2011: 1.4 bill. (or 0.3 percent of GDP)<br>2012: 2.1 bill. (or 0.5 percent of GDP)<br>2013: as of end August 2.3 bill (or 0.5 percent of the estimated GDP).<br>The arrears come almost exclusively from hospitals. However, the expected result in the FY12 PBG was that arrears in the public health will not exceed MKD 1.7 bill. (or 0.4 percent of GDP) in 2011. This target was | FY11 Second Development Policy Loan (DPL)<br>FY12 Policy Based Guarantee (PBG)<br>FY 13 Public Expenditure Policy Based Guarantee | This outcome was affected by the European financial crisis which cannot have been taken into consideration at the time the strategy was adopted. The Bank could have used the opportunity to re-evaluate this outcome at progress report stage, but did not do so. When the 2012 PBG was being prepared, a different outcome was agreed upon. The PBG outcome was met. At the same time, the unachieved objective to reduce public health arrears points in the direction of an unresolved problem on which the Bank may continue to engage with the Government. |

| CPS Outcomes/Cluster of Outcomes and Outcome Indicators | Status and Evaluation Summary | Lending and Non-lending Activities that contributed to the Outcome | Lessons and suggestions for the new CPS |
|---|---|---|---|
| | **achieved** thanks to the health sector reforms which rationalized spending by healthcare institutions and improved their efficiency, such as the introduction of centralized international procurement and adoption of a methodology for setting reference prices for registered drugs. | | |
| - spending on pensions maintained at or below 9 percent of GDP up to 2012 (Baseline 8.5 percent in 2011) | **Achieved.** Pensions spending in 2012 was 8.9 percent of GDP. Instituted pension reforms, including parametric changes to the First Pillar of the Pension Fund, incurred overall cost savings which contributed to maintaining pensions spending below 9 percent. Further changes to the Pension and Disability Insurance Law were adopted to improve the fiscal sustainability of the pension system. | | |
| Strengthen the transparency of corporate financial reporting in line with EU standards. | **Achieved.** The 2014 EC Annual Progress Report noted satisfactory progress in the area of corporate and financial reporting. Macedonian professional association of accountants was admitted to the International Federation of Accountants, which will help ensure reporting in line with EU standards. | FY11-14 Programmatic Western Balkans Financial Sector TA<br>FY11 Regional REPARIS | Alignment of objectives of the Bank, client and other constituencies within the country contributed to the success of these operations. |
| **Strengthen the competitiveness and business environment, focusing on investment in enterprise development, FDI and exports, land administration, judicial services, access to finance, land, and skills development** | | | |
| The institutional framework for FDI attraction and export promotion to be enhanced and small and medium enterprise (SME) development programs to be consolidated. | **Achieved.** A one-stop shop service for issuing licenses, construction permits, state aid and aftercare has been established for enterprises at the Technology Industrial Development Zones.<br>A Strategy for Export Promotion and | FY12 Competitiveness DPL | |

| CPS Outcomes/Cluster of Outcomes and Outcome Indicators | Status and Evaluation Summary | Lending and Non-lending Activities that contributed to the Outcome | Lessons and suggestions for the new CPS |
|---|---|---|---|
| | Action Plan has been adopted, and the first generation of programs to support exporters is under implementation. The SME support programs at the Ministry of Economy have been consolidated on the basis of a functional review. | | |
| Increase the capacity to design and implement technology and innovation programs through the development of a more effective institutional framework and regulations. | **Achieved.** The Government adopted the Innovation Strategy and conducted a functional review leading to a reform of innovation-related institutions. | FY12 Western Balkan Programmatic Innovation Study | |
| Improve the efficiency and transparency of land administration, as indicated by:<br><br>- Increase in land and real estate transactions (baseline: 93,240 in 2009; target 120,000 in 2014).<br><br>- 20 percent increase in registered mortgages using property as collateral by mid-2015 (baseline 6,261 registered mortgages using property as collateral in 2009)<br><br>- Increase in customer satisfaction with the efficiency of land administration (baseline: 3.7 rating on a 1 to 5 scale in 2009; target: rating of 4 by 2015). | **Achieved.** All milestones have been achieved or exceeded. Projects are on target for achieving projected outcomes for 2014 and 2015. In addition to projected outcomes, the cadastre agency developed a Strategy on national spatial data infrastructure in line with EU requirements.<br><br>In 2012 138,000 real estate transactions were registered, which exceeds the target.<br><br>There was a 64 percent increase in registered mortgages using property as collateral between 2009 and 2012. Thus, the target was achieved ahead of schedule.<br>There was a slight decrease in customer satisfaction from 3.7 in 2009 to 3.6 in 2012. | FY10 Additional Financing: Real Estate Cadastre and Registration Project. | Project activities fully integrated with the strategic and mid-term business plans of the implementing agency ensure full ownership, smooth implementation, and timely achievement of anticipated results.<br><br>While being an excellent mechanism to evaluate project impact on the ground, customer surveys sometimes reflect more the opinion based on other, project external, factors, and therefore may not be relevant to assessing the project. A trend of declining citizens' satisfaction with Government services in general was noticed in the region over the past few years. This trend has been related to the prolonged impact of financial crises. Customer satisfaction should not figure as a project outcome unless the project |

| **CPS Outcomes/Cluster of Outcomes and Outcome Indicators** | **Status and Evaluation Summary** | **Lending and Non-lending Activities that contributed to the Outcome** | **Lessons and suggestions for the new CPS** |
|---|---|---|---|
| | | | explicitly addresses this aspect of service delivery. |
| - Cadastre maps digitized and posted online (baseline: maps covering 10 percent of territory in 2010; target: maps covering 50 percent of territory digitized and posted online by 2014 and 70 percent by mid-2015). | Cadastre maps digitized and used for delivery of routine services at 22 percent of the country's territory as of 2013. Project on target to achieve 70 percent by mid-2015. | | Digitization requires uninterrupted loan disbursement. This project could have been accomplished more efficiently had it not been for the imposition of the budget ceiling in 2012. The Bank should try to anticipate potential disruptions to ensure uninterrupted disbursement in such projects. |
| Improve the efficiency and services of the judiciary as indicated by:<br>- Decrease in the share of firms reporting the judiciary as a problem for doing business (baseline: 50 percent in 2008 BEEPS; target: 43 percent in 2011) | **Achieved.** BEEPS report is not available and the share of firms reporting judiciary as a problem in 2011 is not known. The team has used other indicators to gage the efficiency of judiciary service to business: the number of days to enforce a contract was reduced from 370 to 60 days as evidenced in Doing Business report; one third of court houses in the country have been modernized; ICT case management system was introduced; and a new Criminal Court was built in the capital city. | FY06 Legal and Judicial Implementation & Institutional Support Project | The improvement of courts' efficiency was largely due to the introduction of the ICT case management system, and this experience could be extended to other areas of public administration where establishing of a common ICT platform could streamline and facilitate the provision of administrative services more generally. On the other hand, the efficiency agenda in the judiciary sector is far from over. In the future the focus should shift to improving quality of services through better planning, thoughtful capacity building and greater transparency and public oversight. |
| Enhance access of SMEs to financing in key growth sectors. | **Achieved.** Financing provided to commercial bank programs supporting SMEs, particularly in agribusiness, health, and construction. | FY12 Competitiveness DPL<br>**<u>IFC</u>**: Finance and Advisory Services Supporting SMEs | |
| Strengthen the sustainability of the higher | **Mostly achieved.** The legislative | FY11, FY12 Higher Education | The TA has helped a lot in |

| CPS Outcomes/Cluster of Outcomes and Outcome Indicators | Status and Evaluation Summary | Lending and Non-lending Activities that contributed to the Outcome | Lessons and suggestions for the new CPS |
|---|---|---|---|
| education system and quality assurance in line with EU standards. | framework on quality assurance in higher education system was amended to align it with EU standards, the envisaged reforms will be implemented through Skills and Innovation Project. Higher education funding model has been defined and will be implemented through the Skills and Innovation Project. | TA | underpinning the new investment project in education. Two-years-long TA project in the high stake and sensitive areas, such as financing and quality assurance of education, cannot result in implementation of agreed reforms without further financial and TA support. |
| Simplify the process of obtaining visa, residence and work permits (baseline: 45 days required to obtain visa and work permit; target: reduction at least by 10 percent, to 40 days, by 2014). | **Achieved.** The time for the issuing of work permits was shortened to 30 days. Amendments to the Law on Foreigners and the Law on Employment and Work of Foreigners of July 2012, January 2013 and October 2013 simplified the process of granting residence and work permits to foreign employees of foreign-owned companies.<br><br>Obtaining of residence permits for long-term foreign workers has been also facilitated by the provision to grant temporary residence permits to citizens of EU and OECD countries who own property of at least 40,000 € value in Macedonia. | FY12 Competitiveness DPL | The changes in the area of regulating residence and employment of foreign nationals in Macedonia have been incremental, and there is much room for improvement in this area, particularly with the purpose of attracting highly skilled labor and stimulating knowledge and skills spillovers. An assessment of the regulatory constraints in this area in 2012 suggested the introduction of EU Blue Card type of program. |
| **Improve infrastructure to catalyze economic growth, particularly in transport** | | | |
| Improve the quality of the local and regional road network, as indicated by decrease in vehicle operation costs on rehabilitated roads by 10 percent by 2013. (Baseline: 100 percent in 2008) | **Mostly achieved.** The measurement of vehicle operation costs reduction will commence following the completion of road rehabilitation work. Planned road rehabilitation has been mostly achieved. Baseline: 48 km of regional roads rehabilitated in 2010; targets: 280km of regional and | FY08 Regional & Local Roads Program Support Project. | Road safety measures and climate resilience elements should be integrated in road designs.<br><br>Implementing agency should continuously carry out capacity building activities to improve contract management skills of staff. |

| CPS Outcomes/Cluster of Outcomes and Outcome Indicators | Status and Evaluation Summary | Lending and Non-lending Activities that contributed to the Outcome | Lessons and suggestions for the new CPS |
|---|---|---|---|
| | 420 km of local roads rehabilitated by 2013. 284km of regional and 322km of local roads were rehabilitated. | | All Bank projects should consider the need and implementing agency's capacity for monitoring and evaluation. Where necessary, Bank projects should include support for providing evaluation framework and establishing a monitoring system within the implementing agency as an integral part of the operation. |
| Facilitate regional trade by removing bottlenecks at border crossings, as indicated by decrease in waiting time for cars and buses at the border crossing point with Kosovo (baseline average waiting time per vehicle at entrance – 10 minutes (6 vehicles per hour), at exit – 12 minutes (5 vehicles per hour); target: decrease in waiting time by end 2012). | **Achieved.** Significant decrease in border crossing times achieved (entrance: average waiting time per vehicle 2.5 minutes; exit – just under 2 minutes per vehicle). | FY07 Second Trade & Transport Facilitation Project | Investments in border infrastructure should be coupled with softer trade facilitation measures (might include streamlining border procedures, introducing or widening the use of customs processing systems using IT and improving inter-institutional communication). Such trade facilitation measures are not costly, but can have substantial impact on costs of moving freight. |
| Strengthen fYR Macedonia's energy security as indicated by:<br>- reduction of number and duration of energy interruptions by 80 percent (Baseline: 1480 minutes in 2005), and<br><br>- reduction of substation operating and maintenance cost by 25 percent for the unbundled stations by 2014. | **Mostly achieved.** Energy interruptions have been reduced through upgrading of Skopje 5 substation and construction of Greece interconnection. The full effect of interruption reduction will be achieved after the completion of Skopje – Tetovo and Bitola 3-4 lines by November 2015.<br><br>**Achieved.** The rehabilitation of twenty-one 110kV substations resulted in around 25 percent reduction of operation and management costs. | FY06 ECSEE APL3 and FY11 Additional Financing | Land acquisition for infrastructure projects needs to start early and be well coordinated across the involved GoM entities. Time for this process, which must take place either before the project or during its initial stages, needs to be factored into the project design. |

| CPS Outcomes/Cluster of Outcomes and Outcome Indicators | Status and Evaluation Summary | Lending and Non-lending Activities that contributed to the Outcome | Lessons and suggestions for the new CPS |
|---|---|---|---|
| **Strengthen municipal services and infrastructure** | | | |
| Improve transparency, financial sustainability and delivery of municipal services as indicated by:<br>- Involvement of all targeted municipalities in benchmarking exercises. Indicator: involved municipalities. (Baseline: nil in 2010; target: 100 percent in 2014)<br><br>- 75 percent of participating municipalities to report improvements in the delivery of services by 2017. Indicator: number of municipalities reporting improvements. (Baseline: 0 in 2010, target: 2 in 2013, 4 in 2014, 8 in 2017.)<br><br>- Targeted municipalities to achieve increased revenue or cost savings Indicator: percentage of municipalities achieving increased revenue or cost savings (baseline: 0 in 2010; target: 20 percent in 2013, 30 percent in 2014, 60 percent in 2017.) | **Achieved.** All targeted communal enterprises participate in benchmarking exercises.<br><br>**Achieved** and ahead of schedule to achieve 2017 goal. 73 percent of participating municipalities reported improvements by December 2013.<br><br>**Achieved** and on target to achieve 2017 goal. By June 2013 46 percent of participating municipalities achieved increased revenue or cost savings.<br><br>All participating 30 municipalities have demonstrated increased transparency and accountability practices whereas one third (10 municipalities) have undertaken additional institutional reforms in response to performance grants administration mechanism. | FY09 Municipal Services Improvement Project (MSIP)<br><br>FY12 Additional Financing to MSIP | Demand driven multi-sector approach to small infrastructure financing is an excellent platform for providing additional finance and capacity building at the municipal level. MSIP grants are attractive to municipalities, because they are flexible. For a demand driven investment to succeed, the implementing agency needs to devote adequate time and resources to outreach and technical assistance to beneficiary municipalities. Eligibility criteria for access to lending provide incentives for municipalities to adopt higher standards of transparency and accountability. |
| ***Pillar II. More Inclusive Growth by Strengthening Employability and Social Protection*** | | | |
| **Increase employment, particularly among vulnerable groups** | | | |
| Lower the cost of employing workers to | **Mostly achieved.** SICs lowered to 27 | FY11 Development Policy Loan | The Bank should reevaluate this |

| CPS Outcomes/Cluster of Outcomes and Outcome Indicators | Status and Evaluation Summary | Lending and Non-lending Activities that contributed to the Outcome | Lessons and suggestions for the new CPS |
|---|---|---|---|
| businesses as indicated by a decrease in social insurance contributions (SICs), which represent a key component of the labor tax wedge. Indicator: social insurance contributions. Baseline: 28.4 percent of the gross wage in 2009; target: 22.5 percent by 2014. | percent of the gross wage. Although the full reduction was not achieved, this represents a considerable achievement given the EU economic crisis. Financial sustainability of the social funds was maintained. The second stage of the GoM's payroll tax reform was implemented. Although the reform was stalled, the tax base was broadened, the income bases for SICs have been harmonized and the gross wage was introduced as the basis for calculating SICs in 2009. | 2 | target in relation to the global economic crisis and decide whether policy dialogue with the Government regarding further reduction of the social insurance contributions should continue, and if not, under what conditions it may be resumed. |
| **Strengthen the efficiency of the social safety net, including improved targeting of cash benefits** | | | |
| Strengthen the targeting and coverage of fYR Macedonia's social services as indicated by:<br>- Increase in the targeting accuracy of the overall safety net (baseline: 50 percent in 2010; target: 65 percent by 2014).<br><br>- Enroll 40 percent of households in the poorest quintile in the Government's CCT program by 2014. | **Not verified,** as survey data has not been reliable. The overall accuracy of safety nets targeting has been difficult to measure due to inconsistencies in data coming from the Household Budget Survey (HBS). The Statistical Office will provide the data to measure this with the SILC (2011 and 2012 data expected by the end of 2014) and the team will then assess the appropriateness of this indicator.<br>**Achieved.** The current percentage of the CCT program coverage is 86 percent of eligible households. Eligible households are households with children aged 15-18 or older in full-time secondary education receiving social financial assistance (SFA). Due to the unavailability of data on the poorest quintile, the indicator for Conditional Cash Transfer Project was modified after | FY09 Conditional Cash Transfer Project<br><br>FY11 Development Policy Loan 2 | The GoM needs assistance and capacity building in administration and analysis of large scale surveys. It is hard to measure the success of the reforms and Bank projects without a reliable source of data. The Bank needs to devote more effort to providing support to the Government in this area while continuing to stress the importance of data for evidence-based policy-making. |

| CPS Outcomes/Cluster of Outcomes and Outcome Indicators | Status and Evaluation Summary | Lending and Non-lending Activities that contributed to the Outcome | Lessons and suggestions for the new CPS |
|---|---|---|---|
| | CPSPR to take into account the fact that households for CCT program were chosen from households receiving SFA. | | |
| ***Pillar III. Greener Growth: Environmental Sustainability and Climate Action*** | | | |
| **Strengthen knowledge base for policymaking in green growth and climate action** | | | |
| Enhance the Government's knowledge of approaches to the management of green growth agenda, particularly by adapting sectors to evolving constraints and opportunities. | **Achieved**. Policy Notes assessing green growth and climate change challenges in energy supply, energy efficiency, transport, urban, social dimensions, water, agriculture, air pollution, infrastructure adaptation, and public investment and macroeconomic growth developed and presented to and discussed with the Government during multiple meetings of the high-level National Council for Sustainable Development (NCSD).<br>Senior adviser to NCSD was provided to assist in the development of an action plan for implementation of the National Strategy for Sustainable Development in the Secretariat for the NCSD and to support institutional strengthening of NCSD-related inter-ministerial coordination processes and key sector agencies.<br>Government is to revise and approve a new Action Plan for Sustainable Development that will set priorities and guide investments and policies. | Policy Notes in Energy, Energy Efficiency, Transport, Urban, Social Dimensions, Water, Agriculture, Air Pollution, Infrastructure Adaptation, and Public Investment and Macroeconomic Growth (multiple FYs)<br><br>FY13 Green Growth and Climate Change Analytic Study<br><br>Non-lending technical assistance including workshops on water analysis, macroeconomic modeling, and energy efficiency assessment. | |
| Increase in catastrophe insurance penetration to 5 percent by 2014. (Baseline: 2 percent in 2011.) | **Mostly Achieved.** Europa Re has been launched, and it is expected that the target will be achieved in the | FY12 SEEC CRIF | Introduction of new concepts requires a longer preparation phase. While the project is well on its way |

| CPS Outcomes/Cluster of Outcomes and Outcome Indicators | Status and Evaluation Summary | Lending and Non-lending Activities that contributed to the Outcome | Lessons and suggestions for the new CPS |
|---|---|---|---|
| | course of 2014. Longer than expected time was needed for capitalization and establishment of Europa Re reinsurance facility. | | to achieve the target, the timeline has been skewed because of the need to properly introduce the concept to the Government and capitalize Europa Re. The Bank should use more conservative estimates of the time required for ground-breaking activities. |
| **Improve the efficiency of the energy sector and environmental sustainability, particularly by exploiting renewable energy and energy efficiency sources** | | | |
| Strengthen fYR Macedonia's energy security by upgrading select domestic and regional transmission infrastructure including (i) Skopje – Tetovo and (ii) Stip – Serbian border, and the rehabilitation of twenty-one 110kV substations. | **Mostly Achieved.** Original project targets have been met, and FY11 Additional Financing targets are expected to be met by November 2015. Electrical transmission line between Bitola and Greece has been completed. After delays due to land acquisition issues, the project is on track to complete the lines (i) Skopje - Tetovo, and (ii) Stip - Serbian border on time. Twenty-one 110kV substations were rehabilitated. | FY06 ECSEE APL3 and FY11 Additional Financing | Land acquisition for infrastructure projects needs to start early and be well coordinated across the involved Government entities. |
| To derive energy from "new" renewable energy sources and increase their share in national energy supply. Indicator: energy supplied from renewable sources. (Baseline: 0 in 2010; target: 6 MW by 2011, and 40 MW by 2013.) | **Achieved**. 111.3 MW renewable energy by September 2013. Regulatory framework updated to facilitate renewable energy projects, including feed-in tariffs and rules on interconnection. | FY07 Sustainable Energy Project (GEF) | Renewable energy targets can be achieved through comprehensive institutional support including regulatory measures, such as well-tailored feed-in-tariffs and financial facilitation. |
| Improve the efficiency of fYR Macedonia's energy use as indicated by energy savings (lifetime basis) attributable to new energy efficiency projects, primarily in the public sector of 100 GWh by 2014 (baseline 0 in 2013). | **Achieved.** Public sector buildings have been retrofitted to higher energy efficiency standards. 112 GWh in lifetime savings achieved. | FY07 Sustainable Energy Project (GEF) | There are big opportunities for public sector energy efficiency in Macedonia. The Bank should support the GoM in a National Program for Energy Efficiency in Public Buildings that would contribute to sustainable growth. |
| **Strengthen management of water resources in line with EU directives** | | | |

| **CPS Outcomes/Cluster of Outcomes and Outcome Indicators** | **Status and Evaluation Summary** | **Lending and Non-lending Activities that contributed to the Outcome** | **Lessons and suggestions for the new CPS** |
|---|---|---|---|
| Strengthen the management of water resources, particularly in agriculture, as indicated by improved cost recovery in new Water Economies. The collection rate of water fees to reach at least 60 percent for all Water Economies in 2012 (baseline: varied rates from 11 percent to 90 percent in 2010). | **Achieved.** 2012 collection rate for all Water Economies was 80 percent or higher. The expectation for 2013 is between 80 and 90 percent.<br><br>New Water Economies were established ahead of schedule. All Water Economies were structured according to the new law in line with EU directives. Comprehensive assessment of water management challenges in diverse sectors was undertaken, and recommendations developed taking into account threats from climate change.<br><br>Working Note on Methods and Preliminary Results of the Water Sector Analysis was prepared and presented to the GoM under Macedonia Green Growth and Climate Change Program | FY07 Agriculture Strengthening and Accession Project<br><br>FY10 Water Sector Capacity Assessment | A successful mechanism for ensuring a high rate of water fees collection was established: subsidies to individual farmers and whole Water Economies were made conditional on the payment of water fees. The improvement of services was identified as another factor in increasing the rate of fee collection. Improving accountability and communication was key to improving water management. Boards of the Water Economies were expanded to include a member from the Ministry of Agriculture, and this increased their accountability not only to the users, but also to the central Government. The communication lines between Water Economies and the Ministry are improved, and as a result of this, the Ministry is better informed of issues in the irrigation sector. |
| **Strengthen the competitiveness of the agriculture sector, including improvements in the agricultural subsidies and land market and adapting practices to climate change and EU requirements** | | | |
| Improve the delivery of Government assistance to the agricultural sector in a manner consistent with EU pre-accession requirements. | **Achieved.** IPARD accredited Paying Agency is fully functional and in compliance with EU standards.<br>Farm registry and land parcel identification system fully established, and quarterly reports published on key agricultural data.<br><br>While being used for administering budget subsidy funds for farmers, the established Paying Agency fully | FY07 Agriculture Strengthening & Accession Project | The partnership approach applied here has potential to be replicated. While supporting the goals of Macedonia's EU accession, the Bank must be more realistic about the timing of accession. If a future projects focuses on better absorption of pre-accession funds, it must include special components to help potential |

| CPS Outcomes/Cluster of Outcomes and Outcome Indicators | Status and Evaluation Summary | Lending and Non-lending Activities that contributed to the Outcome | Lessons and suggestions for the new CPS |
|---|---|---|---|
| | benefits from using a more efficient, effective and accountable way of transferring subsidies set up to satisfy the EU pre-accession criteria. | | beneficiaries with pre-accession fund applications and improve access to co-financing. |
| Improved management of state-owned agricultural land (baseline: €4.2 million in 2011, target: 20 percent higher rate of collection of lease payments on state-owned land by 2013). | **Mostly Achieved.** The data for 2013 is not yet available as payment deadline has been extended to June 2014. We therefore cannot definitively assess this outcome by the assigned indicator. 4,492,653.35€ was collected in 2012 and thus the DPL1 target of 4.4 million € was exceeded. This constitutes about 7 percent growth relative to the baseline of 2011. Even though the baseline number turned out to be rather high due to successful collection of arrears from large lease holders, there is a tendency of lease payments to grow, and we expect this trend to be sustained. Other significant improvements in the management of state-owned agricultural lands include the adoption of a centralized digital lease contracts register and the enactment of the Law on the Sale of Agricultural Land in State Ownership. The government's commitment to privatization is an exceptional development outcome. Privatization is a superior policy to improved lease collection for putting the 30 percent of country's arable land resources currently owned by the state to their best use. | FY12 Competitiveness DPL;<br>Land policy assessments and policy dialogue fostered by the Competitiveness DPL and TA extended through the MCIIP grant;<br>Strategic ARD Sector Support Engagement. | High level policy dialogue based on comprehensive ESW yielded this substantial policy advancement. |
| Stimulate productive agriculture investments by increasing the share of total | **Achieved**. The share of structural funds surpassed the targeted 25 | FY12 Competitiveness DPL;<br>Policy dialogue fostered by the | |

| CPS Outcomes/Cluster of Outcomes and Outcome Indicators | Status and Evaluation Summary | Lending and Non-lending Activities that contributed to the Outcome | Lessons and suggestions for the new CPS |
|---|---|---|---|
| subsidies allocated to structural measures from 10 percent (baseline in 2011) to 25 percent by 2013. | percent in the 2013 national agricultural support envelope. Multiannual Agricultural Support Program incorporating technical inputs from the Bank's agriculture competitiveness team was adopted by the Government. | DPL; ESW. | |

**Table 2. Planned Lending Program and Actual Deliveries (2011-2014)**

| CPS Plans (FY2011 – 2014) | | | Status | |
|---|---|---|---|---|
| **FY** | **Project** | **US$(M) IBRD** | **Project** | **US$(M) IBRD** |
| | | | | |
| 2011 | Programmatic Development Policy Loan<br>Additional Financing (ECSEE APL3)<br>Disaster Management (CRIF) | 30<br>19<br>5 | PBG 1 (former DPL – Completed)<br>Additional Financing (ECSEE APL3)<br>Disaster Management (CRIF) | 134.9<br>19<br>5 |
| Subtotal | | 54 | | 54 |
| 2012 | Additional Financing (MSIP) | 50 | Additional Financing (MSIP) | 50 |
| Subtotal | | 50 | | 50 |
| 2013 | Competitiveness DPL 1 | 50 | Competitiveness DPL 1 (Completed) | 50 |
| | Public Expenditure PBG | 50 | Public Expenditure PBG 2 (Completed) | 201.5 |
| | Lukovo Pole Project | 50 | Forwarded to next CPS | |
| Subtotal | | 150 | | 251.5 |
| 2014 | Competitiveness DPL 2 | 50 | Competitiveness DPL 2 | 50 |
| | Skills Project | 24 | Skills Project | 24 |
| | | | | |
| Subtotal | | 74 | | 74 |
| | Total | 328 | Total | 534.4 |

**Table 2a. Investment Lending & Budget Support**

| CPS FY 2011 – 2014 | Planned US$(M) | Status US$(M) |
|---|---|---|
| New Investment Lending | 148 | 98 |
| Policy Based Guarantees | 80 | 336.4 |
| Development Policy Loans | 100 | 100 |
| Total Lending | 328 | 534.4 |

**Table 3. Planned Non lending Services and Actual Deliveries (2011-2014)**

| **CAS PLANS (September 2010)** | | **STATUS** |
|---|---|---|
| **2011** | Regional REPARIS | Actual |
| | Higher Education TA | Completed in FY 2012 |
| | Energy Efficiency TA | Dropped |
| | Green Growth Analytical and Advisory Program (incl. TF) | Completed in FY 2013 |
| | Western Balkans Programmatic Poverty Assessment (FY11-14) | Completed in FY 2013 |
| | Accounting and Auditing ROSC Macedonia | Actual |
| | Labor Market Reform TA | Completed in FY 2013 |
| | Reducing vulnerability to Climate Change in Agriculture TA | Completed in FY 2014 |
| | Modular Competitiveness Assessment (TF) | Completed in FY 2012 |
| | Western Balkans Programmatic Financial Sector (FY11-14) | Actual (renamed Western Balkans Financial Sector Development TA Facility (FY11-14) |
| | National Procurement Study | Dropped |
| | Green Growth and Climate Change TA | Actual |
| | Water Capacity Bldg. TA | Completed in FY 2012 (renamed Comprehensive Water Sector Assessment) |
| **PROGRESS REPORT PLANS (1 November 2012)** | | **STATUS** |
| **2013** | Agricultural PER (FY12-13) | Completed in FY 2013 |
| | Strategic ARD Sector Support TA | Completed in FY2014 |
| | IDF Public Accounting | Completed in FY 2010 |
| | FIRST (TF) (FY12-13) | Completed in FY 2013 |
| | Infrastructure Review | Actual |
| | Skills Survey | Completed in FY 2012 |
| | PSIA Health | Dropped |
| | Poverty and Social Impact Assessment (PSIA) TF (for Competitiveness DPL) | Completed in FY 2013 |
| | Open Government (TF) | Actual (renamed: Macedonia ICT TA) |
| | Labor Market Review (FY12-13) | Completed in FY 2013 |
| | Health Policy TA | Dropped |
| | IFC Financial Sector | Completed in FY 2012 |

| **CAS PLANS (September 2010)** | | **STATUS** |
|---|---|---|
| | IFC Real Sector | Completed in FY 2012 |
| | IFC Food Safety Advisory | Actual |
| | IFC PPP Advisory Services: Waste Management in Drisla Municipality | Dropped |
| **2014** | Statistics TA | Completed in FY2012 |
| | Public Sector IT | Actual |
| | IFC PPP Transaction Advisory (hydro power) | Actual |
| | IFC PPP Transaction Advisory (outpatient hemodialysis) | Closed in FY 2014 |
| | IFC PPP Advisory Services: Water management in Ohrid/Struga Municipalities | Dropped |
| | ***Additional Activity**:* | |
| | IFC PPP Transaction Advisory (Transport) | Actual |
| **PROGRESS REPORT PLANS (1 November 2012) – Regional Western Balkans AAA** | | **STATUS** |
| | Monitoring and Evaluation | Actual (renamed M&E Capacity Development) |
| | Western Balkans Regional Study on Innovation | Completed in FY 2014 (renamed WB Regional R&D Study on Innovation) |
| | Programmatic Financial Sector Development | Completed in FY 2012 |
| | Programmatic Gender Monitoring | Completed in FY 2013 (Renamed |
| | Programmatic Poverty Monitoring | Postponed |
| | Smart Safety Nets | Actual (renamed ECCU4 Activation and Smart Safety Nets) |
| | Public Financial Management/PEFA (EC TF) | Actual |
| | Health Finance | Dropped before a code was assigned |
| | Employment and Jobs | Actual (renamed Meeting the Jobs Challenges in the Western Balkans ) |
| | Energy Strategy | Dropped |
| | IFC Trade Logistics | Actual (renamed: IFC Western Balkans Trade Logistics Project) |
| | IFC Renewable Energy Advisory | Actual (renamed: IFC Balkan Renewable Energy Program) |
| | IFC ECA Corporate Governance | Actual |

## Annex 3: Sources of Growth Diagnostic

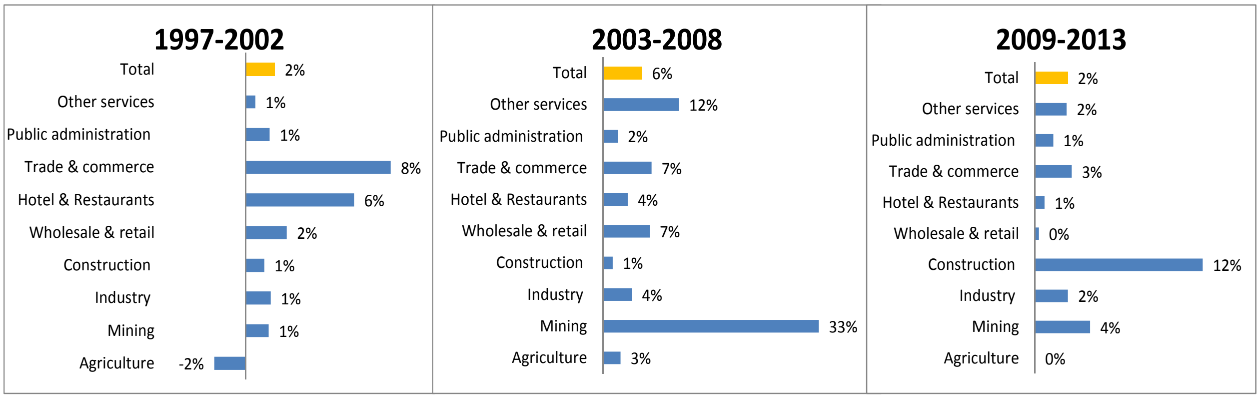
**FYR Macedonia is a small, landlocked and open economy with a sound track record of macro-fiscal stability.** With an openness indicator[34] of 126.3 percent in 2013, it is the most open among the countries of South East Europe (SEE6)[35], although still relatively weak by European and global standards. FYR Macedonia has been able to preserve macroeconomic stability in the presence of adverse shocks. Its exchange rate peg to the Euro, introduced in 1995, has successfully supported price stability, with inflation averaging 2.4 percent over the last 10 years. Macroeconomic policies have been geared towards keeping the external balance manageable, and monetary policy has responded quickly to any possible threats to the peg. General government debt, which reached 36.0 percent of GDP at the end of 2013, remains the fifth lowest among the EU and SEE6 countries. Growth volatility has been low by regional standards, but so has growth.

**Growth would need to accelerate for fYR Macedonia to close its income gap with the new EU member states.** Between 2002 and 2009, fYR Macedonia grew at 3.9 percent annually in real terms which – though below the SEE6 average – enabled fYR Macedonia to reduce the income gap with the EU. Between 2002 and 2009, fYR Macedonia's GDP per capita in international dollars grew from 25 percent of the EU's GDP per capita in international dollars to 36 percent in 2009. Since then, fYR Macedonia's average GDP growth has declined to 2.1 percent per year and convergence to the EU has stalled. Real GDP growth would need to accelerate to around 4.5 percent – which is significantly above the ten-year average annual growth rate of 3.2 percent – for fYR Macedonia to converge to the living standards of the new EU member states within the next 20 years.

**FYR Macedonia's sectoral drivers of growth have changed noticeably over the past 15 years, with trade and commerce declining and construction taking over as the fastest growing sector.** Prior to 2002, more than 80 percent of growth was driven by trade and commerce, industry, wholesale and retail. Since 2002, growth in trade and commerce has significantly declined while industrial growth has remained broadly constant. Since 2009, the construction sector has become the predominant driver of growth as the public sector scaled up capital spending to counterbalance the decline in external demand due to the Euro zone crisis. This seems to have come at the expense of deterioration in the quality of public investment: the share of investment in administrative buildings increased at the expense of investment in infrastructure and maintenance[36], and investment into sectors with a long-term growth potential such as machinery, agriculture and transport equipment also declined. Since 2009, agricultural growth has been zero.

[34] The openness indicator is defined as the sum of imports and exports relative to the GDP.
[35] SEE countries include Albania, Bosnia and Herzegovina, Kosovo, Macedonia fYR, Montenegro and Serbia.
[36] In 2008, 85 percent of all public investment was destined to infrastructure while only 15 percent went to non-residential and residetial buildings. By 2012, investments in non-residential and residential buildings doubled as a share of total public investment, reaching 33 percent.

**Figure 3.1: Annualized growth rates by sector**

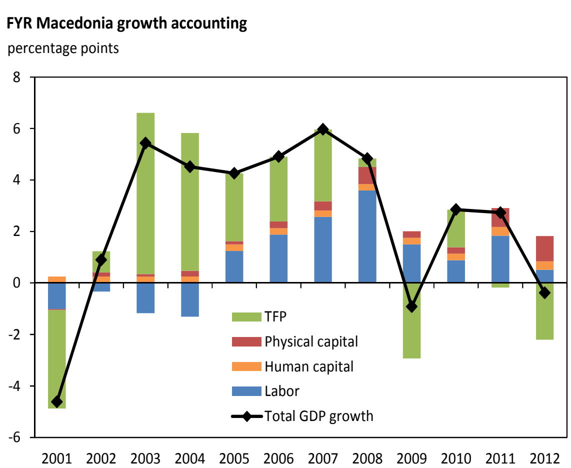



*Source:* State Statistics office and World Bank staff calculations

**FYR Macedonia's growth was driven by both employment and productivity gains before the crisis, but most job creation occurred in low-productivity sectors or in the public sector.** Despite a relatively large and rising capital share of income from 2001-2008 (between 40 and 50 percent), physical capital accumulation accounted for only 0.3 percentage points of the average annual 4.3 percent GDP growth between 2002 and 2008, whereas employment growth contributed 1 percentage point, and Total Factor Productivity (TFP) growth roughly 3 percentage points. After the 2008 crisis, productivity growth decelerated significantly while employment continued to grow. In fact, fYR Macedonia is the only SEE6 country where employment increased in the post-crisis period. Agriculture, construction and public administration have been the main drivers of employment growth over the last decade. However, the jobs created in the past years have been either informal, in low-productivity sectors or in the public sector: 27.1 percent of net jobs created between 2007 and 2011 have been in agriculture and 13 percent in retail trade (predominantly informal) and 19.7 percent in the public sector.

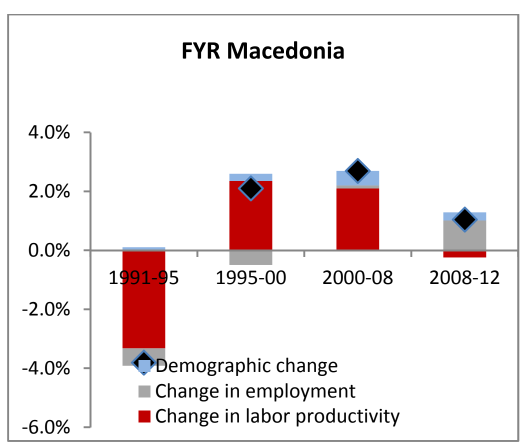
**Figure 3.2: Growth Decomposition**

**Growth accounting**




Source: State Statistical Office, World Bank estimates

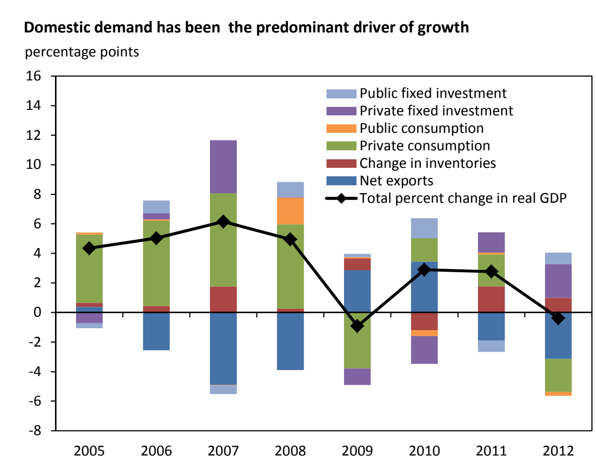
**Growth contribution of productivity growth**



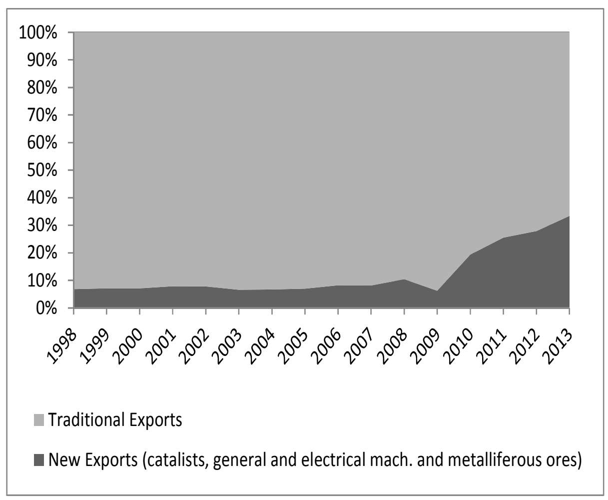
**Growth in the pre-crisis years was almost exclusively powered by domestic demand, engendering large and persistent trade deficits and increasing household indebtedness**. In the years leading up to the 2009 crisis, real GDP growth was underpinned by strong private consumption and rapidly increasing investment, both of which had a large import content and pushed the trade deficit from an already-large 18.4 percent of GDP in 2005 to over 26 percent by 2008. The trade deficit was largely financed by remittances which in turned fueled private consumptions. With their savings rates already exceptionally low, households resorted to borrowing to sustain high rates of private consumption, leading to a rapid rise in household debt, albeit from low levels by regional standards.[37] Since the crisis, however, household disposable income has made a modest recovery, benefitting from strengthening wage growth, increased social transfers as part of the crisis response, and an easing of the tax burden on personal income. At the same time, the uncertain economic environment has tempered household consumption, bringing it closer in line with disposable income and thus on a more anemic growth path given the still-weak labor market and persistently high unemployment. This renewed savings impetus has helped to stabilize the household debt ratio, which stood at 25.8 percent of disposable income at end-2012.

**Figure3.3: Demand composition of growth and change in export structure**

**Demand composition of growth**




**Export structure**




[37] Household debt climbed from a mere 10.4 percent of disposable income in 2005 to 27 percent by 2008.

## Table 1: Key macroeconomic indicators

Key Macroeconomic Indicators

| | 2010 | 2011 | 2012 | 2013 | Projections 2014 | 2015 | 2016 |
|---|---|---|---|---|---|---|---|
| **Real economy** | Annual percentage change, unless otherwise indicated | | | | | | |
| Nominal GDP (MKD billion) | 434.1 | 459.8 | 458.6 | 474.2 | 513.7 | 548.9 | 584.9 |
| Per capita GDP (USD, Atlas method) | 4543 | 5047 | 4634 | 4869 | 5129 | 5495 | 5802 |
| Real GDP | 2.9 | 2.8 | -0.4 | 3.1 | 3.0 | 3.5 | 3.7 |
| Contributions to growth (percentage points): | | | | | | | |
| Consumption | 1.2 | 2.3 | -1.5 | 2.5 | 1.1 | 2.4 | 2.2 |
| Investment | -1.7 | 2.2 | 3.9 | -3.0 | 3.0 | 2.4 | 2.2 |
| Net exports | 3.0 | -1.8 | -2.8 | 3.0 | -1.2 | -1.3 | -0.7 |
| Real imports | 9.5 | 10.4 | 4.2 | -2.1 | 8.2 | 8.0 | 6.8 |
| Real exports | 23.6 | 10.5 | 0.0 | 4.5 | 9.0 | 8.5 | 8.0 |
| Unemployment rate (percent, end-of-period) | 32.0 | 31.4 | 31.0 | 28.7 | – | – | – |
| **Prices** | | | | | | | |
| GDP deflator | 2.8 | 3.1 | 0.1 | 2.5 | 3.5 | 3.3 | 2.8 |
| CPI (end-of-period) | 3.1 | 2.8 | 4.7 | 1.5 | 2.5 | 2.3 | 2.1 |
| CPI (average) | 1.7 | 3.9 | 3.3 | 2.8 | 2.6 | 2.4 | 2.2 |
| **Fiscal accounts** | Percent of GDP, unless otherwise indicated | | | | | | |
| Revenues | 30.4 | 29.8 | 30.1 | 29.6 | 29.7 | 30.3 | 30.4 |
| Expenditures | 32.9 | 32.3 | 34.0 | 33.6 | 33.2 | 33.5 | 32.9 |
| Central government balance | -2.4 | -2.5 | -3.9 | -4.1 | -3.5 | -3.2 | -2.6 |
| Gross central government debt | 24.2 | 27.9 | 34.1 | 35.6 | 34.0 | 35.0 | 35.4 |
| Gross public sector debt 1/ | 27.8 | 32.1 | 39.2 | 43.2 | 44.3 | 47.2 | 49.0 |
| **Selected Monetary Accounts** | Annual percentage change, unless otherwise indicated | | | | | | |
| Base Money | 12.2 | 9.7 | 4.4 | 5.8 | 12.5 | 9.6 | 8.6 |
| Credit to private sector | 7.3 | 7.7 | 5.2 | 6.3 | 3.8 | 3.3 | 2.9 |
| **Balance of Payments** | Percent of GDP, unless otherwise indicated | | | | | | |
| Current account balance | -2.1 | -2.5 | -3.1 | -1.9 | -4.5 | -5.7 | -5.2 |
| Trade balance | -20.5 | -21.9 | -23.6 | -20.6 | -21.4 | -21.6 | -21.3 |
| Imports (BOP basis) | 65.4 | 74.5 | 76.3 | 73.4 | 76.2 | 78.0 | 79.2 |
| Exports (BOP basis) | 45.4 | 53.7 | 52.7 | 52.5 | 54.8 | 56.5 | 57.9 |
| Foreign direct investment (FDI) | 2.2 | 4.5 | 1.0 | 3.3 | 3.5 | 3.8 | 4.3 |
| Gross international reserves (US$ mn, eop) | 2277.8 | 2677.8 | 2892.9 | 2858.7 | 3162.0 | 3353.6 | 3681.5 |
| in months of next year's imports | 3.4 | 4.2 | 4.5 | 4.4 | 4.4 | 4.3 | 4.4 |
| in percent of short-term external debt | 130.6 | 152.7 | 139.6 | 128.9 | 139.5 | 144.7 | 155.5 |
| External debt 2/ | 58.2 | 61.7 | 67.3 | 67.7 | 66.6 | 65.4 | 64.4 |
| Exchange rate (MKD/USD, average) | 46.45 | 44.26 | 47.89 | 46.39 | 48.47 | 48.66 | 48.78 |
| **Memo items:** | | | | | | | |
| Nominal GDP (US$ million) | 9346 | 10388 | 9576 | 10221 | 10598 | 11281 | 11990 |

1/ Includes the debt of municipalities and public enterprises, but not the debt of the Central Bank (NBRM)

2/ Excludes Central Bank repo arrangements

Source: Macedonia State Statistical Office, Ministry of Finance, National Bank of Macedonia, World Bank staff estimates.

**As a small, open economy fYR Macedonia will have to rely on exports to sustain long-term growth.** Supported by an active strategy to promote Foreign Direct Investment (FDI), fYR Macedonia is shifting gradually to a more export-led growth model. In recent years, fYR

Macedonia has diversified its exports both in terms of products and destinations and increased the technological intensity of its export basket due to FDI. Most FDI-related exports are connected to the automobile industry and form part of global value chains, which insulates them somewhat from changes to the European import demand. Still, FDI as a share of GDP is smaller than in other SEE6 countries. Moreover, foreign firms have very limited linkages to domestic companies and their contribution to employment growth has so far been limited. This is expected to change as new, large FDI-related firms start their production. As the Euro zone recovers, fYR Macedonia's traditional labor-intensive exports (iron and steel products, apparel and clothing, which together account for more than 35 percent of all exports) are expected to accelerate. fYR Macedonia will need to further improve its competitiveness in order to boost its export potential by investing in infrastructure and improving trade logistics.

**Expansionary fiscal policy in the aftermath of the crisis led to a widening of the fiscal deficit and a rapid build-up in central government debt.** Revenues fell by over 3 percent of GDP between 2008 and 2011, as economic activity weakened and the Government reduced tax rates and social security contributions to boost competitiveness. Consequently, the fiscal deficit widened consecutively from 0.9 percent of GDP in 2008 to 2.5 percent in 2011, 3.9 percent in 2012 and 4.1 percent in 2013 and central government debt surged from 20.7 percent in 2008 to 35.8 percent by the end of 2013. At the same time, the Government shifted capital expenditure off-budget by transforming the former Road Fund into the Public Enterprise for State Roads (PESR), complicating fiscal management and weakening transparency. At inception, the PESR carried EUR82 million in debt (1.1 percent of GDP), but this is set to rise rapidly in the near term as the PESR executes what is fundamentally a central government investment agenda.

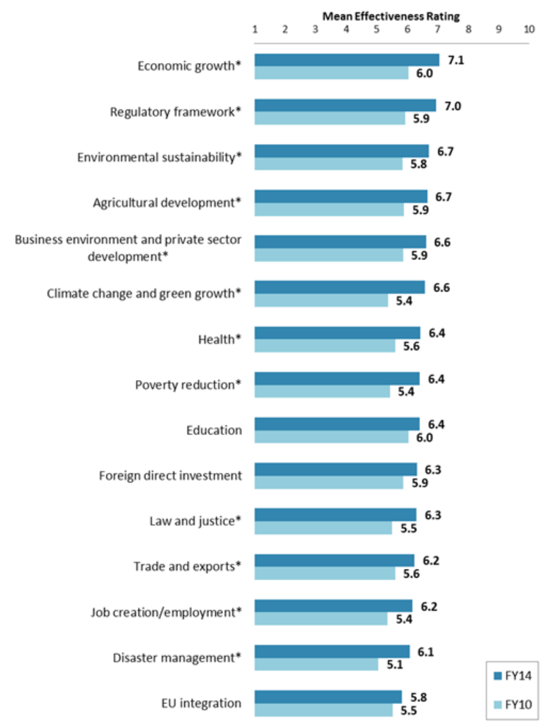
**The Government is pursuing an ambitious public investment program to boost fYR Macedonia's competitiveness, which is expected to lead to a rapid build-up in public debt.** As a landlocked and very open economy, fYR Macedonia is particularly dependent on a well-developed transport network for its economic and social development. At the same time, firms increasingly cite inadequate supply of infrastructure as a major constraint to growth[38]. The Government is therefore pursuing an ambitious investment program, which will be largely implemented by State-Owned Enterprises (SOEs), in particular, the PESR. Total public debt is set to rise rapidly over the medium-term even under the assumption that central government debt will stabilize.

[38] The 2013-14 Global Competitiveness Index ranks the quality of Roads in fYR Macedonia 111th out of 148 countries. While this is slightly better than regional neighbors (Serbia at 119th and Bulgaria at 112th), it lags well behind Albania (76th) and Montenegro (95th).

## Annex 4: FYR Macedonia Country Survey March 2014: Summary of Findings

From December 2013 to January 2014, stakeholders of the World Bank Group in fYR Macedonia were invited to provide their opinions on the Bank's assistance to the country by participating in a country survey. Paper questionnaires were sent to 843 potential respondents. Of those, 159 were completed with a representative of the fielding agency or were received and returned via post (19% response rate; all in Macedonian). Online questionnaires were sent to 23,000 potential respondents via email. Of those, 1,012 were completed (4% response rate; 950 in Macedonian and 62 in English).

The FY14 country survey demonstrates that views of the World Bank Group in fYR Macedonia are very positive, in particular with respect to the way the institution engages on the ground, its work in key sectors, and its overall relevance and alignment. The survey data also show that there are opportunities for improving effectiveness. Key findings are summarized below.



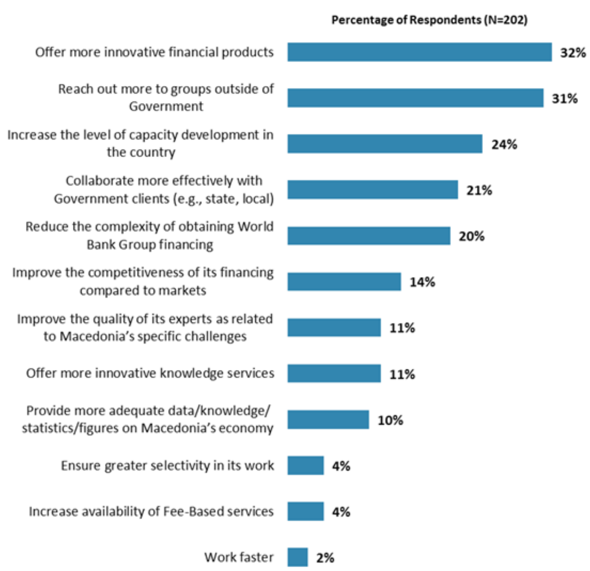
(*Significantly different between FY14 and FY10)

**Sector engagement:** Respondents named economic growth, agricultural development and business environment/ private sector development as the three most important areas for fYR Macedonia's development. Bank's work in all three of these sectors is seen as highly effective, with average ratings above 6. Since the last Country Survey in FY10, there has been an improvement in the assessment of the effectiveness of World Bank engagement in all comparable sector areas. Bank engagement on economic growth, regulatory framework, environmental sustainability and agriculture received the highest ratings for effectiveness. Engagement on climate change and growth also saw the largest improvements in the score from the past survey. In contrast, the effectiveness of Bank's work on EU integration received the least positive assessment (5.8 average rating) and the smallest improvement since FY10. The work on job creation and employment, a topic that is seen as crucial for fYR Macedonia's inclusive growth, also received a relatively lower rating of 6.2.

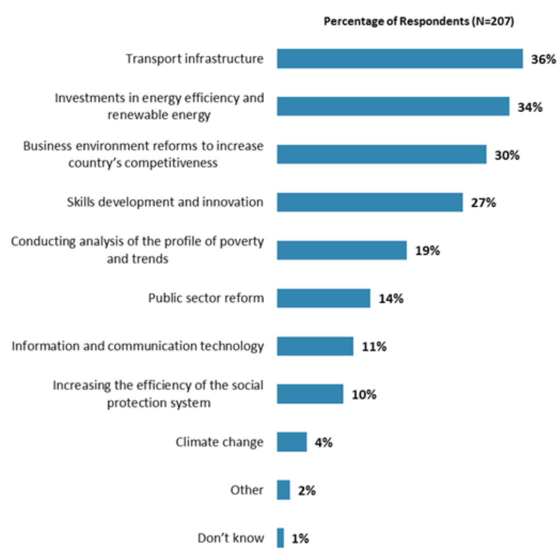
**How the Bank operates:** The way the Bank operates on the ground is also viewed positively. In contrast to many countries across the globe, opinions are very positive with regard to disbursements and speed of decision making. Perceptions of the Bank's relevance and alignment have increased significantly since FY10. Survey findings show high opinions on a number of important aspects of WBG engagement including being a long term partner (average score of 8.2), collaboration with the Government (8.1), straightforwardness and honesty (7.7), responsiveness (7.5) and collaboration with other development partners (7.5). While views of how the Bank collaborates with groups outside government are also positive (6.7), they are significantly lower than most other ratings.

**Areas for improvement:** In FY10 respondents identified bureaucracy and being technocratic as the Bank's top challenges. In this year's survey the top factor identified as limiting the effectiveness of Bank engagement was lack of sensitivity to political and social realities on the ground. The survey also demonstrated low awareness of the information that the World Bank produces and discloses, with three out of four respondents reporting that they were not aware of the WBG's Access to Information policy. Compared to FY10, fewer respondents felt that they can find the information they need on the World Bank website, particularly people who do not collaborate with the World Bank directly. Respondents suggested that the Bank should reach out more to groups outside of government, with three out of ten noting that the biggest obstacle to Bank supported reform is that the Bank is not sensitive enough to realities on the ground and 64 percent noting that to be more effective, the WBG should have a greater local presence. Nearly half of respondents thought that the Bank should step up its engagement with the private sector, and a third of respondents recommended reaching out to local governments. Responses also suggest that translating more of the Bank's knowledge work into Macedonian would help to improve outreach.

**Recommendations for future engagement and adding value:** stakeholders believe there would be great value in the WBG offering more innovative financial instruments. Financial services emerge at the top when respondents consider the combination of services that the Bank offers. Forty five percent of respondents report that the Bank should offer more financial services in fYR Macedonia (versus 25 percent who named knowledge services as the top area for additional focus). Capacity development is also seen as an important area for future Bank involvement. In terms of the sectors of engagement, stakeholders believe that the most important areas for WBG involvement are transport (particularly as related to economic diversification) and growth followed by a range of areas (governance, education, poverty, business environment, job creation).



"Which of the following SHOULD the World Bank Group do to make itself of greater value in Macedonia? (Choose no more than TWO)" (Respondents chose from a list. Responses combined.)



"Please identify the TWO areas related to economic diversification in Macedonia where greater support from the World Bank Group would be most valuable. (Choose no more than TWO)" (Respondents chose from a list. Responses combined.)

## Annex 5: Gender Assessment

**FYR Macedonia has largely closed average gender gaps in education and health; however, gender disparities persist for certain population subgroups.** For example, gender gaps in enrollment rates still exist among ethnic Albanians, and secondary enrollment rates remain particularly low for ethnic Roma men and women. Overall, average learning outcomes are better for women than for men in fYR Macedonia, as in most countries in the region. The rapid expansion of private post-secondary education institutions, the expansion of state-funded programs in Albanian and introduction of compulsory secondary education from 2008, provision of free of charges text books and coverage of transportation, as well as implementation of the conditional cash transfers for the beneficiary households of social financial assistance are contributing to increased participation of females in the educations process.

**Men and women, however, tend to choose different fields of study**. Women are more likely to choose general programs and subjects related to the social sciences. Men are more likely instead to choose engineering, production, or construction. Moreover, a low share of both men and women choose not to pursue additional training, but the reasons for this decision differ by gender. In 2010, less than two percent of women and men declared to have undertaken training in the past month. Both men and women cite lack of interest as a reason for not pursuing additional education, but approximately 19 percent of women and 1.5 percent of men also cite family obligations.

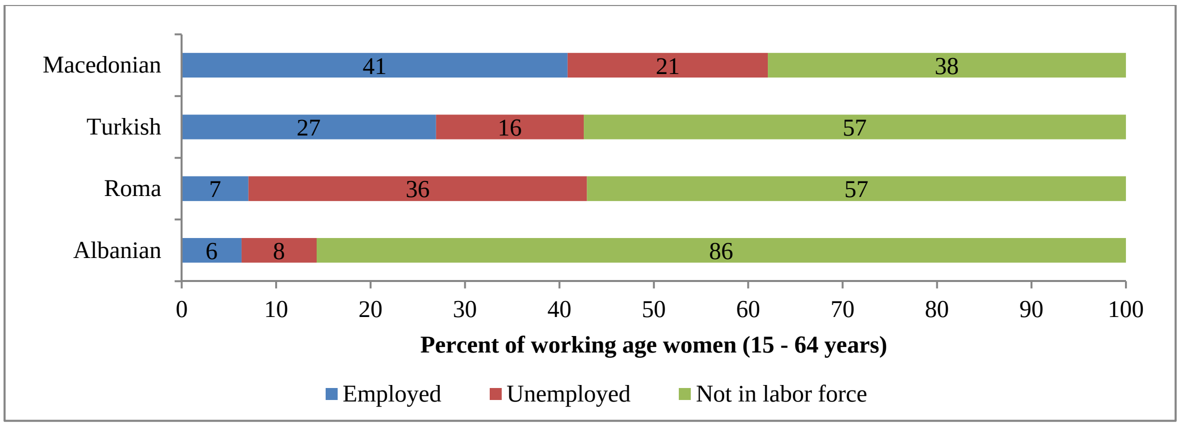
**There is no evidence of gender-based differences in access to health services**. The country performs well when it comes to births attended by skilled health staff and adolescent fertility. Close to 100 percent of births are attended by health staff. The fertility rate (at around 1.4 births per women) is slightly lower compared to the region and so is the maternal mortality rate. Mortality rates are lower compared to income and regional peers and only slightly higher compared to EU countries. Furthermore, women have lower mortality rates (74 per 1,000 adult women compared to 139 per 1,000 adult men) which also translate into higher life expectancy for women (around 77 years, compared to a national average of 73 years).

**Gender inequalities remain in access to economic opportunities in fYR Macedonia.** In 2012, female labor force participation (for women aged 15-65) in fYR Macedonia was 51 percent, which is lower than the regional average of 62 percent. Moreover, between 2004 and 2012, male labor force participation increased by 6 percentage points while female labor force participation increased by 4 percentage points. This indicates a gender gap in participation of 26 percentage points in 2012. For those in the labor market, unemployment rates for men and women are similar. A gender wage gap persists, even after controlling for other characteristics, with men commanding higher wages.

**Gender gaps in labor markets exist between and within socio-economic groups**. For instance, the employment rate for men in the bottom 40 percent in fYR Macedonia is 32 percent (in the remaining 60 percent is 34), while it is 14 percent for women in the same group but 23 percent for women in the top 60 percent

**Gender gaps in accessing economic opportunities are tightly linked to differences across ethnic groups.** The data available indicate that labor force participation among ethnic minorities is often significantly lower than among ethnic Macedonians, especially among women. Whereas ethnic Macedonian women have an employment rate of 41 percent, only 10 percentage points lower than their male counterparts, women who are ethnically Turkish have an employment rate of 27 percent – a 32 percentage point gap with men with the same ethnic background. Roma and ethnic Albanian women lag even further behind in terms of employment, with employment rates of only 7 and 6 percent, respectively. Low employment rates among ethnic minority women are driven by higher inactivity rates rather than by higher unemployment. Generally, activity rates among ethnic minorities are about two or three times lower among women than among men.

**Figure 1: Female Labor Force Statistics by Ethnic Group**




*Source:* "Labor Market Inequalities in fYR Macedonia: New Evidence and Perspectives on Gender and Ethnicity", based on LFS (2006).

*Note:* 2006 is the last year when data is publicly available on ethnicity in the LFS. In this graphs, it is important to note that the LFS data is not representative by ethnicity so there may be some discrepancies with actual data at the population level.

**In terms of entrepreneurship, although female-managed businesses are as productive as male-managed businesses, few women are entrepreneurs.** Fewer women decide to start a business than men, but success rates do not differ according to the gender of the entrepreneur. Analysis based on the 2010 LITS database reveals that 12 percent of women and 19.7 percent of men decided to start-up a firm. Seventy-three percent of men and 74 percent of women who start a business achieve success.

**Few businesses are managed by women, and women managers work mainly in female-owned businesses**. Analysis based on the World Bank Enterprise Survey (2013), which looks at established small, medium, and large businesses, shows that 29.4 percent of firms in fYR Macedonia have female participation in ownership compared to 33 percent in ECA and 37 percent globally. The highest share of female ownership - 37.8 percent - is in exporting firms (direct exports are at least 10 percent of all sales) compared to 31.6 percent in ECA and 36.7 percent in all countries. 26.3 percent of interviewed Macedonian firms have women in top management, which is higher than ECA (21.3 percent) and global (19.0 percent) averages. The share of women managers is again significantly higher in exporting firms - 35.7 percent of firms have a female top manager as compared to 16 percent in ECA, 14.7 percent in all countries, and in 24.9 percent in non-exporting firms in fYR Macedonia.

**Contrary to other countries, men and women in fYR Macedonia differ little in the sector in which they are engaged, whether we identify male and female businesses based on the gender of the manager or on the gender of the owner.** The majority of male- and female-managed businesses are in the retail sector while a larger percentage of male-managed businesses than female-managed businesses can be found in the sectors of transport, construction, garment, and fabricated metal materials. More female- than male-managed businesses can be found in the sectors of retail, chemicals, food, and plastic and rubber industry. Similar distribution patterns across sectors can be found when disaggregating the data by gender of the owner. These differences in business sector affiliation are probably related to preferences for different areas of study at vocational and higher education level.

**Gender gaps are not observed in the share of men and women who attempted to borrow money to start a business, in the success rates of obtaining a loan, or in the source of financing**. On access to credit, the share of females who attempted to borrow money to start a business is low but similar to that of males (approximately 38 percent of females, compared to 41 percent of males). Among them, 75 percent of females and 71 percent of males obtained the loan. Relatives represent the main source of finance for both genders (47 percent and 48 percent respectively), followed by banks in the case of females (35 percent of females and 26 percent of males) and by friends in the case of males (26 percent of men and 10 percent of women).

**FYR Macedonia has made continuous progress in advancing gender relations**. The legal framework for gender equality is comprehensive and provides for equal treatment of both genders. The 2005 Labor Code endorses the definition of gender-based discrimination and provides a framework for anti-discrimination measures. According to the Law on Family all forms of abuse are prohibited, while the Law on Inheritance gives equal rights to both males and females. The Criminal Code punishes gender-based discrimination and all forms of domestic abuse and violence; rape is punishable under Article 186 of the Penal Code for a period of one to ten years.

**The Law on Equal Opportunities was adopted in May 2006 and amended in 2012**; this was followed by establishment of the special Parliamentary commission on equal opportunities in September 2006 and the Sector for Equal Opportunities within the Ministry for Labor and Social Policy in March 2007. A new Strategy for Gender Equality (2013 -2020) was adopted in 2013 and consequently a new National Action Plan for Gender Equality (2013-2016), and the operational plan for 2013.

Annex 6: WB/IFC Collaboration in FYR Macedonia: Update on the Joint Business Plan

## Summary of the Strategy for Joint World Bank-IFC Activities

Following the consultative meetings in early 2013, the WB and IFC country teams developed a *"Note on WB-IFC Collaboration in Macedonia"* which defined a set of specific activities aimed at enhancing the WB–IFC collaboration in the country, to be undertaken in the remaining period of the joint Country Partnership Strategy (FY11-14).

The Note envisaged the following activities and milestones:

- *WB-IFC Collaboration Group* has been established, led by the World Bank Country Manager, Tatiana Proskuryakova and IFC Country Officer, Zoran Martinovski. The Group **identified four priority areas** for WB-IFC collaboration in Macedonia, as follows:
  - (1) **Trade Logistics**,
  - (2) **Job Creation and Employment**
  - (3) **Energy**, with special focus on **Energy Efficiency and Renewables**, and
  - (4) **Working with municipalities**.
- *Joint WB-IFC Contact Groups* have been created for each of the priority areas and tasked to take stock of ongoing and planned activities in each priority area, identify key next steps, points of potential cooperation, timing as well as to report back any encountered constraints and how to address them. The lessons learned were meant to be used to inform the development of the next planning document (CPS or Business Plan) for the period beyond FY14.
- *Goals and Principles of Collaboration*: The collaboration of the World Bank and the IFC in Macedonia is grounded on the World Bank Group's core strengths (knowledge, finance and talent) and organizational culture of risk tolerance, leadership, and collaboration. The objective is to improve our organizational effectiveness and deliver results to our client with the objective of eliminating extreme poverty and boosting shared prosperity in the country.

## Progress Update

### Current Operations and Cooperation in the Priority Areas

### (1) Trade Logistics

Operations:

a. *Western Balkans Regional Trade Logistics Project*. The goal of the Project is reduction of regulatory and administrative bottlenecks to regional cross-border trade by streamlining export and import procedures, harmonizing inter-agency cooperation within and between countries, and championing risk-based controls, including wider use of electronic systems for data exchange and trade logistics -related payments.

Project Manager Violane Konar-Leacy (Operations Officer, CEUIC). Duration: 2012-October 2014.

b. *Programmatic Competitiveness Development Policy Loan* (DPL), a series of two DPLs ($50 USD million equivalent, each) The objective of the project is to strengthen the competitiveness of fYR Macedonia's economy by incentivizing productive investment and technology upgrading in the manufacturing, agribusiness and trade logistics sectors, and establishing enabling conditions to progressively increase labor market flexibility and innovation capacity. Task Team Leader, John Gabriel Goddard (Senior Economist, ECSF2). Duration: 2012-October 2014.

c. *Macedonia Competitive Industries and Innovation Support Program* (MCIISP), aims at increasing the impact of the Programmatic Competitiveness DPL series and a Skills Development and Innovation Support Project and provide seed funding that will help identify future operations. The Program encompasses four sectoral components (manufacturing, agribusiness, trade logistics and tourism) while skills development and innovation are cross-cutting areas. Team Leaders: John Gabriel Goddard (Senior Economist, ECSF2) and Gordana Popovikj Friedman (Private Sector Development Specialist, ECSF3). Duration: July 2013-June 2016.

<u>Areas of Cooperation</u>:

The World Bank Competitiveness DPL and MCIISP Team and IFC's Western Balkans Trade Logistics Project Team continued the collaboration on completing the design and the implementation of the policies under the Third Pillar (Trade Logistics) of Competitiveness DPL series. The prior actions under the Third Pillar (Improving the efficiency of trade logistics services) were successfully completed by January 2014. The preparation of DPL2 was completed and the operation was approved by the World Bank Board of Directors on March 13, 2014.

DPL2 is supporting comprehensive improvements in the risk-based approach to border controls performed by the technical inspections (Food and Veterinary Agency and State Sanitary and Health Inspectorate), in line with EU best practice. The Bank Team has provided technical assistance for these activities under the CIIP grant, in close cooperation with IFC's Western Balkans Trade Logistics Project. The capacity building of the State Sanitary and Health Inspectorate and Food and Veterinary Agency in the risk-based approach methodology implementation is continuing through in–country workshops with international technical experts. In addition, the team is reviewing a request from the Food and Veterinary Agency for design of a software platform for data collection as the prerequisite for a successful application of the risk-based approach to technical inspections. A request for similar software has also been announced by the State Sanitary and Health Inspectorate.

Successful application of the risk-based approach is a critical trade facilitation improvement to address the costs and delays from unnecessary controls and inspections.

## (2) Job Creation and Employment:

Operations:

a. *Applying the 2013 WDR Framework in ECA Technical Assistance* consists of four pieces of analytical work: Macedonia Labor Market Assessment 2011-2011; Gender Gaps in Labor Markets in Macedonia; Assessment of Labor Regulations in Macedonia; and A Regional Review of Labor Regulations in the Western Balkans. The objective of this work is to underpin a broader Jobs Strategy which would address constraints to job creation in Macedonia, and could serve for continued collaboration, in particular the development of the National Jobs Strategy for 2015. The Jobs Strategy will be a critical analytical underpinning for the new CPS (FY14-17). Team Leader: Indhira Vanessa Santos, Economist (ECSH4). Duration: 2013-2015.

b. *Skills Development and Innovation Support Project* ($24 million USD investment loan), aims to improve transparency of resource allocation and promote accountability in higher education, enhance the relevance of secondary technical vocational education, and support innovation capacity in Macedonia. Team Leader: Bojana Naceva, Senior Education Specialist (ECSH1). Duration: January 2014-May 2019.

c. *Let's Work Initiative* will implement job-creation strategies both at the country level and also at the company level. These pilot programs will identify sectors and areas that have the most potential to create more and better jobs, help remove obstacles and get going private sector -led job growth. At the country level, the *Let's Work* initiative will produce guidance notes, good-practice lessons and training and learning events. At the company level, the partnership will work with specific organizations to articulate and strengthen their job creation effects by focusing on value chain development. It will also develop and refine methods and data for estimating direct and indirect jobs. Duration 2013-2016.

### Collaboration on Job Creation and Employment

In November 2013 the IFC, under the *Let's Work* Initiative and the World Bank (Country Unit and MCIISP Team) jointly organized a high level round table discussion in Skopje which brought together the government of fYR Macedonia and private sector leaders from two key sectors –automotive and agribusiness –to discuss opportunities for creating jobs and stimulating growth in the automotive and agribusiness sectors. The discussions helped to identify and arrive at a consensus on key priorities for action for further developing these two sectors and creating jobs in the country. Following the joint event, the WB and IFC developed a joint plan of initiatives to advance the development of the sectors.

One of the areas for collaboration in the near term is development of a supplier linkages program around anchor firms, likely foreign investors, with resources and technical assistance from the IFC and the MCIISP. The IFC has approached foreign manufacturing companies located in the special economic zone Skopje 1 and identified opportunities for backward linkages for local suppliers through innovation, technology transfer and investment which could be facilitated through knowledge from the MCIISP, grants from the World Bank-funded Skills Development and Innovation Project, knowledge through MCIISP and the IFC and future investments by the IFC.

The IFC and the World Bank FPD Team continued the discussions and cooperation in the following period, which has resulted in development of a concept for a program to support development of backward linkages.

The goal of the proposed program is to foster spillover effects to the domestic economy through established backward linkages around the foreign automotive companies present in fYR Macedonia, thereby generating more sales, and increasing direct and indirect employment opportunities for local firms. The future growth of the Macedonian economy depends on a stronger integration between foreign investors and local supply chains. This will contribute to country's economic diversification and enhanced resistance to external shocks.

The concept note envisions the following objectives:

- <u>Increased availability of information about opportunities for linkages</u> through the development of a catalog of products and services available from local suppliers and of products and services requested by foreign investors; organize targeted B2B/Networking events to bring together local suppliers with foreign investors;
- <u>Improved Supply Chain Enabling Regulatory Environment</u> through addressing regulatory obstacles arising from investors already operating in the TIDZ and develop Incentive Schemes to motivate local suppliers to work with foreign investors;
- <u>Strengthened linkages between local suppliers and foreign investors</u> through technical assistance for upgrading existing and potential local suppliers' capacities;
- <u>Enhanced access to finance</u> through facilitation of financial assistance offered by foreign companies to local suppliers; increasing the awareness for existing funding schemes of relevance to foreign investors and local companies;

Next steps: As part of the pre-implementation (preparation) phase, further analysis and mapping will be carried out in order to confirm and deepen the findings from previously undertaken activities, which would allow more specific tailor-made activities and objectives to be set. The pre-implementation phase would allow to better understand the market, the supply chain challenges, the competitive advantages around which the program should be specifically focused and draw a baseline for the program. This phase would be a critical one that would help the program to find better focus, i.e., to be more effective.

The pre-implementation phase will be supported with technical assistance and policy advice through the MCIISP grant.

### (3) Energy (Energy Efficiency and Renewables)

**Operations:**

a. *Balkans Renewable Energy Program (BREP)* provides technical assistance to the Ministry of Economy (MOE) and Ministry of Environment and Physical Planning (MOEPP) on regulatory and investment promotion related improvements in the RE sector. Through BREP, IFC also provides technical assistance for a private developer of biomass power plant in the country. Team Leader: Dimitar Dimitrovski, Operations Officer (CEUSB), Duration (in fYR Macedonia): January 2012-June 2016.
b. *Transcation Advisory:* IFC successfully completed "Crna River HPP" transaction mandate, and provides continuous support of the country to improve the operational

efficiency of its distribution system through its investment in the private operator, EVN Macedonia. December 2010-ongoing.

c. *Energy Community of South East Europe (ECSEE) APL3*. The Project supports the functioning of AD MEPSO in the context of the regional power market through financing investments necessary to rehabilitate and upgrade the power transmission network, increase the level of interconnection with neighboring power systems, and to strengthen the institutional capacity of AD MEPSO. Team Leader: Peter Johansen Senior Energy Specialist (EASWE). Duration: March 2006-November 2015.

**Collaboration on Energy (Renewable Energy Sources and Energy Efficiency)**

The Balkans Renewable Energy Program (BREP) team is providing technical assistance to the Ministry of Economy (MOE) and Ministry of Environment and Physical Planning (MOEPP) in the country on regulatory and investment promotion related improvements in the RE sector. Through BREP, IFC is also focused at providing technical assistance for a private developer of biomass power plant in the country. IFC is also focused on successful closure of “Crna River HPP” transaction mandate, and will provide continuous support to improve the operational efficiency of the country’s distribution system through its investment in the private operator, EVN Macedonia.

The BREP team in cooperation with the World Bank (WB) and Investment Climate (IC) teams delivered investment promotion tools for MOEPP related to the forthcoming and further Small Hydro Power Plant (SHPP) tenders, namely, (i) the SHPP MS Power Point presentation to be delivered at targeted markets through the Invest in Macedonia Agency offices abroad, and (ii) the SHPP investor friendly portal. In addition, BREP team delivered a Methodology for FiTs for Geothermal sources, with suggested FiT tariff price to the MOE, in order to facilitate Government’s efforts for increased use of RE sources in the country. Finally, BREP team continuously advises MOEPP on the forthcoming 6$^{th}$ tender on SHPPs. As a result, the Government is in the process of bundling of SHPP sites to become more investor attractive, revising the FiT price for SHPPs (incentivizing smaller sites), and revising the Grid Distribution Code (to enhance SHPP’s connection to the distribution grid).

The team organized workshops and conducted wide (private sector and cross donor) consultation for the improved regulatory framework on RE/SHPPs (PPA, Connection Agreement, and Concession Contract). Outputs delivered to the MOE, MOEPP.

Revised tender documents for “Crna River HPP” have been provided to the Government as part of the transaction mandate.

Challenges: Coordination between the WB and IFC Project teams should be improved. Information flow is limited. Developments by the Government in creating RE market (re: results of the 6th SHPP tender; support adoption of regulatory improvements; provision of RE/SHPP Project Finance training to the country’s financing institutions). Successful closure of “Crna River HPP” transaction mandate.

**Next steps**:

- Further promote investment opportunities for SHPP sector in the country in collaboration with the Government and WB.
- Support the Government in adoption process of the final texts of regulatory improvements in the RE/SHPPs.
- Deliver bankable Feasibility Study for Biomass Power Plant for the private sector client.
- Provide RE/SHPP Project Finance training for a financing institution in the country
- Closely follow development regarding "Crna River HPP" transaction.
- Continuously support EVN Macedonia in improvements of the operational efficiency of its distribution system private operator.

### (4) Working with Municipalities

**Operations:**

a. *Macedonia Competitive Industries and Innovation Support Program* (MCIISP), aims at increasing the impact of the Programmatic Competitiveness DPL series and a Skills Development and Innovation Support Project and provide seed funding that will help identify future operations. The Program encompasses four sectoral components (manufacturing, agribusiness, trade logistics and tourism) while skills development and innovation are cross-cutting areas. Team Leaders: John Gabriel Goddard (Senior Economist, ECSF2) and Gordana Popovikj Friedman (Private Sector Development Specialist, ECSF3). Duration: July 2013-June 2016. Work on tourism in particular focuses on local and regional competitiveness dimension and is carried out by the joint IFC-Bank team.
b. *Possible future joint operation on IPA 2 local competitiveness/ tourism program.*
c. *Macedonia Municipal Services Improvement Project* (MSIP) aims improve transparency, financial sustainability and delivery of targeted municipal services in the participating municipalities. Team leader: Toshiaki Keicho (Senior Urban Development Specialist, GURDR). The project in in the process of receiving additional financing from IPA funds.

**Collaboration on work with municipalities**

A joint IFC-Bank team is already working on the tourism and local development component of the MCIISP. This work will continue in the future. Discussions are also underway for a possible joint Bank-IFC operation in support of the IPA2 local competitiveness/ tourism agenda. NO current opportunities have been identified for closer collaboration under MSIP, however, the opportunities will be reevaluated periodically as program implementation progresses.

# Annex B2: Selected Indicators* of Bank Portfolio Performance and Management

As Of Date 7/25/2014

| Indicator | 2012 | 2013 | 2014 | 0 |
|---|---|---|---|---|
| ***Portfolio Assessment*** | | | | |
| Number of Projects Under Implementation [a] | 7 | 5 | 7 | 0 |
| Average Implementation Period (years) [b] | 5.0 | 5.8 | 5.0 | 0.0 |
| Percent of Problem Projects by Number [a, c] | 42.9 | 40.0 | 0.0 | 0.0 |
| Percent of Problem Projects by Amount [a, c] | 29.8 | 54.4 | 0.0 | 0.0 |
| Percent of Projects at Risk by Number [a, d] | 42.9 | 40.0 | 0.0 | 0.0 |
| Percent of Projects at Risk by Amount [a, d] | 29.8 | 54.4 | 0.0 | 0.0 |
| Disbursement Ratio (%) [e] | 26.1 | 10.9 | 25.4 | 0.0 |
| ***Portfolio Management*** | | | | |
| CPPR during the year (yes/no) | | | | |
| Supervision Resources (total US$) | | | | |
| Average Supervision (US$/project) | | | | |

| Memorandum Item | Since FY 80 | Last Five FYs |
|---|---|---|
| Proj Eval by OED by Number | 41 | 8 |
| Proj Eval by OED by Amt (US$ millions) | 851.1 | 107.2 |
| % of OED Projects Rated U or HU by Number | 17.5 | 12.5 |
| % of OED Projects Rated U or HU by Amt | 6.8 | 12.2 |

a. As shown in the Annual Report on Portfolio Performance (except for current FY).
b. Average age of projects in the Bank's country portfolio.
c. Percent of projects rated U or HU on development objectives (DO) and/or implementation progress (IP).
d. As defined under the Portfolio Improvement Program.
e. Ratio of disbursements during the year to the undisbursed balance of the Bank's portfolio at the beginning of the year: Investment projects only.
* All indicators are for projects active in the Portfolio, with the exception of Disbursement Ratio, which includes all active projects as well as projects which exited during the fiscal year.
which includes all active projects as well as projects which exited during the fiscal year.

## Annex B3: IBRD/IDA Program Summary

**IBRD/IDA Program Summary**

**As of date July 29 2014**

Country **Macedonia, former Yugoslav Republic of**

**Proposed IBRD/IDA Base-Case Lending Program**

| *Fiscal year* | *Project name* [a] | *US$(M)* [b] |
|---|---|---|
| 2015 | Small Hydro/Water Storage | 60.0 |
| | Macedonia Public Finance DPL | 70.0 |
| | Road Rehabilitation | 70.0 |
| | Subtotal | 200.0 |
| 2016 | Macedonia Energy Efficiency Fund | 20.0 |
| | Macedonia Competitiveness DPL3 | 70.0 |
| | Solid Waste/Wastewater | 20.0 |
| | ICT Based Jobs | 10.0 |
| | Subtotal | 120.0 |
| 2017 | Road Upgrading | 80.0 |
| | Social Protection Reform | TBD |
| | Subtotal | 80.0 |
| | **Total** | **400.0** |

a. This table presents the proposed program for the next three fiscal years.

b. The loan amount for planned operations is indicative. Decision on the choice among possible new operations will be made during CPS implementation.

# Annex B3 (IFC)

## IFC Investment Operations Program

| | 2011 | 2012 | 2013 | 2014 |
|---|---|---|---|---|
| **Original Commitments (US$m)** | | | | |
| IFC and Participants | | 18.29 | 6.77 | 5.60 |
| IFC's Own Accounts only | | 18.29 | 6.77 | 5.60 |
| **Original Commitments by Sector (%)- IFC Accounts only** | | | | |
| ELECTRIC POWER | | 25.22 | | |
| FINANCE & INSURANCE | | 74.78 | 100 | 100 |
| **Total** | 0 | 100 | 100 | 100 |
| **Original Commitments by Investment Instrument (%) - IFC Accounts only** | | | | |
| Guarantee | | 1.28 | 100 | 100 |
| Loan | | 98.72 | | |
| **Total** | 0 | 100 | 100 | 100 |

# Annex B3 (MIGA)

Outstanding Guarantee Exposure as of 5/31/2014

| Host Country | Effective Date | Expiry Date | Investor Name | Project Name | Investor Country | Business Sector | MaximumAggregate Liability ($USD) |
|---|---|---|---|---|---|---|---|
| Macedonia, former Yugoslav Republic of | 12/22/2010 | 12/21/2020 | ProCredit Holding AG | ProCredit Group Central Bank Mandatory Reserves Coverage | Germany | Financial | 12,930,925 |
| | 03/31/2014 | 03/30/2017 | National Bank of Greece S.A. | NBG Central Bank Mandatory Reserves Coverage in Macedonia | Greece | Financial | 142,240,175 |
| Macedonia, former Yugoslav Republic of Total | | | | | | | 155,171,100 |

# Annex B4: Summary of Non-lending Services

## Summary of Nonlending Services

As of July 29, 2014

| *Product* | *Completion FY* | *Audience*[a] | *Objective*[b] |
|---|---|---|---|
| **Recent** | | | |
| Green Growth & Climate Change | FY14 | G, D, P | KG, PD |
| Infrastructure Review | FY14 | G, B | KG |
| Standard ARD Sector Support | FY14 | G, B | KG |
| Macedonia ICT TA | FY14 | G, B | KG |
| WB Regional R&D Study on Innovation | FY14 | G, B, P | KG, PD |
| IPA2 Co-financing preparation | FY13 | G. B | KG |
| **Underway** | | | |
| PFM Review | FY15 | G, B | KG |
| Poverty Assessment | FY15 | G, B, P | KG, PD |
| Gender Diagnostics and Monitoring | FY15 | G, B, P | KG, PD |
| Mainstreaming Social Accountability | FY15 | G, B | KG |
| Employment and Job Creation in FYR Macedonia | FY16 | G, B | KG |
| ROSC Accounting and Auditing | FY15 | G, B | KG |
| Macedonia Competitiveness Industries and Innovation Support | FY16 | G, B | KG |
| Growth and Shared Prosperity ESW | FY15 | G, B | KG |

a. Government, donor, Bank, public dissemination.

b. Knowledge generation, public debate, problem-solving.

## Annex B6: FYR Macedonia – Key Economic Indicators

| Indicator | Actual | | | | | | | Estimate | Projected |
|---|---|---|---|---|---|---|---|---|---|
| | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 |
| **National accounts (as % of GDP)** | | | | | | | | | |
| Gross domestic product[a] | 100 | 100 | 100 | 100 | 100 | 100 | 100 | 100 | 100 |
| Agriculture | 9 | 10 | 10 | 10 | 10 | 9 | 9 | 10 | 10 |
| Industry | 27 | 26 | 24 | 25 | 25 | 22 | 23 | 23 | 23 |
| Services | 64 | 64 | 66 | 65 | 65 | 69 | 68 | 67 | 67 |
| Total Consumption | 94 | 98 | 96 | 94 | 93 | 93 | 95 | 93 | 93 |
| Gross domestic fixed inv | 25 | 27 | 26 | 25 | 26 | 29 | 24 | 23 | 23 |
| Government investmen | 4 | 5 | 5 | 6 | 6 | 7 | 7 | 3 | 3 |
| Private investment | 16 | 16 | 15 | 13 | 15 | 16 | 16 | 19 | 20 |
| Exports (GNFS)[b] | 52 | 51 | 39 | 47 | 55 | 54 | 54 | 55 | 56 |
| Imports (GNFS) | 71 | 76 | 61 | 65 | 74 | 76 | 73 | 76 | 78 |
| Gross domestic savings | 6 | 2 | 4 | 6 | 7 | 7 | 5 | 7 | 7 |
| Gross national savings[c] | 18 | 15 | 21 | 25 | 26 | 26 | 25 | 26 | 27 |
| *Memorandum items* | | | | | | | | | |
| Gross domestic product (US$ million at current prices) | 8160 | 9834 | 9314 | 9138 | 10439 | 9576 | 10221 | 10598 | 11281 |
| GNI per capita (US$, Atl | 3650 | 4290 | 4600 | 4770 | 4910 | 4890 | 5090 | 5243 | 5426 |
| Real annual growth rates (%, calculated from 95 prices) | | | | | | | | | |
| Gross domestic produ | 6.1 | 5.0 | -0.9 | 2.9 | 2.8 | -0.4 | 2.9 | 3.0 | 3.5 |
| Gross Domestic Incom | 9.2 | 3.3 | -1.9 | 2.4 | 5.4 | -0.6 | 2.5 | 2.8 | -0.6 |
| Real annual per capita growth rates (%, calculated from 95 prices) | | | | | | | | | |
| Gross domestic produ | 6.1 | 5.0 | -0.9 | 2.9 | 2.8 | -0.4 | 2.9 | 3.0 | 3.5 |
| Total consumption | 6.5 | 8.0 | -3.7 | 1.3 | 2.4 | -2.7 | 2.7 | 3.0 | 2.4 |
| Private consumption | 8.1 | 7.4 | -4.7 | 2.1 | 2.9 | -3.0 | 4.2 | 2.6 | 1.6 |
| **Balance of Payments (US$ )** | | | | | | | | | |
| Exports (GNFS)[b] | 4214 | 5001 | 3564 | 4245 | 5583 | 5043 | 5420 | 5809 | 6368 |
| Merchandise FOB | 3391 | 3983 | 2702 | 3345 | 4473 | 3993 | 4260 | 4523 | 4940 |
| Imports (GNFS)[b] | 5814 | 7575 | 5709 | 6117 | 7732 | 7248 | 7421 | 8072 | 8803 |
| Merchandise FOB | 5030 | 6573 | 4871 | 5264 | 6757 | 6255 | 6364 | 7002 | 7658 |
| Resource balance | -1639 | -2590 | -2169 | -1919 | -2284 | -2262 | -2105 | -2264 | -2435 |
| Net current transfers | 1383 | 1458 | 1602 | 1805 | 2075 | 2095 | 2049 | 1971 | 2042 |
| Current account balanc | -606 | -1236 | -610 | -198 | -261 | -300 | -194 | -478 | -639 |
| Net private foreign dire | 700 | 601 | 186 | 209 | 463 | 98 | 336 | 371 | 429 |
| Long-term loans (net) | -178 | 117 | 409 | 59 | 78 | 635 | 94 | 395 | 421 |
| Official | -147 | 639 | 223 | 101 | 52 | 120 | 160 | -39 | 288 |
| Private | -31 | -64 | -22 | -101 | -52 | 515 | -66 | 476 | 169 |
| Other capital (net, incl. e | 178 | 438 | 162 | 7 | 164 | -248 | -283 | 50 | 50 |
| Change in reserves[d] | -133 | 80 | -147 | -77 | -444 | -185 | 48 | -417 | -343 |
| *Memorandum items* | | | | | | | | | |
| Resource balance (% of | -20.1 | -26.3 | -23.3 | -20.5 | -21.9 | -23.6 | -20.6 | -21.4 | -21.6 |
| Real annual growth rates ( YR95 prices) | | | | | | | | | |
| Merchandise exports (I | 11.8 | -6.3 | -15.8 | 22.9 | 10.3 | 0.0 | 4.6 | 7.6 | 9.0 |
| Primary | | | | | | | | | |
| Manufactures | | | | | | | | | |
| Merchandise imports (( | 16.1 | 0.8 | -14.3 | 7.6 | 10.5 | 4.2 | -2.1 | 6.0 | 8.0 |

*(Continued)*

## Macedonia, FYR - Key Economic Indicators (Continued)

| Indicator Indicator | 2007 | 2008 | 2009 | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 |
|---|---|---|---|---|---|---|---|---|---|
| | Actual | | | | | | | Estimate | Projected |
| **Public finance (as % of GDP at market prices)[e]** | | | | | | | | | |
| Current revenues | 32.8 | 33.1 | 31.3 | 30.4 | 29.8 | 30.1 | 29.6 | 29.7 | 30.3 |
| Current expenditures | 32.2 | 34.1 | 33.9 | 32.9 | 32.3 | 34.0 | 33.6 | 33.2 | 33.5 |
| Current account surplus | 0.6 | -0.9 | -2.7 | -2.4 | -2.5 | -3.9 | -4.1 | -3.5 | -3.2 |
| Capital expenditure | 3.8 | 4.9 | 3.3 | 3.5 | 3.9 | 4.1 | 3.5 | 4.0 | 4.0 |
| Foreign financing | 1.0 | 0.6 | 3.2 | 1.7 | 5.2 | 1.7 | 4.0 | 6.2 | 1.4 |
| **Monetary indicators** | | | | | | | | | |
| M2/GDP | 45.7 | 43.4 | 45.3 | 46.4 | 47.1 | 47.5 | 46.0 | 47.1 | 48.3 |
| Growth of M2 (%) | 28.1 | 7.1 | 4.0 | 8.4 | 7.5 | 0.5 | 0.2 | 1.9 | 2.4 |
| Private sector credit gro total credit growth (%) | 39.2 | 34.4 | 3.5 | 7.1 | 8.5 | 5.4 | 6.4 | 6.1 | 7.8 |
| **Price indices( YR95 =100)** | | | | | | | | | |
| Merchandise export pric | 278.7 | 330.4 | 223.5 | 274.2 | 370.0 | 332.4 | 266.9 | 266.0 | 276.8 |
| Merchandise import pric | 304.1 | 398.6 | 293.4 | 317.1 | 407.7 | 378.8 | 237.6 | 249.1 | 253.7 |
| Merchandise terms of tr | 91.7 | 82.9 | 76.2 | 86.5 | 90.8 | 87.7 | 112.3 | 106.8 | 109.1 |
| Real exchange rate (US$ | 85.4 | 85.4 | 85.4 | 85.4 | 85.4 | 85.4 | 85.4 | .. | .. |
| Real interest rates | | | | | | | | | |
| Consumer price index ( | 2.2 | 8.3 | -0.7 | 1.6 | 3.9 | 3.1 | 2.8 | 2.5 | 2.0 |
| GDP deflator (% change | 7.4 | 7.5 | 0.7 | 2.7 | 3.0 | 0.1 | 0.3 | 0.2 | 2.8 |

a. GDP at factor cost

b. "GNFS" denotes "goods and nonfactor services."

c. Includes net unrequited transfers excluding official capital grants.

d. Includes use of IMF resources.

e. Consolidated central government.

f. "LCU" denotes "local currency units." An increase in US$/LCU denotes appreciation.

# Annex B8: Operations Portfolio

**Operations Portfolio (IBRD/IDA and Grants)**

**As Of Date 7/25/2014**

**Closed Projects** **41**

| **IBRD/IDA** * | |
|---|---|
| Total Disbursed (Active) | 164.98 |
| of which has been repaid | 17.03 |
| Total Disbursed (Closed) | 438.69 |
| of which has been repaid | 346.91 |
| Total Disbursed (Active + Closed) | 603.67 |
| of which has been repaid | 363.94 |
| Total Undisbursed (Active) | 180.65 |
| Total Undisbursed (Closed) | 0.00 |
| Total Undisbursed (Active + Closed) | 180.65 |

**Active Projects**

| | | Last PSR Supervision Rating | | | Original Amount in US$ Millions | | | | | Difference Between Expected and Actual Disbursements[a] | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| Project ID | Project Name | Development Objectives | Implementation Progress | Fiscal Year | IBRD | IDA | GRANT | Cancel. | Undisb. | Orig. | Frm Rev'd |
| P103974 | CCT (Conditional Cash Transfers) | MS | MS | 2009 | 25 | | | | 15.42756 | 14.97161 | |
| P082337 | ECSEE APL #3 (FYR MACEDONIA) | MS | MS | 2006 | 44.1 | | | | 16.47529 | -6.154768 | -0.62192 |
| P130847 | MK Competitiveness DPL 2 | # | # | 2014 | 50 | | | | 50 | | |
| P096481 | MUNICIPAL DEVELOPMENT | S | S | 2009 | 75 | | | | 49.58991 | -0.807468 | 1.592532 |
| P083126 | REG & REAL ESTATE (CRL) | MS | MS | 2005 | 26.1 | | | 0.94395148 | 4.620098 | -7.054352 | 0.719836 |
| P107840 | REGIONAL AND LOCAL RDS PROG SUPPORT F | MS | MS | 2008 | 105.2 | | | | 21.9562 | 29.55278 | |
| P128378 | Skills Development & Innovation Support | S | S | 2014 | 24 | | | | 22.58407 | 0.052455 | |
| Overall Result | | | | | 349.4 | | | 0.94395148 | 180.6531 | 30.56026 | 1.690447 |

a. Intended disbursements to date minus actual disbursements to date as projected at appraisal.

# Annex B8 (IFC)

**Macedonia, FYR**
**Committed and Disbursed Outstanding Investment Portfolio**
**As of 6/30/2014**
**(In USD Millions)**

| | | Committed | | | | | Disbursed Outstanding | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| FY Approval | Company | Loan | Equity | **Quasi Equity | *GT/RM | Partici pant | Loan | Equity | **Quasi Equity | *GT/RM | Partici pant |
| 2008/12 | EVN Macedonia | 35.43 | 0 | 0 | 0 | 0 | 35.43 | 0 | 0 | 0 | 0 |
| 1998/1999 | Macedonia Telcom | 0 | 6.85 | 0 | 0 | 0 | 0 | 6.85 | 0 | 0 | 0 |
| 2010/12/13/14 | NLB Tutunska Bk | 5.66 | 0 | 0 | 0.68 | 0 | 5.66 | 0 | 0 | 0.68 | 0 |
| 2012/14 | Ohridska Banka | 10.63 | 0 | 0 | 0.29 | 0 | 10.63 | 0 | 0 | 0.29 | 0 |
| 1998/2000/02/03/13/14 | Stopanska Banka | 0 | 0 | 0 | 0.05 | 0 | 0 | 0 | 0 | 0.05 | 0 |
| 2013/2014 | UNIBank Skopje | 0 | 0 | 0 | 0.14 | 0 | 0 | 0 | 0 | 0.14 | 0 |
| **Total Portfolio:** | | **51.72** | **6.85** | **0** | **1.16** | **0** | **51.72** | **6.85** | **0** | **1.16** | **0** |

* Denotes Guarantee and Risk Management Products.
** Quasi Equity includes both loan and equity types.

## FYR Macedonia Map