Republic of Macedonia

NATIONAL ECONOMIC REFORM PROGRAMME

2015

January, 2015

Contents

ABBREVIATIONS

AE	Adult education
AREC	Agency for Real Estate Cadastre
AFSARD	Agency for Financial Support of Agriculture and Rural Development
CA	Customs Administration
CB bills	Central Bank bills
CEB	Council of Europe Development Bank
CEFTA	Central European Free Trade Association
EARM	Employment Agency of the Republic of Macedonia
EBRD	European Bank for Reconstruction and Development
EC	European Commission
EFTA	European Free Trade Association
EIB	European Investment Bank
ELEM	Macedonian Power Plants
ESA	European System of Accounts
EU	European Union
FDI	Foreign Direct Investments
FITD	Fund on Innovation and Technical Development
FX	Foreign Exchange
GDP	Gross Domestic Product
GIS	Georgaphic Information System
GS	Government Securities
GWP	Gross written premium
HPP	Hydro Power Plants
IAIS	International Association of Insurance Supervisors
ICT	Information and communication technologies
IIP	International investment position
ILO	International labour organisation
IOSCO	International Organization of Securities Commissions
IOPS	International Organization of Pension Supervisors
IPA	The Instrument for Pre-Accession Assistance
IPARD	Instrument for Pre-Accession Assistance for Rural Development
IT	Information Technology
ISA	Insurance Supervision Agency
ISCO	International Standard Classification of Occupations
KfW	Kreditanstalt für Wiederaufbau (Reconstruction Credit Institute)
LGU	Local Government Units
MAPAS	Agency for Supervision of Fully Funded Pension Insurance
MSEI-10	Macedonian Stock Exchange Index
MBDP	Macedonian Bank for Development Promotion
MEPSO	Electricity Transmission System Operator of Macedonia
SEC	Macedonian Securities and Exchange Commission
Mw	Mega watt
NCTS	New Computerized Transit System
NECC	National Entrepreneurship and Competitiveness Council
NEER	Nominal Effective Exchange Rate
NERP	National Economic Reform Programme
PIFC	Public internal financial control
PEM	Pan-Euro-Mediterranean
PEFA	Public Expenditure and Financial Accountability
p.p.	Percentage Point
PIFC	Public Internal Financial Control
REER	Real Effective Exchange Rate
RES	Renewable energy sources
ROAA	Return on Average Assets
ROAE	Return On Average Equity
SAA	Stabilization and Association Agreement
SEE	South -eastern Europe
SEETO	South East European Transport Observatory
SIGMA	Support for Improvement in Governance and Management
SLI	State Labour Inspectorate
SMEs	Small and Medium-Sized Enterprises
OTC	Over the counter
TAIB	Transition Assistance and Institution Building
TIDZ	Technological and Industrial Development Zones
TFP	Total Factor Productivity
USAID	United States Agency for International Development
VAT	Value Added Tax
VET	Vocational Education and Training
WB	World Bank

INTRODUCTION

2015 National Economic Reforms Programme (NERP) is the first document of this type prepared in line with the instructions given by the European Commission (EC). It comprises two parts; the first part refers to the medium-term macroeconomic and fiscal framework, while the second one presents the sectoral structural reforms for promoting competitiveness and growth.

The Programme is prepared in line with the 2014-2018 Programme on Government Operations of the Republic of Macedonia, as well as the other national strategic documents, such as the National Programme for Adoption of the Acquis Communautaire, the Stabilisation and Association Agreement and the national sectoral strategies. In addition, the Programme is in line with the EU Strategy for fast, sustainable and comprehensive economic development "Europe 2020", as well as the SEE - 2020 Strategy of the Council for Regional Cooperation, called "Jobs and Prosperity in a European Perspective", which closely follows the vision of the "Europe 2020" Strategy. Remarks and recommendations indicated in the 2014 Progress Report on the Republic of Macedonia were also taken into consideration during the Programme preparation, as well as the country specific guidelines from the Ministerial dialogue held on 6 May 2014.

NERP is a coherent strategic document presenting the national economic policy of the Republic of Macedonia and the agenda of key structural reforms and measures. All competent state institutions participate in its preparation, however, the social partners and the business community also contributed to the creation of this document.

PART I

1. OVERALL POLICY FRAMEWORK AND OBJECTIVES

Macroeconomic policy of the Republic of Macedonia is aimed at achieving the strategic goals of the Republic of Macedonia for long-term and sustainable economic growth, maintaining financial and macroeconomic stability, increasing the competitiveness of the economy, increasing employment and improving the living standards of the population. These objectives will be achieved by improving the business environment, conducting tax and customs policy that supports growth, encouraging investment activity and attracting foreign direct investment (FDI), developing human capital and economic infrastructure in the country.

Republic of Macedonia will continue to conduct adequate fiscal policy aimed at achieving reasonable balance between both strategic goals, referring to preserving macroeconomic stability and encouraging economic activity by increasing the quality of public finances, mainly by increasing capital expenditures for improving the infrastructure, and strengthening the ability of private sector for growth and job creation.

Main goal of the monetary policy will be maintenance of price stability by retaining the stable Denar exchange rate in relation to the euro, to the end of creating favourable macroeconomic climate for long-term economic development.

Fiscal policy, in coordination with the monetary policy, will be aimed at achieving sustainability of the external position of the country and ensuring inflation level to underpin economic activity of the country.

In line with the identified priorities for the economic policy, key areas in the structural reforms agenda will be the following: reduction of unemployment and improvement of the conditions on the labour market, continuous business climate improvement, support of innovation, entrepreneurship and small-and medium-sized enterprises (SMEs), enhancement of human capital, as well as greater support of export. Economic policy will also be focused on implementing reforms in order to create effective and professional public administration, strengthening legal security and executing the contracts.

2. MACROECONOMIC FRAMEWORK

2.1. RECENT ECONOMIC DEVELOPMENTS

International economic environment. Growth rate is expected to amount to 3.3% in 2014 at global level and to surge to 3.8% in 2015 and 4.1% in 2016. Thereby, non-European developed economies are expected to recover, whereas it appeared that some of the factors slowing down the growth in the first half of the year have been only temporary. Economic growth in 2014 in the EU is expected to account for 1.3% and 0.8% in the Eurozone. Economic activity is expected to gradually intensify during 2015 and 2016, mainly as a result of the structural reforms effects, the labour market improvements, the support policies and the better financing conditions. Therefore, GDP growth in the EU is envisaged to increase to 1.5% in 2015 and to 2% in 2016, while as for the Eurozone, the growth is expected to reach 1.1% in 2015 and 1.7% in 2016. Domestic demand is expected to be the main driver of growth in this period.

Table 2.1. Macroeconomic indicators in the Eurozobe and EU

	GDP				Inflation				Unemployment rate			
Year	2013	2014	2015	2016	2013	2014	2015	2016	2013	2014	2015	2016
Eurozone	-0,5	0,8	1,1	1,7	1,4	0,5	0,8	1,5	11,9	11,6	11,3	10,8
EO	0,0	1,3	1,5	2,0	1,5	0,6	1,0	1,6	10,8	10,3	10,0	9,5

Source: European Economic Forecast (Autumn 2014)

Expected intensification of global trade and depreciation of the euro will contribute to supporting the EU export. However, net export will only marginally contribute to the GDP growth during this period, taking into account that import will be also increased by intensifying the domestic demand.

Recovery of the labour market in the EU continues, however it remains suppressed from the weak economic activity. Unemployment rate will reduced to 9.5% in the EU and 10.8% in the Eurozone in 2016. Slowdown trend of inflation rate in the EU continues, driven by lower prices of goods, mainly the prices of energy and food, as well as the previous euro appreciation. Inflation rate in the Eurozone is expected to amount to 0.8% in 2015 and 1.5% in 2016. Inflation rate in the EU is expected to amount to 1% in 2015 and 1.6% in 2016.

Recent Economic Trends in the Republic of Macedonia.

Gross domestic product. Growth of economic activity continued in 2014, however, more intensively compared to the previous year. Hence, real GDP growth rate in the first quarter amounted to 3.2%, reaching 4.4% in the second quarter and 4.1% in the third quarter, hence the average GDP growth in the first nine months in 2014 accounted for 3.9%. These growth rates are among the highest ones compared to the EU Member States and the region.

GDP growth during this period is on broad basis, whereby positive growth rates were registered across all sectors. Industrial production continued its positive trends, registering 4.8% growth in the first nine months, as a result of the growth in the manufacturing industry (10.7%). More significant growth in this category was observed at the production of motor vehicles (multiple increase), electrical equipment (31%), rubber and plastic products (23.5%) and machinery and equipment (23.5%), above all as a result of the effects from the increased production by the capacities in the free economic zones. Additional positive impulse was given by growth in the production of clothing (7.0%), textile (11.7%), food products (5.3%) and beverages (6.6%), etc.

Construction continued to contribute significantly to the economic growth, accounting for 4.4% in the first three quarters in 2014. Services sector grew by 3.7% in the same period, wherein Trade, transport and catering industry and Real estate activities had the highest contribution to growth, registering growth of 3.9%. Agriculture sector registered growth of 3.9% in the first three quarters of 2014.

Table 2.2. GDP growth rates in the Republic of Macedonia (production and expenditure methods)

	2013	2013				2014			
		I	II	III	IV	I	II	III	Average
GDP	2,7	1,9	2,1	2,5	4,1	3,2	4,4	4,1	3,9
GDP by production method									
Agriculture	9,0	16,0	7,3	1,7	14,3	3,2	9,2	0,3	3,9
Industry	5,8	6,7	5,8	4,5	6,2	2,6	5,8	5,8	4,8
Construction	6,0	5,8	4,0	8,9	5,7	9,3	0,5	2,6	4,4
Services	2,5	-0,3	2,0	4,0	3,7	3,3	4,2	3,5	3,7
GDP by expenditure method									
Final consumption	2,1	5,8	3,1	-0,5	0,3	-0,4	3,1	1,0	1,3
Private	2,1	6,1	4,0	-0,9	-0,7	-0,1	3,8	2,5	2,1
Public	2,5	4,4	-0,1	1,2	4,4	-1,6	0,1	-5,2	-2,2
Gross capital formation	-16,6	-32,6	-9,8	-15,2	-9,6	30,2	7,8	17,0	17,4
Export of goods and services	-2,7	-5,0	-0,7	-3,3	-1,9	14,4	16,0	15,4	15,3
Import of goods and services	-10,0	-13,1	-3,4	-12,9	-10,7	14,8	11,5	14,0	13,3

Source: State Statistical Office and Ministry of Finance's calculations
Note: Estimated data according to the European System of Accounts (ESA) 2010, published on 12.12.2014

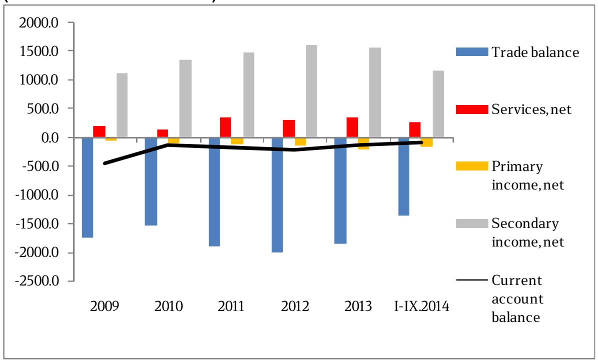
Analyzed according to the expenditure side, growth in the first three quarters in 2014 was driven by gross investments, experiencing real growth of 17.4%. Growth of gross investments corresponds to public sector's infrastructure investments and investments in capacities in the technological-industrial development zones (TIDZs) and industrial zones. Export of goods and services, which experienced 15.3% real growth, also contributed positively to the growth. Increase in export of goods was mainly a result of the increased export potential of the country. Export growth was accompanied by the change in the structure of the export towards products with higher value added, in line with the production and exports of companies in the TIDZs and industrial zones. Growth of gross investments and export growth inevitably influenced the import growth, increasing by 13.3%.

Personal consumption grew by 2.1%, as a result of the growth of disposable income of households in terms of growth in employment, wages and pensions, as well as by the intensified growth of crediting to households in this period, mainly in the form of consumer loans.

External sector. The current account developments were under the influence of structural changes in the domestic economy, which provided resistance to exports, amid still relatively unfavorable external environment. In the period January - September 2014, the cumulative deficit of the current account of the balance of payments amounted to Euro 96 million, which is by 8.2% higher compared with the same period last year. The expansion of the current account deficit was mainly caused by the higher deficit in the primary income and the lower surplus in the trade in services, despite the slight improvement in the trade balance and the higher net inflows of secondary income. Within the secondary income, net cash purchased in the currency exchange market was lower by 2.7%, reflecting the gradual normalization of these flows after their strong growth in 2011 and 2012.

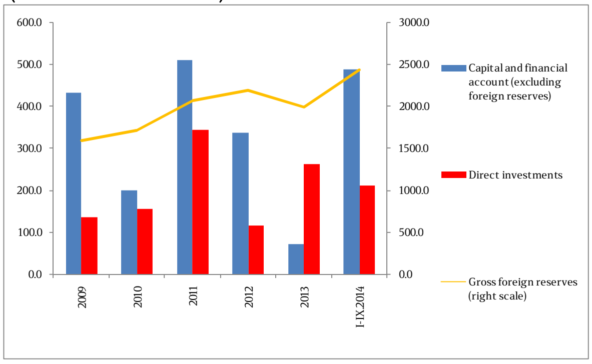
In the first nine months of 2014, the most significant contribution to the financial account inflows was made by the net inflows based on government external borrowing and FDIs. Namely, in the period January - September 2014, FDIs amounted to Euro 213 million, which is by 5% more than the same period last year. Within the structure, the majority (about 83%) refers to the intercompany debt, versus the smaller share of inflows in the form of equity capital and reinvested earnings. At the end of September 2014, gross foreign reserves stood at Euro 2,435 million, which is an increase of 22.2% compared with the end of 2013, mainly due to the high inflow based on the government Eurobond. Foreign reserves are maintained at an adequate level, providing average import coverage of five months in the next year.

Chart 2.1. Current account components
(in millions of euros)



Source: NBRM

Chart. 2.2. Capital inflows and foreign reserves
(in millions of euros)

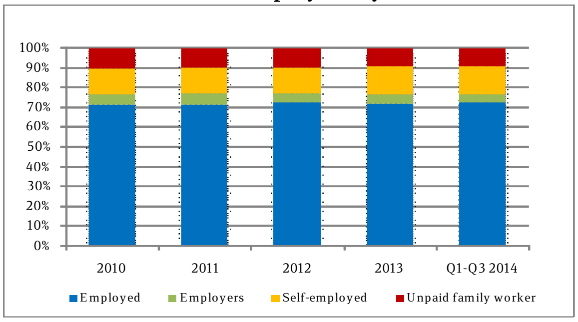


Source: NBRM

Labour market. Positive trends on the labour market continued in 2014. According to the Labour Force Survey, the number of employed persons in the first three quarters in 2014 was higher by 1.7% compared to the same period in the previous year. Increase of employment was accompanied by the drop of the number of unemployed persons, decreasing by 2.9% on annual basis. Such trends on the labour market caused for the unemployment rate in Q3 2014 to reduce to 27.9%, i.e. to drop by 0.8 p.p. compared to the same quarter of the previous year. In fact, in Q3 2014, unemployment was at the lowest level since the independence of the country until today.

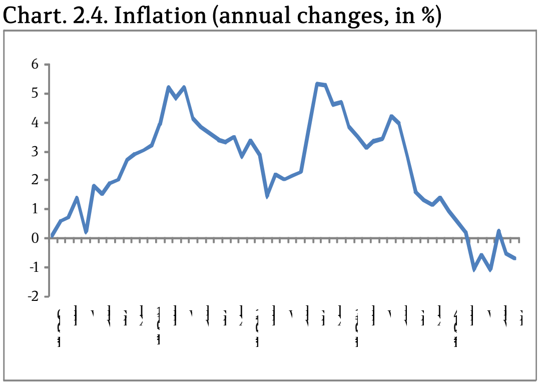
Employment rate in Q3 2014 amounted to 41.3%, being higher by 0.5 p.p. compared to the same quarter of the previous year. Active population in Q3 2014 accounted for 57.3% of total working-able population. Average net salary in the first nine months in 2014 was higher by 0.6% in nominal terms and by 0.8% in real terms in relation to the same period in 2013, while average gross salary grew by 0.4% in nominal terms and by 0.6% in real terms.

Chart 2.3. Structure of employees by economic status



Source: SSO

Chart. 2.4. Inflation (annual changes, in %)

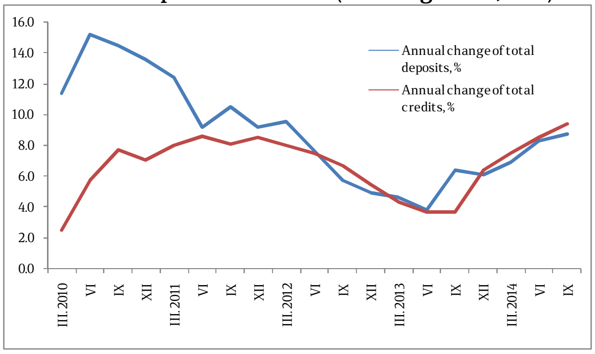


Source: SSO

Inflation. The average annual inflation in the period January-September 2014 mainly registered a downward trend of -0.2%. Observing components, the most significant contribution to the deceleration of average inflation was made by food prices, in line with the movements in world markets. The average annual core inflation, which excludes variable categories (food and energy) equals 0.8%.

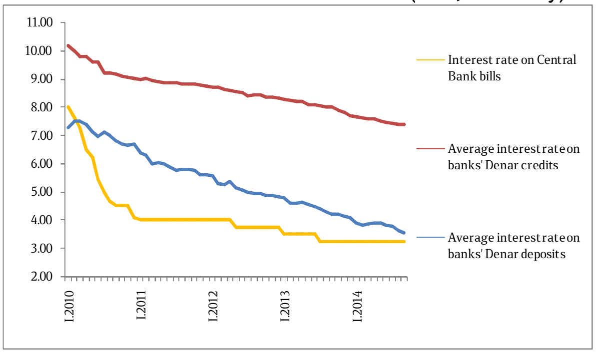
Monetary Developments and Exchange Rate. In the first three quarters of 2014, the environment for implementation of monetary policy can be assessed as favorable, with further conduct of accommodative monetary policy, mainly through non-standard measures. Given the solid economic activity, the annual growth of broad money M4 accelerated and in September 2014, climbed to 8.9%. At the same time, total deposits of domestic non-financial sector increased annually by 8.7%, with faster growth of Denar deposits (11.6%), compared with the increase in foreign currency deposits (5.3%), with the growth of Denar deposits making up about three quarters of the growth of total deposits. The average share of foreign currency deposits in total deposits in the crisis period reduced from about 55% in mid-2009 to approximately 43% in September 2014 (which is even slightly lower than the pre-crisis level of the end of 2007). Such a change in currency preference of entities is largely determined by the uncertainty regarding the crisis in the euro area, as well as the higher yields on Denar instruments, and also points out the credibility of the central bank. Analyzing by sector, the total deposits of households increased by 8%, and corporate deposits increased by 12.9%, with about two-thirds of the growth resulting from the growth of household deposits.

Chart.2.5.
Total banks' deposits and loans (annual growth, in %)



Source: NBRM

Chart. 2.6.
Interest rates of the NBRM and banks (in %, annually)



Source: NBRM

At the end of September 2014, bank loans to domestic non-financial sector registered a significant annual growth of 9.4%, given the continuing acceleration since the last quarter of 2013. The accelerated credit growth is in line with the growth in deposits and the more stable banks' perceptions for the domestic economic environment. The loan-deposit ratio averages around 90%, indicating room for higher lending. Analyzing by currency, most (95%) of the credit growth is mainly explained by the growth of Denar loans (11.6%), while foreign currency loans registered a small increase (1.9%). Such developments in the currency structure of loans are largely due to changes in the liabilities side driven by the growth of Denar deposits. The sector-by-sector analysis indicates that in the first nine months of the year, one should note the increased contribution of corporate loans from about 36% at the end of 2013 to 45% at the end of September 2014, amid reduced contribution of lending to households. The majority, or about 63% of total loans, is long-term.

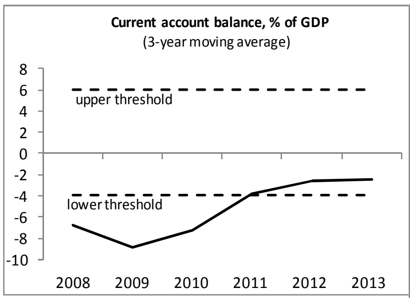
Interest rates in the banking sector registered a moderate decrease. The interest rate on total Denar loans decreased from 7.7% in December 2013 to 7.4% in September 2014. At the same time, the average deposit interest rate was down from 4.1% in December 2013 to 3.6% in September 2014. Given the greater reduction of the deposit interest rate, the interest rate spread increased to 3.8 percentage points. In December 2013, interest rates on foreign currency loans and foreign currency deposits equaled 6.4% and 1.6%, and in September 2014, they decreased to 6.2% and 1.3%, respectively.

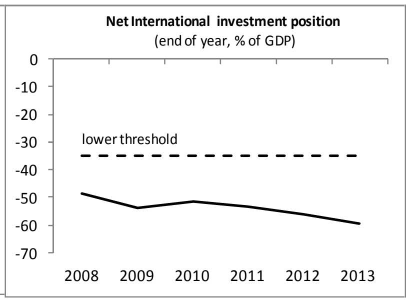
Box 2.1. Indicators for the Macedonian Economy in 2013 under the Macroeconomic Imbalances Procedure of the European Commission – prepared by NBRM

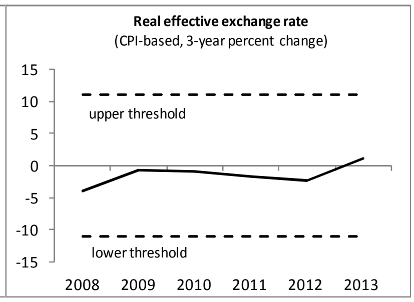
The Macroeconomic Imbalances Procedures - MIP[1] of the European Commission (EC), implemented for the member states of the European Union (EU), is aimed at monitoring, prevention and correction of macroeconomic imbalances on the basis of a list of scoreboard indicators to identify external and internal imbalances relative to indicative thresholds. This approach may be useful to determine the main areas of vulnerability in the candidate countries as well, and to see the extent of their convergence to the EU. The

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

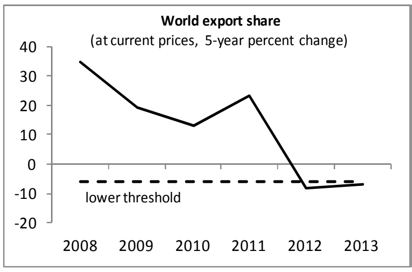
main indicators of macroeconomic imbalances within this approach for the Macedonian economy in 2013, according to the given thresholds, are given bellow.

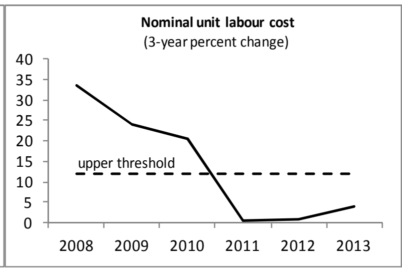


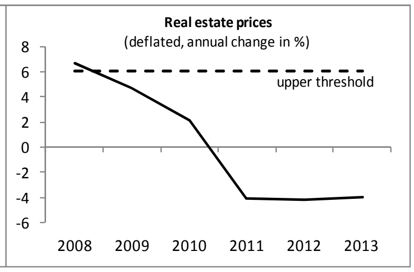




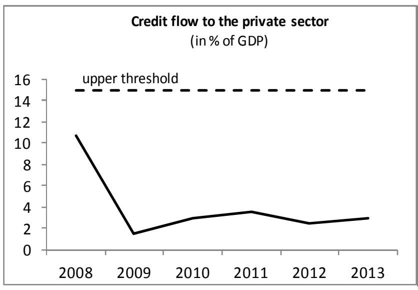
The current account deficit of the Republic of Macedonia, as a three-year moving average, mainly ranged at or below the lower threshold of vulnerability, thus presenting a zone of vulnerability of the economy in the years of rapid economic growth. In 2012 and 2013, this indicator narrowed, which is smaller than the minimum threshold of vulnerability (-4% of GDP) and swings within the allowable range. However, the EC's approach recognizes the need for flexible interpretation of this indicator in the converging countries, implying that a higher level of deficit would be acceptable if it is sustainable in the light of inflows on the capital and financial account.

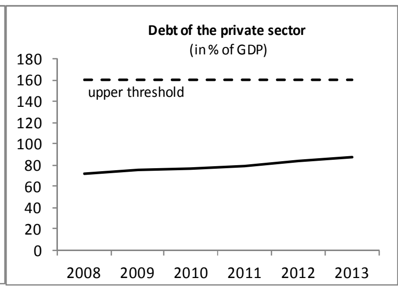


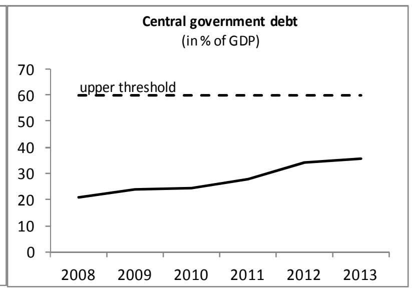


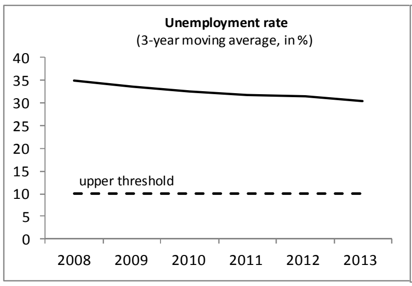


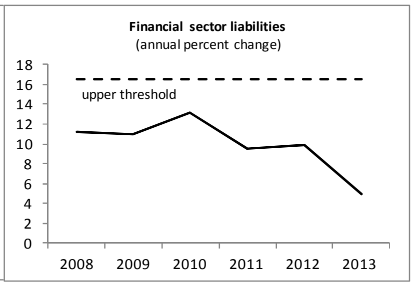
Since 2007, the net international investment position of the country has been widening, with some improvement in 2010 and re-expansion in the next three years. Thus, in 2013, it reached -56.2% of GDP. This level is well below the threshold of vulnerability of -35% of GDP, and therefore, the net debt of the economy abroad is considered a potential area of vulnerability. It should be borne in mind that the net international position on the liabilities side also includes foreign direct investments, which make up nearly half of the increase in total liabilities abroad in the past three years. In this light, when analyzing the converging countries, just because of the effect of foreign direct investment, under the EC's approach, other indicators should also be considered, such as net external debt, which covers only debt instruments, on a net basis. At the end of 2013, the net external debt of the Republic of Macedonia equaled 18.7% of GDP.











The real effective exchange rate (REER) is mainly depreciating, which contributes to the competitiveness of the economy. In 2013, the three-year change in REER indicates moderate appreciation of about 1%

(determined by the nominal effective exchange rate), which is within the allowable range. In 2005, the export market share of the economy in the world exports, as a five-year change, left the zone of vulnerability of the economy, registering a slower growth at the beginning of the global crisis, with some improvement in 2011. In 2012, this indicator dropped below the lower threshold (-6%), but in 2013, the rate of annual decline reduced and the indicator came closer to the threshold. Since 2007, the nominal unit labor costs, as a three-year change, entered the area of vulnerability, with a downward trajectory since 2009. In 2011, they entered the safe zone, and remained there over the next two years. *Generally speaking, in the area of external imbalances, the Macedonian economy shows potential vulnerability in the area of liabilities abroad. Although there are arguments to alleviate this issue, there is an obvious need for greater caution in this area. It could be expected that the export market share will gradually strengthen in line with the exports expectations in the period ahead.*

In the area of internal imbalances, the annual changes in banks' loans to the private sector are constantly below the threshold of vulnerability, with the highest annual change in loans of about 11% of GDP in 2008 being below the threshold of 15% of GDP. In 2013, changes in loans moderately accelerated to 3% of GDP, which is significantly lower than the threshold. At the same time, in 2013, the financial sector' liabilities recorded a slower rate of annual growth of about 5%, which is below the threshold (16.5%). Changes in property prices, after their peak in the period of economic expansion in 2008, when they were in the area of vulnerability, registered a downward trend beyond the zone of vulnerability, and in the period 2011-2013, they registered a negative annual change. The total domestic and foreign debt of the private sector (loans from domestic banks and abroad) was also constantly below the threshold of vulnerability. In 2013, it constituted 86.9% of GDP, which is half the threshold of 160% of GDP, but on the other hand, it should be noted that in recent years, it has recorded a steady growth trend. The government debt is also at a level that is almost twice as low compared to the threshold of 60% of GDP, but constantly growing in recent years. Unemployment is the biggest issue in the Macedonian economy, as confirmed by this approach. The unemployment rate, as a three-year moving average, although abating in recent years, has consistently been well above the threshold, which is set at 10%. *Hence, regarding internal imbalances, the Macedonian economy shows significant vulnerability to unemployment.*

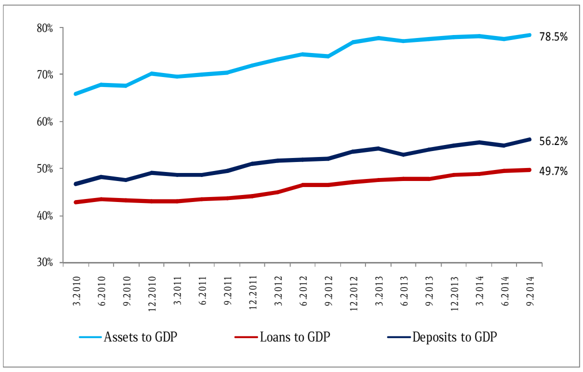
Latest developments in the financial sector.

Banking System. The banking system is the dominant segment of the financial system of the Republic of Macedonia, with the share in total assets of 87.6%. The banking system has preserved its safety and soundness, maintaining high and stable liquidity and solvency. As of September 2014, the banking system of the Republic of Macedonia comprises 15 banks. The ownership structure is prevailed by foreign capital, especially from the EU countries. Eleven banks are in dominant foreign ownership, seven of which are subsidiaries of foreign banks.

The activities of the Macedonian banks continued accelerating in 2014, which further increases the level of financial intermediation. At the end of September 2014, the shares of the total assets of the banking system, loans and deposits in GDP increased in comparison with the level at the end of 2013 (by 0.4 p.p., 1 p.p. and 1.4 p.p., respectively). At the same time, the trend of denarization on both the assets and the liabilities side of banks continued.

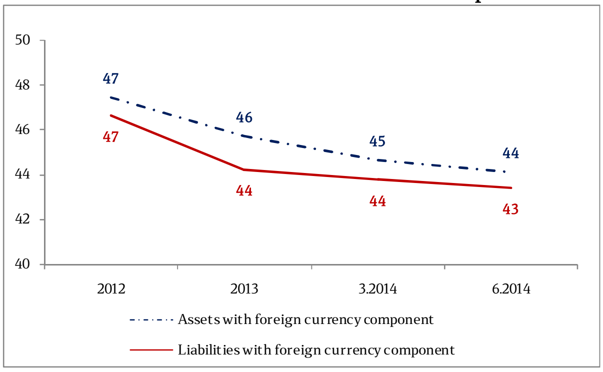
The credit risk is the most significant risk for the operations and stability of banks, which has still been maintained at a moderate level. In the second and the third quarter of 2014, the quality of loan portfolio of the banking system somewhat deteriorated, thus interrupting the trend of improvement in the previous three quarters. At the end of the third quarter of 2014, the share of non-performing loans to total loans equaled 12.2%, which is by 0.4 percentage points higher than in September 2013, exclusively due to the higher non-performing loans to the corporate sector. However, it should be noted that in the last three years, the share of non-performing loans is relatively stable (11.3% on average) and that during 2014, their annual growth rates have declined. The expectations that the economy will remain in the area of solid annual growth give grounds to assume that any further increase in non-performing loans in the corporate sector is significantly exhausted, taking into account the support of banks to some clients by reconstructing loans. The coverage of non-performing loans with impairments remained at a high level (about 100%), which reduces the risk to the stability of the banks from full non-collectability of non-performing loans.

Chart. 2.7. Level of financial intermediation



Source: NBRM.

Chart. 2.8. Assets and liabilities with FX component



Source: NBRM.

At the end of 2013, the total debt of the corporate sector[2] accounted for 66.1% of GDP, which is an increase of 1.3 percentage points. Yet, this is a slower pace of growth compared with 2012. The largest contribution (72.2%) to the growth of the debt was made by the debt to foreign creditors (mostly intercompany loans and trade credits). Observing structure, debt to nonresidents has the largest share in total debt (55.8%), followed by debt to domestic banks (42.7%), while the share of other segments of the financial system in the financing of domestic corporate sector is negligible. However, when determining the debt of companies abroad, one should also consider their claims from abroad (mainly on parent companies and trading partners), covering nearly half of the amount of external liabilities. In 2013, the indebtedness of households increased by 1.2 percentage points of GDP, yet retaining the relatively low level of 20.7% of GDP. Most of the debt (94%) is to domestic banks and the rest mainly refers to other domestic financial institutions.

Table 2.3. Basic bank risks indicators (in %)

	2012 Q4	2013 Q4	2014 Q3
Capital adequacy			
Capital adequacy ratio	17.1	16.8	16.5
Asset quality			
NPLs / gross loans - nonfinancial sector	10.5	11.5	12.2
Total provisions to NPL - nonfinancial sector	107.5	103.3	100.6
Profitability			
ROAA	0.4	0.6	0.9
ROAE	3.8	5.7	7.6
Cost to income	63.2	60.6	56.2
Liquidity			
Liquid assets/total assets	32.4	31.2	31.6
Liquid assets/short term liabilities	53.0	54.6	56.0
Sensitivity to market risk			
Net open foreign exchange position / own funds	11.4	15.6	14.0

Source: NBRM.

In the first nine months of 2014, the profit of the Macedonian banking system was by one third higher than the same period of 2013, and accordingly, improved the profitability indicators. ROA and ROE equal 0.9% and 7.6%, respectively. The main factor for the increase in profit is the decrease in interest expenses (mainly to households, primarily due to the downward trend of interest rates on term deposits) and the decrease of impairments of loans, which corresponds to the lower rate of growth of non-performing loans.

High and stable solvency and liquidity of the banking system contribute to solid resilience of the banking system to simulated shocks. The capital adequacy ratio in September 2014 equals 16.5% and it is twice as higher compared to the capital requirement. At the end of September 2014, one third of the assets were liquid assets that cover nearly 60% of total household deposits.

[2] Latest available data.

The resilience of the Macedonian banking system to unfavorable movements in the macroeconomic environment was tested using two adverse macroeconomic scenarios, which helped to assess the effects on the share of non-performing loans in total loans, the return on assets and the capital adequacy ratio of the banking system. The first adverse macroeconomic scenario is based on the scenario developed by the European Systemic Risk Board in April 2014[3] and the assumption that the adverse events in the EU would have effects on the Macedonian economy[4]. The second adverse macroeconomic scenario is the so-called historical scenario, which in a two-year period (Q1 2014 - Q4 2015) assumes mapping of the movements in the analyzed macroeconomic variables, generated in a selected past period (a period when the annual growth rate of GDP recorded the lowest value in the last eleven years under observation). The historical scenario is more extreme compared with the hypothetical macroeconomic scenario in the EU and assumes somewhat unfavorable movements in some macroeconomic variables.[5]

Macro stress tests use the so-called long-term elasticity coefficients, which takes into account the cumulative effect of the assumed changes in macroeconomic variables on the indicators for the banking sector. The results from the macro stress-testing indicate satisfactory resilience of the banking system to adverse developments in the macroeconomic environment. Although, according to these scenarios, non-performing loans would increase and the rate of return on average assets would reduce, the capital adequacy ratio of the banking system does not fall below 13%.

Relatively high resilience of the banking system to shocks is also confirmed by the sensitivity tests that are conducted on a regular quarterly basis. Simulations show that only in extremely high growth of non-performing loan exposure to non-financial companies (of 95%), or at doubling the rate of non-performing loans to non-financial companies, the capital adequacy of the banking system would stoop to 8%.

Capital market. In the period of January-September 2014, 9 issuers issued 337.709 ordinary shares and 2.500 priority shares on the prime capital market, in total amount of 1.181,78 denar million. In the period January-September 2014, the total turnover (classic trading and block transactions) on the Macedonian Stock Exchange was around 2.313,84 denar million. The number of listed companies by the end of September is 116 and their total market capitalization is around 93.901,87 denar million. On 30 September 2014 the Stock Exchange index MBI10 was 1.713,44 index points.

The number of joint stock companies with special report obligations that are listed on the MSEC Register by the end of September 2014 is 18.

In this period, 4 investment funds management companies that are managing 11 open ended investment funds are present on the capital market. In September MSEC gave approval for establishment of a new investment fund management company that plans to manage 2 open ended investment funds. On 30 September 2014 the net value of all open ended investment funds was around 1.512,96 denar million.

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[3] The scenario reflects the most important systemic risks assessed to be a relevant threat to the stability of the banking sector in the EU, estimating that the GDP growth rate of the EU would be lower than the projected in the baseline macroeconomic scenario (developed by the European Commission), by 2.2 percentage points in 2014, and by 5.6 percentage points in 2015, the unemployment rate in the EU would exceed the projections by 0.6 percentage points in 2014 and by 1.9 percentage points in 2015, etc. (for more details also visit https://www.eba.europa.eu/documents/10180/669262/2014-04-29_ESRB_Adverse_macroeconomic_scenario_-_specification_and_results_finall_version.pdf).

[4] According to the adverse scenario for the EU, the growth of the Macedonian economy would be lower than projected by 1.3 percentage points on average in 2014, or by 2.2 percentage points in 2015 (yet, the growth of the domestic economy would not enter the negative zone). The nominal lending interest rate would be by about 1 percentage point higher, on average, while the divergence in the real lending interest rate would be somewhat greater (about +3 percentage points, on average), given the reduction in the price level in the economy (in one part of the included time horizon, the annualized quarterly inflation rate would be negative). The employment rate in 2015 would be lower by almost 1 percentage point.

[5] This primarily refers to the annual GDP growth, which would be negative for three consecutive quarters.

Insurance Sector. The insurance market is characterised by a small share in the financial system. As of September 2014, there are 15 insurance companies, 27 insurance brokerage companies, and 11 insurance agencies active on the insurance market. There is moderate market concentration among the insurance companies, even though this trend is continuously declining. As of Q3 2014, 3 insurance companies have a market share over 10%, whereas the first 5 have a market share of 55.28%. Fourteen insurance companies are predominantly owned by foreign investors, owning 88% of the total equity, and only 1 insurance company is fully owned by domestic shareholders.

As of Q3 2014, the insurance companies issued gross written premium (GWP) in the total amount of 5.86 billion denars, of which 9.71% were from life insurance, and 90.29% from non-life insurance. Compared to the same period in 2013, there is 4.60% growth of GWP in the non-life insurance segment, and higher GWP growth of 21.86% in life insurance segment. The GWP growth in both insurance segments was 6.06%. Analysed by insurance class, motor vehicle insurance policies are predominant in the non-life insurance segment. The highest contribution comes from the compulsory third party liability motor vehicle insurance which has increased by 5%. The voluntary motor vehicle insurance (Casco) has decreased by 4.31%, whereas property insurance has increased by 5.43% and accident insurance has increased by 4.9%.

Fully – funded pension insurance. As of September 2014, the number of second pillar members is 368.031, out of which around 19% (69.513) are voluntary members and around 81% (298.518) are mandatory members. The value of the net assets in the second pillar is around 31,2 billion denars, which is a 20% increase compared to September 2013. About 25% of the assets are invested abroad, and the remaining 75% in domestic financial instruments.

As of September 2014 the number of third pillar members is 19.341, out of which around 28% are individual members and around 72% are members in occupational pension schemes. The assets of voluntary pension funds amounted to around 427 million denars, which is a 38% increase compared to September 2013. About 26% of the assets are invested abroad, and the remaining 74% in domestic financial instruments.

Leasing. On 30.09.2014, there are 8 leasing companies actively operating on the financial leasing market. In the ownership structure, foreign capital has dominant participation with 94.7%, which is 90% owned by foreign banks and financial institutions, while the remaining part is owned by foreign non-financial entities. The funds of the leasing sector amounted to Denar 5,562 million, decreasing by 14.6% compared to 30.09.2013. In the first 3 quarters of 2014, leasing companies realised total operating profit in the amount of Denar 26.3 million.

Number of new concluded contracts amounts to 779, which is an increase by 4.1% compared to the same period last year. The value of concluded contracts is Denar 834 million, which is an increase by 0.7%. Legal entities retained the main position in the structure of newly concluded contracts, accounting for 74.6%. The average interest rate of newly concluded contracts is 8.52%, decreasing by 0.46 p.p. compared to the same period last year.

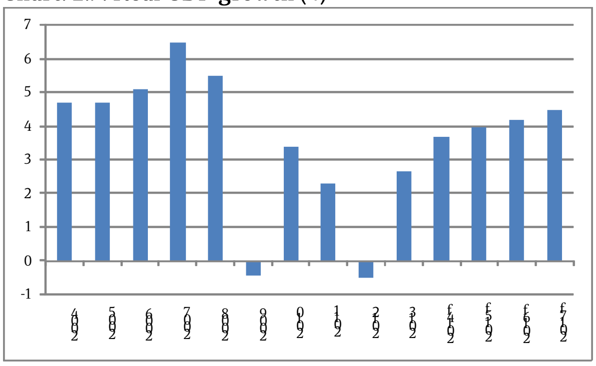
Financial companies. On 30.09.2014, there are 6 financial companies on the financial market in the Republic of Macedonia, which is unchanged compared to last year. Domestic capital has the largest share in the ownership structure of 56.3%, out of which 98.8% is owned by domestic natural persons. Foreign capital accounts for 43.7% and is owned by non-financial legal entities. Total assets of financial companies is 798.6 million denars, which is an increase by 8.1% compared to the same period last year. As of 30.09.2014, the financial companies realised 19.2 million denars profit and all of them presented gain in their balance sheets. The number of new contracts is 1,625 which is a decrease of 26.1% compared to last year. The value of new contracts was 538.9 million denars, which is a decrease of 45.4% compared to last year. Issued credit cards have the highest share in the structure of the new contracts with 50.5%, followed by approved loans with 37.1% and factoring with 12.4%. Natural persons kept the main position in the structure of new contracts.

2.2. MEDIUM-TERM MACROECONOMIC SCENARIO

Macroeconomic policy of the Republic of Macedonia is aimed at fulfilling the strategic commitments of the Republic of Macedonia to long-term and sustainable economic growth, boosting competitiveness of the economy, job creation and better living standard of the population.

Fiscal policy in the period 2015-2017 will be aimed at supporting the economic growth by realising major investment projects, ensuring at the same time sustainable level of budget deficit and public debt. Such approach will contribute to higher economic growth rates in the short run, and boosted competitiveness of domestic economy in the medium and long run. In addition, in coordination with the monetary policy, it will contribute to achieving sustainability of the external position of the country and preserving macroeconomic stability.

Chart. 2.9. Real GDP growth (%)



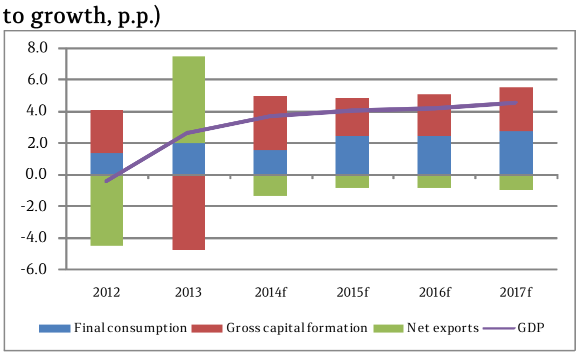
Source: SSO and calculations of MoF, f - forecast

With respect to the EU, as the most significant trading partner to the Republic of Macedonia, following the stagnation of the economic activity in 2013, slow economic recovery and achieving low economic growth rates, with prospects for certain growth intensification (see table 2.1) is expected in the next medium-term period. Taking into account such expectations for the external surrounding, as well as the active fiscal policy of the Government of the Republic of Macedonia and the structural reforms for boosting competitiveness of the country, certain intensification of the economic growth of the Republic of Macedonia is expected in the period 2015-2017.

Gross Domestic Product. On the basis of the above-mentioned assumptions, in the period 2015-2017, growth of economic activity in the Republic of Macedonia is expected to account for 4.2% in average, with prospects for certain growth intensification. Economic growth is expected to be 4% in 2015 and 4.2% in 2016. They are revised downwards compared to the expectations of the last year's Programme, as a result of the deteriorated expectations for the EU growth. In 2017, the economic growth is envisaged to amount to 4.5%.

Positive growth of industrial production, as well as its diversification, is envisaged to continue during the next medium-term period as well, in line with the expectations for the foreign demand and the increased production potential of the country as a result of the investments in the free economic zones. Thus, in the period 2015-2017, industry growth is expected to account for 4.8% in average. Construction sector is expected to realise average 7.5% growth rate in real terms in the observed period, as a result of the planned infrastructure projects and announced investments in the TIDZs and the industrial zones. Real growth rates by years and sectors are shown in table 1e of

Chart. 2.10. GDP by expenditure method (contribution to growth, p.p.)

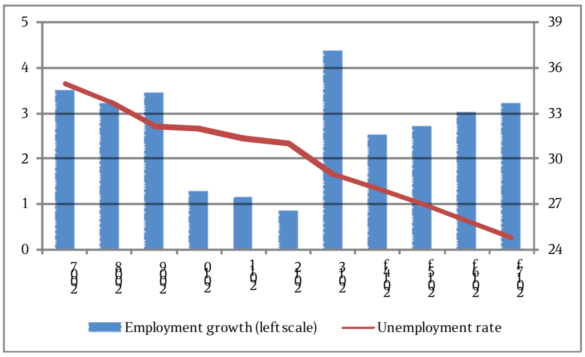


Source: MoF calculations and projections, f - forecast

Annex 1. The services sector accounting for the most in the GDP creation is expected to record average 3.5% growth rate in real terms in the analysed period, while the agriculture is expected to surge by 2.4%.

Analysed according to the expenditure side of GDP (Chart 2.10), domestic demand is expected to make a positive contribution to the economic growth. Projection for growth of gross investments in the analysed period amounts to 8.1% in average in real terms. Projected growth of gross investments is based upon the expectations for gradual growth of private investments (driven mainly from FDIs) and the increased investments of the public sector, as main driver of investments in the infrastructure. As for the public investments, realisation of major infrastructure projects is envisaged, aimed at improvement of the transportation network in the country, improvement of energy and utilities infrastructure, investments aimed at improvement of the conditions in the education, social and health system. These investments will contribute to boosting the competitiveness of the country in longer run, being of key importance for increasing production and productivity of economy. During the period 2015-2017, personal consumption is expected to experience average real growth of 3.4%, mainly as a result of the expected increase in the number of employees. Public spending is expected to surge by 1.1% in average in this period.

Chart. 2.11. Employment growth and unemployment rate



Source: SSO and calculations of MoF, f - forecast

Export of goods and services is expected to achieve average real growth of 8.8% in the analysed period, mainly as a result of the increased activity of the existing and opening new export capacities as a result of FDIs, in conditions of low growth of economic activity in the EU, i.e. foreign demand. Growth of export of goods is expected to be also accompanied by further improvement of the export structure of the country. Anticipated increase of domestic demand and export activity also provide for increase of import which, in this period, is expected to be 7.9% in average.

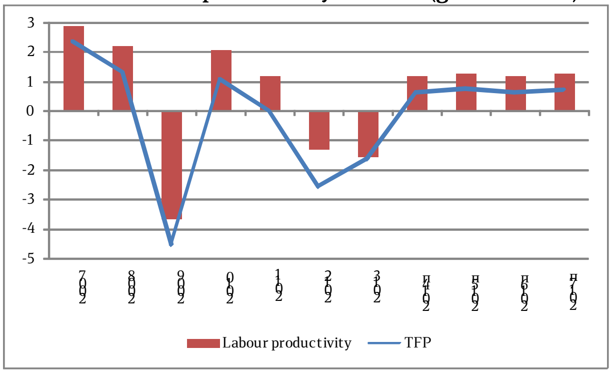
Labour market. Envisaged economic growth in the period 2015-2017 is expected to have positive effects on the labour market trends. According to the projections, number of employees is expected to experience average annual growth of 3% in the analysed period, as a result of the expected investment of foreign companies in the TIDZs and industrial zones, active labour market policies and measures that will be implemented during this period, facilitated access to finance for companies and the realisation of capital infrastructure projects. This will, on other hand, result in decline in the number of unemployed persons by 2.7% in average in the analysed period. Demand growth in this period is expected to reflect on the labor supply, projected to surge by 1.4% in average. Such trends on the labour market imply for average employment rate to increase to 44.4% in 2017, while unemployment rate is projected to reduce to 24.8%. Active population in 2017 is expected to reach 58.4% of the working-able population. Labour market indicators by years are shown in Table 1c, Annex 1. Average net salary is expected to amount to 3.5% in nominal terms in the analysed period.

Sources of Growth. Chart 2.12 shows growth of both labour productivity and total factor productivity (TFP)[6] in the period 2007-2017. Taking into account the projected growth rates of investments in fixed assets and the number of employees, TFP growth in 2014 is envisaged to transfer into positive zone, i.e. to account for 0.7%. In the period 2015 – 2017, as shown in the

[6] TFP is residual of growth of other factors to economic growth, labour and capital.

chart, productivity of production factors is expected to have positive contribution to the economic growth. TFP contribution to growth in the period has an average share of around 17%. Labour is expected to contribute to economic growth with 54.7%. Physical capital, according to the projections on investment growth, in the analysed period, is expected to grow by 5.4% in average, contributing by 28.3% to total economic growth.

Chart. 2.12. Labour productivity and TFP (growth rates)



Source: SSO and calculations of MoF, f - forecast

Potential Growth. Calculation of potential output is basis for assessing the cyclical position of the economy. Hodrick Prescott filter was used for calculating the potential output. This method belongs to the group of statistical approaches and, according to it, potential GDP growth is estimated at 3.4%. Still, estimated rate of potential growth should be interpreted with caution, taking into account that the method applied is based solely on GDP historical data[7]. Production gap in percentage of the potential output for the period 2013 - 2017 is shown in table 5 of Annex 1. In line with the projections on production growth in the coming medium-term period and the assessments of the trends, in 2015, cyclical component of output is to be in the negative zone in average throughout the year. In 2016, production gap is expected to transfer into positive zone and to remain positive in 2017.

Monetary and exchange rate policy. During 2013, at relatively stable inflation and solid level of foreign reserves, the basic interest rate of the NBRM was cut twice (in January and July, by 25 basis points each time), and was reduced to the record low of 3.25%. Additional relaxation was made through the change in the instrument of reserve requirement that came into force at the beginning of 2013, which reduced the reserve requirement base of the banks for the amount of newly approved loans to sectors whose growth reduces the external vulnerability of the economy (net exporters and energy sector). It is a non-standard measure, with a period of application by the end-2014. In July 2013, the reserve requirement on banks' Denar liabilities was reduced from 10% to 8% with a simultaneous increase in the ratio for foreign currency liabilities from 13% to 15%. Moreover, a 0% reserve requirement was introduced on liabilities to non-residents. These changes are intended to support the process of de-euroisation, to release the liquidity of banks and to increase inflow of funds from non-residents, especially foreign financial institutions.

Amid slower inflation and favorable balance of payments position, in the first three quarters of 2014, the NBRM continued to conduct accommodative monetary policy, mainly through further implementation of non-standard measures (in reserve requirement) taken in 2013. Additionally, since the beginning of January 2014, the NBRM does not pay reserve requirement remuneration, for the purposes of further use of available tools and active use of the advantages provided by the measures adopted. In February, the interest rate on seven-day deposit facilities decreased from 1.5% to 1.25%, bringing it closer to the interest rate on overnight deposit facilities (0.75%). Additionally, in October, both interest rates were cut by 25 basis points to 0.5% and 1% on overnight deposit facilities and seven-day deposit facilities, respectively, which emphasized the role of these tools exclusively for balancing short-term liquidity fluctuations, and also strengthened the mechanism for further investment of banks' excess liquidity in long-term investments.

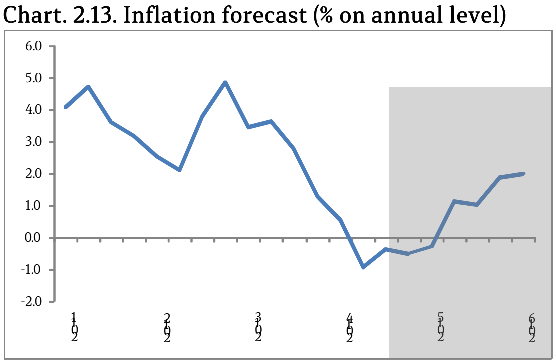
[7]Trend value is assessed by minimising the gap between the real production and the trend and the variability thereof for the whole sample.

Given the slowing rate of inflation (determined by exogenous factors), the external sector developments, the solid growth of the economy, the recovery of loans and expectations that previously made changes in different monetary instruments will give effects on the credit growth in the coming period, in the first three quarters of 2014, the monetary policy preserved the policy rate unchanged. At the end of September, in order to further support credit growth, the effectiveness of the decision to release the reserve requirement for loans to the export and energy sector was extended to the end of 2015 (previously to end-2014), which is expected to make contribution to maintain credit growth.

In the next three years, the monetary policy will remain oriented towards preserving price stability by maintaining a stable exchange rate of the denar against the euro. The results of the models for assessing the equilibrium real effective exchange rate[8] of the denar as of the last quarter of 2013, do not indicate major misalignments from the equilibrium level and in the period 2003 - 2013, they are maintained within acceptable range of +/- 4%, and in 2013, they indicate a small undervaluation of the rate[9].

In the period of turbulent external environment, the monetary policy confirmed its flexibility and appropriately adjusted its monetary instruments, in order to encourage credit growth, while achieving its primary and intermediary monetary goal. In this context, the monetary policy provided sufficient stimulus, the credit growth revived, and some of the measures are expected to produce effects in the next period. According to the forecasts of the other segments of the economy, in the next three years, we can expect moderate inflation developments and generally favorable movements in the foreign exchange market, although accompanied by risks. Fiscal policy, and in particular the way of financing the budget deficit in the period ahead, remains a significant factor for the environment for conducting monetary policy, which also emphasizes the importance of monetary and fiscal coordination. The dynamics and structure of credit growth in terms of consumer lending against investment lending, and the foreign exchange market developments will be crucial for the monetary setup in the next period. Monetary authorities remain ready to take appropriate measures, if necessary, to maintain price and financial stability in the economy.

Chart. 2.13. Inflation forecast (% on annual level)



Source: NBRM

Inflation. Global inflation factors in the medium term suggest moderate acceleration of domestic inflation after its low level in 2014. In 2014, the foreign effective inflation[10] is estimated at 0.3%, given the low inflation in all import partners. In 2015, foreign inflation is expected to reach 1.3% and in 2016, it is expected to increase moderately to 1.8%.

In 2014, the price of oil decreased, due to the high supply, weaker demand and the strengthening of the US dollar. Imbalances between market fundamentals are expected to continue next year, while the downward trend in the oil price is expected to exhaust greatly in 2016 and 2017. Risks surrounding oil prices are mostly upward, with the main uncertainty arising from the possible escalation of geopolitical tensions in the world. In the second half of 2014, food prices registered

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

[9] IMF's analyses also confirm that there is no significant misalignment in the real exchange rate (IMF Staff Report for 2013 Article IV Consultation and first post program monitoring discussions, June 2013, p.17).

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

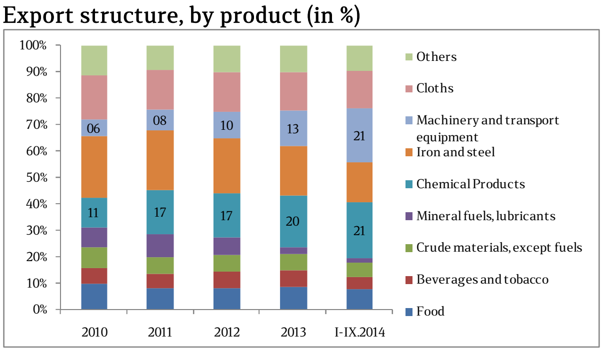
pronounced downward movements. The price reduction in the global market of primary food products is expected to continue in 2015, given the higher yields of wheat and corn from the current harvest, the increased inventory and improved prospects for future production. On the other hand, prices of wheat and corn are expected to follow an upward trajectory during 2016. The main risk with regard to these prices remains associated with the uncertainty of the weather in the coming period.

In the last quarter of 2014, the average annual inflation rate in the Macedonian economy is expected to keep pace from the previous quarter. Consequently, the average inflation rate in 2014 is expected to be around 0%. The unchanged average price level compared to the previous year reflects the negative changes in the prices of energy and food, with a relatively small increase in core inflation. Compared with last year's scenario, when inflation was expected to equal about 2.3%, in 2014, in this scenario, the inflation is estimated at a lower level, which is mainly due to the greater reduction in the global prices of food and oil than expected and their second-round effect on others prices in the economy. Under assessment of negative output gap, inflationary pressures from the demand side were not present.

In 2015, the price level is expected to gradually increase and inflation to be around 1%. The growth of prices in the next year will primarily reflect the price changes of food products, and to a lesser extent, the effects of further growth of the domestic demand. On the other hand, it is expected that energy prices in 2015 will have a negative impact on the overall rate of inflation, assuming the absence of a possible growth of the regulated price of electricity. The risks to the projected path of inflation in 2015 are attributable to the uncertainty about the global economy and movements in the prices of global primary products. It is expected that the acceleration of the rate of inflation will continue throughout 2016 and 2017, when it is expected to slowly approach the historical average and to equal about 2%.

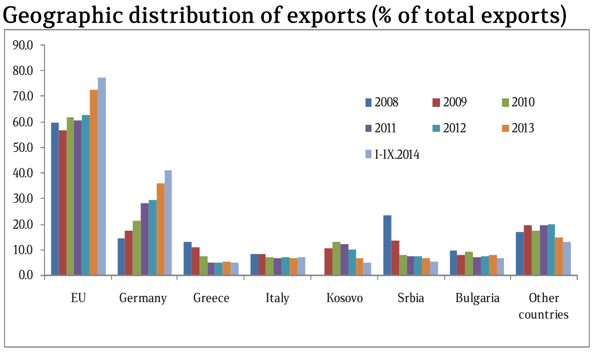
External Sector and Its Sustainability in the Medium Term. The developments in the current account of the balance of payments of the Republic of Macedonia in 2014 are in line with the acceleration of economic growth, given the strengthening of the positive effects of new production facilities on the total exports, amid still relatively weak import demand. According to the trends and estimates for the last quarter of the year, the current account deficit for 2014 was estimated at 2.7% of GDP, which would be a moderate widening of 0.8 percentage points compared to the previous year. This change mainly results from the reduced surplus in secondary income and the small widening of the deficit in trade in goods and services abroad. However, the estimated deficit for 2014 is lower than expected in the macroeconomic scenario for the period 2014-2016 (4.6% of GDP), mainly due to the lower trade deficit than expected.

Chart. 2.14.
Export structure, by product (in %)



Source: SSO.

Chart. 2.15.
Geographic distribution of exports (% of total exports)



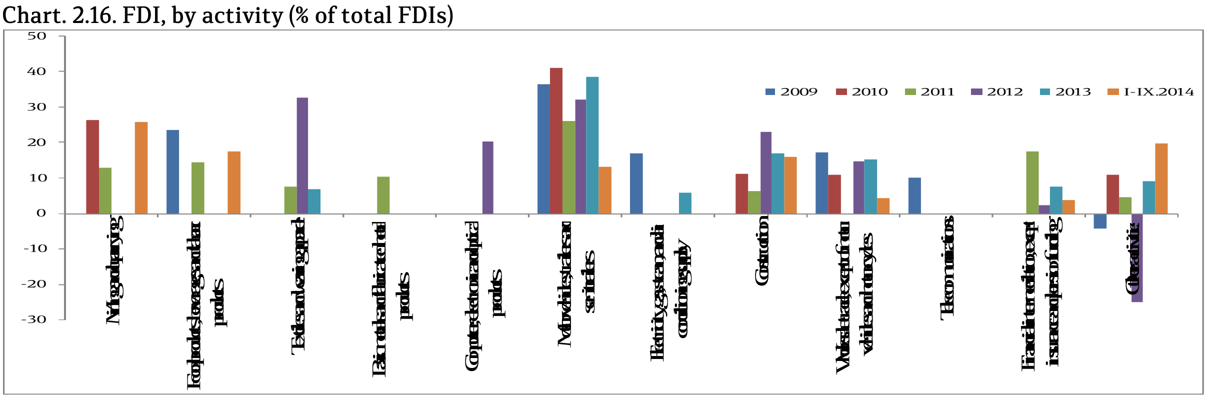
Source: SSO.

In the period January - September 2014[11], the trade deficit totaled Euro 1,268 million, which is by 1.3% lower relative to the same period last year, with the export growth (16.2%) exceeding the import growth (by 10%). The increase in exports is mainly due to higher export of machinery and transport equipment and chemical industry products, which mainly reflects the impact of new production facilities in the technological industrial development zones. The increase in imports was mainly due to the higher import of raw materials and equipment, in line with the accelerated pace of economic activity. In the period January - September 2014, the highest deficits in goods were registered in the trade with Great Britain and Greece, while significant surpluses were registered in the trade with Germany and Kosovo.

Analyzing the structure, as a result of new capacities in the economy, the export structure significantly improved. It is based on the gradual increase in the share of products with higher value added on the export side, mainly chemical products, and machinery and transport equipment. Changes in export structure correspond with foreign direct investment, which in the recent years, were mainly concentrated in these sectors. In the period 2009-2013, on average, about 66% of the new foreign capital is invested in the tradable sector, where one can expect its further contribution to greater export diversification. On the other hand, there is a decrease in the share of traditional export products - iron and steel and textile products, with a slight decrease in textiles versus the faster decline in iron and steel. In recent years, unfavorable trends in export of iron and steel have been influenced by the unfavorable movements in the international market of metals and the fall in their prices. Exports of mineral fuels and lubricants have seen permanent reduction on the export side in recent years, which mainly reflects the change in the business orientation of the oil refinery, which is in foreign ownership (with reflection on both sides of the trade).

The analysis of geographic distribution of Macedonian exports confirms the dominance of the EU as a major export destination, where in the period January-September 2014, around 77% of the Macedonian exports were realized, with the share of exports to Germany increasing (positive developments have also been registered in the export to Belgium, at lower initial share). In the period January - September 2014, the total trade of the Republic of Macedonia to the EU increased by 17.7% on an annual basis and constituted 69% of the total trade of the Republic of Macedonia. Moreover, in the trade with the EU, there was a 16.3% annual narrowing of the deficit.

Chart. 2.16. FDI, by activity (% of total FDIs)



Source: NBRM.

In the period from January to September 2014, the real effective exchange rate (REER)[12] of the denar deflated by the consumer price index and the producer price index registered a slight annual appreciation of 1% and 0.9%, respectively. Given the favorable price ratio, i.e. faster

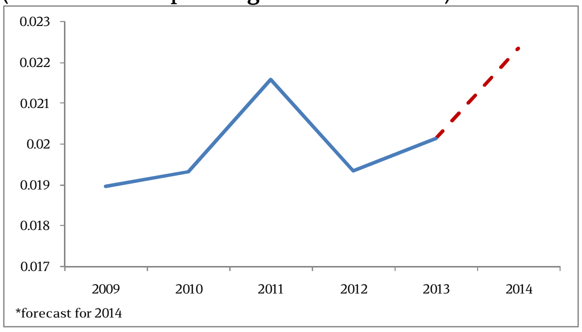
[11] According to foreign trade statistics, where imports are presented on CIF basis.

[12] Within the REER, the calculation of the nominal effective exchange rate and relative prices includes 15 major trade partners of the Republic of Macedonia by their share in foreign trade in the period 2010-2012 and the base period 2010.

growth of foreign domestic prices in both indices, this change reflects the appreciation of the nominal effective exchange rate of the denar against the currencies of some of the most important trading partners. In the first two quarters of 2014, the nominal unit labor costs decreased by 1.9%.

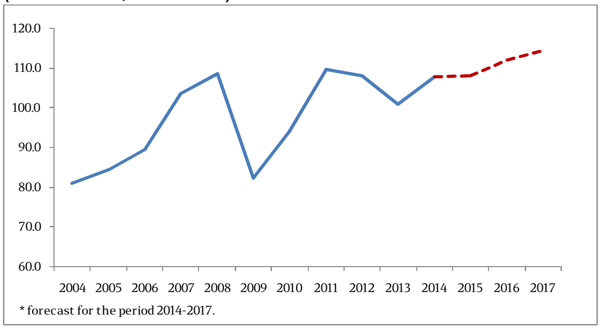
Export market share of the economy in the world exports, after the slowdown at the onset of the global crisis, increased in the period 2010-2011, but in 2012, it slowed down again (given the slight decline of the Macedonian exports amid increase in the world exports). However, the adverse change in the export market share was adjusted in 2013, given the actual increase in exports, in line with the recovery of the Macedonian economy. The growth in export market share is estimated to have continued in 2014, given the rapid growth of the Macedonian exports. The degree of trade openness of the Macedonian economy is generally high, at about 100% in recent years, with a slight slowdown in 2012 and 2013, reflecting the reduced trade during the second wave of the crisis. After the recovery in 2014, the degree of trade openness of the economy is expected to gradually increase in the period ahead.

Chart. 2.17. Export market share (in % of world export of goods and services)



Source: NBRM, IMF.

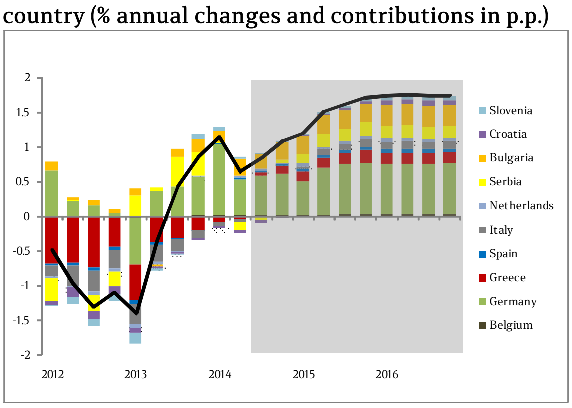
Chart. 2.18. Trade openness (total trade, % of GDP)



Source: NBRM.

Balance of Payments Forecast - Assumptions about the External Environment. The global economic recovery that began in early 2013, despite the slowdown in 2014, is expected to continue in the coming years. In this light, in 2014, the foreign effective demand for Macedonian products[13] is estimated to have recovered on an annual basis, registering an increase of 0.9%, which is less than expected in the last scenario (1.2%). Economic activity of trading partners is expected to further intensify in 2015, when the growth in foreign demand is projected at 1.5% (versus 1.8% as previously expected), and at 1.8% in 2016. Observed through the contributions of individual countries, the most significant contribution to the strengthening of foreign demand is expected from the German economy, followed by the Bulgarian economy and additionally, from the recovery of the Serbian and Greek economy.

Chart.2.19. Foreign effective demand, total and by country (% annual changes and contributions in p.p.)



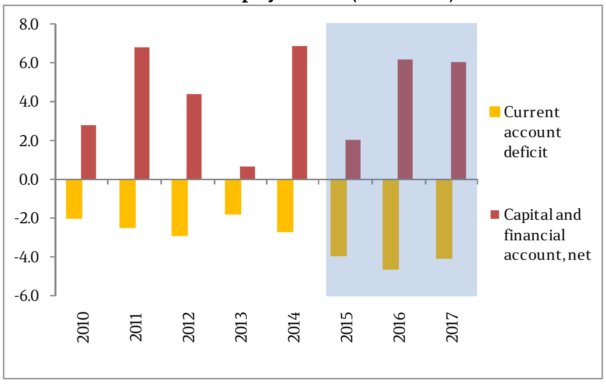
Source: NBRM, Consensus Forecast.

The latest external sector estimates indicate a moderate current account deficit, as well as further growth of foreign reserves in the next three years and their maintenance at an adequate level. Namely, the stronger demand in the economy in the following period is expected to create

[13] The calculation of external demand takes into account the GDP growth rates (from Consensus Forecast) of the ten most important trading partners, according to their share in the Macedonian exports in the period 2010-2012.

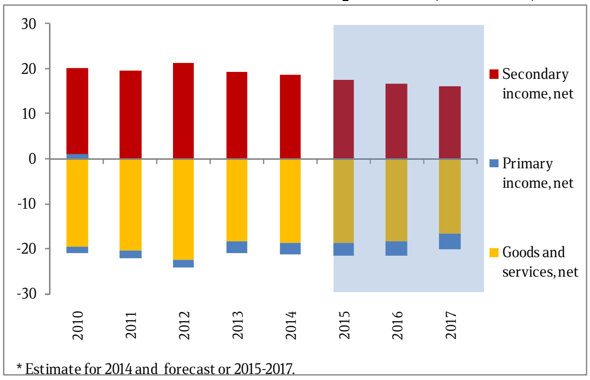
import pressures, but they would be relatively modest. In addition, the increasing exploitation of the potential of the new facilities with foreign capital is estimated to mitigate to some extent the effects on imports caused by the growth of exports and increasing investment and private consumption. In the next three years, the needs for external funding are expected to be covered by borrowing and direct investments to the extent sufficient for further accumulation of foreign reserves. Hence, it is expected that capital inflows would ensure retention of an adequate level of foreign reserves.

Chart. 2.20. Balance of payments (% of GDP)



Source: NBRM.

Chart. 2.21. Current account components (% of GDP)



Source: NBRM.

Along with the recovery of foreign demand, with further positive effect of existing companies with foreign capital, as well as those pending to be established and to start production, exports of goods and services in the next three years is expected to grow further. The imports of goods and services in the next three years would be driven by growth in imports for the needs of production intended for exports, as well as imports caused by increased investment and personal consumption. Thus, part of the new FDI inflows during the establishment of capacities reflect the increased import of machinery and equipment. At the same time, some of the planned public infrastructure works in the medium term are expected to increase import of services. In 2014, despite the high exports, especially of new industrial capacities, it is estimated that more intensive import of raw materials intended for production for export will contribute to a moderate expansion of the estimated deficit in the balance of goods and services to 18.8% of GDP (18.5% of GDP in 2013). In 2015 and 2016, the deficit in trade in goods and services is expected to stabilize and to equal about 18.4% of GDP. In 2017, given the expected slowdown in imports and retention of the growth rates of exports as a result of the contribution of the new facilities, the deficit in the trade in goods and services is expected to moderately narrow to 16.8% of GDP.

An important part of the deficit in the trade in goods and services will continue to be funded from the inflows based on secondary income, which in 2014 are expected to remain relatively high, but lower compared to the previous year. Namely, within the secondary income, in 2013 and 2014, the level of private transfers gradually normalized, after exhaustion of the effects associated with the uncertainty and the crisis in the euro area, which were present at the end of 2011 and in 2012 during the higher net purchase in the currency exchange market (main component of private transfers). In 2014, the level of net inflows based on secondary income is estimated at 18.6% of GDP, compared to 19.3% of GDP in 2013. The reduction in the relative importance of this category is expected to continue in the next three years, at a moderate pace. For 2015 and 2016, it is projected at about 17%, and in 2017, it would be 16% of GDP. Thus, these inflows would be approaching the level achieved in the years of economic expansion, which is consistent with their counter-cyclical nature. The deficit in the category of "primary income" in the current account for 2014 is estimated at 2.5% of GDP, while in the next three years, it is expected to be maintained at about 3% of GDP.

In such projected movements in the current account items, for 2014, the current account deficit is estimated at 2.7% of GDP, while in 2015 it is expected to moderately widen to 3.9% of GDP. This trend is expected to continue in 2016, when the negative current account balance is expected to reach 4.6% of GDP, which amid relatively stable trade deficit in goods and services will result from the expected further reduction of inflows of private transfers. However, in 2017, the current account deficit would slow down to 4.1% of GDP considering that the expected significant narrowing of the trade deficit exceeds the effect of the expected slowdown in private transfers. This forecast of the current account balance mainly reflects the expected long-term effects of the FDI inflows in the tradable sector in recent years, which have already contributed to changes in the structure of the economy, greater export diversification, and in the long term, given the expected favorable external environment and strengthening of their export potential, they are expected to contribute to the narrowing of the trade deficit.

In 2014 and the next year, capital inflows will mainly result from the expected FDIs, the projected external debt of the public sector and the expected debt of the private sector. The growth of the domestic economy, the improvement of global environment and the stabilization of global financial markets are expected to contribute to maintaining positive perceptions among investors. In 2014, the FDI were estimated at 3.6% of GDP and in the next three years, they are expected to gradually grow and in 2017 to reach 4.2% of GDP. In 2014, the total net inflows on the financial account are estimated at nearly 7% of GDP, and in 2015, they would be lower (around 2% of GDP) considering the projected outflows for repayment of the government Eurobond. In the next two years, net financial inflows are expected to be maintained at around 6% of GDP. Projected trends in the current and financial account are estimated to provide additional accumulation of foreign reserves in the next three years and further maintenance of relatively stable and adequate coverage of the average imports of each coming year.

International investment position and external debt. In the first three quarters of 2014, the negative international investment position (IIP) increased by 5.2% compared to the end of 2013, amid faster growth in liabilities to abroad in absolute terms compared to the growth in the foreign assets. Thus, the negative IIP in September equals 56.7% of GDP, which relative to the end-2013 it is a moderate enlargement by 0.5 p.p. of GDP. The largest contribution in the widening of the negative net IIP came from the government sector[14], considering its borrowings from abroad, and also the "other sectors" contributed in the same direction reflecting net liabilities based on FDI. On the other hand, the monetary authority improved its net positive IIP, considering the significant increase in the foreign reserves (mainly due to inflows from the Eurobond), which largely offset the widening of the Government net position. Additionally, the banks registered lower negative IIP, net.

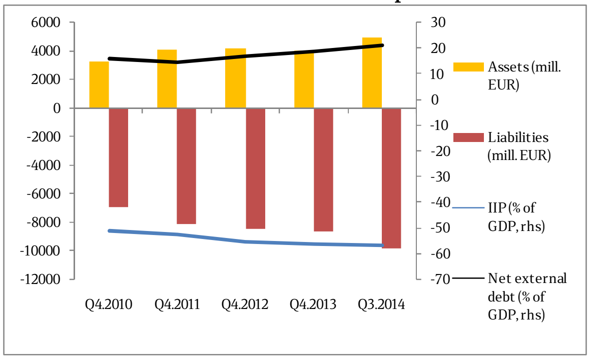
Having in mind the significant share of the FDI on the foreign liabilities side (about 50% in the last several years), which is characteristic for the converging economies, when analyze the external position, it is desirable to consider other indicators, as well, such as the net external debt, which encompasses the debt instruments only, on a net basis. At the end of the third quarter of 2014, the net external debt of the Republic of Macedonia amounted to 20.9% of GDP, which is an acceleration of 2.2 percentage points of GDP relative to end-2013.

At the end of the third quarter of 2014, the gross external debt amounted to Euro 6,029.9 million (excluding repo transactions of the NBRM, which appear in almost the same amount on both, the liabilities and the claims to non-residents, as well). The gross debt equals 71.3% of GDP and compared to the end of 2013 it is higher by 7 percentage points of GDP. This increase is almost entirely due to higher debt of the public sector, while the external debt of the private sector only slightly increased (by 0.2 p.p. of GDP). The growth of public sector debt mainly reflects the net

[14] The government sector includes: central government, local government and social insurance funds.

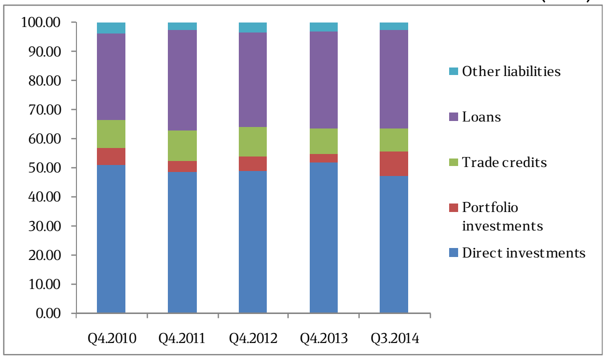
borrowings of the Government based on the issued Eurobond. The funds of the Eurobond are intended for financing in the next year, therefore they reflected in increase of the Government's foreign currency deposits. The long-term debt continues to dominate the debt structure, with a share of around 70%.

Chart.2.22. International investment position



Source: NBRM.

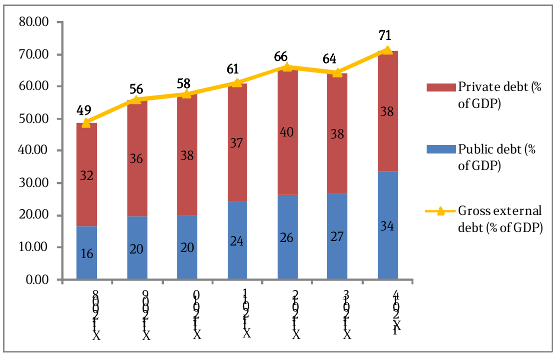
Chart.2.23. Structure of the international liabilities (in %)



Source: NBRM.

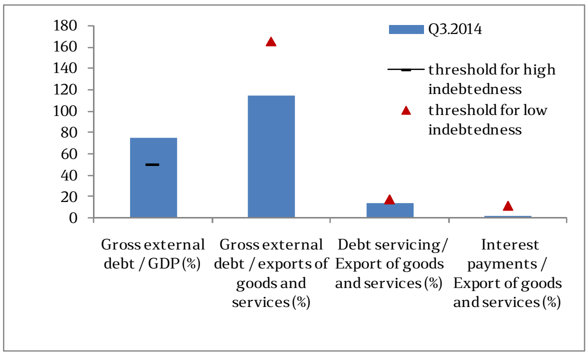
The indicator of the coverage of the short-term debt by residual maturity with the foreign reserves at the end of the third quarter of 2014 equals 1.2 which points out a solid liquidity in the payments to abroad. The analysis of the external indebtedness[15] of the Republic of Macedonia points to low indebted country according to three indicators (gross external debt, debt servicing and interest repayment relative to the exports of goods and services, individually), while the share of the gross external debt to GDP is the only indicator that points to high indebtedness. The forecast regarding the financial account of the balance of payments for the 2015-2017, suggests that the first three debt indicators calculated as ratios to exports of goods and services are expected to improve in the next three-year horizon, given the expected acceleration of the export, mainly as a result of the new companies with foreign capital. In terms of maturity structure, the long-term debt is expected to remain dominant.

Chart. 2.24. Gross external debt



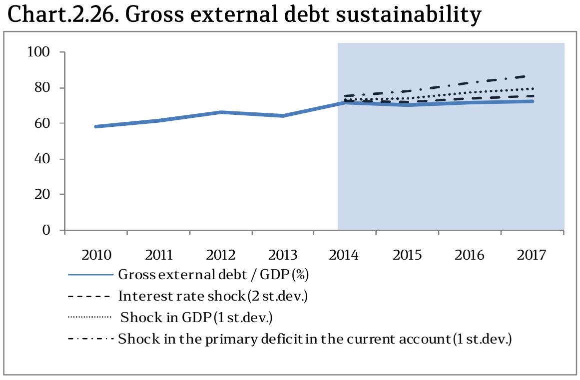
Source: NBRM

Chart.2.25. Indicators of indebtedness



Source: NBRM.

Chart.2.26. Gross external debt sustainability



Source: NBRM.

[15] Based on the approach of the World Bank, in which in the calculation of the indicators three-year moving averages of GDP and exports of goods and services are used as denominators. The methodology defines also the indebtedness criteria as reference values for the degree of indebtedness.

The base scenario of the external debt sustainability analysis[16] indicates that after the increase of the gross external debt in 2014, in the next three years it will remain at similar level, with small fluctuations from year to year. The primary deficit of the current account (excluding interest payment) is the main debt crating flow, amid an increase in foreign reserves is expected in the analyzed period. On the other hand, the automatic debt dynamics (which includes the impacts of GDP growth, changes in the nominal interest rate, price and exchange rate changes) as well as non-debt capital flows contribute towards debt decline. The stress tests show that the expected external debt stabilization of the medium run, however, is particularly sensitive to the shocks in the primary deficit of the current account and in the economic growth.

Banking system. The intensification of economic activity and stabilization of risk perceptions are expected to contribute to further maintenance of solid banks' credit growth during the coming period. Namely, it is estimated that credit growth in 2014 will be 8.7%, and over the next two years, the credit dynamics is expected to further accelerate (about 9% and 10%, respectively). The expected credit growth reflects the positive signals on both supply and demand sides. Namely, the growth in household consumption and investments will contribute to a stable demand for loans. On the supply side, a positive contribution is expected from the continued growth of the deposit base, as well as the banks' stable risk perceptions. In addition, favorable effects over lending are still expected from the standard and non-standard measures undertaken by the NBRM. Concerning the deposit potential, it is estimated that by the end of 2014, the growth of deposits in the banking system will continue, and at the end of the year, it will reach 8.8%. The expected acceleration of economic growth and particularly the growth in employment and wages are estimated to lead to further growth of the deposit base with relatively high rates of around 9% and 10% in the next two years.

2.3. ALTERNATIVE SCENARIO AND RISKS

Risks. Risks to the projected economic growth rates are generally related to the global economic trends, above all the pace of EU’s economic recovery. On the shorter run, low economic growth in the Eurozone will most probably be the most serious potential risk to the growth in the developing countries such as the Republic of Macedonia. Materialisation of risks pertaining to weaker economic performance in the EU and other trade partners to the country can worsen the prospects for growth of the economic activity in the Republic of Macedonia. On the other hand, faster progress of the structural reforms in the Eurozone than the expectations and strengthening of the investors’ confidence are positive risks, the materialisation of which can contribute to higher growth of the Macedonian export and industrial production and higher inflow of capital in the country. In addition, effect of new FDIs, being in the phase of realisation or being announced, can be expected to fully materialise in the next several years.

The main risks to the presented scenario for the external sector in the next period still arise from the dynamics of the global recovery and its influence on the growth of the domestic economy and investor perceptions. Any weaker external demand may have adverse effects on the presence of domestic exporters in foreign markets. In addition, the movements of world prices is accompanied by uncertainty. Also, risks of lower capital inflows of non-debt financing or possible capital outflows in order to finance parent companies are not excluded, although in this scenario, private capital inflows are projected at a lower level, and therefore, this risk is partially covered.

Assessment and scope of the effects of new export capacities in the economy is crucial for the trade balance forecast. The number of export capacities in the economy has been increasing and after the establishment of production, they begin to contribute to the country's exports. The

[16] External debt sustainability analysis is according to the IMF approach. The base scenario assumes average GDP growth rate of 4.5% and balance of payment forecast presented in this document.

trade deficit in 2014 was lower than expected, mainly as a result of the new export companies, which pointed to an upward risk (potential risk for the future, too). In the medium term, changes in the production structure are expected to lead to further diversification of exports and to improve export performance, which goes in favor of strengthening the resilience of the economy to external shocks. Given the growing number of new production capacities in the economy, and the expected improvement of the global environment, the expectations in this regard are justified. At the same time, the forecast of net inflows from secondary income (within their frameworks of the net cash purchased on the currency exchange market), which assumes a gradual slowdown of their share in GDP, can generally be assessed as conservative, which reduces the downward risks to the this category and also leaves room to compensate for possible downward risks in the trade balance within the current account.

The risks to the inflation forecast is mainly conditioned by the assumptions about the movements in the prices of primary commodities, changes in regulated prices and their possible second-round effect on other prices in the economy. Thus, the projected inflation rate of about 1% in 2015 does not include the effect of a possible increase in electricity prices. The estimated effect on the average annual inflation of eventual increase in the price of electricity in mid-2015 of 10% would equal 0.4 percentage points. In the light of conditionality of inflation mainly from exogenous factors on the supply side, the risks to the projected path of inflation in the medium term is difficult to assess.

Expectations for credit growth in banks are mainly associated with balanced risks. Positive trends in the economy can stimulate higher credit growth, given the room within banks' balance sheets for further lending. On the other hand, the dynamics of global recovery in the context of its impact on domestic economic growth and quality of the loan portfolio, as before, would affect the banks' risk perceptions and consequently, the lending. The risks associated with the business strategies of foreign banking groups would also have effects on the operations of their subsidiaries in the country.

It is worth mentioning that the overall macroeconomic scenario is largely conditioned upon the implementation of the fiscal strategy for 2015-2017. The fore mentioned risks to the macroeconomic scenario for the next three years point to a need for constant monitoring of any changes in the external and domestic economic conditions in the period ahead and timely taking of adequate measures by policy makers.

Alternative scenario. Alternative macroeconomic scenario is based on the assumption for lower economic growth in the EU and other trade partners to the country in the analysed period. According to this scenario, real GDP growth in 2015 is projected at 2.7%, at 2.9% in 2016 and at 3.2% in 2017.

Such scenario implies weaker external demand and adverse effects on the domestic exporters, i.e. lower growth of export of goods and of industrial production in the country. This is expected to also affect the inflow of capital in the country in the form of direct investments, implying slower growth of gross investments in the medium term, as a result of the lower growth of investments in the construction sector and of import of investment goods (equipment, machines, etc.).

According to this scenario, real export growth is projected at 5.5% on average in the analysed period. Real growth of gross investments is expected to account for 4.7% in 2015, 5% in 2016 and 5.2% in 2017. Lower growth of gross investments in relation to the baseline scenario is mainly due to the slower growth of private investments, and growth of public investments to a certain extent. Effects on the consumption are expected to be modest as a result of the slower recovery of foreign demand in relation to the baseline scenario. Hence, real growth of public consumption is projected at 0.8% on average in the analysed period. Real growth of private consumption is projected at 2.6% on average. Lower growth of both export and domestic demand implies slower growth of import of goods which, on average in the analysed period, is envisaged to surge by 4.8%.

As regards labour market, sluggish economic growth implies slower growth of the number of employees and slower pace of reduction of unemployment rate compared to the baseline scenario. Hence, according to the alternative scenario, average annual increase in the number of employees is expected to be 2%, resulting in drop of the number of unemployed persons by 1.8% on average in the analysed period, assuming that projected rates of both reduction of inactive population and of growth of working-able population have not changed in relation to the baseline scenario. Such trends on the labour market caused for the employment rate at the end of 2017 to drop to 25.8% and employment rate to surge to 43.6%. Active population in 2017 is expected to account for 58.7% of the working-able population.

As regards inflation rate, it is assumed that trends of primary commodity prices remain unchanged in relation to the baseline scenario, i.e. we assume similar projections as regards the developments on the supply side and the level of foreign prices. Slower economic growth, according to the alternative scenario, implies that no inflationary pressures by the demand are expected, taking into account that negative production gap is projected to be closed in 2017. Hence, unlike the baseline scenario, no upward pressure of domestic demand is expected on the inflation rate in 2017, and it is projected to be 2% (see table 1b to compare).

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

3. Fiscal Framework

3.1. Policy Strategy and Medium-Term Objectives

Medium-term fiscal framework defines the most important goals and policies, as well as the medium-term macroeconomic and fiscal projections, through which stronger linkage between the defined strategic priorities and the available sources of financing is established. Government of the Republic of Macedonia has adopted 2015-2017 Medium-Term Fiscal Strategy. Defined goals for increasing the economic growth and employment, as precondition for higher living standard of citizens, integration of the Republic of Macedonia in the EU and NATO, mean successful management of public finances and continuous improvement of the structure of public expenditures in direction of significant share of capital investments in total expenditures.

Table 3.1. Consolidated general government budget (Denar million)

	2015	2016	2017
Consolidated general government budget - Revenues	175,072	181,305	188,129
% of GDP	31.6	31.0	30.2
Consolidated general government budget - Expenditures	193,569	200,263	206,391
% of GDP	35.0	34.2	33.2
Consolidated general government budget - Deficit	-18,497	-18,958	-18,262
% of GDP	-3.3	-3.2	-2.9
Central Budget - Revenues	113,001	116,368	120,233
% of GDP	20.4	19.9	19.3
Central Budget - Expenditures	131,448	135,326	138,495
% of GDP	23.8	23.1	22.3

Central Budget - Deficit	-18,447	-18,958	-18,262
% of GDP	-3.3	-3.2	-2.9
Budget Funds - Revenues	33,151	35,387	37,714
% of GDP	6.0	6.0	6.1
Budget Funds - Expenditures	33,201	35,387	37,714
% of GDP	6.0	6.0	6.1
Budget Funds - Deficit	-50	0	0
% of GDP	0.0	0.0	0.0
Local Government Budget - Revenues	28,920	29,550	30,182
% of GDP	5.2	5.0	4.9
Local Government Budget - Expenditures	28,920	29,550	30,182
% of GDP	5.2	5.0	4.9
Local Government Budget - Deficit	0	0	0
% of GDP	0.0	0.0	0.0

Source: Ministry of Finance

Projection of public finances in the next medium-term period is based on the commitment for gradual fiscal consolidation, in line with the expectations for the macroeconomic indicators in the coming period, as well as the effects of the planned structural reforms and expected FDI inflows.

Projected revenues of the consolidated government budget in the next three-year period decline relatively as a share of GDP, from 31.6% of GDP in 2015 to 30.2% in 2017. As a result of continuity in implementing disciplined budget policy and strengthened consolidation of public spending, in the period 2015-2017, total expenditures will also decline from 35% in 2015 to 33.2% in 2017. Set basic postulates of the fiscal policy in the coming period provide for gradual reduction of the deficit level and its positioning at optimal level of around 2.9% of the projected GDP in 2017.

3.2. BUDGET IMPLEMENTATION IN 2014

Under the 2014 Budget of the Republic of Macedonia, total revenues are projected at Denar 155,554 million, total expenditures at Denar 175,157 million, i.e. deficit of Denar 19,603 million was projected, core budget deficit out of which amounts to Denar 15,553 million, deficit on the own revenue accounts is Denar 3,950 million, deficit of Pension and Disability Insurance Fund is Denar 100 million, as well as balanced budgets of Health Insurance Fund and Employment Agency.

In the period January-September 2014, total realised revenues of the Budget of the Republic of Macedonia amounted to Denar 104,564 million or 67.2% of the annual projections. Within the total revenues, Denar 92,931 million was realised on the basis of tax revenues and social contributions, i.e. 88.9% of total realised revenues. Tax revenues accounted for the most in the structure of total revenues with 58%, followed by contributions with 31%, non-tax revenues with 7%, while capital revenues and other revenues accounted for 2% and 2% respectively.

Tax revenues in the period January-September 2014 were realised in the amount of Denar 60,777 million. VAT revenues accounted for the most in the structure of realised tax revenues with 53%, excises participated with 21%, personal income tax with 14%, profit tax with 6%, import duties with 5%, while other tax revenues participated with 1%. Revenues on the basis of social contributions, as genuine revenues of the Pension and Disability Insurance Fund and the Employment Agency were generated in the amount of Denar 32,154 million in the analysed period.

In the period January-September 2014, total expenditures of the Budget of the Republic of Macedonia were realised in the amount of Denar 122,018 million or 69.7% of the expenditures projected for 2014. Denar 110,424 million out of them was spent for current expenditures, while the capital expenditures amounted to Denar 11,594 million. During this period, Denar 17,194 million was paid for salaries and allowances to the employees in the institutions, being budget users, while expenditures related to goods and services accounted for Denar 11,038 million. Transfers accounted for the most in total budget expenditures, for which Denar 78,682 million was paid in this period, which, in addition to social transfers in the total amount of Denar 57,789 million (on the basis of pensions, health protection, employment and social welfare benefits) also include the transfers to the municipalities on the basis of VAT and block and earmarked grants in the amount of Denar 11,510 million for financing the transferred competences at local level. Category transfers also include the expenditures on the basis of agricultural subsidies paid by the Agency for Financial Support in Agriculture and Rural Development.

In the same period, the repayment of principal amounted to Denar 7,171 million, while interest-related payments amounted to Denar 3,510 million. Out of the total outflows on the basis of repayment of credits, outflows for repayment of principal to domestic creditors amounted to Denar 1,584 million, while Denar 5,587 million were outflows for repayment of principal to non-resident creditors.

In the period January-September 2014, deficit was realised in the amount of Denar 17,454 million, as a result of the realised revenues in the amount of Denar 104,564 million and the realised expenditures in the amount of Denar 122,018 million.

Financing of budget needs was provided from foreign and domestic sources, mainly by issuing Eurobond in the amount of EUR 500 million funding in 2014 and 2015 was thus provided), through regular disbursement of credit lines earmarked for individual projects, as well as by borrowing under World Bank's Development Policy Loan II for Competitiveness. In order to promote government securities market, quality of government securities structure was continuously improved in the course of 2014 in order to increase the maturity by new issues of government bonds with 2-, 3-, 5- and 10-year maturity and completely excluding maturities shorter than 1 year.

Table 3.2. Budget of the Republic of Macedonia 2014 (Denar million)

(Denar million)	Budget 2014	Realisation in the period January-September 2014
1. Total revenues	**155.554**	**104.564**
1.1. Tax revenues and contributions	131.376	92.931
1.1.1 Tax revenues	86.673	60.777
1.1.2 Contributions	44.703	32.154
1. 2. Non-tax revenues	14.697	7.679
1.3. Capital revenues	4.177	1.563
1.4. Donations	5.304	2.391
2. Total expenditures	**175.157**	**122.018**
2.1. Current expenditures	154.073	110.424
2.1.1 Salaries and allowances	23.605	17.194
2.1.2 Goods and services	18.636	11.038
2.1.3 Transfers	107.431	78.682
2.1.4 Interest	4.401	3.510
2.2. Capital expenditures	21.084	11.594
3. Deficit	**-19.603**	**-17.454**
4. Deficit financing	**19.603**	**17.454**

4.1 Inflow	30.463	24.625
4.1.3 External sources	36.889	35.643
4.1.3 Domestic sources	6.150	5.363
4.1.4 Deposits/Additional sources	-12.676	-16.391
4.1.5 Revenues on the basis of sale of shares	100	10
4.2 Outflow	10.860	7.171
4.2.1 Repayment upon foreign borrowing	9.133	5.587
4.2.2 Repayment upon domestic borrowing	1.727	1.584

Source: Ministry of Finance

3.3. MEDIUM-TERM BUDGETARY OUTLOOK

Total genuine revenues of the Budget of the Republic of Macedonia (central government) for the period 2015-2017 are projected to around 28.8% of GDP, whereby their share in GDP by years is reduced, in conditions of unchanged tax policy, i.e. keeping low tax rates and low the tax burden of the business sector. Thereby, tax revenues account for around 54.5% in the projected revenue structure, followed by revenues on the basis of social contributions with around 30%, non-tax revenues and capital revenues with around 12.5%, while the rest of the revenues are expected to be realised from IPA Funds and other donations. With respect to tax revenues, most revenues will be realised on the basis of VAT, personal income tax and excises.

Projections for social contributions, which are genuine revenues of the Pension and Disability Insurance Fund, Health Insurance Fund and the Employment Agency, in the next medium-term period, are based on the expected economic trends and structural reforms in this area. The legal obligation for payment of social contributions for persons engaged with contractual and author agreement will provide greater social protection for these persons, they will enjoy all the rights arising from the healthcare and pension insurance systems, and simultaneously the fiscal position of social funds will be improved. Non-tax revenues in the next medium-term period account for around 10.2% of the total revenues, and the most significant is the share of revenues on the basis of administrative fees, concessions from mineral raw materials and other non-tax revenues the budget users realise to their own accounts.

Projection of the revenues of the Budget, with respect to foreign donations, in the coming period include the donations the budget users would realise for specific projects, as well as the disbursements from the EU pre-accession funds.

Expenditure side of the Budget in the next medium-term period is planned for the purpose of fully supporting Macedonian economy through increased investments in infrastructure projects, as well as adequate protection of targeted groups of the population (pensioners and beneficiaries of social benefits). Thereby, disciplined budget spending will continue to be implemented, with an emphasis to restrictiveness and rigorous control over less productive costs, on one hand, and increase of investments in capital projects on the other. Average share of expenditures in the Budget in the period 2015-2017 is around 31.9% of GDP.

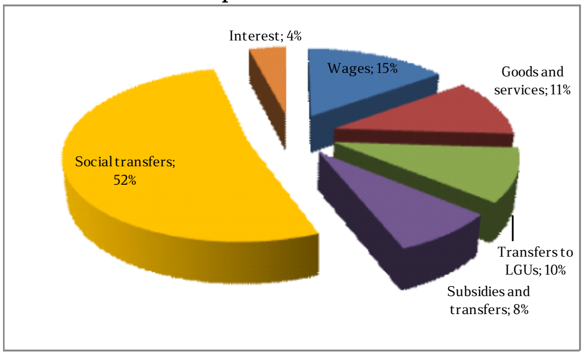
When projecting the current expenditures for the next period, the following assumptions were taken into account:

- as regards expenditures related to salaries and allowances, continuation of strict control over new employments and effect from the increase of salaries in the public sector in 2014. Further increase of salaries will be a result of detailed calculations for each fiscal year, according to the possibilities of the Budget, and depending on the fiscal condition and effects from the external economic trends;

- total and timely payment of increased pensions and social benefits, for the purpose of ensuring the well being of the beneficiaries of these rights. Expenditures for pensions are planned for the purpose of ensuring further protection of this category of citizens, which will be realised according to the possibilities of the Budget. Within the medium-term projections, what is planned is increase of social benefits for socially most vulnerable families and regular servicing of liabilities on the basis of child allowance, allowances on the basis of rights of disabled persons, invalids of war and civilian invalids and asylum seekers. Planned reforms in the social sphere, by simplifying the procedures for exercising these rights, as well as the effects from the integration of social centers in unique information system, will provide certain savings at the same time extending the scope and proper targeting of these allowances towards the most vulnerable categories. Activities regarding social policy are supported under the Conditional Cash Transfers Project, financed by the World Bank's (WB) loan, aimed at supporting the Government of the Republic of Macedonia in its efforts to reduce poverty of vulnerable groups by conditioning the existing pecuniary allowances.

- further provision of funds for payment of agricultural subsidies, to the end of supporting competitiveness of this sector. Planned reforms in the agricultural sector, as well as the significant amount of subsidies and funds under IPARD Programme will provide for its further enhancement and support, create conditions for establishing efficient and competitive agricultural sector and its successful EU integration, also contributing to boosting export of Macedonian agricultural products and conquering new markets.

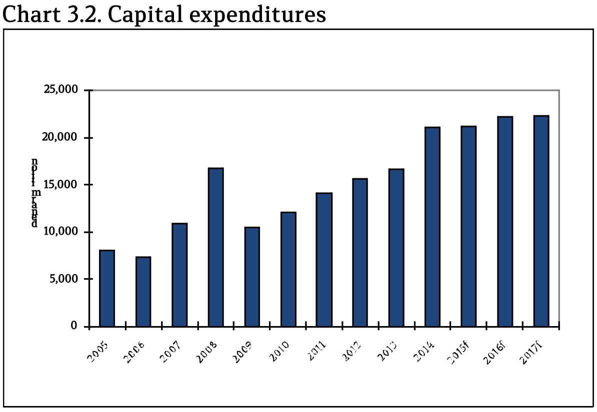
Chart. 3.1. Current expenditure structure



Source: Ministry of Finance

- improvement of the quality of higher education, improvement of vocational education, as well as stimulating the innovation capacity in Macedonian companies. The realisation of the Skills Development and Innovation Support Project was commenced during 2014 aimed at strengthening institutional capacities of universities, strengthening of quality of vocational education and defining the necessary vocational skills and their advancement in the course of the educational process, i.e. advancement of the skills needed for work. The Fund for Innovation and Technological Development (FITD) will stimulate and support innovation activities in micro, small and medium enterprises and newly established enterprises. The capacity of companies will be improved by transfer of knowledge and technology, research and development and innovation. Through its work the Fund will support projects that basically lead to establishment of new businesses, creating new jobs (especially for young and high qualified / specialized persons), fostering sustainable growth of businesses, connecting research with entrepreneurship and consequently development of products and services that would be competitive in the global market. FITD activities are presented in depth in the part Better industrial structures.

Chart 3.2. Capital expenditures



Source: MoF

Capital expenditures include public investment, which represent the development component of the fiscal policy and are a prerequisite for improving economic prospects and better quality life of citizens. In the past few years, capital projects financed from the Budget fully confirmed its viability and strongly influenced in dealing with the effects of the economic crisis. In order to achieve and maintain positive rates of economic growth, a significant amount of the Budget is expected to be allocated for public investment in the next 3 years, while in the 2015 Budget amount of Denar 21,208 million is provided for this purpose.

In the next medium-term period the focus of public investment will be on implementation of several key projects which support policies and measures in many areas. For implementation of these policies and measures funds through loans from several international financial institutions are provided.

Efficient and reliable transport infrastructure facilitates and encourages mobility of people and goods, exceeds limitations of local markets, creates preconditions for balanced regional development and enables stronger integration with the markets from the region and connecting with the common EU market. The Republic of Macedonia has made significant progress in the implementation of projects for construction of road and railway sections along Corridor VIII and Corridor X (Xd) that are part of the South East Europe Transport Observatory (SEETO) and are in accordance with the Multiannual SEETO Plan. Sectoral reforms, measures and projects in the transport sector are presented in detail in the section Physical capital.

Activities for modernisation of existing energy infrastructure and construction of new energy facilities are planned in the next period, enabling increased reliability in energy supply, taking into account the greater inclusion of renewable energy sources (RES) in energy consumption, which is one of the main strategic objectives of the Government of the Republic of Macedonia in the energy sector.

Construction of National Gasification System will supply the business sector, public sector and households with cheap and environmentally friendly energy, at the same time reducing the emission of harmful gases in the atmosphere. Public calls for stakeholders interested in building gas distribution networks in Skopje, Eastern and Western part of the country are published. Other sectoral reforms, measures and projects in the energy sector are presented in detail in the section Physical capital.

Public investment at local level include number of measures and activities in several areas. Strengthening of management at local level and improving municipal services is presented in detail in the section Local government budget. Increasing the quality of life, especially in rural areas, supply of clean drinking water and waste water drainage, modernisation of irrigation systems and creating new employment opportunities will be achieved through implementation of several projects in different regions.

In the field of health, improving health infrastructure, delivery of appropriate health services and introducing new and upgraded equipment and technology is realised through many reforms and activities. In 2015, implementation of the Project for construction, reconstruction and modernisation of the University Clinical Centre “Mother Teresa” in Skopje and the Regional Clinical Hospital in Shtip will commence, which will be financed with budget funds and Council of Europe Development Bank (CEB) loan.

Measures and activities for building physical education facilities in primary and secondary schools, as will as rehabilitation of primary and secondary schools in the Republic of Macedonia, financed with CEB loan and Budget funds will continue to be realised in the period to come.

One of the important elements in the social policy is to increase the quality of life of low-income persons and the vulnerable groups by providing appropriate housing. Investments in construction of flats for low-income persons are supported under the Project for Housing of Vulnerable Groups. The funds are provided from the Budget and a CEB loan. Also, under the IPA

Human Resources Development Component, rehabilitation and equipping of local social welfare centers and local centers of the Employment Agency is planned in 2015, in order to modernize conditions in these facilities and increase quality of services provided to socially vulnerable and unemployed citizens.

To the end of ensuring human rights as regards conditions for accommodation, hygiene, health protection and leisure time of the convicted and detained persons, the implementation of the Project for Reconstruction of Penitentiary Institutions, financed with CEB loan amounting to Euro 46 million, will continue. The realisation of this Project will contribute to reconstruction of 4 houses of correction, by implementing the standards set in the European Prison Rules.

To the end of continuing the reforms for protection of property and legal relations and registration of property rights, activities related to the already commenced cadastre reform for improving delivery of public services in the real estate cadastre and registration of rights, having direct impact on the economic development through the real estate market, will be completed in 2015.

Projected Deficit and its Financing. Financing of the projected deficit will be provided from foreign sources (favourable loans from international financial institutions, credit lines intended for financing certain projects, Eurobonds and other type of foreign borrowing) and domestic sources (issues of government securities). As a result of the good macroeconomic situation and the moderate level of indebtedness of the country, entrance of foreign investments and strong exports, as well as reduction of unemployment rate, Republic of Macedonia issued the third Eurobond on the international capital market under exceptionally favourable conditions, thus providing funds for financing the budget needs in 2015 and repayment of the Eurobond in the amount of EUR 150 million, falling due in December 2015.

Table.3.3. Projected deficit and sources of its financing (Denar million).

	2015	2016	2017
Bugdet balance	**-18,497**	**-18,958**	**-18,262**
Deficit financing	**18,497**	**18,958**	**18,262**
Inflows	**44,667**	**39,181**	**37,470**
External sources	16,159	23,000	18,137
Domestic sources	5,137	15,898	20,290
Deposits	23,371	283	-957
Outflows	**26,170**	**20,223**	**19,208**
Repayment upon foreign borrowing	20,001	14,004	8,992
Repayment upon domestic borrowing	6,169	6,219	10,216

Source: Ministry of Finance, Fiscal strategy 2015-2017

In the next period, the developments on the international capital market will continue to be monitored. Foreign borrowing as source of financing will be used by budget users for realisation of specific projects.

As for the borrowing on the domestic market, Ministry of Finance will continue to issue government securities in the next period as well. The purpose is, by regular issuance of government securities, to provide for more efficient financing of budget needs in the short and long run, reduction of financing costs, as well as encouragement of the further development of the financial markets in the Republic of Macedonia. In the upcoming period, Ministry of Finance will intend to retain regular issuance of treasury bills, as well as staying focused on expanding the maturity structure of the portfolio of government securities with longer maturities. Thus, special emphasis will be put on continuation of the maturity of the existing portfolio of government securities by issuing longer-term securities, i.e. by issuing 2-, 3-, 5-, 7- and 10-year government bonds. Special interest in investing in long-term securities issued by the Republic of Macedonia is expected from the pension companies, as well as from commercial banks and insurance companies.

Local Government Budget. The process of successful administration and collection of own revenues, in particular revenues on the basis of taxes on real estate, fully including the tax base of natural persons and legal entities and re-assessment of the value of real estate, as well as enhancing the capacity for execution of transferred competences and management of financial resources, continues in the course of 2014.

Compared to 2005, when the fiscal decentralisation process commenced, the municipal revenues increased by five times (from Denar 5.9 billion in 2005 to Denar 28.2 billion in 2013). Collection of local taxes experienced more than two-fold increase, while share of local taxes in GDP of 1% in 2005 surged to 1.5% in 2013, by improving the collection structure, showing that local government capacity continuously strengthens.

In the coming medium-term period, additional revenues from the VAT grant will be provided for the municipalities showing success in the collection of local taxes. New revenues will be provided by allocating funds from lease of state-owned agricultural land to the municipalities the proportion of which for 2018 is 50% for the Republic of Macedonia and 50% for the municipalities, depending on the location of the agricultural land being under lease if the revenue performance on the basis of property tax exceeds 80% in relation to the projected ones, with gradual increase during the interim period.

By providing favourable loans in all municipalities, the Government has provided credit lines from international financial institutions (WB, EIB, KfW and EBRD) for financing significant investment operations. Funds will be used for raising the level of local services and improving the utilities infrastructure.

Implementation of the Municipal Services Improvement Project, financed by the World Bank continues in 2015. So far, 55 municipalities have expressed interest in participating in the project, out of which 38 have concluded one or more sub- loan contracts and have started to implement their projects, while the remaining 17 are in the process of preparation of project documentation. The Ministry of Finance has signed 51 sub-loan contracts with 38 municipalities totaling 30.1 million euros or 63% of the available funds. The value of municipal projects that are in the phase of preparation amounts to 16.5 million or 34%. Currently only 3% of this credit line (1.4 million Euros) are undistributed.

As of 2015, IPA funds for rural development that EU allocated for the Republic of Macedonia under IPA structural funds for 2013, in the 5th IPA Component - Improvement and development of rural infrastructure, will be implemented under the abovementioned project. This is a joint project of the Republic of Macedonia, the EU and the WB, aimed at improving quality of life in rural areas, reducing the gap between urban and rural areas and improving competitiveness of rural areas. The IPA project funds' will be awarded to 79 municipalities as grants that can be used exclusively to finance infrastructure projects in rural areas.

Municipalities in the Republic of Macedonia will continue to use funds from the Programs for cross-border cooperation with neighboring countries (Bulgaria, Greece and Albania), funded by the EU. These projects are in support of local economic development and strengthening the cooperation and partnership of municipalities in border areas of neighboring countries.

In order to support the municipalities in the Republic of Macedonia that use resources from the IPA Component II (Cross-Border Cooperation), the Ministry of Finance, Ministry of Local Self-government and the Macedonian Bank for Reconstruction and Development (MBDP) created a special lending facility as part of MBDP for short term lending to municipalities - beneficiaries of funds from this IPA component. This instrument allows municipalities to bridge the gap and provide funds for advance payments of invoices for works executed in a project funded by the IPA Component II. The instrument is active from 01.01.2014 in order to ensure accelerated implementation of the Cross-border cooperation programme and increase capacity of municipalities for co-financing of EU-funded projects at local level. So far this instrument has been used by 3 municipalities, while 1 municipality is in the process of getting funds.

Further, the adopted Strategy on Modifications and Amendments to the 2009-2019 Strategy for Regional Development of the Republic of Macedonia will contribute to creating equal opportunities in all regions and their active integration in the economic development.

3.4. Structural balance

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

Table 3.4. Aggregate fiscal indicators and production gap

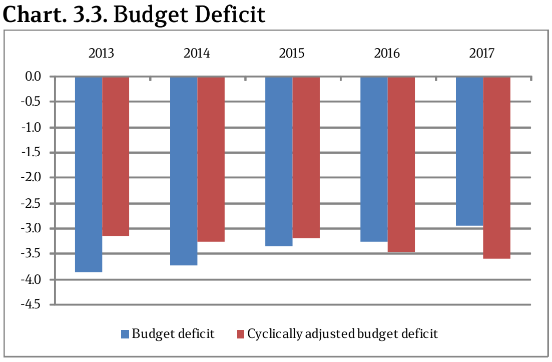
	2015	2016	2017
Total budget balance	**-3,3**	**-3,2**	**-2,9**
Primary budget balance	-2,3	-2,0	-1,6
Production gap	-0,5	0,6	2,1
Cyclical component of the budget	-0,2	0,2	0,6
Cyclically adjusted total budget balance	-3,2	-3,4	-3,6
Cyclically adjusted primary budget balance	-2,1	-2,2	-2,3

Source: Calculations of the Ministry of Finance

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

Calculations point out that cyclically adjusted budget deficit accounted for 3.2% in 2014, and it was lower than the projected budget deficit in the respective year, taking into account that the cyclical budget component has a negative value, as a result of the assessed negative production gap.

Chart. 3.3. Budget Deficit



Source: Calculations of the Ministry of Finance

In 2015, taking into account that projected GDP is expected to remain below the potential one, cyclical component of the budget is negative, and the cyclically adjusted budget deficit accounts for 3.2%. In 2016 and 2017, in conditions of positive output gap, value of cyclically adjusted deficit is higher than the planned budget deficit, i.e. it amounts to 3.4% in 2016 and 3.6% in 2017. During the analysed period, cyclically adjusted primary budget deficit accounts for 2.2% in average (see table 3.4).

3.5. DEBT LEVELS AND DEVELOPMENTS, ANALYSIS OF BELOW-THE-LINE OPERATIONS AND STOCK-FLOW ADJUSTMENTS

Government debt of the Republic of Macedonia[17] at the end of Q3 2014 amounted to EUR 3,355.8 million, i.e. 39.2% of GDP. Total public debt, which includes the government and guaranteed debt, amounted to EUR 3,984.0 million or 46.5% of GDP at the end of the third quarter. During the analysed period, domestic government debt accounted for 37.2% in the total government debt, while the external government debt accounted for 62.8%. Share of external government debt increased by 5.2 p.p. compared to the end of 2013, as a result of the Eurobond issued on the international capital market. In terms of its interest structure, fixed interest rate debt increased by 7.1 p.p. compared to end-2013, by which the ratio between fixed interest rate debt and variable interest rate debt was 61.6% to 38.4% respectively, which is a result of the increase of the issued bonds in the government securities portfolio, as well as the Eurobond issued on the international capital market. From currency point of view, share of euro-denominated debt in the foreign currency debt portfolio accounted for 80.4% and, compared to end-2013, it increased by 5.8 p.p..

Table 3.5. Public debt stock (EUR million)

	2010	2011	2012	2013	30.09.2014
External Public Debt	1388.3	1882.0	1941.2	2078.7	2709.8
Government Debt	1173.8	1582.1	1615.9	1597.5	2108.2
Guaranteed debt	214.5	299.9	325.3	481.2	601.6
Domestic Public Debt	548.0	532.9	967.6	1202.7	1274.2
Government Debt	537	510.8	938.6	1174.1	1247.6
Guaranteed debt	11.0	22.1	29.0	28.6	26.6
Total Public Debt according Public Debt Law	1936.3	2414.9	2908.8	3281.4	3984.0
Total Public Debt as % GDP	27.2	32.0	38.3	40.5	46.5
Total Government Debt	1710.8	2092.9	2554.5	2771.6	3355.8
Total Government Debt as % GDP	24.1	27.7	33.7	34.2	39.2
Guaranteed Debt	225.5	322.0	354.3	509.8	628.2
Guaranteed Debt as % of GDP	3.2	4.3	4.7	6.3	7.3

Source: MoF and NBRM

In September 2014, the Law on Modifications and Amendments to the Law on Public Debt was adopted, in which key amendments are the defining of the public debt as sum of the government debt and the guaranteed debt of public enterprises and state-owned joint stock companies, as well as finalisation of the procedure for borrowing by public debt issuers. Medium-Term Fiscal Strategy, covering 3-year period, is the framework determining the public debt management policy in the Republic of Macedonia.

On the basis of the commitments to finance the state needs with the lowest possible costs in the medium and the long run, sustainable level of risk and low level of public debt, as well as realisation of the planned infrastructure investments, public debt trends, including the government debt and the guaranteed debt, will remain within the projections. Hence, public debt is not expected to exceed the level of 49.9% of GDP in the long run. This projection is based on comprehensive analysis by preparing detailed scenarios for the movement of government and public debt for the Medium-Term Fiscal Strategy 2015-2017. According to this document, moderate and controlled growth of government debt to 38.7% of GDP at the end of 2017 is expected, while the public debt in the same period is expected not to exceed the level of 49.9% of GDP. The fiscal strategy is submitted to Parliament of the Republic of Macedonia, which enables the legislative authority to have insight in the public debt management policy.

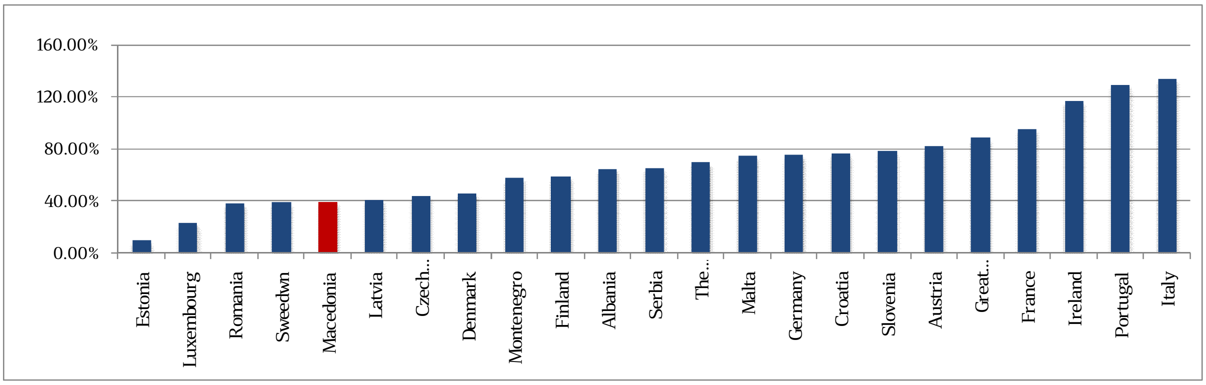
[17] Government debt comprises financial liabilities incurred on the basis of borrowing by the Republic of Macedonia, public institutions established by the Republic of Macedonia and the municipalities, the municipalities within the City of Skopje and the City of Skopje.

In order to reduce the exchange rate risk, hence the interest rate risk, optimal currency structure of the portfolio of the foreign currency government debt is determined, whereby share of euro-denominated debt in the structure of foreign currency debt portfolio should not exceed the level of 70%. Therefore, in the period 2015-2017, the level of government debt with fixed interest rate should not be below 50%.

In order to protect the central government debt portfolio against the refinancing risk, the minimum level of the "average time to maturity" indicator in 2015 should be 3 years. In order to protect the central government debt portfolio against the interest rate risk, the minimum level of the "average time to refixing" indicator in 2015 should be 2 years.

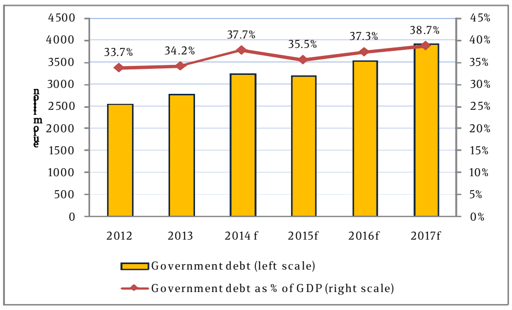
Republic of Macedonia remains to be moderately indebted country as a result of the carefully and successfully conducted fiscal policy in past years.

Chart 3.4. Government debt of EU Member States and candidate countries in Q2 2014 (% of GDP)



Source: Ministry of Finance, Eurostat, October 2014

Chart. 3.5. Government debt trends



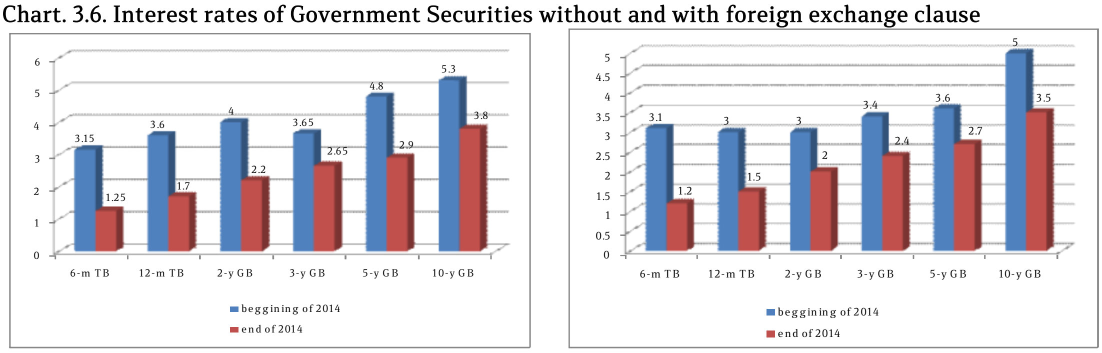
Source: Ministry of finance

Moderate growth of investment activity is projected in the course of 2015, by using credit support from abroad. In addition, in the period 2015 - 2017, investments are expected to be carried out in the field of road and railway infrastructure, water supply and sewage network, construction of social flats, as well as investments in the field of education and health aimed at increasing productivity, i.e. boosting the competitiveness of the economy in the long run. In the period 2015-2017, guaranteed debt in relation to GDP is expected to experience a moderate increase, as a result of the new planned projects in the field of road infrastructure, energy sector, projects for financing SMSs for which the state will issue guarantees. However, when making new borrowings, account is taken of the long-term sustainability of the debt, whereby the process of issuing new guarantees is strictly regulated and subject to the borrowing procedure determined in the Law on Public Debt, according to which the claimants of guarantees should fulfill certain criteria so as for the country to be able to issue guarantee. As of 30th September 2014 inclusive, the issued sovereign guarantees amount to EUR 628.2 million, accounting for 7.3% of GDP (and are included in public debt of 46.5% of GDP).

According to the last amendments to the Law on Public Debt, Ministry of Finance upgraded the presentation of public debt data, whereby a comprehensive table for the stock of the total public debt, including the central government debt, the debt of municipalities and the guaranteed debt of public enterprises and state-owned companies is published on regular basis. This procedure demonstrates progress in terms of transparency when publishing the debt taking into account that the central government debt was published in the previous period, and the publication of the other public debt segments were publicly available, however dispersed at several places and sources.

Primary Government Securities Market. According to the Calendar for issuance of government securities on the domestic market, in the course of 2014, Ministry of Finance issued 6- and 12- month treasury bills on regular basis, as well as 2- 3-, 5- and 10-year government bonds. In the period January – September 2014, total of 56 auctions of government securities were carried out, i.e. 30 auctions of treasury bills and 26 auctions of government bonds. Total amount offered for sale at the auctions was Denar 44,518.67 million, demand amounted to Denar 43,485.52 million, and the amount realised was Denar 42,331.78 million.

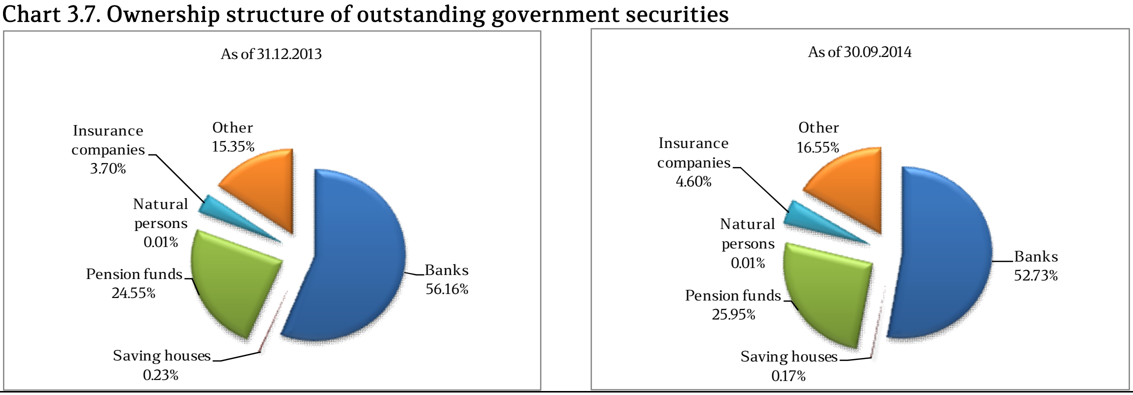
Chart. 3.6. Interest rates of Government Securities without and with foreign exchange clause



Source: Ministry of Finance

As of September 2014 inclusive, stock of outstanding government securities amounted to Denar 70,914.84 million, Denar 43,887.47 million out of which as treasury bills and Denar 27,027.37 million as government bonds. During 2014 interest rates on government securities experienced multiple decrease. Chart 3.6. shows interest rates of Government Securities at the beginning of 2014 and at the end of 2014, after their decrease.

Chart 3.7. Ownership structure of outstanding government securities



Source: Ministry of Finance

Despite the reduced share of banks in the ownership structure of outstanding government securities, trends of their dominant share in the ownership structure of government securities continued in the course of 2014 as well (Chart 3.7). In the period January - September 2014, except for the pension funds, the insurance companies and the "other" category, all other categories of market participants experienced decrease of their share in the ownership structure. During the analysed period, share of banks dropped by 3.43 p.p. in relation to the share of other market participants. As of September 2014 inclusive, ratio between banks and other market entities was 52.73% to 47.27% respectively.

Secondary Government Securities Market. Legal regulations on secondary trading in the Republic of Macedonia provide for trading in all structural government securities on the

Macedonian Stock Exchange AD, as well as trading in continuous government securities on the OTC markets.

In the period January - September 2014, Macedonian Stock Exchange registered trading only in government denationalisation bonds, whereby total of 461 transactions were realised. Total volume of trading realised during this period amounted to Denar 455.14 million, reducing by 68.2% compared to the same period in the previous year.

During the same period, total of 8 transactions with government securities were realised on the OTC market, pertaining to treasury bills, while transactions pertaining to government bonds were not realised. Total nominal trading amount amounted to Denar 654.31 million. Compared to the trading in the same period in 2013, it can be concluded that smaller number of transactions with government securities were realised in 2014, while total nominal trading amount was lower by Denar 1,249.52 million.

International Capital Market. As a result of the stable credit rating, as well as the stable economic policies of the country, in July 2014, Ministry of Finance issued new Eurobond with maturity period of 7 years, and interest rate amounting to 3.975%. As for the primary issue, Eurobonds in the total amount of EUR 500 million were issued, although the demand by investors reached doubled amount of EUR 1.2 billion. Eurobond was issued at the Irish Stock Exchange in line with Regulation S/Rule 144A. This enabled the creation of a broad base of investors - owners of Eurobond from Europe and the USA. More precisely, the issue was placed at 100 institutional investors, including 16% investors from Great Britain, 35% investors from Continental Europe and 49% American investors. In general, owners are fund and asset management companies (89%), private banks (4%), insurance funds (3%) and others (4%).

In the course of 2014, in addition to the newly issued Eurobond, the Eurobond, issued by the Republic of Macedonia in 2005, falling due in December 2015, continued to be traded on the international capital market. As of September 2014 inclusive, the purchase price of the 2005 Eurobond amounted to 101. 250, while the yield to maturity accounted for 3.503%, while purchase price of the 2014 Eurobond amounted to 101.625, and the yield to maturity accounted for 3.698%.

Credit Rating of the Republic of Macedonia. On 5th September 2014, "Fitch" credit rating agency announced that it affirmed the previously awarded credit rating for foreign and domestic currency of the Republic of Macedonia BB+, as well as the stable outlook of the country. Affirmation of the credit rating is based upon the GDP growth in the first quarter of 2014, low level of inflation, moderate budget deficit, relatively low public debt, and well-capitalised banking sector.

On 31st October 2014, "Standard & Poor's" Credit Rating affirmed the previously awarded credit rating for foreign and domestic currency of the Republic of Macedonia BB-, at the same time affirming the stable outlook of the country. Affirmed credit rating is based upon the moderate level of external debt and public debt, as well as the positive expectations for average growth of economy of around 3.4% of GDP, being based upon the stable inflows from foreign direct investments.

3.6. SENSITIVITY ANALYSIS

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

Taking into account that medium-term fiscal scenario is based on macroeconomic assumptions, we believe they are a factor with potential effect on the fiscal trends. Thus, as first scenario we assume lower economic growth, in line with the alternative scenario, being explained in point

2.3. In fact, the baseline scenario, upon which budget revenues and expenditures are based, envisages real GDP growth of 4% in 2015, 4.2% in 2016 and 4.5% in 2017, while in line with the alternative scenario, the projection of real GDP growth is 2.7%in 2015, 2.9% in 2016 and 3.2% in 2017. Accordingly, budget deficit as percentage of GDP is higher by 0.3 p.p. in 2015, 0.5 p.p. in 2016 and 0.8 p.p. in 2017 compared to the baseline scenario. Table 3.6 shows the budget deficit in the analysed period compared to the baseline scenario and the alternative scenarios.

Table 3.6. Sensitivity analysis of budget deficit

	2015	2016	2017
GDP, real growth rate	4,0	4,2	4,5
Budget revenues, growth rate	5,0	3,4	3,7
Budget expenditures, growth rate	3,8	3,4	3,0
Budget deficit (% of GDP)			
Baseline Scenario	**-3,3**	**-3,2**	**-2,9**
Scenario 1. Lower GDP growth rate in the analysed period according to the alternative scenario	-3,6	-3,7	-3,7
Scenario 2. Lower growth rate of revenues by 20% in 2015 and 2016	-3,6	-3,7	-3,4
Scenario 3. Higher growth rate of expenditures by 25% in 2016	-3,4	-3,5	-3,2

Source: Calculations of the Ministry of finance

As a second scenario, we assume for economic entities to refrain from spending, and the result thereof would be reduction of the annual growth rate of total budget revenues in 2015 and 2016 by 1/5 compared to the previously projected rates presented in Table 3.6. Thus, by assuming that growth of budget revenues in 2015 and 2016 will amount to 4% and 2.8% respectively, budget deficit would amount to 3.6% in 2015, 3.7% in 2016 and 3.4% of GDP in 2017.

Under the third scenario, one-off shock is envisaged on the budget expenditure side in 2016, which generates 1/4 higher growth rate of budget expenditures in relation to the growth rate projected in the baseline scenario. As a result, i.e. increase of budget expenditures by 4.2% in 2016, budget deficit is higher by 0.3 p.p. in 2016 and 2017 than the level envisaged in the basic projections, reaching 3.5% of GDP in 2016 and 3.2% of GDP in 2017.

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

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

Sensitivity of Public Debt. To the end of analysing sensitivity of public debt portfolio in the Republic of Macedonia to exposure to market risk, i.e. interest rate risk and exchange rate risk, analysis was made of the effects of variation of interest rates and the exchange rate on the external government debt. Sensitivity analysis is based upon the following assumptions: by changing a single variable, all other variables remain the same, i.e. ceteris paribus; during possible trends in the other currencies in relation to the euro, Denar exchange rate in relation to the euro retains the stable value and lack of correlation between interest trends and exchange rate trends.

Analysis covers the period 2015-2017, being based upon scenarios of increase of interest rate by 1 p.p. and 2 p.p. of the baseline scenario, as well as appreciation and depreciation of the euro compared to the other currencies by 10%.

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

	2015	2016	2017
Baseline scenario	100.0	100.0	100.0
Scenario 1: increase of respective interest rates by 1 pp.	108.1	107.8	107.1
Scenario 2: increase of respective interest rates by 2 pp.	116.2	115.6	114.2
Scenario 3: appreciation of other currencies of the portfolio in relation to the euro by 10%	103.5	101.9	101.2
Scenario 4: depreciation of other currencies of the portfolio in relation to the euro by 10%	96.5	98.1	98.8

Source: Calculations of the Ministry of finance

Main conclusions under this analysis are the following:

- Interest servicing-related costs on the basis of external government debt are sensitive to the trends of interest rates. If the interest rates in the period 2015 - 2017 increase by 1 p.p., it would cause increase of the interest-related costs by 8.1% at the most, as a result of the exposure of the debt portfolio to the interest rate risk, being a result of the relatively high share of the debt with variable interest rates.
- In this period, possible unfavourable trends at exchange rates of other currencies, in relation to the euro, will not cause any more significant increases of the servicing-related costs, due to the fact that most of the external government debt is denominated in euros. Therefore, future euro appreciation, i.e. depreciation, in relation to the other currencies in the portfolio (US dollar, Japanese yen and special drawing rights) by 10% will cause an increase, i.e. decrease of servicing-related costs by 3.5% in 2015, 1.9% in 2016 and 1.2% in 2017 at the most. In addition, due to the de facto fixed Denar exchange rate in relation to the euro, this risk is minimised, i.e. sensitivity of public debt portfolio is at lower level.

3.7. SUSTAINABILITY OF PUBLIC FINANCES

Calculations for long-term sustainability of public finances[18] are based upon the following assumptions:

- average labour productivity growth of 1.9%,
- increase of male participation rate from 76.3% in 2010 to 89.7% in 2060,
- more intensive increase of female participation rate (from 51.8% in 2010 to 75.2% in 2060), by which share of female population in the total active population is expected to reach 45.6% in 2060,
- reduction of unemployment rate with higher intensity in the first thirty years (from 32.2% in 2010 to 11.2% in 2040) and with lower intensity in the remaining 20 years, thus projected unemployment rate accounts for around 5% in 2060,
- gradual increase of the share of population at the age above 65 years, reaching 11.7% in 2060.

In addition, it is assumed that non-tax budget revenues as percentage of GDP will not be changed. On the basis of the above-mentioned assumptions, as well as the employment growth projections, certain increase of the share of revenues on the basis of pension insurance contributions is envisaged, from 6.2% of GDP in 2010 to 6.7% in 2030 and stabilisation at 6.4% in the remaining analysed period. As for pension-related expenditures, it is worth mentioning that those of the Pension and Disability Insurance Fund are taken into account, while expenditures

[18] See Table 7 in Annex 1.

of the private pension insurance funds are not taken into account. Thus, share of pension-related expenditures in GDP in the period by 2030 is expected to amount to 9.1%, and in the next period, gradual reduction of this share is envisaged, if one takes into account that share of the pensioners whose pensions have been fully paid from the first pillar will reduce, while share of the pensioners who will receive part of their pensions from the second pillar will increase. Public expenditures for health protection as percentage of GDP are projected to gradually increase from 5% in 2020 to 5.5% in 2060. Such projected growth of expenditures was partially a result of the effects of population aging. Expenditures for education as percentage of GDP are envisaged to range from 5% to 5.5% during the analysed period. Interest-related costs in relation to GDP are expected to increase to 1.5% in 2020, while in 2060, it is expected for the share to reduce to 1%, in line with the projected trend of budget balance, i.e. government debt.

3.8. INSTITUTIONAL FEATURES

During 2014 the budget process began at the beginning of the year and resulted in adoption of the 2015Budget much earlier than the legally defined deadline. Along with the 2015 Budget, the Fiscal Strategy 2015-2017 was adopted, which presents medium-term projections of the main fiscal parameters and provides a gradual fiscal consolidation in the next period.

Following the example of the European countries, Government of the Republic of Macedonia continued to introduce fiscal rules providing:

- framework for conducting stable, envisageable and sustainable fiscal policy;
- increase of budgetary discipline and responsibility;
- increase of the macroeconomic policy credibility;
- fair and sustainable distribution of expenditures among the present and future generation of public goods users.

Determination of fiscal rules is basis for fiscal responsibility, transparency and earmarked use of Budget funds. Limitation of the two main fiscal targets -deficit of the Budget of the Republic of Macedonia and the public debt are envisaged to be governed under the highest legal act – the Constitution. The procedure is in its final stage. At the beginning of 2015, legislation developing and clarifying the implementation and monitoring of fiscal rules is anticipated to be prepared.

Improving the public finance management by establishing medium-term budget framework, as well as increasing the transparency (regular fiscal reports, preparation of Budget in Brief) will remain the key priority in the next medium-term period as well.

In the coming period, implementation of reforms for improving the budget process, particularly in cooperation with the EU will continue. Starting from 2015, the implementation Project for building up the capacity within the department dealing with central government budget and strengthening medium-term policy making capacity through IPA TAIB 2011 should start, the main activities of which will be aimed at determining the programme classification of expenditures, strengthening the capacities of the Ministry of Finance for medium-term planning and reporting to EC Staff in line with the ESA Methodology, as well as strengthening the capacity of part of the main budget users, all to the end of improving the quality of public expenditures.

Funds are received for implementation of the Project "Development of Proposals for Implementation of a Modern Integrated Financial Management Information System" from 2011 IPA Technical Assistance Facility Envelope. Under the Project, the Ministry of Finance will hire experts to prepare a Study, by which the current status of the public finance management information systems in the Ministry of Finance will be analysed and evaluated, and solutions for establishing modern integrated public finance management information system will also be offered.

As regards the enhancement of public finance management, Public Finance Review is an ongoing activity, in cooperation with the World Bank. This review should provide general recommendations for future development of certain segments in the field of legislation, public finances and budget process. The World Bank has drawn initial conclusions that the budget process and the medium-term fiscal projections are solid and realistic, however, certain segments should be improved. In the first quarter of 2015, as part of the Public administration reform project, special emphasis will be done in the area of public finance management. The EC, through SIGMA and in cooperation with the Ministry of Finance, will provide data on public finances in order to prepare a Public finances management review in the Republic of Macedonia.

Based on recommendations from the reviews of the World Bank and SIGMA, assessment will be done whether there is a need for making PEFA or they can serve as the basis for drafting a Public finance management reform program in the second half of 2015.

Public Internal Financial Control (PIFC). Republic of Macedonia will continue to intensify the measures for enhancing the internal financial control in the public sector in the next period, in line with the 2015-2017 Policy Paper for Development of Public Internal Financial Control, the Government of the Republic of Macedonia adopted in August 2014. This is third Policy Paper in this field and its goal is to further develop the established internal financial control system in the public sector as a tool that will serve to the management for responsible, successful and transparent management of national and EU funds. Development of the PIFC system, which components are financial management and control, internal audit and their harmonisation, is carried out in line with the international standards and good practices of the EU taking into account the specific features of the public sector in the Republic of Macedonia.

In line with the Action Plan under the Policy Paper, the focus in the next period will be placed on enhancing the internal financial control system and increasing the awareness of the significance and benefits of this system. In addition, the managerial responsibility will be strengthened and the activities for completing the certification of internal auditors and enhancing the performance of internal audits will continue. Special emphasis will be put on the activities related to carrying out the instructions for risk management and preparation of risk management strategies. In 2015, the Law on Financial Inspection will start to be applied, and measures and activities will be additionally undertaken so as for the PIFC reform to be better integrated in the ongoing public administration reform process.

In terms of EU assistance management, national decentralized management structures continue to undertake all necessary activities to establish the necessary control mechanisms for EU assistance to end of its efficient utilization and sound financial management. Their institutional capacity is continually upgraded and strengthened through increase in the number of employees, as well as their skills and knowledge. In 2015, all activities will be undertaken for transferring EC Budget management tasks within IPA 2 from the EC staff to the already established EU assistance decentralized management structures at national level.

This will ensure continuity in the decentralized implementation of EU assistance and support to all reform processes supported by the EU during the accession of the Republic of Macedonia.

In addition, 2015-2017 National Strategy for Prevention of Fraud and Protection of EU's Financial Interests will be adopted, and activities will be undertaken so as for the relevant institutions to be able to use the new established electronic database on counterfeit money within the Ministry of Internal Affairs.

State Audit Office's independence will be safeguarded in the Constitution, and the efforts for determining a procedure, by which the Parliament of the Republic of Macedonia will review the audit reports of the State Audit Office, will continue.

4. REFORMS UNDERPINNING THE MACRO/FISCAL STRATEGY

4.1. OBSTACLES TO GROWTH AND THE MACROCONOMIC STRUCTURAL REFORM AGENDA

One of the main risks for achieving the projected growth rates is the potential deterioration of the economic outlook in the Eurozone. Given that the Republic of Macedonia is small and limited internal market that can hardly sustain very high growth rates by itself, slower recovery of the Eurozone than the projected one could lead to lower export and lower inflow of FDI, thus lower growth than the expected one.

Taking into account the geographic location and the size of the country, FDI increase, improvement of linkages among foreign companies and local suppliers, reduction of energy import, boosted competitiveness and productivity, as well as increase of industrial high value-added production will be especially important for increasing the resistance of the Republic of Macedonia to external risks.

One of the main preconditions for boosting competitiveness of the country and achieving higher economic growth rates is the good transport infrastructure, for which as in the past period, significant public investments are planned in the next period as well.

Although Macedonian economy shows improvement as regards unemployment, which significantly reduced in the past period, it is still high within European context. In line with the analysis of indicators under the Macroeconomic Imbalance Procedure of EC (Box 2.1.), high unemployment rate is the biggest obstacle to Macedonian economy. Although in the past period a number of measures were undertaken, being aimed at improving the conditions and yielded positive results, it is still necessary for the Government to continue implementing the employment policies, which will be focused on encouraging the demand on the labour market, matching the supply with the demand of labour force in line with the labour market needs, improving the supply of labour force, as well as reducing the grey economy.

Access to capital for the private sector, mainly for SMEs as main drivers of economic growth is also an obstacle to the economic growth and the structural reform agenda in the next medium-term period. Therefore, in the coming medium-term period, Government of the Republic of Macedonia will continue to support the private sector from the aspect of new projects, new employments, increased liquidity and strong exports. In addition, Republic of Macedonia faces the need to improve and enhance the quality of higher education that will contribute to development of skills in line with the labour market needs.

4.2. KEY AREAS OF MACROECONOMIC STRUCTURAL REFORMS

4.2.1 Products markets and business environment

Government Interventions in the Economy. Economic activities in the Republic of Macedonia are based on dominant private ownership with overall functioning of market economy on the principles of free mutual action of supply and demand.

Further privatisation process covers the market liberalistion of the restructured public sector (“Macedonian Railways", “Public Enterprise for Managing Housing and Business Premises”, Public Enterprise "Macedonia Road", Public Enterprise "Macedonian Post" etc.), by determining possibility for further sale of certain parts thereof, also including the sale of activities, as well as sale of government shares or shares of the Pension and Disability Insurance Fund.

There is ongoing defining of further activities related to the status and privatisation of the three big companies: JSC EMO Ohrid, JSC OHIS Skopje and JSC Eurokompozit Prilep. As for the case with JSC Tutunski kombinat Prilep, strategic partnership is being realised with Philip Morris International Management SA.

There is ongoing preparation of new Law on Usage and Management of State Capital, governing the privatisation of the state capital.

Business climate. In line with the last World Bank "Doing Business 2015" Report, Macedonia is ranked at the high 30th place among 189 countries worldwide, advancing by 1 place compared to last year. Macedonia remained leader in the region this year as well, according to the conditions for doing business. Republic of Macedonia is again listed among the countries where the conditions for doing business continuously improve and which carried out key reforms in many areas last year.

In December 2014, Government of the Republic of Macedonia adopted Action Plan, accompanied with measures to further improve the doing business requirements in the country. To the end of streamlining the requirements for starting a business, category "registration agent" is envisaged to be expanded so as to also include lawyers, and measures are envisaged for continuous training and support to the registration agents, thus additionally facilitating the process of establishing a company. Payment of the fee for arrangement of construction land will be made through POS terminals instead through the banks as was the case so far, while the procedure for obtaining urban plan extract will be carried out through the e-building permit system by its connecting to the e-urbanism system. Grid code on electricity distribution will be amended to the end of shortening the time necessary to obtain an Energy Consent to Connect a Customer to the Distribution Network. Also, the time necessary to assess property value will be shortened, thus shortening the period for preparation of a Decision on payment of property sales tax. As regards improvement of tax payment, possibility will be provided to pay taxes and fees electronically through the e-banking service, as well as by using virtual POS terminals for electronic payment of unpaid taxes.

To the end of shortening the periods for carrying out bankruptcy proceedings, e-bankruptcy system will be monitored and improved, bankruptcy trustee will be selected electronically in a fair and equitable manner and electronic access for the bankruptcy trustees to obtain information on different institutions will be expanded.

National Entrepreneurship and Competitiveness Council (NECC) of the Republic of Macedonia will continue implementing activities aimed at building and promoting sustainable three-party dialogue between the business community, the academic community and the Government in the process of policy creation and implementation. Problematic areas will be identified and national strategies on enhancing the competitiveness of the Macedonian economy will be prepared through the permanent and temporary committees and working groups in the field of SMEs, investments, automotive industry, textile industry, IT sector, craftsmanship, human resources, etc.

Activities within the "Learning from the Business Community" Project will continue to be implemented in the coming medium-term period as well, to the end of achieving broad consensus and strengthening the dialogue with the business community. Four cycles of visits to the companies were carried out, whereby the competent institutions undertake adequate measures, all to the end of improving the doing business conditions.

Property rights. For the purpose of further promoting of property rights, Agency for Real Estate Cadastre (AREC) has established direct cooperation with all relevant state institutions and professional users. The E-Desk provides easy, fast, reliable and efficient electronic delivery of applications and requests for registration of changes and issuing GCIS data. In 2014, 35% of the total requests in AREC were received via the E-desk.

AREC enabled registration of ownership title of all types of infrastructure facilities (underground and aboveground) and their graphic display. According to the Action Plan for digitalization of cadastral maps, 1,497 cadastral municipalities were imported in the MAK EDIT (coverage of 80%). In the centralized database 1,117 cadastral municipalities (67% coverage) were made in production. Until now 66.82% of the territory of the Republic of Macedonia is digitalized. At the end of 2015 AREC plans to complete the entire process of digitization of cadastral maps.

A detailed gravimetric survey of the entire territory of the Republic of Macedonia is executed, which created technical preconditions for introduction of ETRS89 coordinate system. AREC is working to develop a distribution system (GIS Portal) under which data will be issued online, services for spatial data will be synchronized with the INSPIRE Directive and legal entities and individuals can use information from the cadastre in real time. The process is expected to be completed by the end of 2015.

Competition and state aid. In January 2014 the twinning project of IPA TAIB 2009 “Assistance to the Commission for Protection of Competition for state aid control” was finished, whereby strengthening of the administrative capacity of the Commission for Protection of Competition (CPC) in the field of state aid was achieved, as well as strengthening of the administrative capacity of the other stakeholders in the process of the control of state aid (providers of state aid, business community and judiciary).

In December 2014 Handbook for discovering unlawfully bid rigging at public procurements was enacted, which is intended for state (contracting) authorities which implement public procurements. The preparation of Guidelines for application of article 7 of the Law on Protection of Competition regarding agreements for horizontal cooperation and Guidelines for vertical restraints is ongoing, which should be enacted until June 2015. These guidelines are additionally clarifying the three bylaws enacted upon the Law on Protection of Competition i.e. Decree on the detailed conditions for block exemption of certain types of research and development agreements, Decree on the detailed conditions for block exemption of certain types horizontal agreements for specialization and Decree on the detailed conditions for block exemption of certain types of vertical agreements.

For further strengthening of the administrative capacity of the CPC a project funded through British Embassy “Enforcing EU competition and state aid policy in Macedonia” is realized. The project started in June 2014 and will end in April 2015. The administrative capacity of the CPC will be also strengthened through advanced trainings (TAIEX).

4.2.2 Financial Stability

Banking Sector. New Law on Payment Operations will be adopted by the end of 2016, which will transpose Directive 2007/64/EC on payment services in the internal market. The new Law will be prepared with a technical assistance provided through IPA 2010 "Further Harmonisation with EU acquis in field of Movement of Capital and Payments and Financial Services - Securities markets and Investment services" (EuropeAid /132948 /D /SER /MK). The Project is expected to be launched in the first quarter in 2015. Under the new Law, in addition to establishing the European standards on payment services, basis will be created for such services to be also rendered by entities, other than commercial banks, which will have positive effects on the competition at payment operations services.

By 2017, banking regulations will be aligned with the new 2012 Basel principles on efficient banking supervision, Directive 2013/36/EU on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms and Regulation (EU) No. 575/2013 on prudential requirements for credit institutions and investment firms. Special Law will be adopted by 2017, implementing the Directive 2014/59/EU establishing a framework for the recovery and resolution of credit institutions and investment firms. Objective of these activities is to strengthen the banks’ capacity for adequate risk management, which is related to their activities, as well as for loss absorption, which can occur from their business operations. At the same time, conditions will be created for quick response by the supervisory authorities in case of risks arising from the banks' operations.

Capital Market. New Law on Capital Market will be adopted by the end of 2016, which will be fully aligned with EU acquis in the field of capital market, providing for greater protection of minority shareholders in joint stock companies, greater transparency of companies and introduction of new financial instruments. For the purpose of preparing the new Law, Project was approved through IPA 2010 (EuropeAid /132948 /D /SER /MK), which is expected to commence in the first quarter in 2015. Following the adoption of the Law, Securities and Exchange Commission will adopt the bylaws necessary for its implementation.

Continuous process of harmonisation of the regulations by incorporating the goals and the priorities in line with IOSCO's Strategic Direction 2010-2015 will resume in the coming period, above all by accepting the directions on establishment of mechanisms for cooperation between the national regulators for the purpose of more efficient implementation of supervision and exchange of data and information.

Two new software solutions are expected to start applying at the beginning of 2015 through EBRD financial support. The first solution refers to a consistent application of the Law on Taking Over Joint Stock Companies in terms of acquiring shares by the shareholders above the threshold prescribed by law. The second one pertains to better supervision of investment funds and investment fund management companies, which will be an integrated system for monitoring the operations of both the funds and the companies on the basis of adopted Rulebook of the SEC pursuant to the Law on Investment Funds.

Insurance Sector. New Insurance Law implementing EU Directive 2009/138/EC (Solvency II) will be adopted. The implementation of this activity is supported by EU under the Project MK12/IB/FI/01 "Further harmonization with EU in the field of insurance and increase of market operations" financed by IPA TAIB 2012-2013. At the same time, ISA will work on improving the bylaws. The project will enable full participation in the internal market at the time of joining the EU, and further strengthening of administrative and operational capacity.

Effective corporate governance as a condition for a healthy and stable insurance sector will be one of the priorities. In this regard, in November 2014, ISA in cooperation with the Macedonian Institute of Directors and the International Finance Corporation, promoted the Principles for corporate governance of the insurance companies in Macedonia. During 2015, new obligation will be introduced for the companies - to report on an annual basis on the extent of application of the good corporate governance principles. During the programming period, special emphasis will be put on strengthening the supervisory capacity of ISA. Therefore, TAIEX technical assistance will be provided, and the cooperation with the Dutch Central Bank will continue through trainings on relevant topics. ISA will continue its cooperation with supervisory bodies from EU Member States with whom it has signed memorandum of cooperation, mostly by performing joint supervisions with the regulators in the domicile countries of parent companies, and by participating in supervisory colleges upon invitations from regulators in the domicile countries of insurance companies operating on the Macedonian market.

In the period 2015-2017, ISA will perform self-assessment of the degree of implementation and compliance with basic insurance principles: ICP9-Supervisory review and reporting, ICP10-Preventive and corrective measures and ICP11-Enforcement. ISA is already in compliance with ICP 1- Objectives, powers and responsibilities of the supervisor and ICP2- Supervisor. For full compliance, the International Association of Insurance Supervisors will conduct training for ISA employees.

Fully-funded pension insurance. MAPAS as supervisor and regulator of the Fully Funded Pension Insurance and member of IOPS (International Organisation of Pension Supervisors), constantly strengthens its capacity and undertakes measures to protect the interests of pension funds. Applications for advisory mission by TAIEX are submitted to EC, for portfolio of pension funds, control of the listing system when choosing pension products, issuing measures and risk management. Implementation of this mission is expected to be completed during 2015/2016. MAPAS joined the global organization for the development and implementation of policies to increase access to appropriate financial services - Alliance for financial inclusion. Thus, opportunities are created for exchange of knowledge and information on regulation and policy creation related to protection of interests of the individual and introduction with his rights and obligations.

In the next period MAPAS will continue its activities related to risk based supervision and the Law on payment of pensions and pension benefits in fully funded pension insurance.

MAPAS constantly revises and improves supervision approaches. Risk based supervision allowed MAPAS to develop a system with special attention to management of supervised entities and improve supervision in order to better assess the risks in the operation of each supervised entity. Through the activities of the Committee for Risk Assessment all potential risks to the pension system will be regularly reviewed and appropriate control mechanisms will be proposed.

Attendance to workshops organized by IOPS for financial education is planned, as well as to seminars for risk based supervision, in order to obtain certificates for risk management. Training of staff for development of IT processes and software for risk based supervision, asset management, analysis and building a portfolio of pension funds, development of an electronic system for listing on pensions and pension benefits, and compliance with EU practices are also planned.

Financial Infrastructure. 2014 Progress Report of the Republic of Macedonia, Chapter 9 Financial Services, notes that legislation on financial market infrastructure is only partially aligned with the Financial Collateral Directive (2003/47/EC), while alignment with the Settlement Finality Directive (98/26/EC) has not yet begun. Law on Settlement Finality in Payment and Securities Settlement Systems will be adopted by the end of 2016, implementing the Settlement Finality Directive (98/26/EC). Adoption of this Law will provide for minimizing the systemic risks of the participants in the existing payment system and the existing securities settlement system, as well as maintaining system stability. In the medium term, provisions in the Law on Financial Collateral will be additionally aligned with the Financial Collateral Directive (2003/47/EC).

4.2.3 Labour market

Labor market policies are defined in the Employment Strategy of the Republic of Macedonia 2011-2015, Employment National Action Plan 2014-2015, Youth Employment National Action Plan 2015, and the Action Plan on reduction of gray economy 2014, while active measures are defined annually in Operational Plans on Active Employment Programmes and Measures. They are prepared in cooperation with the social partners.

Preparation of New employment strategy will commence in 2015 which will be in line with the SEE 2020 Strategy, taking into account the country's specific needs.

The preparation of the Employment and Social Reform Programmes is in its initial stage. The programme will identify major challenges and will present planned reforms for smart and sustainable growth with regard to the labor market and employment, human capital and skills, social inclusion and social protection. By the end of January 2015 an action plan for development of the program will be prepared, and the programme should be completed by the end of 2015.

In 2015, 525 million denars are allocated in the ESA budget to fund programs and measures for employment promotion, which is higher by 7.5 million denars compared to last year. Active programs and measures for employment will be co-financed with about 160 million denars provided by IPA Human Resources Development Component. With financial support from EU, implementation of training programs for known employer, internships, training to meet the needs for demanded occupations on the labor market, training for advanced IT skills and education for starting a business continues, which in the future is expected to increase employment of more than 4,700 young people, long-term unemployed and women by increasing their competence.

Also, the implementation of the Project Self-employment by crediting and the Project lending to legal entities to create new jobs continue. In 2014, in order to create better conditions for young people, two new programs were created: Project lending to young people up to 29 years and Project lending to legal entities to create new jobs for young people up to 29 years.

In order to facilitate employment of young people, exemption from payment of social contributions and personal income tax in the first year of employment is provided. This measure covered about 5,500 people so far, and it will apply until May 2016.

In the next period implementation of innovative projects will begin funded through a call for grants which is co-financed by IPA Human Resource Development Component aimed at social inclusion of persons in an unfavourable position in the labor market. Projects will be implemented by civil society organizations active in this area, in partnership with municipalities, social partners, public institutions that will develop service packages for successful integration of people in an unfavourable position in the labor market, with special emphasis on economic migrants, persons without documents, Rhoma women etc.

In order to connect supply and demand in the labor market, improvement of electronic services of ESA continues, through which interested unemployed persons can check current listings for available job positions, and employers have insight on data on the current state of unemployed persons actively seeking work according to the profile of education.

At the same time, with support from EU, in cooperation with the administration from Germany provided through a twinning instrument, ESA is working on strengthening its capacity and further restructuring of its operations to assess the relevance, effectiveness and results of the implemented active measures on the labor market and regular implementation of evaluation of the success of active measures. The results of the evaluation will be used to better targeting, developing new and implementing active employment measures.

With EU funding, capacity building for implementation of the legal framework for social entrepreneurship will be supported, as a model for achieving social inclusion and employment of certain social groups that are in unfavorable position compared with other citizens. A set of measures will be developed to promote social entrepreneurship and to improve access to financial instruments for social enterprises. Support to at least 10 social enterprises is planned by providing specialized consulting support according to the needs of the particular company.

In 2015 and 2016, in cooperation with ILO and with financial support from EU, under the project for promoting social dialogue, an effective system for peaceful resolution of labor disputes will be established, as well as base of specialized arbitrators for labor disputes by training 90 arbitrators. The system will support social partners in prevention and resolution of disputes in the collective bargaining process. In cooperation with ILO and EU a new office for the Economic and Social Council will be opened, as well as strengthening the Economic and Social Council at the national level, strengthening of the capacity of social partners and the Government in collective bargaining, implementation of a database of collective agreements and increasing the number of local economic and social councils.

Activities for adoption of a Law prohibiting and preventing unregistered activity are underway. The purpose of the law is to prevent exercise of unregistered activities of larger scale or larger businesses that are not registered and are part of the gray economy. This law will introduce standards and procedures to regulate this partially regulated area, improving the business environment for companies, creating jobs, protecting workers' rights and social security for all workers. Opportunities for unfair competition and avoiding paying taxes and contributions will be eliminated. The law will also penalize the demand of unregistered activity or complicity in performing unregistered activity. To reduce informal employment among young people preventive measures are implemented through the Project - Refuse undeclared work.

The effectiveness of fight against undeclared work will be increased by strengthening the capacity of the State Labour Inspectorate (SLI), as well as improving the systematic and coordinated involvement of relevant institutional actors and social partners in the fight against undeclared work. A research is prepared on the nature, causes and effects of undeclared work, measuring its size, the relationship between unemployment and undeclared work, and the effectiveness of the measures already taken in the Republic of Macedonia. A program is prepared to strengthen the capacity of SLI in order to implement an improved approach to tackle undeclared work.

Based on the amendments to the Law on employment and work of foreigners, a single procedure and single residence and work permit for foreigners will be introduced, as well as issuance of work and residence permits for foreigners in one place.

New Law on Employment of Persons with Disabilities is being prepared, which provides introduction of a quota system that will allow inclusion of these individuals in the open labor market. With EU funding, the development and implementation of standardized services for vocational rehabilitation and professional assistance to persons with special needs will be implemented, as a prerequisite for their successful involvement in the work process.

4.2.4. Public finance reforms

Possibility to prolong retirement and voluntary extension of retirement age. By amending the Labour Relations Law dated July 2014, possibility is introduced for voluntary extension of retirement age and instead of retiring at the age of 62 for women and 64 for men (as so far), the persons can, with a written statement submitted to the employer, request extension of the employment contract up to 65 years of age for women and 67 years of age for men, at the most. The employer is obliged to extend the employment contract up to the age for which the employee requests the extension. Hence, the employees are given the possibility to remain at work, certainly if they feel capable of extending their years of service. The legal solution is to the benefit of all, the employees, the employers and the Government. Extension of the years of service is positive for those citizens who at that age are competitive on the market, and the employers can keep the employees they need. Employees will continue paying mandatory social insurance contributions for these persons.

According to the projections, from 1st January 2015 the Pension and Disability Insurance Fund (PDIF) would realise Denar 604.80 million in 2015, Denar 1,321.60 million in 2016 and Denar 2,096.87 million in 2017 as revenues collected on the basis of contributions from this insurees. Savings on the basis of lower pension-related expenditures are expected to amount to Denar 2,592 million in 2015, Denar 5,477 million in 2016 and Denar 8,523 million in 2017, or total of Denar 16,592 million for the period 2015 - 2017.

Introduction of the obligation to pay mandatory social insurance contributions for persons engaged under contractual agreement and/or author contract. Pursuant to the amendments to the Law on Mandatory Social Insurance Contributions dated July 2014, new category of contributors is introduced, i.e. persons generating income from physical and/or intellectual work on the basis of contractual agreement and/or author contract in amount higher than the minimum wage in the country. Hence, the employer will have to pay pension, disability and health insurance if the contract/agreement is concluded for an amount higher than the minimum wage. Social safety will thus be provided for all employed persons, contributing to preventing the abuses made so far by some of the employers which substituted the full-time employment with concluding contractual agreement and author contract, paying only the personal income tax, and not paying the social contributions. According to the recent data, total number of persons engaged on the basis of contractual agreement or author contract is around 107,000 persons, 41,000 out of which generated income only on the basis of contractual agreement and/or author contract, and 65,000 persons generated income on the basis of salary and contractual agreement and/or author contract. By applying these amendments, increased revenues in PDIF are expected of around Denar 1,500 million, covering 66,895 employed and unemployed persons having concluded contractual agreement or author contract and receiving salary higher than the minimum one.

Under the **new Profit Tax Law** adopted in July 2014, the anti-crisis measure introduced in 2009 (the period of the global economic crisis) under which the profit was subject to taxation only in cases of profit distribution by way of dividends and other payments on the basis of profit generated, is abolished. As so far, re-invested profit will be tax exempted, i.e. profit invested for development purposes of the company in tangible assets (real estate, facilities and equipment) and in intangible assets (computer software and patents) for the purpose of expanding the activities of the taxpayer will be exempted from paying profit tax. The new law started to apply from 1st January 2015 by having the 2014 profit determined. Its application is expected to have positive fiscal implications on the Budget of the Republic of Macedonia.

Reducing the VAT registration threshold from Denar 2,000,000 to Denar 1,000,000. By adopting the Law on Modifications and Amendments to the Value Added Tax, VAT registration threshold was reduced from Denar 2,000,000 to Denar 1,000,000, applicable from 1st January 2015. This solution is expected to increase the number of taxpayers with the obligation to register for VAT purposes and will provide for reduction of the number of entities not registered as VAT taxpayers, which activities provide for higher value added (services sector), thus creating fair competition on the market. All taxpayers whose total turnover in the past calendar year exceeded Denar 1,000,000 or whose total turnover is envisaged to exceed this amount from the beginning of performing the business activity or is envisaged to exceed this amount in the course on the year, are obliged to register as VAT taxpayers. The total amount of expected Budget revenue based on this legal solution would be Denar 375.4 million.

4.3. BUDGETARY IMPLICATIONS OF MAJOR MACROECONOMIC SRUCTURAL REFORMS

Projected expenditures of the Budget of Republic of Macedonia also include the expenditures for the key structural reforms shown in both parts of NERP.

Table 4.1. Net budget impact from the key planned reformatory measures (Denar million)

	2014	2015	2016	2017
Business environment	-1.2	357.7	314.7	325.9
Labour market	-506.6	-669.8	-536.6	-395.8
Enterprise sector	-16.9	-15.6	-16.0	-15.5
Financial system	12.4	28.6	21.1	-
Administrative reforms	-10.5	-30.1	-33.6	-40.1
Customs system	-	122.1	84.6	37.4
Transport	-907.3	-1,313.6	-3,150.8	-2,869.2
Total impact on the Budget	-1,442.5	-1,549.2	-3,337.7	-2,957.2
Total impact on the Budget (% of GDP)	**0,27**	**0.28**	**0.58**	**0.49**

Source: Ministry of Finance

Table 4.1. shows the net-budget impact[19] of the envisaged measures in the separate areas. Net budget impact is the biggest in the field of transport, as a result of the large number of infrastructural projects being implemented in order to improve competitiveness of the country, and in the labour market, mainly as a result of the commitment of the Government to reduce unemployment, being identified in Part 2 (Box 2.1.) as a serious internal imbalance.

5. IMPLEMENTATION OF THE 2014 TARGETED POLICY GUIDANCE

With regard to the conclusions for Republic of Macedonia on the 16th Dialogue of Economics and Finance Ministers of the EU, candidate countries, representatives of the Commission and the European Central Bank and representatives of the central banks of the candidate countries, the Republic of Macedonia informs about the following:

1. *Implement the 2014-2016 medium-term fiscal strategy as planned and protect the execution of growth-enhancing capital spending by preparing contingency fiscal measures to compensate for unexpected revenue shortfalls or expenditure pressures; adopt a cautious and selective approach to the issuance of sovereign guarantees.*

To the end of achieving the planned fiscal consolidation and strengthening budgetary responsibility, the Government of the Republic of Macedonia proposed introduction of fiscal rules limiting the two main fiscal targets - Budget deficit (at a level no higher than 3% of GDP) and public debt (at a level no higher than 60% of GDP).

The Ministry of Finance closely monitors the realisation of the projected revenues and other inflows and the expenditures and other outflows of Budget, whereby appropriate measures are being undertaken for preserving the established fiscal target and providing space for implementation of priority infrastructure investments.

Process of issuance of new guarantees is strictly regulated and is subject to the borrowing procedure stipulated in the Law on Public Debt, according to which the claimants of guarantees should fulfill certain criteria so as for the state to issue a guarantee. According to the legal framework, in order for the Government to issue state guarantee, it is necessary that the project that is financed is in line with the Government strategic documents and co-financing funds are provided for uninterrupted implementation of the project.

2. *Continue to improve the composition of spending, by prioritising investment projects according to their productive potential on the basis of cost-benefit evaluations; increase the efficiency of social spending.*

Expenditure side of the Budget of the Republic of Macedonia in the next medium-term period is projected to the end of fully supporting the Macedonian economy through increased level of investments in infrastructure projects, as well as improvement of the economic situation of targeted groups of the population (pensioners and beneficiaries of social benefits). Thereby, disciplined budget spending will continue to be implemented, with an emphasis to restrictiveness and rigorous control over less productive costs, on one hand, and increase of investments in capital projects on the other, primarily in the infrastructure.

Public investments presenting the development component of the fiscal policy are precondition for improving the economic perspectives and better and more quality life of citizens, for which Denar 21,208 million are envisaged in the 2015 Budget.

Within budget funds allocated for capital expenditures, significant investments are envisaged in construction of highway and railway infrastructure, energy and utilities infrastructures, as

[19] Net budget impact from certain measure is difference between the funds from the Budget of the Republic of Macedonia for certain area and the revenues from IPA, as well as other revenues in the form of donations.

well as capital investments in improving the conditions in the educational, social and health system, agriculture, environment protection and judiciary.

Planned investments in 2015 and the next period, especially the ones in infrastructure projects, with their production and development potential will have a direct input in the construction sector, i.e. a positive impact on gross domestic product.

During preparation of these projects, preparation of a Feasibility study for the viability of the project is mandatory, where a cost-benefit analysis must also be included. This study is a mandatory document based on which a decision to finance the project is made.

Planned reforms in the social sphere, by simplifying the procedures for exercising these rights, as well as the effects from the integration of social centers in a unique information system, will provide for certain savings, at the same time extending the scope and properly targeting these allowances towards the most vulnerable categories.

In that direction, software for administration of cash benefits was introduced, by which the database on beneficiaries of social financial assistance is unified. The software enabled unification of the process for administering the rights and payment of benefits to the bank account of the end user, which significantly reduced budgetary expenditures for bank fees and postal services. The software has also provided for electronic connection of the competent institutions so as to gather the necessary data on exercising and using the concerned right. Hence, the competent Social Work Center provides, in a fast in efficient manner, the documentation necessary to determine the right to social financial assistance, such as information on the property and income of SFA applicants and of the members of their households.

With respect to the coming period, it is planned for the Project on Interconnectivity and Electronic Exchange of Information between the Ministry of Labour and Social Policy and 13 other institutions to be implemented. Documents available in an electronic form, which are necessary to complete the service, will be obtained directly, automatically, by the institutions. Effects to be achieved by implementing this activity are shortening the time necessary to administer the social allowances, reducing costs, reducing the overburdening of the social workers, increasing the control and better targeting the social allowances, improving the communication between the institutions included etc.

Pursuant to the latest amendments to the Law on Social Protection, obligation has been introduced for the unemployed persons - holders of the right to social financial assistance to mandatory be persons actively seeking job pursuant to the Law on Employment and Unemployment Insurance, all to the end of their easier and faster inclusion on the labour market.

3. *Improve medium-term budget planning and execution; increase fiscal transparency by providing more detailed data on planned and executed capital expenditure, including of public enterprises, in the context of the annual budget cycle and the medium-term strategy; adhere to EU accounting standards, notably ESA 2010; and resume the submission of fiscal notifications.*

Improvement of fiscal planning is a continuous process to which the Ministry of Finance is committed. In order to improve the public finance management as regards budget execution of budget users, the Treasury Information System was updated in 2014 with a new module for reporting multiannual liabilities. In addition to the recording of reported multiannual assumed liabilities, reports producing and providing initial framework in terms of assumed liabilities in the coming years are of utmost significance, on the basis of which the Ministry of Finance and the budget users will be able to more adequately plan the budgets for the coming years.

During 2014, the Project “Strengthening the Capacity of the Ministry of Finance for Macroeconomic Analysis and Policy Formulation” was prepared with support of IPA 2009. Under this Project, activities aimed at setting the fundamentals for introducing fiscal rules, improving the budget process and preparing new programme classification were carried out.

Activities aimed at improving the public finance management will be resumed and intensified through the Project for Building up the Capacity within the Department Dealing with Central Government Budget and Strengthening Medium-Term Policy Making Capacity- IPA TAIB 2011, being in line with the recommendations presented in the World Bank's Public Finance Review.

In the period to come, the reforms related to public finances, will be focused on medium-term projections and developing public revenues-related scenarios and determining fiscal room for financing priority policies that will contribute to higher economic growth rates. Thus, it is expected for the reforms to be accompanied with enhancement of the legislation for full harmonisation with the Acquis Communautaire, strengthened fiscal discipline by introducing fiscal rules, shifting of the time frame of the budget process, introduction of programme classification of expenditures and notification of the budget execution in line with ESA 2010.

In order to increase the transparency of public finances, as well as the need of citizens to understand the projects, activities and strategies included in the Budget in a simple, straightforward and transparent manner, 2015 Budget in Brief is prepared.

Monthly realisation of the Budget is available to the general public, through regular monthly reports that are published on the website of the Ministry of Finance.

According to the last amendments to the Law on Public Debt, Ministry of Finance upgraded the presentation of public debt data, whereby a comprehensive table for the stock of the total public debt, including the central government debt, the debt of municipalities and the guaranteed debt of public enterprises and state-owned companies is published on regular basis. This procedure demonstrates progress in terms of transparency when publishing the debt taking into account that the central government debt was published in the previous period, and the publication of the other public debt segments were publicly available, however dispersed at several places and sources. Additionally, data on the stock of the debt and portfolio structure are additionally published in the Bulletin of the Ministry of Finance and the Annual Report on Public Debt.

During 2014, the data on GDP were revised by implementing the calculation methods in line with ESA 95 and ESA 2010 for the series of data 2000—2012. Activities are a result of the harmonised Action Plan submitted to Eurostat, with respect to the phases of implementing ESA 2010. The following activities are preparing data in line with the transmission programme, covering preparation of data from the sectoral accounts, the regional accounts and data from the financial account.

4. *Improve the employability of workers, by better aligning vocational and tertiary education with labour demand needs, better target active labour market policies and publish regular performance evaluations.*

Within the past period, there has been detected improved situations on the labor market, i.e. the reduction of unemployment, by simultaneously increasing employment and activity.

	2012	2013	2013 (Q3)	2014 (Q3)
Unemployment rate (15-74)	31,0	29,3	28,7	27,9
Activity rate (15-64)	63,9	64,9	65,1	65,2
Employment rate (15-64)	44,0	46,0	46,3	46,9

Source: State statistical office

Considering the fact that the economic growth, employment and competitiveness depend largely on the existence of a properly trained workforce, through the project "Support to skills and competences development", the activities will continue to better align the vocational and higher education to the labor market needs.

One of the most important components of the project is modernization of four-year vocational education and training (VET), as a continuation of the project funded through IPA funds, through which have been reformed the two and three-year vocational education. The project will finance activities aimed at building the foundations of a modern and effective vocational education and training, which are characterized by later directing students toward professional specialization, increasing the relevance of standards and curricula in relation to the labor market and improving the mechanisms cooperation between schools and industry. These changes are expected to lead to transformation of VET, from a tightly professional to more general and broader technical education, that will ultimately result in greater relevance to the labor market and portability of skills, as well as increased flexibility of students that have completed school.

These more general skills will contribute, the student that has completed school, to be more qualified to adapt to the economic environment and possibly to change it, as well as to increase the internal and external mobility of students. The project will develop a proposal for consolidation of existing profiles based on national priorities for economic development and the labor market needs. Interventions to improve the VET system through this project will mainly go on 2 axes: harmonization of quality and relevance of vocational education and the labor market and grants for establishing cooperation between schools and industry.

Within the project, there has been planned a purchase of laboratories for vocational schools needs, because the new curricula will be more focused on practical training.

Through the IPA funding will continue the reforms in 2 and 3-year vocational education and training i.e. strengthening the system of lifelong learning by establishing a dynamic link between education and the labor market, which will strengthen the national systems of vocational education and training and adult education. The process of modernization of the 2 and 3 year vocational education and training started with the twinning project "Support to the modernization of the educational and training system." Within the project there have been developed 25 vocational standards and standards of professional qualifications, and reformed 13 two and three-year curricula, using an approach based on the learning and competencies outcomes, which are in use in 52 secondary schools. In terms of sustainability, the focus has been put on training of mentors and professional teachers to deliver the practical training of students in companies.

Within the project "Centers for completion of education and acquisition of skills competitive on the labor market for adults," the program for establishing vocational education for adults who have completed primary education, so far have completed more than 500 people.

Also, within the completed twinning project "Support for capacity building of the Centre for Adult Education and Development of Programs for adult education and literacy and completion of primary education for excluded persons" through the application of “learning by doing” methodology, there have been developed and tested six pilot programs for adult education with a total of 99 trained people. Into the 6 pilot programs for literacy and completion of primary education for excluded persons, have been covered 95 persons.

In order the vocational education and training in the Republic of Macedonia to develop in accordance with the European priorities and strategy for development of vocational education and training, our country actively participate in the process, "Turin", which is a participatory process of building policy for vocational education and training based on evidence and analysis.

In the area of higher education one of the most important measures being taken in line with the labor market demands, is the establishment of Boards for cooperation and trust with the public institutions of higher education, established in 2014. Boards have an advisory role and their members are actually relevant members of the business community or the economy of the scope of study programs.

The role of the Board for cooperation and trust with the public, is to discuss and give opinions, suggestions and recommendations for:

- the social use of the curricula of all study cycles;
- the content of the curricula of all study cycles;
- the social use, content, meaning, purpose and ethical dimensions of scientific-research and applied projects;
- the curricula for training and professional development programs;
- the criteria for enrollment of students;
- the practical training of students.

To the end of alleviating the employment of young persons, exemption from payment of social contributions and personal income tax in the first year of employment is envisaged[20]. The measure is aimed at reducing cost for employment of young people, which will facilitate school to work transfer. In 2014, 5.473 persons were employed under this measure.

Through the Project on Self-Employment Through Crediting and Project on Crediting Legal Entities over Job Opening 1,356 persons were covered in 2014.

In the course of 2014, in line with the set dynamics, Operational Plan on Active Employment Programmes and Measure (OP) continued to be intensively implemented, under which 21,048 persons were included. The measure Selfemployment and formalisation covered 879 persons in 2014. To reduce the mismatch between supply and demand, 3144 persons took part in training programs for known employer, internships, training for demanded occupations in the labor market, training for advanced IT skills and education for starting a businesses. To the end of activation and inclusion of the vulnerable groups in the labor market, 15,622 persons were included in motivational training. 640 persons were covered in the Programme on Subsidized Employment, and 96 with the Programme on Subsidized Employment of Young Persons SFA Beneficiaries.

In 2014 over 200,000 individual employment plans of unemployed persons were prepared with ESA support. Under the professional orientation programme 3,581 unemployed people were supported in choosing their occupation or employment through counseling, testing and informing them about the needs for certain occupations and employment opportunities. Modules for: personal development, job search skills, communication skills and presentation skills, appropriate behavior in the workplace, teamwork and leadership, safety, rights and obligations of work and financial skills, were developed for implementation of professional orientation, and career counselors were trained.

In order to facilitate the access of services to employers and unemployed persons, 7 regional employment fairs were held, where employers had the opportunity to present their work and to interact with the unemployed - potential workers. At the local level, Forums with employers were conducted in 30 municipalities in order to increase the awareness of employers for the active employment measures, diagnosis of barriers employers are facing in new employments and strengthening social dialogue between employers, local government units and state institutions at local level. 30 Info meetings with young people were held at local level in order

[20]For employed persons aged up to 29, Personal income tax and social insurance contributions are not paid..

for them to better understand the opportunities for (self-) employment and the current situation on the labor market.

Impact assessment of 6 active employment programs and research of the manner of implementation of services and measures intended for youth were conducted by ESA in 2014, with ILO support. The results were taken into account in preparation of active measures so as to increase the coverage of programs that have proven to be more effective (internships, training for a known employer), and adjust the remaining ones to improve their effectiveness (self-employment, subsided employment, training for demanded occupations).

With EU support, ESA is strengthening its capacity to assess the relevance, effectiveness and results of the implemented active measures on the labor market and to regular conduct evaluation of the effectiveness of active measures. The results of the evaluation will be used for better targeting and implementation of active measures.

5. *Accelerate the further implementation of the "regulatory guillotine", including the facilitation of licensing procedures for new companies through the quick completion of the one-stop shop system for business registration; and establish a fast and inexpensive bankruptcy procedure; implement the innovation strategy, including the efficient functioning of the Innovation Fund.*

To the end of further streamlining of the conditions for doing business, the remaining measures from the II, III and IV phase of the Regulatory Guillotine Project will continue to be implemented. Second phase comprises 51 measure, out of which 43 are fully implemented and 3 are abolished. Third phase comprises a total of 40 measures, out of which 37 are completely realised. Measures from the second and third phase contributed to simplification of most of the procedures in the Customs Administration, as well as the procedures for issuing approvals and licenses for doing business.

There is ongoing implementation of the measures under the Regulatory Guillotine – “Advantages for the Small Ones” Phase IV, simplifying the procedures for obtaining documents by the government institutions, shortening the deadlines for obtaining permits for building production capacities in some areas of the industry, expanding the interoperability process by including additional institutions therein, informative campaigns, etc. This phase comprises 40 measures, out of which 33 are implemented so far.

One stop shop company registration system is fully operational, and as of March 2014 company registration is carried out only electronically, through a "registration agent". As of December 2014 inclusive, total of 4,840 applications for registration were submitted, with average time for their approval of only 64 minutes.

The duration of the bankruptcy procedure in the first 9 months of 2014 is 0.28 years, being significantly shorter compared to the same period last year (0.39 years), while the recovery rate increased to 49.51%. The amendments to the Bankruptcy Law provided for: shortening of the deadlines for court proceedings, introduction of electronic sale of the bankruptcy estate, introduction of possibility for implementing plan for reorganisation of the debtor, transparency of the bankruptcy procedure and introduction of registry of authorised bankruptcy trustees.

	Voluntary liquidation		Bankruptcy procedures initiate/conclude		Concluded bankruptcy procedures		Total	
	01.01. - 30.09.2013	01.01. - 30.09.2014	01.01. - 30.09.2013	01.01. - 30.09.2014	01.01. - 30.09.2013	01.01. - 30.09.2014	01.01. - 30.09.2013	01.01. - 30.09.2014
Number of cases	1407	1369	1007	1373	84	86	2498	2828
Average duration (years)	0,43	0,45	0	0	4,51	2,05	0,39	0,28
Recovery rate (%)	100%	100%	0	0	12,48	13,77	48,79	49,51

For almost one year there have been continuous activities for carrying out the Action Plan of the 2013-2015 Innovation Strategy, being aimed at enhancing the affinity of the business sector to innovations, strengthening the human resources for innovations, creating adequate regulatory surrounding for innovation support and increasing the flow of knowledge between participants in innovation-related process. Implementation of the measures under the Action Plan is expected to boost competitiveness and encourage economic development based on knowledge and innovations, which is in line with the pillar: Smart growth, Dimension E of the "SEE 2020" Strategy.

During the past months, Operational Rulebook on the Instruments of FITD was prepared, and activities were also undertaken aimed at revising the rulebooks for each instrument separately. Fund participated in several workshops and conferences for possibilities for development of instruments for support of innovations, exchange of experience etc. First official promotion of FITD was held on 10th April 2014 in the Association of Chambers of Commerce, meetings were held with the management of the technical faculties, as well as many promotional activities. In cooperation with the Macedonian Bank for Development Promotion, the financing possibilities the Fund and MBDP offer were presented to potential candidates. FITD also promotes itself on its website, supported by Ministry of Education and Science, where all activities, information and programmes of FITD can be seen.

6. *Continue to take measures to repair the bank lending channel, including by fostering the clean-up of non-performing loan portfolios and make further progress to reduce indirect financial stability risks by promoting the use of the domestic currency.*

Non-performing loans continue to present a challenge for banks and their customers, as well as for the National Bank, which constantly monitor their movements. In 2013, the growth of non-performing loans averaged about 20% annually, with a noticeable slowdown in the second half of the year, which has been maintained throughout 2014. In September 2014, the annual growth rate of non-performing loans equaled 13.8%, while the average for the first nine months of the year is about 7%. As a result of the new credit risk management regulations, which entered into force on 1 December 2013, the banks have stepped up restructuring of loans, adjusting the period of repayment and installments to the customer needs. The effects of the restructuring were visible a few months later, when the analysis showed that about half of the restructurings proved to be successful. Additionally, it should be stated that the banks are rather reluctant to write off their claims, so that 52% of non-performing loans are 100% covered by provisions and are still kept in the bank records (probably due to the existence of collateral). It can be expected that the economic recovery will improve the quality of the loan portfolio of banks, which, however, in the crisis period has been preserved among the best in the region.

During 2014, the trend of denarization on both sides of the banks' balance sheet has continued. This trend is typical for the entire crisis period and is mainly driven by the denarization on the liabilities side, coupled with the denarization on the assets side. As explained above, the change in currency preference of entities towards increased share of deposits in national currency was largely influenced by the uncertainty regarding the crisis in the euro area, as well as the higher yields of Denar instruments. Additionally, the NBRM also supported this process through appropriate changes in the reserve requirement ratio (July 2013): reduction of the reserve requirement on liabilities in domestic currency and increase in the reserve requirement on liabilities in foreign currency. The NBRM continuously monitors the movements in the currency structure of deposits and loans, as well as in the interest rate differential for instruments in domestic and foreign currency. Monetary decisions are aimed at maintaining favorable trends in this domain, which in turn, increases the credibility of monetary policy based on the stability of the exchange rate of the denar against the euro.

6. SUMMARY DATA

Table 1a. Macroeconomic prospects

	ESA Code	2013	2013	2014	2015	2016	2017
		Level (bn EUR)	Rate of change				
1. Real GDP at market prices	B1*g	7.510	2.7	3.7	4.0	4.2	4.5
2. GDP at market prices	B1*g	7.585	7.0	5.5	5.0	5.8	6.3
Components of real GDP							
3. Private consumption expenditure	P3	5.643	2.1	2.7	3.2	3.3	3.8
4. Government consumption expenditure	P3	1.400	2.5	-2.1	1.2	1.0	1.0
5. Gross fixed capital formation[21]	P51	2.237	-16.6	12.0	8.0	8.2	8.2
6. Changes in inventories and net acquisition of valuables (% of GDP)	P52+P53	:	:	:	:	:	:
7. Exports of goods and services	P6	3.624	-2.7	14.7	8.5	8.8	9.2
8. Imports of goods and services	P7	5.395	-10.0	12.5	7.6	7.8	8.3
Contribution to real GDP growth							
9. Final domestic demand		9.280	-2.8	5.0	4.9	5.0	5.5
10. Change in inventories and net acquisition of valuables	P52+P53	:	:	:	:	:	:
11. External balance of goods/services	B11	-1.770	5.5	-1.3	-0.8	-0.8	-1.0

Source: SSO and calculations of the Ministry of finance

Table 1b. Price developments

		2013	2014	2015	2016	2017
1. GDP deflator	%, yoy	4.3	1.7	1.0	1.5	1.7
2. Private consumption deflator	%, yoy	2.1	0.0	0.8	1.4	1.5
3. HICP	%, yoy	:	:	:	:	:
4. National CPI	%, yoy	2.8	-0.3	2.0	2.2	2.2
5. Public consumption deflator	%, yoy	-0.8	0.4	2.4	2.0	2.5
6. Investment deflator	%, yoy	26.5	0.1	1.2	1.7	1.9
7. Export price deflator (goods & services)	%, yoy	6.1	1.7	2.0	2.0	2.0
8. Import price deflator (goods & services)	%, yoy	10.2	-1.2	2.0	2.0	2.0

Source: Calculations of the Ministry of finance

Table 1c. Labor market developments[22]

	ESA Code	2013	2013	2014	2015	2016	2017
		Level	Rate of change				
1. Population (thousands)			2,064.0	2,068.1	2,071.2	2,074.3	2,077.4
2. Population (growth rate in %)			0.14	0.20	0.15	0.15	0.15
3. Working-age population (persons)			1,672.5	1,678.3	1,687.0	1,697.8	1,710.4
4. Participation rate			57.2	57.6	58.0	58.5	59.0
5. Employment, persons			678.8	695.8	714.6	736.0	759.6
6. Employment, hours worked			:	:	:	:	:
7. Employment (growth rate in %)			4.3	2.5	2.7	3.0	3.2
8. Public sector employment (persons)			:	:	:	:	:
9. Public sector employment (growth in %)			:	:	:	:	:
10. Unemployment rate			29.0	28.0	27.0	25.9	24.8
11. Labour productivity, persons		705.8	-1.6	1.2	1.3	1.2	1.3
12. Labour productivity, hours worked			:	:	:	:	:
13. Compensation of employees	D1	:	:	:	:	:	:

Source: SSO and calculations of the Ministry of Finance

[21] Data refers to gross capital formation.
[22] ILO definition (15+) is used for the labor market indicators.

Table 1d. Sectoral balance

% of GDP	ESA	2013	2014	2015	2016	2017
1. Net lending/borrowing vis-à-vis the rest of the world	B9	-0.5	4.4	-1.8	1.6	2.0
of which:						
- Balance of goods and services		-18.5	-18.6	-18.4	-18.4	-16.9
- Balance of primary incomes and transfers		16.8	16.1	14.5	13.8	12.8
- Capital account		1.1	6.9	2.1	6.2	6.1
2. Net lending/borrowing of the private sector	B9/EDP B9	3.5	8.1	1.5	4.8	5.0
3. Net lending/borrowing of general government		-4.0	-3.7	-3.3	-3.2	-2.9
4. Statistical discrepancy		0.0	0.0	0.0	0.0	0.0

Source: National Bank of the Republic of Macedonia

Table 1e. GDP, investment and gross value added

	ESA	2013	2014	2015	2016	2017
GDP and investment						
GDP *level* at *current* market prices (in Denars)	B1g	499.6	526.8	553.4	585.3	622.0
Investment ratio (% of GDP)		28.5	30.3	31.6	32.8	34.1
Growth of Gross Value Added, percentage changes at constant prices						
1. Agriculture		9.0	3.0	2.5	2.2	2.4
2. Industry (excluding construction)		5.8	5.1	4.4	4.8	5.1
3. Construction		6.0	4.8	7.5	7.2	7.8
4. Services		2.5	3.6	3.3	3.6	3.7

Source: SSO and calculations of the Ministry of Finance

Table 1f. External sector developments

Euro billion	2013	2014	2015	2016	2017
1. Current account balance (% of GDP)	-1.8	-2.7	-3.9	-4.6	-4.1
2. Export of goods	2.37	2.69	2.85	3.16	3.53
3. Import of goods	4.23	4.65	4.94	5.44	5.88
4. Trade balance	-1.86	-1.96	-2.10	-2.28	-2.35
5. Export of services	1.14	1.28	1.39	:	:
6. Import of services	0.78	0.91	0.95	:	:
7. Service balance	0.36	0.37	0.44	0.53	0.63
8. Net interest payments from abroad	:	:	:	:	:
9. Other net factor income from abroad	-0.21	-0.21	-0.26	-0.29	-0.33
10. Current transfers	1.56	1.57	1.57	1.60	1.63
11. Of which from EU	:	:	:	:	:
12. Current account balance	-0.15	-0.23	-0.35	-0.44	-0.41
13. Capital and Financial Account	0.06	0.58	0.19	0.59	0.62
14. Foreign direct investment	0.26	0.31	0.34	0.38	0.43
15. Foreign reserves*	1.99	2.44	:	:	:
16. Foreign debt*	5.22	6.03	:	:	:
17. Of which: public*	2.17	2.84	:	:	:
18. O/w: foreign currency denominated	:	:	:	:	:
19.O/w: repayments due	:	:	:	:	:
20. Exchange rate vis-à-vis EUR (end-year)	61.51	61.50	61.50	61.50	61.50
21. Exchange rate vis-à-vis EUR (annual average)	61.58	61.50	61.50	61.50	61.50
22. Net foreign saving (lines 21-25: percentages of GDP)	:	:	:	:	:
23. Domestic private saving	:	:	:	:	:
24. Domestic private investment	:	:	:	:	:
25. Domestic public saving	:	:	:	:	:
26. Domestic public investment	:	:	:	:	:

Source: National Bank of the Republic of Macedonia
* Data for 2014 are as of September 2014

Table 1g. Sustainability indicators

	Dimension	2010	2011	2012	2013	2014
1. Current Account Balance	% of GDP	-2.0	-2.5	-3.0	-1.8	-2.7
2. Net International Investment Position	% of GDP	-51.1	-52.6	-55.1	-56.2	:
3. Export market shares	% yoy	0.0	13.6	-12.0	4.5	:
4. Real Effective Exchange Rate (CPI based, 2006=100)*	% yoy	-2.9	0.0	1.4	1.9	-0.8
5. Nominal Unit Labour Costs	% yoy	3.7	-3.4	3.3	1.9	:
6. Private sector credit flow	% of GDP	2.9	3.5	2.4	2.8	2.7
7. Private sector debt	% of GDP	76.5	77.8	82.8	82.5	:
8. General Government Debt	% of GDP	24.1	27.7	33.7	34.1	37.7

Source: National Bank of the Republic of Macedonia and Ministry of Finance
* Data for 2014 are as of September 2014

Table 2a. General government budgetary prospects

	ESA	2013	2013	2014[23]	2015	2016	2017
		Level (bn denars)	% of GDP				
Net lending (B9) by sub-sectors							
1. General government	S13	-20.0	-4.0	-3.7	-3.3	-3.2	-2.9
2. Central government	S1311	-19.3	-3.9	-3.7	-3.3	-3.2	-2.9
3. State government	S1312	:	:	:	:	:	:
4. Local government	S1313	-0.8	-0.2	0.0	0.0	0.0	0.0
5. Social security funds	S1314	0.2	0.0	0.0	0.0	0.0	0.0
General government (S13)							
6. Total revenue	TR	150.9	30.2	31.6	31.6	31.0	30.2
7. Total expenditure	TE	170.9	34.2	35.4	35.0	34.2	33.2
8. Net borrowing/lending	EDP.B9	-20.0	-4.0	-3.7	-3.3	-3.2	-2.9
9. Interest expenditure	EDP.D41	4.6	0.9	0.8	1.1	1.2	1.3
10. Primary balance		-15.4	-3.1	-2.9	-2.3	-2.0	-1.6
11. One-off and other temporary measures		:	:	:	:	:	:
Components of revenues							
12. Total taxes (11 = 11a+11b+11c)		85.2	17.1	17.8	17.4	17.0	16.6
12a. Taxes on production and imports	D2	68.1	13.6	14.2	13.9	13.5	13.3
12b. Current taxes on income and wealth	D5	14.8	3.0	3.1	3.0	3.0	2.9
12c. Capital taxes	D91	2.4	0.5	0.5	0.5	0.5	0.5
13. Social contributions	D61	42.4	8.5	8.5	8.8	8.7	8.6
14. Property income	D4	5.6	1.1	1.3	1.3	1.2	1.2
15. Other (15 = 16-(12+13+14))		17.6	3.5	4.1	4.1	4.1	3.9
16 = 6. Total revenue	TR	150.9	30.2	31.6	31.6	31.0	30.2
p.m.: Tax burden (D2+D5+D61+D91-D995)		127.7	25.6	26.3	26.2	25.7	25.2
Selected components of expenditures							
17. Collective consumption	P32	58.0	11.6	11.9	11.6	10.9	10.3
18. Total social transfers	D62 + D63	74.3	14.9	15.0	14.9	14.8	14.6
18a. Social transfers in kind	P31 = D63	:	:	:	:	:	:
18b. Social transfers other than in kind	D62	74.3	14.9	15.0	14.9	14.8	14.6
19 = 9. Interest expenditure (incl. FISIM)	EDP.D41	4.6	0.9	0.8	1.1	1.2	1.3
20. Subsidies	D3	12.2	2.4	2.6	2.4	2.3	2.1
21. Gross fixed capital formation	P51	21.8	4.4	5.1	5.0	5.0	4.8
22. Other (23 = 23-(17+18+19+20+21)		:	:	:	:	:	:
23. Total expenditures	TE	170.9	34.2	35.4	35.0	34.2	33.2
p.m. compensation of public sector employees	D1	36.1	7.2	7.1	7.0	6.6	6.2

Source: Ministry of Finance

[23] Fiscal data for 2014 are from the 2014 supplementary Budget.

Table 2b. General government budgetary prospects

	ESA	2013	2014[24]	2015	2016	2017
		Level (bn denars)				
Net lending (B9) by sub-sectors						
1. General government	S13	-20.0	-19.6	-18.5	-19.0	-18.3
2. Central government	S1311	-19.3	-19.6	-18.5	-19.0	-18.3
3. State government	S1312	:	:	:	:	:
4. Local government	S1313	-0.8	0.0	0.0	0.0	0.0
5. Social security funds	S1314	0.2	-0.1	-0.1	0.0	0.0
General government (S13)						
6. Total revenue	TR	150.9	166.7	175.1	181.3	188.1
7. Total expenditure	TE	170.9	186.3	193.6	200.3	206.4
8. Net borrowing/lending	EDP.B9	-20.0	-19.6	-18.5	-19.0	-18.3
9. Interest expenditure	EDP.D41	4.6	4.4	6.0	7.1	8.2
10. Primary balance		-15.4	-15.2	-12.5	-11.9	-10.1
11. One-off and other temporary measures		:	:	:	:	:
Components of revenues						
12. Total taxes (11 = 11a+11b+11c)		85.2	93.6	96.4	99.5	103.5
12a. Taxes on production and imports	D2	68.1	74.8	76.9	79.2	82.5
12b. Current taxes on income and wealth	D5	14.8	16.3	16.8	17.3	18.0
12c. Capital taxes	D91	2.4	2.5	2.7	2.9	3.0
13. Social contributions	D61	42.4	44.7	48.7	51.0	53.3
14. Property income	D4	5.6	6.9	7.0	7.1	7.2
15. Other (15 = 16-(12+13+14))		17.6	21.4	22.9	23.8	24.1
16 = 6. Total revenue	TR	150.9	166.7	175.1	181.3	188.1
p.m.: Tax burden (D2+D5+D61+D91-D995)		127.7	138.3	145.1	150.4	156.8
Selected components of expenditures						
17. Collective consumption	P32	58.0	62.7	64.0	64.0	64.0
18. Total social transfers	D62 + D63	74.3	78.8	82.6	86.7	91.0
18a. Social transfers in kind	P31 = D63	:	:	:	:	:
18b. Social transfers other than in kind	D62	74.3	78.8	82.6	86.7	91.0
19 = 9. Interest expenditure (incl. FISIM)	EDP.D41	4.6	4.4	6.0	7.1	8.2
20. Subsidies	D3	12.2	13.5	13.4	13.4	13.4
21. Gross fixed capital formation	P51	21.8	26.8	27.5	29.1	29.8
22. Other (23 = 23-(17+18+19+20+21)		:	:	:	:	:
23. Total expenditures	TE	170.9	186.3	193.6	200.3	206.4
p.m. compensation of public sector employees	D1	36.1	37.4	38.7	38.7	38.7

Source: Ministry of Finance

Table 3. General government expenditure by function

Percentage of GDP	COFOG	2013	2014	2015	2016	2017
1. General public services	1	3.8	4.4	4.1	:	:
2. Defence	2	1.1	1.1	1.1	:	:
3. Public order and safety	3	2.4	2.5	2.4	:	:
4. Economic affairs	4	3.1	3.6	3.7	:	:
5. Environmental protection	5	0.1	0.2	0.2	:	:
6. Housing and community amenities	6	2.2	2.1	2.2	:	:
7. Health	7	5.1	5.0	5.0	:	:
8. Recreation, culture and religion	8	0.8	0.8	0.8	:	:
9. Education	9	4.1	4.2	4.1	:	:
10. Social protection	10	11.3	11.4	11.4	:	:
11. Total expenditure (item 7 = 23 in Table 2)	TE	34.2	35.4	35.0	34.2	33.2

Source: Ministry of Finance

[24] Fiscal data for 2014 are from the 2014 supplementary Budget.

Table 4. General government debt developments

Percentages of GDP	ESA	2013	2014	2015	2016	2017
1. Gross debt[25]		34.1	37.7	35.5	37.3	38.7
2. Change in gross debt ratio		0.5	3.6	-2.2	1.7	1.4
Contributions to change in gross debt						
3. Primary balance[26]		3.1	2.9	2.3	2.0	1.6
4. Interest expenditure (incl. FISIM)[27]		0.9	0.8	1.1	1.2	1.3
5. Stock-flow adjustment		-3.6	-0.1	-5.5	-1.5	-1.5
of which:						
- Differences between cash and accruals		:	:	:	:	:
- Net accumulation of financial assets		:	:	:	:	:
of which:						
- Privatisation proceeds		:	:	:	:	:
- Valuation effects and other		:	:	:	:	:
p.m. implicit interest rate on debt		3.0	2.6	3.0	3.6	3.8
Other relevant variables						
6. Liquid financial assets		:	:	:	:	:
7. Net financial debt (7 = 1 - 6)		:	:	:	:	:

Source: Ministry of Finance

Table 5. Cyclical developments

Percentage of GDP	ESA	2013	2014	2015	2016	2017
1. Real GDP growth (%)	B1g	2.7	3.7	4.0	4.2	4.5
2. Net lending of general government	EDP.B.9	-4.0	-3.7	-3.3	-3.2	-2.9
3. Interest expenditure	EDP.D.41	0.9	0.8	1.1	1.2	1.3
4. One-off and other temporary measure		:	:	:	:	:
5. Potential GDP growth (%)		2.7	2.9	3.0	3.1	3.0
Contributions (percentage points):						
- *labor*		:	:	:	:	:
- *capital*		:	:	:	:	:
- *total factor productivity*		:	:	:	:	:
6. Output gap		-2.2	-1.4	-0.5	0.6	2.1
7. Cyclical budgetary component		-0.7	-0.5	-0.2	0.2	0.6
8. Cyclically-adjusted balance (2-7)		-3.3	-3.2	-3.2	-3.4	-3.6
9. Cyclically-adjusted primary balance (8-3)		-2.4	-2.4	-2.1	-2.2	-2.3
10. Structural balance (8-4)		:	:	:	:	:

Source: Ministry of Finance

Table 6. Divergence from previous programme (Pre-accesion economic programme)

	2013	2014	2015	2016	2017
1. GDP growth (% points)					
Previous programme	3.3	3.2	3.8	4.5	:
Latest programme	2.7	3.7	4.0	4.2	4.5
Difference	-0.6	0.5	0.2	-0.3	:
2. General government net lending (% of GDP)					
Previous programme	-3.9	-3.5	-3.2	-2.6	:
Latest programme	-4.0	-3.7	-3.3	-3.2	-2.9
Difference	-0.1	-0.2	-0.1	-0.6	:
3. General government gross debt (% of GDP)					
Previous programme	34.2	33.4	35.7	37	:
Latest programme	34.1	37.7	35.5	37.3	38.7
Difference	-0.1	4.3	-0.2	0.3	:

Source: Calculations of the Ministry of Finance

[25] As defined in Regulation 3605/93 (not an ESA concept).
[26] Cf. item 10 in Table 2.
[27] Cf. item 9 in Table 2.

Table 7. Long-term sustainability of public finances

Percentage of GDP	2007	2010	2020	2030	2040	2050	2060
Total expenditure	32.8	35.9	32.4	31.4	30.6	30.0	29.7
of which:	:	:	:	:	:	:	:
- Age-related expenditures	:	:	:	:	:	:	:
- Pension expenditure	7.7	8.9	9.0	9.1	8.8	8.6	8.5
- Social security pension	:	:	:	:	:	:	:
- Old-age and early pensions	:	:	:	:	:	:	:
- Other pensions (disability, survivors)	:	:	:	:	:	:	:
- Occupational pensions (if in general government)	:	:	:	:	:	:	:
- Health care	4.4	4.5	5.0	5.0	5.2	5.4	5.5
- Long-term care (this was earlier included in the health care)	:	:	:	:	:	:	:
Education expenditure	:	4.6	5.2	5.3	5.4	5.4	5.4
Other age-related expenditures	:	:	:	:	:	:	:
Interest expenditure	0.8	0.7	1.5	1.5	1.4	1.2	1.0
Total revenues	32.2	33.4	30.0	29.8	29.5	29.5	29.5
of which: property income	:	:	:	:	:	:	:
of which: from pensions contributions (or social contributions, if appropriate)	6.0	6.2	6.4	6.7	6.5	6.4	6.4
Pension reserve fund assets	:	:	:	:	:	:	:
of which: consolidated public pension fund assets (assets other than government liabilities)	:	:	:	:	:	:	:
Assumptions							
Labour productivity growth	2.9	2.2	1.6	1.8	2.1	2.1	2.0
Real GDP growth	6.5	3.4	3.8	4.1	4.0	3.7	3.5
Participation rate males (aged 20-64)[28]	74.8	76.3	80.1	83.6	86.3	88.4	89.7
Participation rates females (aged 20-64)	50.4	51.8	56.8	61.8	66.5	70.9	75.2
Total participation rates (20-64)	62.8	64.2	68.5	72.7	76.4	79.6	82.5
Unemployment rate	35.2	32.2	24.5	16.3	11.2	7.6	4.9
Population aged 65+ over total population	9.6	9.7	10.0	10.4	10.8	11.2	11.7

Source: Calculations of the Ministry of Finance

Table 7a. Contingent liabilities

% of GDP	2014	2015
Public guarantees	8.2	:
Of which: linked to the financial sector	:	:

Source: Ministry of Finance

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

	Dimension	2013	2014	2015	2016	2017
Short-term interest rate	Annual average	:	:	:	:	:
Long-term interest rate	Annual average	:	:	:	:	:
USD/EUR exchange	Annual average	1.3281	1.3324	1.2678	1.2678	1.2678
Nominal effective exchange rate	Annual average	:	:	:	:	:
Exchange rate vis-à-vis the EUR	Annual average	61.5	61.5	61.5	61.5	61.5
Global GDP growth, excluding EU	Annual average	3.8	3.7	4.3	4.5	:
EU GDP growth	Annual average	0.0	1.3	1.5	2.0	:
Growth of relevant foreign markets	Annual average	:	:	:	:	:
World import volumes, excluding EU (y-o-y)	Annual average	3.4	2.9	4.9	5.6	:
Oil prices (Brent, USD/barrel)	Annual average	108.8	102.6	91	92.8	:

Source: European Commission, European Economic Forecast, Autumn 2014; IMF, World economic outlook, October 2014

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

PART II

SECTORAL STRUCTURAL REFORMS TO PROMOTE COMPETITIVENESS AND GROWTH

1. INTRODUCTION

Growth of economic activity continued in 2014, however, more intensively compared to the previous year. Hence, real GDP growth rate in the first quarter amounted to 3.2%, reaching 4.4% in the second quarter and 4.1% in the third quarter, hence the average GDP growth in the first nine months in 2014 accounted for 3.9%. These growth rates are among the highest ones compared to the EU Member States and the region.

Growth in the first three quarters in 2014 was driven by gross investments, experiencing real growth of 17.4%. Growth of gross investments corresponds to public sector's infrastructure investments and investments in capacities in the technological-industrial development zones (TIDZs) and industrial zones. Export of goods and services, which experienced 15.3% real growth, also contributed positively to the growth. Increase in export of goods was mainly a result of the increased export potential of the country. Export growth was accompanied by the change in the structure of the export towards products with higher value added, in line with the production and exports of companies in the TIDZs and industrial zones. Growth of gross investments and export growth inevitably influenced the import growth, increasing by 13.3%. Personal consumption grew by 2.1%, as a result of the growth of disposable income of households in terms of growth in employment, wages and pensions, as well as by the intensified growth of crediting to households in this period, mainly in the form of consumer loans.

Taking into account the expectations for uncertain external surrounding, the Government will continue to conduct active economic policy in 2015. Real GDP growth in 2015 is envisaged to account for 4%. Domestic demand is expected to positive contribution to economic growth. Gross investments in 2015 are expected to achieve 8% growth in real terms, based on gradual increase of private investments mainly driven by FDIs and increase of budget capital expenditures through realisation of major infrastructure projects. Envisaged economic growth is expected to have positive effect on labour market trends and further reduction of the average unemployment rate to 27% in 2015.Monetary policy will be focused on preserving price stability in 2015 as well, by maintaining stable Denar exchange rate in relation to the euro, whereby inflation rate is envisaged to amount to 1%.

Activities in the coming period will be aimed at further improvement of physical capital, human potential, better industrial structure, business environment and trade integration, in order to increase the competitiveness and economic growth of the country.

The efficient and safe transport infrastructure facilitates and encourages mobility of both people and goods, overcomes the limitations of local markets and creates opportunities for equal regional development. In the future period, activities have been defined for modernisation of the existing energy infrastructure and building of new energy facilities which shall provide for increase in the safety of power supply, taking into account the increased inclusion of renewable energy sources (RES) in the energy consumption, which is one of the main strategic objectives of the Government of the Republic of Macedonia in the energy sector. Hence, the construction and improvement of the infrastructure shall lead to reduction of the unemployment and poverty, improvement of the living standard, increase of competitiveness of the national economy and realisation of accelerated economic growth.

Republic of Macedonia will continue with activities supporting human capital development through further increasing the quality of education. Government will stimulate investments in the field of science and connection of universities and firms for commercialisation of innovations, improvement of the quality of learning programmes and their adjustment to the needs of the private sector, as well as additional training of the teaching staff.

Regarding better industrial structure, policies and activities are aimed at SMEs support and development. They are arising from the National SMEs development strategy 2002-203, EU Small Business Act, Strategy for development of crafts 2011-2020, Innovation strategy 2012-2020 and the annual SMEs programmes. The documents are following the recommendations and related communications from the Strategy EU 2020, Strategy SEE 2020, and other relevant regional initiatives.

As an additional opportunity to support projects from the private sector are also European projects where Macedonia participates: COSME, Horizon 2020. Also, Macedonia participates in the regional project Platform for enterprise development and innovation facility for the Western Balkans - EDIF, supported by the EC, EBRD and the European Investment Fund.

Improving the business environment will be realised by further reducing the regulatory and administrative burden on business by facilitating the process of starting a business, obtaining construction permits, registering property, electronic payment of taxes and resolving insolvency.

In the area of trade integration of the Republic of Macedonia will continue to strive for promotion of regional trade in goods and services by creating a free trade area within CEFTA and implementation of the Regional Convention on Pan Euro-Mediterranean rules of origin. Through the implementation of a new computerized transit system, transit procedure will be further facilitated and enhanced.

2. MACROECONOMIC CONTEXT AND SCENARIO

Macroeconomic policy will continue to realise the strategic commitments to long-term and sustainable economic growth of the country in 2015. Policy will provide for preserving macroeconomic and financial stability, thus boosting the competitiveness of the economy, increasing employment and improving the living standard and quality of life of the population. This will be achieved by improving the business environment, conducting tax and customs policy for supporting development of economic entities, encouraging investment activity and attracting foreign direct investments, developing human capital and economic infrastructure of the country.

Economic activity. In 2015, global economic growth is expected to be moderate, while in the EU, the growth of economic activity is expected to remain low and vulnerable. Taking into account the expectations for uncertain external surrounding, the Government will continue to conduct active economic policy. In 2015, positive economic trends are expected to continue in Macedonia, whereby it is envisaged for the real GDP growth to account for 4%. Positive growth of industrial production, as well as its diversification are envisaged to continue during 2015 as well. Industry growth projection amounts to 4.4%, in line with the increased production potential of the country as a result of the investments in the free economic zones. Construction sector is expected to realise 7.5% growth rate in real terms, as a result of the realisation of major infrastructure projects and the announced investments in the technological industrial development zones and the industrial zones. Growth in agriculture sector is expected to amount to 2.5%, while the services sector is expected to realise 3.3% growth. Analysed according to the expenditure side of GDP, domestic demand is expected contribute positively to economic growth. Gross investments in 2015 are expected to achieve 8% growth in real terms. Growth projections are based on gradual increase of private investments mainly driven by FDIs and increase of budget capital expenditures. To that end, realisation of major infrastructure projects is envisaged, aimed at improvement of the transportation network in the country, improvement of energy and utilities infrastructure, capital expenditures aimed at improvement of the conditions in the education, social and health system. Growth of personal consumption in 2015 is expected to be 3.3%, as a result of the expected increase of salaries and the number of employees, while growth of public consumption is projected at 1.2%. Export of goods and services is expected to achieve average real growth of 8.5%, as a result of the increased activity of the existing and opening new export capacities. This will contribute to further improvement of the export structure. Anticipated increase of domestic demand and export activity provide for increase of import which is expected to be 7.6% in real terms in 2015.

Monetary Policy. Monetary policy will be focused on preserving price stability in 2015 as well, by maintaining stable Denar exchange rate in relation to the euro. At the same time, the Central Bank will be focused on further maintenance of financial stability, as significant component of macroeconomic stability. Thus, the Central Bank will continue to regularly monitor the trends in the domestic economy and the international surrounding, as basis for timely undertaking of measures to the end of achieving its goals.

Inflation. Moderate increase of inflation by around 1% is expected in 2015. Increase of prices in the next year will primarily reflect the price changes of food products and to a lesser extent the effects of the further increase of domestic demand. Risks for the projected inflation trajectory in 2015 are related to the uncertainty about the global economy and the price trends of global primary products. It is expected for the inflation rate to continue to pick up during 2016 as well, when it is expected to account for around 2%.

Labour market. Envisaged economic growth in 2015 is expected to have positive effect on labour market trends. Number of employees is envisaged to increase by 2.7%, which will result in reducing the number of unemployed persons by 2.4% in 2015. Job creation is also expected from the increase of labour force, projected to surge by 0.5%. Such trends imply for average employment rate to increase to 42.4% in 2014, while average unemployment rate is projected to reduce to 27%. Active population in 2015 is expected to account for 58% of the working-able population. Nominal growth of average gross salary is expected to be 3% in 2015.

External Sector. As in 2014, new companies with foreign capital will have significant positive effects on export in the coming years as well. Some of the new inflows of foreign direct investments, in the period of establishing the facilities will have certain effects on import of machines and equipment, which will contribute to keeping the deficit of goods and services in the next two years at similar level as in 2014. However, in the medium run, in line with the expected more significant strengthening of the export potential on the basis of foreign investments, its gradual narrowing is expected. As for private transfers (approximated through net purchase on the foreign exchange market), average slowdown of their share in GDP is expected. In such projected trends of the main current account items, the current account deficit in 2015 is expected to gradually deepen to 3.9% of GDP. Such trend is expected to continue in 2016 as well, when the negative current account balance is expected to account for 4.6% of GDP which, even in conditions of relatively stable trade deficit as regards goods and services, will result from the expected reduction of private transfers. Projections for BOP current account balance in the period 2015-2016 is accompanied by risks, mainly related to the global economic recovery and the prices on the global markets.

Net inflows in the **financial account** in the period 2015-2016 will mainly arise from the expected foreign direct investments, the planned external borrowing by the state and the expected borrowing by the private sector. Growth of domestic economy, improvement of global climate and stabilisation of global financial markets is expected to contribute to preserving investors' positive perceptions. Total net inflows in the financial account in 2015 will be lower as a result of the maturity of higher amounts of repayments of debt towards abroad, being expected to increase to around 6% of GDP in 2016. Risks about capital inflows are mainly related to the dynamics of global recovery, which would influence the decisions of investors. Projected trends in the current and financial accounts are expected to provide for additional accumulation of foreign currency reserves in the next period and further maintenance of relatively stable and satisfactory coverage of average import of goods and services as of each next year, to the end of preserving the capacity for support of the stability of the Denar exchange rate.

3. Sectoral reform measures being implemented and planned to achieve economic policy objectives 2014-2017

3.1. Physical capital

The economic infrastructure is an important pre-condition for the economic development of a country, and the same having an impact on the business opportunities, as well as on the attractiveness of the country for work and investment. The efficient and safe transport infrastructure facilitates and encourages mobility of both people and goods, overcomes the limitations of local markets and creates opportunities for equal regional development. In the future period, activities have been defined for modernisation of the existing energy infrastructure and building of new energy facilities which shall provide for increase in the safety of power supply, taking into account the increased inclusion of renewable energy sources (RES) in the energy consumption, which is one of the main strategic objectives of the Government of the Republic of Macedonia in the energy sector. Hence, the construction and improvement of the infrastructure shall lead to reduction of the unemployment and poverty, improvement of the living standard, increase of competitiveness of the national economy and realisation of accelerated economic growth.

3.1.1. Transport

The Republic of Macedonia has achieved significant progress in the implementation of construction projects, that is, the preparation of the construction documentation for road and railway sections along Corridor VIII and X (Xd). The road and railway infrastructure along Corridor VII and X(Xd) is being build and reconstructed in continuity, representing part of the network of the South East Europe Transport Observatory (SEETO). Besides projects that are already started or planned through co-financing with the IPA Component for regional development, roads are also envisaged to be constructed with a loan from EBRD and WB. By realising these investments, the competitiveness of the country shall significantly improve in terms of safer, cost-efficient and more efficient transport. Parts of the covered sections are also part of the SEETO network of priority road corridors in SEE. The investment priorities in the transport infrastructure are in accordance with the multi-annual plan of SEETO.

The construction of the corridors shall be of particular importance for both the economy and the citizens. By developing the network of corridors that are passing through the Republic of Macedonia, the markets of countries in the region shall be more integrated and the connection with the common EU market shall be secured.

Measure: Project for preparation of a Study and an Action Plan for improvement of the safety on the overall SEETO network (Corridor X, X-d, VIII, route 6 and route 8)

Type of measure: Study and Action Plan

Description of how the measure contributes to national economic policy objectives: By preparing the study and the action plan, recommendations shall be provided for improvement of the standards for designing of new road systems, reduction of the risk for accidents on roads in the Republic of Macedonia and significant reduction of casualties (automobile and motor drivers, pedestrians, bikers, etc.).

Current status of preparation/implementation: For the purposes of realisation of this project a contract was signed with a consultant for duration of 12 months in September 2014.

Timetable for implementation: The Study shall be prepared in the second half of 2015.

Contribution to SEE 2020 Strategy: The measure contributes to the pillar Sustainable growth, Dimension I. Transport.

Potential implementation challenges and risks: Poor quality of the Study and the Action Plan.

Budgetary implications: The contract value is 145.271 euros, of which 85% from IPA and 15% from the national Budget.

Foreseen impact of the measure: The objective of this project is to prepare the Study and the Action Plan for improvement of the safety along the SEETO network of (Corridor X, X-d, VIII, route 6 and route 8).

Flagship measure: UPGRADING AND REHABILITATION OF CORRIDOR 10

Measure: Railway infrastructure

Type of measure: Investment.

Description of how the measure contributes to national economic policy objectives, current status of preparation/implementation, timetable for implementation and budgetary implications:

- Reconstruction of the railway Corridor 10

With funds secured from a loan from EBRD in amount of 17.600.000 euros during 2015, the reconstruction of the third and last section of Corridor 10 shall be completed, that is, the section Negotino – Nogaevci (L=30 km). In the previous period, reconstruction was performed on the sections Tabanovce – Kuamnovo (L=12 km) and Miravci – Smokvica (L=12km). The works carried out on the three sections enabled increase of the speed limit up to 120 km/h, which reduced the travel time.

- Rehabilitation and upgrading of the Railway Station Skopje according to the best EU practices

The group of projects within this operation were financed through IPA Component 3 – Regional development. The objective of the Project is to modernise the Railway Station in Skopje in accordance with the best European practices so as to meet the requirements and needs of the passengers, including the passengers with special needs. The operation shall also contribute to improvement of security and safety, as well as modernisation of signalisation and passenger information system. The packet of projects (one agreement for framework services, two procurement contracts and one construction contract) amounts to 2.141.075 euros.

On 30.04.2014, a contract was concluded with the selected company. The duration of the contract as of the moment of its signing is 11 months. By the end of October 2014, 45% of the works were completed.

Contribution to SEE 2020 Strategy: The measure contributes to the pillar Sustainable Growth, Dimension I. Transport.

Potential implementation challenges and risks: Not completing the construction activities on time and poor performance quality.

Foreseen impact of the measure: The realisation of the projects shall provide for stronger integration with the markets from countries of the region and connection with the common EU market.

Measure: Road infrastructure

Type of measure: Investment.

Description of how the measure contributes to national economic policy objectives, current status of preparation, timetable for implementation and budgetary implications:

- Construction of the section Demir Kapija - Smokvica

By completing the road Corridor X at a motorway level, the capacity and the overall efficiency of the route E-75 North – South shall improve, thus obtaining safe and faster transport. The construction of the motorway section in length of 28.3 km is realised with funds from the IPA Component for Regional Development, from EBRD, EIB, as well as from budget funds. The construction activities have commenced in 2012, and have continued throughout 2014. By October 2014, 50,6% of the construction works have been completed. The construction of the section Demir Kapija – Smokvica is envisaged to be completed in 2016. The total value of the project is 219.125.677 euros, out of which IPA funds are 45.000.000 euros and the remaining part are funds secured from EIB - 89.947.799 euros and EBRD - 84.177.878 euros.

- Rehabilitation of the motorway section Veles - Katlanovo

The rehabilitation of the motorway section Veles – Katlanovo shall improve the capacity and overall efficiency of the route E-75 South – North and shall provide safe and faster transport. The total contract value, which was signed in July 2014, amounts 5.674.232 euros of which 85% of the funds are provided from IPA and 15% from the Budget. The construction works are ongoing, whereas the duration of the construction works in accordance with the contract is 12 months.

- Rehabilitation of bridges with grant from NATO (Road Corridor 10)

The third phase of the project relates to the strengthening of 13 bridge constructions along the section: Veles – Katlanovo, rehabilitation of the secondary elements of the bridge constructions such as the drainage storm water systems, replacement of the protective railings, as well as replacement and correction of the carriageway construction on these bridges. The activities should be completed by 31.08.2015. The funds are grant from NATO in amount of 8.5 million euros. The realisation of this project shall improve the capacity and the overall efficiency of the route E-75 South – North and shall provide for safe and faster transport.

- Rehabilitation and upgrading of the motorway section Smokvica - Gevgelija

The rehabilitation of this part of Corridor X shall secure conditions for safe and faster transport on this part of the motorway, thus improving the capacity of the overall efficiency of the route A1 (E-75). The envisaged contract value is 8.971.170 euros, of which 85% are IPA funds, and the other 15% are budget funds. The duration of the construction works following the contract signing shall be 18 months. The tenders submitted for the published construction contract notice are currently being reviewed.

- Construction of road A1 and Pan-European Corridor Xd Gradsko – Prilep at an express road level, section Most (bridge) on river Raec – interchange Drenovo

The road in length of 10,2 km shall be financed with an EBRD loan, and shall be realised in the period 2015 – 2019.

Contribution to SEE 2020 Strategy: The measure contributes to the pillar Sustainable Growth, Dimension I. Transport.

Potential implementation challenges and risks: Not completing the construction activities on time and poor performance quality.

Foreseen impact of the measure:The realisation of the projects shall provide for improved integration with the markets from the countries of the region and connection with the common EU market.

Flagship measure: UPGRADING AND REHABILITATION OF CORRIDOR 8

Measure: Railway infrastructure

Type of measure: Investment.

Description of how the measure contributes to national economic policy objectives, current status of preparation/implementation, timetable for implementation and budgetary implications:

The objective of the construction of Corridor 8 is the connection of the Black Sea with the Ionian Sea, hence the significant strategic and economic importance of this project.

- Reconstruction of the railway section from Kumanovo to Beljakovce (30,8 km);

Using the funds in amount of 46.400.000 euros, secured through loan from EBRD, in March 2014 the construction works on the first section of the Eastern part of the railway Corridor 8, Kumanovo – Beljakovce commenced. The construction is envisaged to be completed within a period of 30 months, that is, in the third quarter of 2016.

- Construction of new and reconstruction of the existing railway section from Beljakovce to Kriva Palanka (34 km)

For the second section of the Eastern part of the railway corridor 8, Beljakovce – Kriva Palanka, in December 2014, a loan was secured from EBRD in amount of 145.000.000 euros for the execution of the construction works. In the fourth quarter of 2015, it is envisaged for a contract to be concluded with a selected construction company, and to perform the reconstruction of the existing bridges, tunnels, alignment and to build new ones in a period of 48 months.

Contribution to SEE 2020 Strategy: The measure contributes to the pillar Sustainable Growth, Dimension I. Transport.

Potential implementation challenges and risks: Not completing the construction activities on time and poor performance quality.

Foreseen impact of the measure: The realisation of the projects shall provide for improved integration with the markets from the countries of the region and connection with the common EU market.

Measure: Road infrastructure

Type of measure: Investment.

Description of how the measure contributes to national economic policy objectives, current status of preparation/implementation, timetable for implementation and budgetary implications:

This investment shall contribute to the construction of the national road A2 and the Pan-European Corridor VIII at motorway level, thus improving the competitiveness of the country as regards the increase of the transport quantity, increase in the transport safety and reduction of the travel time. This section is also part of the SEETO network of priority road corridors in SEE. In addition to the international frames, this investment shall contribute to the increase in the economic growth at national level, especially in the western part of the Republic of Macedonia.

- Construction of motorway A2, section Kichevo – Ohrid, in length of 57 km

This project shall be of particular importance for the tourism development, having in mind that it connects several of the most important tourist destinations in that part of the country: Ohrid – Struga region, the Debarca area and the ski-centre Mavrovo. In addition, this motorway shall provide for facilitated connection with Albania and Greece. The timeframe for completion of the investment is February 2018. The investment value is USD 505 million, and the funds are provided with a loan from the China Exim Bank. The project is being realised in accordance with the envisaged dynamic without any major problems, and is expected to be completed within the envisaged timeframe.

- Construction of the national road A2 and the Pan-European Corridor VIII at motorway level, section Trebenishte – Struga, in length of about 8 km

The funds for this project were secured through an EBRD loan, and the same shall be realised in the period 2015-2019.

- Construction of express road A2, Kumanovo – border with Bulgaria, section Rankovci – Kriva Palanka, with possibility for future motorway upgrading, in length of about 22 km

The funds for this project shall be secured through a WB loan in 2015, and the same shall be realised in the period 2015 – 2019.

Contribution to SEE 2020 Strategy: The measure contributes to the pillar Sustainable Growth, Dimension I. Transport.

Potential implementation challenges and risks: Not completing the construction activities on time and poor performance quality.

Foreseen impact of the measure: The realisation of the projects shall provide for improved integration with the markets from the countries of the region and connection with the common EU market.

Flagship measure: UPGRADING AND REHABILITATION OF THE LOCAL AND REGIONAL ROAD INFRASTRUCTURE

Type of measure: Investment.

Description of how the measure contributes to national economic policy objectives, current status of preparation/implementation, timetable for implementation and budgetary implications:

- Construction of the motorway A4 section Miladinovci – Sv. Nikole – Shtip, in length of 47 km

This investment shall be the first motorway section in the eastern part of the Republic of Macedonia, which shall contribute to the increase of the economic growth on national level, especially in the East and Southeast region. The project is currently in the construction phase, by November 2014, 7% of the contract for construction works have been realised. The timeframe for completion of the investment is May 2017. The investment value is USD 278 million, and the funds were secured with a loan from the China Exim Bank. The project is being realised in accordance with the envisaged dynamics without any significant problems, and is expected to be completed within the envisaged timeframe.

- Project for construction, reconstruction and rehabilitation of national and regional roads

The realisation of these investments shall significantly improve the competitiveness of the country as regards the traffic increase, increase of the transport safety and reduction of the travel time.

(A) The investment value is 160.000.000 euros, and the funds were secured with a loan from EBRD. All sections are currently in the design phase, and it is expected that the construction of the projects from Tranche 1 to commence at the end of 2015. This investment in the period 2015 – 2019 shall contribute to the construction of the following sections: Rehabilitation and reconstruction of the existing road A3, section Shtip – Kochani at express road level, in length of about 25 km, Construction of state road A3 at express road level, section Ohrid – Peshtani, in length of about 12 km.

(B) The project is divided into two loans from the WB.

The first loan in amount of 52 million euros, in the period 2015-2019, is envisaged to be used for construction of 12 road routes in total length of 149 km. The tender documentation for 4 road routes is currently in its phase of preparation, whereas the others are in the design phase. It is expected that the construction of the first four road routes shall commence at the beginning of 2015.

The second loan in amount of about 105 million euros is planned to be signed in 2015, and in the period 2015-2019 is envisaged to be used for construction of 4 road routes in total length of 60,8 km.

Contribution to SEE 2020 Strategy: The measure contributes to the pillar Sustainable Growth, Dimension I. Transport.

Potential implementation challenges and risks: Not completing the construction activities on time and poor performance quality.

Foreseen impact of the measure: Improvement of the competitiveness of the country regarding the increase of the traffic, increase of the transport safety and reduction of the travel time.

3.1.2.Energy

The priorities of the Government in the Republic of Macedonia in the energy sector, which are related to national objectives for security and development, include: security of supply, sustainable economic development and competitiveness of the economy.

Flagship measure: ENERGY DEVELOPMENT AND STRENGTHING OF INTERCONECTIVITY WITH NEIGHBORING COUNTRY

The primary energy consumption in the Republic of Macedonia is around 120.000 TJ yearly from which about 55% are provided from domestic production and the rest is from import. Total needs of oil derivates, natural gas and coal are provided from import. The annual electricity demand in the last several years is around 8000 GWH, out of which about 70% are provided from domestic production and the remaining quantity is imported.

Energy infrastructure includes electricity sector, coal sector, oil and petroleum product sector, natural gas sector and heat sector.

Total installed capacity in the electricity sector is around 1963,8 MW (hydro power plants with 638 MW, thermal power plants with 1035 MW, thermal power plants on natural gas with 287 MW, renewable energy sources- PV with 3,8 MW).

Main gas pipeline enters in Macedonia at Deve Bair and stretches trough Kriva Palanka, Kratovo and Kumanovo to Skopje. The main gas pipeline has a capacity of 800 million Nm^3 per year with the possibilities to have it increased to 1200 million Nm^3 per year.

Republic of Macedonia does not have domestic production of crude oil. Crude oil is processed in the OKTA refinery, with a maximum capacity of 2.5 million tons per year. Crude oil is transported via pipeline Skopje - Thessaloniki, with a length of 213 km and maximum capacity of 2.5 million tons per year.

The total installed capacity of the heating systems is about 630 MW. Biggest heating system is the one operated by Balkan Energie Group on which are connected approximately 550 MW.

The Energy Development Strategy defines activities regarding modernization of the existing energy infrastructure and construction of new energy facilities. These activities enable increasing of security of supply.

Measure: Revise of Energy Development Strategy in the Republic of Macedonia until 2035

Type of measure: Strategic document

Description of how the measure contributes to national economic policy objectives: Energy policy is determined by the Strategy for Energy Development. The energy policy should secure reliable, safe and quality supply to consumers with all types of energy, establishment of transparent and stable terms and conditions for competitive and economically viable energy sector, promotion of market competition in energy services provision, based on the principles of non-discrimination and transparency, integration of the Republic of Macedonia's energy markets into the regional and international energy markets, promotion of energy efficiency and use of renewable energy sources ant other.

Current status of preparation/implementation: Government of the Republic of Macedonia adopted the Energy Development Strategy until 2030in 2010. In accordance with the Energy Law, Energy Development Strategy shall be adopted every five years and shall cover the period of next 20 years at least. The Energy Development Strategy shall stipulate: long-term objectives on particular energy activities development, for the purpose of securing reliability of supply of different energy types, identification and use of energy resources and facilities of strategic importance for the state, long-term forecasting of investment needs in generation, transmission and distribution facilities for the purpose of addressing energy demand and securing reliability of supply, financial means required to implement anticipated investments and manner of securing funds needed, incentives to invest in energy facilities that use renewable energy sources etc. In 2014, the preparation of Energy Development Strategy of the Republic of Macedonia until 2035 started with technical support from USAID and is prepared by the Macedonian Academy of Arts and Sciences as a local consultant. The adoption of this strategy is planned in 2015.

Timetable for implementation: The strategy covers the period until 2035. After one year from the adoption of the Energy Development Strategy the latest, the Government of the Republic of Macedonia on proposal from the Ministry of Economy, shall adopt the Implementation Program for the Strategy on Energy Development covering a period of five years. The program shall stipulate the measures, terms, manner and dynamics of Strategy implementation, as well as responsibilities of state authorities, LGUs and entities performing energy activities having the obligation on public service provision. The program shall determine the financial means required for its implementation, as well as the sources and manner of securing funds needed.

Contribution to SEE 2020 Strategy: The measure contributes to the pillar Sustainable growth, Dimension H. Energy from the Strategy for SEE 2020 and is in accordance with the Regional Energy Strategy of the Energy Community.

Potential implementation challenges and risks: Untimely implementation of measures and activities defined in this document.

Budgetary implications: For preparation of the Strategy technical assistance funding is provided by USAID.

Foreseen impact of the measure: In the future period measures and activities implemented in the energy sector are expeced to contribute to ensuring the security of supply of all types of fuel and energy consumers, and reduce the energy dependence of the country.

Measure: Construction of 400 kV Interconnection overhead line TS Stip-Macedonian Serbian border

Type of measure: Investment for construction of 400 kV Interconnection overhead which is the first interconnection between Macedonia and Serbia and is of significance for increasing the reliability of the electricity supply system of the Republic of Macedonia.

Description of how the measure contributes to national economic policy objectives: Benefits from the construction of the interconnection is reflected by revenues: reducing electricity losses

(~40,000 Euros/yearly), increasing cross-border transmission capacity (~1,300,000 Euros/yearly), an increase of transit between systems in the region (~ 450,000 Euros/yearly) and leveling of the difference in price of electricity in the region (~ 1,650,000 Euros/yearly).

Current status of preparation/implementation: The construction is ongoing

Timetable of implementation: Investor has final approval for construction, has completed delivery of conductors and OPGW, has completed test of towers, supervisor of construction is selected, the delivery of the towers is ongoing and the construction of 400 kV transmission bay in s/s 400/110 kV Shtip and the construction of 400 kV transmission line has started, which are expected to finish by the end of 2015.

Contribution to SEE 2020 Strategy: The measure contributes to the pillar Sustainable growth, Dimension H. Energy from Strategy for SEE 2020 and is in accordance with the Regional Energy Strategy of the Energy Community .

Potential implementation challenges and risks: Untimely implementation of activities because of the difficult weather conditions for construction. No additional risks for the project are foreseen (such as overcoming budget, endangering the environment, etc.) because the project is in its advance stage, all necessary documents and permits are completed, contractor is selected, purchase of land is regulated and construction has started.

Budgetary implications: 10 million euros loan from the World Bank and 5.15 million euros MEPSO's own funds.

Foreseen impact of the measure: The new interconnection has significance for increasing the reliability of the electricity supply system of the Republic of Macedonia, because it removes the risk of insecure regimes and partial collapse of systems in SEE that have already happened several times. Increased transmission capacity and market development is a prerequisite for regional dispatching leading to reduced production costs globally due to the availability of production facilities with different types of propulsion and low cost of production. New interconnection reduces the need for exchange of reactive power in the region. After start-up, transmission line will generate 100 Mvar to be injected into the network and will positively affect the voltage profile in the surrounding nodes.

Measure: Construction of 400 kV Interconnection overhead line TS Bitola 2- Macedonian Albanian border and 400/110 KV OHRID

Type of measure: Investment for construction of 400 kV Interconnection overhead line TS Bitola 2 - Macedonian Albanian border and 400/110 KV Ohrid, being the last part of the realization of Corridor 8 for electricity transmission between Bulgaria, Macedonia, Albania and Italy.

Description of how the measure contributes to national economic policy objectives: Direct benefits[29] for MEPSO from construction of this interconnection are reflected by revenues, reduced electricity losses (approximately 1.9 mil. euros/yearly), a decrease of undelivered electricity (approximately 1.5 mil. euros/yearly), increased production of electricity (average of 0.7 mil. euros/yearly), effective dispatching and balancing generators (average 0.4 mil. euros/yearly), increased transmission capacity and greater transit of electricity (approximately 0.07 mil. euros/yearly). Interconnectivity electricity connection between Macedonia and Albania brings significant benefits to overcome "bottlenecks" in the network that restrict access of generators to the regional market of EE. This reduces production cost, both in national systems and on regional level. Additionally, imported energy and overflow reservoirs are reduced in both systems (final effect is "liberation" of existing "green energy").

[29] Feasibility Study and ESIA for Elbasan (AL) - Bitola (MK) 400 kV Transmission Line, COWI – IPF Consortium, January 2013.

Current status of preparation/implementation: Preparation of final EIA by inserting comments from public debates and obtaining a decision on approval of the study by the Ministry of environment. Preparation of tender documents for selecting the best bidder who will prepare the overall technical documentation.

Timetable of implementation: Until now Feasibility study and Study for EIA are prepared, as well as the procedure for obtaining approval from the Ministry of environment regarding EIA. The procedure for showing interest in making the overall technical documentation is completed. In 2015 the most suitable designer who will develop the overall technical documentation will be selected. In the next period, negotiations with financial institution for approval of a loan are expected to begin, as well as expropriation of land and beginning of building. It is expected that by the end of 2019 the construction of transmission line and transformer station will be completed.

Contribution to SEE 2020 Strategy: The measure contributes to the pillar Sustainable growth, Dimension H. Energy from Strategy for SEE 2020.

Potential implementation challenges and risks: Beginning of construction will depend on timely preparation of the technical documentation, expropriation of land and obtaining construction permit, as well as on negotiations with the financial institution providing the loan.

Budgetary implications: Grant from WBIF in the amount of 800,000 euros is used for preparation of the feasibility study and EIA and grant from WBIF in the amount of 900,000 euros is approved for preparation of technical documentation. According to the Study, the total estimated value of building transmission lines and transformer station is 43.5 million euros, with proposal 37.3 million euros to be obtained with a loan, and 6.2 million euros to be provided by MEPSO's own funds.

Foreseen impact of the measure: In terms of the impact of the project on the national and regional transmission network, following effects can be expected: creating 400 kV contour Albania - Macedonia - Greece, increased transmission capacity of the network to support the forecasted load growth and transit of electricity and connection of new production capacity, improve reliability of the regional network, security of supply and stability of the transmission system, reduction of technical losses in electricity transmission system, improve the quality of power supply (normalizing the voltage profile, stabilize the flow of power and frequency fluctuations, etc.) support the development of a regional electricity market in SEE and creating opportunities for trade with Bulgaria and Italy, reducing the cost of providing spare capacity and the ability to support emergency situations.

Measure: Rehabilitation and modernization of the transmission network and power system

Type of measure: Investment for revitalization and modernization of the transmission network and power system consists of four components: revitalization of 110 kV transmission lines, new equipment for transformer stations, completely closing the optical ring transmission network and installation of the monitoring and management of substations.

Description of how the measure contributes to national economic policy objectives: This project will achieve: increased reliability of operation, reducing the level of depreciation of equipment installed in the 110's transmission fields kV substations, significantly reducing the number of outages of pylons and therefore reduce the configurable dry condition for consumers in Macedonia, raising the level of the continuous supply of electricity to consumers, reduce the cost of maintenance and management problems with the old lines, increasing the quality of electricity at the transmission system, increased security to workers and the environment.

Current status of preparation/implementation: The tender procedure for selecting the best consultant is completed, consultant is selected and signing of the contract will follow. Preparation of necessary technical documentation is underway.

Timetable of implementation: Projects from the four components should be e implemented by the end of 2017. In 2015 preparation of technical documentation will continue and the tender documents and publishing of the tenders will be realized.

Contribution to SEE 2020 Strategy: The measure contributes to the pillar Sustainable growth, Dimension H. Energy from Strategy for SEE 2020 and is in accordance with the Regional Energy Strategy of the Energy Community.

Potential implementation challenges and risks: Start of the implementation will depend on the timely preparation of the technical documentation, expropriation of land where necessary, and the reconstruction of existing interconnection over head line and replacement of equipment in existing TC will depend on the possibility of their exclusion from the transmission network to work under voltage.

Budgetary implications: 25 million euros loan from the EBRD and 15.5 million euros MEPSO's own funds.

Foreseen impact of the measure: The rehabilitation and modernization of the transmission network will achieve accuracy, reliability and secure operation of the transmission network, will facilitate the exchange of data between the National Dispatch Center and power facilities, transmission of data in business and financial operations, data transfer for remote keeping and management and providing video surveillance of all objects connected to the transmission network connectivity with neighboring telecommunication networks for data transmission with Serbia, Bulgaria, Greece and Albania through existing and new interconnection lines, meeting the requirements of ENTSO-E for providing digital electronic connection with at least two neighboring transmission system operators for data exchange of vital importance of keeping the system and stability of the region.

Flagship measure: INCREASING THE RENEWABLE ENERGY SOURCES UTILIZATION

Increased use of renewable energy sources (RES) is one of the priorities of the Government of the Republic of Macedonia in the energy sector. In 2010 the Strategy for use of RES in the Republic of Macedonia until 2020 was adopted. The Strategy defines objectives for RES use and the ways in which these goals are achieved. Under this strategy, the percentage share of renewable energy in final energy consumption by 2020 should be 21%.

Increasing the share of renewables in final energy consumption contributes to fulfillment of the obligations arising from the Treaty for Establishing Energy Community in terms of increasing the share of renewable energy in final energy consumption, monitoring EU policies in the field of renewable energy and implementation of measures defined in the state strategic documents.

Renewable energy sources in final energy consumption contributes to the pillar Sustainable growth, Dimension - Energy from Strategy for SEE 2020 and is in accordance with the Regional Energy Strategy of the Energy Community.

In order to stimulate construction of new power plants using renewable energy sources, these generation facilities can obtain the status of preferential generator, and thereby the right to sell electricity under feed-in tariffs. The electricity market operator shall be obliged to purchase the electricity generated by preferential electricity generators.

Measure: Construction of small hydro power plants (SHPP) based on granting water concession for produce electricity

Type of measure: Construction of SHPP.

Description of how the measure contributes to national economic policy objectives: Construction of SHPP in Macedonia positively affects local economic development through improvement of the local infrastructure, new access roads, transmission lines, substations. The production of electricity from SHPP will contribute to reduce the import of electricity for tariff consumers. The annual electricity production of 66 built SHPP is estimated at about 230 GWh and in relation to the current production of electricity from hydropower would mean increase of 15% of electricity produced by hydropower plants, while total electricity production in Macedonia would increase by about 4%.

Current status of preparation/implementation: So far 25 SHPP are already constructed with an investment of over 30 million euros, while the construction of 21 SHPP with an investment of more than 20 million euros is ongoing. The construction of another 20 SHPP is at the stage of providing documents for starting the construction. Based on the proceedings conducted by the Ministry of Environment and Physical Planning, the Government adopted 23 decisions on selecting the best bidder for the construction of 32 SHPP, to be built by the end of 2018.

Timetable of implementation: During 2015 and 2016 21 SHPP that are currently under construction are expected to be finished, while the remaining 20 SHPP are expected to be built by 2017.

Contribution to SEE 2020 Strategy: Exploitation of renewable energy sources is in line with pillar Sustainable growth, Dimension H. Energy.

Potential implementation challenges and risks: Untimely providing technical documentation and construction of SHPP under the terms specified in the concession agreement, lack of interest by private investors, risk in terms of the impact on the environment and etc.

Budgetary implications: No budgetary resources are foreseen for the construction od SHPP. Concessioners are obliged to pay a one-time fee for water concessions and concession fee to the state in the amount of 2% of the total income for generated and purchased electricity in each year of use. The electricity market operator shall be obliged to purchase the electricity generated by preferential electricity generators – SHPP based on feed-in tariffs for separate blocks, pursuant to the table below:

Block	*Quantity of electricity delivered per block (kWh)*	*Feed-in tariff for electricity delivered per block (€¢/kWh)*
I	*≤ 85.000*	*12,00*
II	*> 85.000 и ≤ 170.000*	*8,00*
III	*> 170.000 и ≤ 350.000*	*6,00*
IV	*> 350.000 и ≤ 700.000*	*5,00*
V	*> 700.000*	*4,50*

Foreseen impact of the measure: Construction of SHPP in Macedonia positively affects local economic development through improvement of local infrastructure, new access roads, transmission lines, substations. It creates new jobs in the construction sector, in the phase of construction both workers and highly qualified staff are engaged.

3.2. HUMAN CAPITAL

The quality of education is the foundation for economic growth and development, the biggest challenge in this regard is addressing the needs of the private sector by improving the quality of formal, non-formal and informal education and training.

Higher education. In order to provide quality higher education based on the convergence of students' knowledge to the requirements of the labor market, as well as equalization of the quality of higher education, the process of reforms will continue through implementation of international and European standards for evaluation and self-evaluation on the level of higher education institutions and on the level of study programs, accreditation of study programs in English language, development of study programs with involvement of practical and clinical lessons, involvement of distinguished experts managers from the real sector (middle and high management). In this direction the further implementation of the Bologna process will continue, especially in terms of the quality of higher education, the inter-disciplinary of the study programs, development of doctoral studies, exchange of students and teaching and research staff. In order to provide quality higher education, institutional strengthening of all stakeholders and reformulating higher education funding model will be in focus. In this regard, external evaluation in higher education will be introduced. The amendments to the Law on Higher Education dated January 2015, stipulated that the content of the first cycle of academic studies program (excluding national history, philology and art) should have at least 80% matching content and learning outcomes with a same or similar programme which is taught at a university listed among the top 50 its area on the list prepared by the Center for World-Class Universities at Shanghai Jiao Tong University, except for free elective subjects. Alignment of the curriculum should be completed as of the next academic year.

In terms of higher education, in the Republic of Macedonia, according to the data, the number of people admitted to the 5 state universities and 9 private universities in academic year 2013/14 is about 58.000 students, out of which 85% attend state universities. The rate of people leaving the higher education, according to data from 2010, was approximately 38,8% of the total number of students who have completed their studies on time. There is continuous growth of students' enrollment at universities in the field of technical and natural sciences and the field of IT.

In terms of sustainability of the realized project "Equipping laboratories for scientific research and applied activities", the Ministry of Education and Science together with the Institute for Accreditation of the Republic of Macedonia, according to the prepared analysis, identified 42 laboratories that are recommended for initiating the accreditation procedure. Seven laboratories have already completed the procedure for accreditation and another 35 laboratories have initiated activities for accreditation. The accreditation of laboratories should be completed in the first half of 2015. After the accreditation of the laboratories, their higher utilization is expected both by companies and students and universities, which will enable their self-sustainability.

The project for "Translation of 1000 professional, scientific books and textbooks taught at the best and most respected universities in the United States and England, and in the area of law in France and Germany", created a favorable climate that allow students, scholars and practitioners to acquire knowledge of certain areas that will help in their further development and training. The total number of translated, printed and promoted and books till now, is 907 titles. The remaining 93 titles of books should be printed by 2016. Those books are freely available for all students in the university libraries as well as in a separate facility "Reading-room 1.000 books," whose daily attendance is 300 visits.

Primary and secondary education. Under the support of equal access to all levels of education, the providing of: free textbooks, free transport, free accommodation of primary and secondary school students, scholarships for high school students, for students with disabilities, for social category students, gifted students and talented students – athletes, will continue.

The school subject "Business and Entrepreneurship" will continue to be taught in high schools. Starting from this year, the school subject "Innovation" is introduced in primary school (9th grade). The purpose of introducing this curricula is developing a propensity for innovation of students. From the academic year 2015/2016, "programming" will be introduced in primary education as part of the curriculum.

In the school year 2015/2016, the Ministry of Education and Science will continue with the implementation of Cambridge curricula in primary education. From the next school year, Cambridge curricula will be introduced in mathematics and natural sciences from 4th to 6th grade, in addition to Cambridge curricula in mathematics and natural sciences from 1st to 3rd grade introduced this academic year. Starting from the academic year 2016/2017 academic year, these programs will be introduced from 7th to 9th grade.

Vocational education and training. The reforms in vocational education and training are focused on increasing the economic efficiency of the system of vocational education and training through cooperation of vocational schools with employers and companies - introducing curricula according to the labor market needs and creating curricula that will meet the need for specialized skills of the workforce, including lifelong learning.

The improvement of the system of vocational education is done through harmonization of quality and relevance of vocational education with the labor market and establishing cooperation of schools with the industry.

The need to develop a model for later directing students toward professional specialization is supported by the existence of a consensus between the experts that early direction could hurt students and that diversification should start after acquiring basic skills. The need for development of this model is the fact that the early beginning of excessive specialization and diversification have created a base of high school graduates with a tight range of skills, and particularly worrying is the lack of basic skills (linguistic and mathematical literacy, knowledge of foreign language, skills for natural sciences and IT) needed for lifelong learning, which is mandatory in modern economies.

Of great importance is the procurement of equipment for practical training in schools, which will be implemented in parallel with the introduction of the reformed curriculum that will enable the student to acquire skills in accordance with the needs of the industry.

To establish cooperation between the schools and the industry, there are foreseen activities to identify successful models involving enterprises in practical training. There will be funded grants to support joint projects between vocational schools and enterprises in order to improve the practical training where the students will be directly acquainted with the challenges of the profession they have chosen.

Adult education. The implementation of the Strategy for adult education will continue through implementation of annual action plans.

Within the system for informal adult education the verification of bidders and programs for adult education will continue. So far 86 programs for adult education have been verified, and according to the Analysis of the labor market, certain verified programs will be part of the Operational plan for active measures and employment programs for 2015. It is expected that the growing trend of participation of verified bidders of programs for adult education within the realization of the Operational plan will continue. Starting from 2015, the larger companies in the Republic of Macedonia are expected to be engaged in the implementation of the plan, through providing training programs for people within their own profession, which will be approved and verified in educational centers.

Science and research. In the following period building up of the national capacities through workshops and trainings will continue, in direction of more successful participation in the new EU Program HORIZON 2020.

Flagship measure: REFORMING THE SECONDARY AND TERTIARY EDUCATION SYSTEM TO FIT THE NEEDS OF THE PRIVATE SECTOR

Measure: Improving the transparency of higher education in the Republic of Macedonia by providing quality higher education

Type of measure: Project.

Description of how the measure contributes to national economic policy objectives: This measure is a component of the "Skills Development and Innovation Support Project". It is aimed at transparency and efficiency of he quality ensuring system, as well as to the financial mechanisms in higher education.

Current status of preparation/implementation: The project started in March 2014, and the activities of this component are expected to be realized within the period 2015-2017. Within Component 1: Improving the transparency of higher education, the following sub-components are envisaged:

1. Quality assurance in higher education by administrative strengthening of the Board of accreditation and evaluation and other stakeholders in the field of quality management in higher education, support to external evaluation in the tertiary education and upgrade of the EMIS system.

In relation with this activity, analysis of the needs of the Board for Accreditation and Evaluation is planned in 2015, in terms of meeting the criteria for membership in ENKA. For this purpose an international consultant in the project to develop skills and support innovation is already hired.

2. Reforming the financing of higher education through the assessment and selection of the most appropriate funding model, designing a financial model, formula and plan for implementation, identifying indicators of performance and output framework for monitoring and evaluation and to begin the implementation of the new model.

In relation with this activity, hiring of an international consultant in the project to develop skills and support innovation is planned in 2015, as well as execution of the first task phase of the consultant, i.e. assessment of different financing models and analysing their strengths and weaknesses in Macedonian context.

3. Establishment of a National Office for Technology Transfer and its operational functioning, procurement of patents and creating a data base.

Defining the necessary steps for establishment of the National Office for Technology Transfer as a legal entity is planned in 2015, including a timeline, defining entities responsible for each stage of establishment, defining the National Office organizational structure design, hardware and software requrements, defining the operational procedures, processes and operational rules for the various products offered by the National Office for technology Transfer.

Contribution to SEE 2020 Strategy: It is connected to the goal - Connecting the education with the labor market needs -Dimension D.

Potential implementation challenges and risks: Delayed realization of the project activities.

Budgetary implications: Funds in the amount of 4.000.000 US dollars have been provided for implementation of the activities under this component, under a loan from the WB.

Measure: Modernization of secondary technical vocational education and training

Type of measure: IPA Project (OPDHR 2007-2013).

Description of how the measure contributes to national economic policy objectives: This measure is a component of the "Skills Development and Innovation Support Project" and resourses for each of the following activities are provided within the project.

The secondary vocational education system will be modernized through technical support for transformation from a narrow and specific occupations oriented system towards a system that will enable broader and general technical education that will enable students to quickly adapt to the needs of a dynamic labor market. In order to ensure good connectivity with future market needs, active involvement of the business community is planned in the process of developing the curriculum. In 2015, through the Skills Development and Innovation Support Project, hiring a consulting company is planned, which together with local public institutions and other stakeholders will work on secondary technical and vocational education reform.

Within this activity, the following documents and activities are planned in 2015 and 2016:

• Preparation of Methodology for development of occupational standards and providing technical assistance for development of occupational standards,

• Preparation of Methodology for development of standards of qualifications and providing technical assistance for development of standards of qualifications,

• Preparation of Methodology for development of educational profiles and plans and providing technical assistance for development of educational profiles and plans,

• Preparation of Methodology for development of new curricula and relevant modules and providing technical assistance for development of new curricula and relevant modules,

• Preparation of questionnaires, collecting and analyzing data and preparing a report on rationalisation of the vocational schools network,

• Organizing training focused on the new system and new curricula,

• Preparation of detailed technical specifications for each vocational school regarding the needs of equipment for practical training in the context of the needs of the new curriculum.

Grants will be also provided for cooperation between schools and industry. For the implementation of all planned activities under this component USD 4.4 million are provided.
This component will be implemented through the following sub-components:
1. Providing quality and labor market relevance of secondary technical education through development of a comprehensive transformation model, developing occupational standards, curricula based on competencies, assessment of vocational schools network performance, as well solution for its improvement, developing a training program for teachers based on identified skills needs, preparation of training materials and implementation of the training program, analysis for needed equipment and purchase of equipment for implementation of practical training in schools.

Current status of preparation/implementation: The project started in March 2014 and the activities of this component are expected to be realized within the period 2015-2017.

Contribution to SEE 2020 Strategy: Linked to the goal - Connecting education with the labor market needs –Dimension D.

Potential implementation challenges and risks: Delayed realization of the project activities.

Budgetary implications: Funds have been provided in the amount of 4.500.000 US dollars for implementation of the activities under this component, under a loan from WB.

Foreseen impact of the measure: The modernization of secondary technical vocational education contributes to increased competitiveness of the labor force in the labor market.

Measure: Promoting lifelong learning through modernizing the vocational education and training and adult education systems

Type of measure: Project

Description of how the measure contributes to national economic policy objectives: The objective of the project is further support of human resources development by strengthening the lifelong learning system and modernisation of Vocational Education and Training (VET) and Adult Education (AE):

- Further strengthening of the VET Center in close cooperation with the private sector and social partners in line with the relevant strategies,

- Further strengthening of the VET system in cooperation with the private sector and social partners in accordance with the relevant strategies through preparation of a new occupational standards, standards for qualifications and curricula, implementation of practical training system, strengthening career centers and career counseling in secondary schools, and promoting attractiveness of VET,

Further strengthening of AE system by building capacities of LGU to analyze the labor market and providing information pursuant to Adult education law, development and testing programs for adults in cooperation with the private sector and social partners, support for concepts for formation of public institutions for adult education at local level, preparation of a new AE strategic document, and promoting the attractiveness of AE programs,

- Strengthening the overall capacity of the national lifelong learning system, with special attention to VET and AE by building the capacity of relevant institutions and

- Preparation of technical specifications for procurement of systems for monitoring and evaluation of VET and AE and purchasing teaching equipment for vocational training.

Current status of preparation/implementation: The start of the project is envisaged for May 2015, and its implementation is foreseen in the period May 2015 – May 2017.

Contribution to SEE 2020 Strategy: Link to the goal - Connecting education with the labour market needs –Dimension D.

Potential implementation challenges and risks: Inadequate technical specification that may affect the timely execution of the procurement.

Budgetary implications: The total cost of this project is 2,300,000 euros, out of which 85% will be covered from IPA funds and 15 % from national co-financing.

Foreseen impact of the measure: The modernization of vocational education and training and adult education contributes toward alignment of the labour market needs and labour force skills, which leads to further increase of the competitiveness of the labour force in the labour market.

Flagship measure: STRENGTHENING THE LINKAGES BETWEEN BUSINESS AND ACADEMIA

Measure: Provision of financial instruments aimed at improving innovation capacity of enterprises and cooperation with research organisations

Type of measure: Project

Description of how the measure contributes to national economic policy objectives: Within this measure, steps will be taken to build institutional capacity for stimulation of innovation activities and financial instruments will be introduced to support innovation and technological development within enterprises. The first public call for awarding grants from the Fund is scheduled in February 2015, and will apply to co-financed grants for spin-off and start-up companies.

Current status of preparation/implementation: The project started in March 2014, and the activities of this component are expected to be realized within the period 2015-2017.

Contribution to SEE 2020 Strategy: Link to the goal - Connecting education with the labor market needs –Dimension D.

Potential implementation challenges and risks: Delayed realization of the project activities.

Budgetary implications: Funds for the first payments are provided by the Rural Development Programme and World Bank loan.

The planned amount of funds for payment in 2015, divided by instrument is as follows:

• Co-financed grants for start-ups, spin-offs and innovation – 345,000 euros,
• Co-financed grants and contingent loans for innovations commercialisation - 75,000 euros,
• Co-financed grants for technology transfer - 50.000 euros.

Total - 470,000 euros.

Foreseen impact of the measure: Increasing the enterprises' capacities for research and innovation.

3.3. Better industrial structure

Flagship measure: SUPPORT OF COMPETITIVENESS AND SME DEVELOPMENT

To encourage competitiveness as a basis for sustainable economic growth, a number of documents were adopted: Industrial policy - as an integrated and proactive document to encourage the competitiveness of the Macedonian economy (where five areas of intervention were identified - research, development and innovation; internationalization and encouraging FDI; development of SMEs and entrepreneurship; development of cluster association and eco products and services for sustainable development), Strategy for export promotion; Innovation strategy, Strategy for development of crafts 2011-2020, Strategy for development of tourism and other.
The documents are following the recommendations and related communications from the Strategy EU 2020, Strategy SEE 2020, EU Small Business Act and other relevant regional initiatives.

Strategic documents and policies are implemented through: a) annual budget programs that are implemented by ministries and agencies b) action plans - such as the action plan for innovation, action plan for improving competitiveness of the Republic of Macedonia according to the Global Competitiveness Index, the action plan for improving the results of the Republic of Macedonia according to the Global innovation Index, etc. c) projects - such as "Top management" for training of management, "Foreign experts for the domestic companies" with purpose to transfer knowledge and strengthen skills in companies, "Learning from the business community," as a form of direct dialogue with companies and the like.

For greater transparency, better information and more effective promotion of the programs and measures all programs and projects of the Government, donors and European programs that provide support to companies in their growth and development are presented on the portal www.konkurentnost.mk, which is continuously updated. Monthly visit of this website is about 8,000 visits.

With reference to the export promotion, the web portal of ASIPIRM is continuously upgraded in terms of functionality and availability of information relevant for exporters.

In terms of improved information of the private sector, the opportunities offered by EICM advisory assistance will be also used, with reference to the opportunities to establish business cooperation and information related to the legal and business framework of the EU and EU programs.

One of the determinants for the competitiveness of the country is the access to finance. Facilitating access to finance contributes to support business creation and for existing companies it contributes to support growth and development, export and innovation.

In order to improve access to finance for enterprises the support through MBDP will continue in 2015 for access to the credit line financed by the EIB with lower interest rate, and activities aimed at promoting the concept of financing enterprises through business angels will be undertaken.

As an additional opportunity to support projects from the private sector are also European projects where Macedonia participates: COSME, Horizon 2020. Also, Macedonia participates in the regional project Platform for enterprise development and innovation facility for the Western Balkans - EDIF, supported by the EC, EBRD and the European Investment Fund.

Development of industry and improving access to finance will be encouraged in order to create products with higher added value, i.e. the creation of a competitive domestic industry, prepared for participation in the global market, based on knowledge, innovation and cooperation between the actors of industrial development.

All activities are correlated with the recommendations of the Report of the Commission on the Progress of Macedonia - Chapter 20, Enterprise and industrial policy, the National Action Plan for the implementation of the Strategy SEE 2020 areas: Sustainable, Integrated and Smart Growth, the Conclusions of the Ministerial Dialogue between ministers of finance and economy of the EU and candidate countries of 24.04.2014.

Measure: Implementation of annual programmes for SMEs and clusters support

Type of measure: Program

Description of how the measure contributes to national economic policy objectives: Aimed to further realization of activities for improvement of competitiveness and growth of enterprises, the Ministry of Economy and APPRM will continue to implement annual programs for support of competitiveness, innovation and entrepreneurship by co-financing activities for development of companies such as the following measures given in the programmes:

- Support of infrastructure for SME (support of projects of business centers and craft chambers)
- Support of implementation of quality standards: ISO, HACCP, HALLAL
- Support of women entrepreneurship
- Craft promotion
- Increase of productivity and production diversification through development of new or improvement of existing product
- Market development
- Support of patents
- Various specialized trainings to strengthen the skills of management and of employees related to technology development, innovations and export
- Trainings for business plan preparation and entrepreneurship trainings for teachers, professors and students
- Implementation of consultancy voucher schemes
- Preparation of annual report-Observatory for SMEs,
- Support of organization of promotional events for SMEs
- Measures for support of clusters and cluster associations.

Current status of preparation/implementation: Planned budget Program for 2105

Timeframe for implementation: It is realized through posting public calls in 2015

Contribution to SEE 2020 Strategy: Contributes for realization of measures under the pillar Sustainable growth, dimension K. Competitiveness, as well as for the pillars: Integrated growth and Smart growth.

Potential implementation challenges and risks: Potential risk for insufficient planned funds due to the great interest from companies for the proposed measures.

Budgetary implications: 15.9 million denars from the Budget of the Republic of Macedonia. It is the total value of only two programs funded by the budget:

- Competitiveness, Innovation and Entrepreneurship Programme 2015, implemented by Ministry of Economy, in the amount of Denar 12.07 million;

- Entrepreneurship, innovation and competitiveness of SMEs support programme 2015, implemented by APPRME, in the amount of Denar 3.9 million.

Foreseen impact of the measure: Strengthening the capacity and competitiveness of companies, increased export, increased employment in SMEs, increased number of SMEs.

Measure: Stimulation and support of innovation activities among SMEs

Type of measure: Program

Description of how the measure contributes to national economic policy objectives: This measure refers to encouraging and supporting innovation activities in micro, small and medium sized enterprises and start-ups and to encourage rapid technological development. The aim is to improve the capacity of companies through the transfer of knowledge and technology, research development and innovation.

To achieve this objective, the Fund for Innovation and Technology Development has developed four instruments (grant schemes) to finance projects:

1. Co-financing grants for start-up, spin-off companies and innovations
2. Co-financing grants and conditional loans for commercialization of innovations
3. Co-financing grants for technology transfer
4. Technical assistance through business-technology accelerators.

Strengthening the capacity of companies through transfer of knowledge and technology, research development and innovation will contribute to increasing the competitiveness of companies, leading to improved economic climate, economic growth and development. In addition, it will contribute to the promotion and support of innovation activities in the country.

By allocating funds for the above stated objectives the following economic performances of the Republic of Macedonia would improve:

- Increased public investment in activities related to innovation and technology transfer;
- Increased share of private funding in activities related to research and development, innovation and technology transfer;
- Increase and promotion of innovation activities in the private sector;
- Incited cooperation between the private sector and universities/research institutions;
- Promotion of entrepreneurial culture;
- Increase in the number of innovative businesses that create sustainable and high quality jobs;
- Improved competitiveness of SMEs;
- Improved economic climate for sustainable development.

Current status of preparation/implementation: In order to successfully implement this measure, the following activities were organized in 2014:

- Establishing a Fund for innovation and technology development (development and adoption of the founding legal acts, physical equipping and staffing);
- Development and adoption of program documents for implementation and monitoring of FITD's instruments;
- Promotional activities with Economic Chamber of Macedonia and the MBDP in 5 cities with 126 people present.

At the moment, the preparation for the first public call for the instrument of the Fund - Co-financing grants for start ups, spin off companies and innovation is in progress.

Timeframe for implementation: It is foreseen that instruments will be piloted during 2015. According to the implementation schedule, it is planned to publish at least one public call per instrument per year till 2017.

Contribution to SEE 2020 Strategy: Contributes to the implementation of measures in the pillar Sustainable growth, Dimension K. Competitiveness, and pillars Integrated Growth and Smart Growth Dimension E. R & D and innovation.

Potential implementation challenges and risks: There are two types of potential challenges to successful implementation of this measure:

Internal risks include:

- Insufficient institutional/human resources of FITD for implementation and monitoring of the instruments (in terms of the complexity and size of the task);
- Potential weaknesses in procedures developed for implementation and monitoring of the instruments;
- Inadequate budget planning (in terms of providing the necessary/programmed funds for grants and conditional loans based on the planned dynamics).

External risks include:

- Lack of interest among potential applicants for the instruments of the Fund;
- Lack of business readiness (and knowledge) among potential applicants for project development (business plans);
- Insufficient potential among users for successful implementation of projects under the agreed objectives, budget and schedule.

Budgetary implications: 9.159.750 euros are provided from World bank loan for realisation of activities in the period 2015-2019. In 2015: 10.375.000 denars (from WB loan), 514.000 denars from FITD budget and 18.005.000 denars from IPARD after signing a memorandum between FITD and AFSARD.

Description of the projected impact of the measure: Considering that the Republic of Macedonia is a developing country, the strategic impact of this measure would contribute to economic convergence of the country by supporting projects that basically lead to the establishment of new businesses, creation of new jobs (especially for young qualified people), fostering sustainable growth of businesses, connecting research with entrepreneurship and consequently the development of products and services that would be competitive on the global market. In addition, through its operations, the Fund will contribute to the creation of an effective system of innovation, sustainable regulatory environment to support innovation, strengthening the propensity of businesses to enter innovation and increase in the flow of knowledge between actors in innovation.

Measure: Financial support to SMEs through the MBDP instruments

Type of measure: Credit line from EIB – fourth phase in the amount of 100 million euros.

Description of how the measure contributes to national economic policy objectives: Access of SMEs to quality credit line with fixed annual interest rate of 5.5% for investment support in fixed assets and working capital, priority projects, decrease of unemployment, increase in exports and liquidity improvement.

Current status of preparation/implementation: In terms of access to finance, the Finance Contracts between EIB and MBDP intended for credit support to SMEs and priority projects were, so far, successfully and fully realized, that is: first phase in the amount of 100 million euros, second phase in the amount of 50 million euros and third phase in the amount of 100 million euros. Funds have been disbursed to final beneficiaries through commercial banks, that is, for SME up to 3.5 million euros and repayment period of up to 8 years per credit beneficiary. Up till now, 282 million euros were withdrawn from the EIB credit line to finance 1,378 projects, thus creating 5,868 new jobs. The MBDP's planned activities for further improvement of the access to finance in 2015 are the following:

- to realize the credit line from EIB – fourth phase,
- to intensify the promotion of EIB credit lines and the other Bank projects.

Timeframe for implementation: Activities have been carried out continuously for withdrawal of new funds/tranches or for improvement of credit line conditions and for other products.

Contribution to SEE 2020 Strategy: It contributes to realization of measures in the pillar Sustainable Growth, Dimension K, Competitiveness.

Potential implementation challenges and risks: High liquidity of commercial banks may reduce the interest for using funds from EIB credit line and the future movement of the portfolio at risk rate, as well as quality of projects and banks' assessment of the credit ability-to-pay of companies.

Budgetary implications: The Budget of the Republic of Macedonia provides between 200-350 thousand euros on annual basis to subsidize the interest rate of the EIB credit line depending on the movement of EURIBOR.

Foreseen impact of the measure: Easier access to finance for SMEs, attractive interest rate, favourable credit conditions to improve competitiveness, increase in exports, development of underdeveloped areas and creation of new jobs. It is expected that EIB IV credit line will support around 480 projects and around 2080 new jobs.

3.4. Good business environment

In the next medium-term period the implementation of activities will continue, aimed at improvement of business climate, enhancement of competitiveness of Macedonian economy and establishment of equal conditions for operations of the economic entities. Best experience of many European countries and recommendations of international institutions are incorporated in these measures and activities. Implementation of these projects is expected to directly contribute to increase of economic growth, increase competitiveness and reduce unemployment.

Flagship measure: FURTHER REDUCTION OF REGULATORY AND ADMINISTRATIVE BURDEN ON BUSINESSES

Measure: Implementation of measures for improvement of the business environment

Type of measure: Programme

Description of how the measure contributes to national economic policy objectives: The implementation of the proposed measures and activities will contribute to further facilitate the conditions for doing business in the country, both for domestic and foreign companies.

Starting a business

- Expanding the category of Registration Agents by including lawyers in the category and implementing measures for continuous training and support of registration agents.

Dealinig with construction permits

- Facilitating the procedure for obtaining an urban plan extract in digital form via the electronic system for building permits and detailed specification of legal provisions that hydrotechnical conditions are not requested in the procedure for issuance of a building permit.

Registering property

- Digitalization of cadastral maps - specific program

The project Digitalization of cadastral maps supports the process of their conversion from paper form into vector form. After completing the harmonization of the graphic data from the cadastral maps with the attribute data, they are stored in a central database (e-Kat base). According to the Action Plan for digitalization of cadastral maps, 1497 cadastral municipalities have been imported in MAK-EDIT i.e. coverage of 80% of the territory, while the centralized database has 1117 cadastral municipalities in production i.e. coverage of 67% of the territory.

The implementation process is planned to be completed by the end of 2015. This activity is funded by the WB through the Real Estate Cadastre and Registration Project - Additional Financing and with Budget funds.

- Development of the distribution system-specific program

In order to further develop the AREC GIS portal, AREC initiated activities to develop a distribution system which will represent a single point of access to the digital geospatial data under the authority of AREC.

The digital cadastral maps and the creation of a platform for internet based geographic information system (WEB GIS) for exchange and distribution of data will provide complete coverage of the entire territory of the Republic of Macedonia with basic sets of digital spatial data and on-line availability.

The implementation process will last until the end of 2015. This activity is funded with World Bank resources through the Real Estate Cadastre and Registration Project - Additional Financing. Budget: 380,000 euros.

- National NSDI Geo-Portal - specific program

AREC is currently working on the development of software for the national NSDI Geo-Portal. In the first phase, the National Geo-portal will make available data sets from AREC, the City of Skopje, the Ministry of Environment and Spatial Planning, the Centre for Crisis Management and the State Statistical Office.

Implementation of the software solution for the national NSDI Geo-Portal of the Republic of Macedonia will be carried out during 2015. This activity is funded with World Bank resources through the Real Estate Cadastre and Registration Project - Additional Financing. Budget: 66,800 euros

- Registry of prices and leases - specific program

AREC, in accordance with the amendments to the Law on Real Estate Cadastre, has been given the authority to establish a registry of prices and has prescribed the manner in which the property prices will be registered. Namely, they will be recorded using the legal basis for transfer of the real property, which are submitted in the real estate cadastre during applying for registration, or applying for changes in the REC. The Registry will also record the value of the real property on the basis of which the property sales tax has been calculated, as well as other real property data contained in the statement provided by the seller, verified by a notary.

Through the published quarterly, semi-annual and annual reports made available online, AREC will enable citizens to have access to the data for all real property sales and leases.

During 2015, AREC will start recording the value of real properties in the GCIS- Registry of prices. This activity is financed from the budget of the Republic of Macedonia. For upgrading the e-Kat system with the objective to feed the data in the Registry of prices, the budgeted amount is 30,000 euros.

Paying taxes

- Using virtual POS terminal for electronic payment of taxes and payment of taxes and fees through electronic banking.

Resolving insolvency

- Electronic selection of a trustee – fair and equitable selection of trustees.

Current status of preparation/implementation: Measures are based of inter-ministerial coordination of several institutions in charge and are adopted by the Government of the Republic of Macedonia.

Timetable of implementation: Most of the activities are planned to be implemented in 2015, while longer-term measures will be implemented in 2016 and 2017.

Contribution to SEE 2020 Strategy: Contributes to realization of measures from the pillar Sustainable growth, Dimension K. Competitiveness.

Potential implementation challenges and risks: Commitment to the implementation of measures by the institutions in charge.

Budgetary implications: Additional funds from the budget are not necessary for implementation of the activities, the measures do not require additional financial resources and they are already provided within the budgets of the institutions in charge.

Foreseen impact of the measure: Implementation of the measures will improve the business climate in the country.

Measure: One stop shop system for foreign and domestic investors

Type of measure: Project

Description of how the measure contributes to national economic policy objectives: In the next mid term period forming and establishing of One stop shop system for foreign and domestic investors is envisaged. The system will enable all licenses and permits for starting and running a business to be issued from one place. The main benefits of the system are decreasing of the time needed and costs for issuing business licenses and permits, which is a recommendation in the last EC Progress report for Macedonia. This system will be established as “umbrella” system which will integrate all related one stop shop systems in the country

Current status of preparation/implementation: The establishment of the electronic system and using of the electronic access in issuing business licenses and permits will be carried out in phases. This system will be implemented first in the institutions which issue the largest number of business licenses and permits and have the greatest coverage over the business community.

Timetable of implementation: In 2015 Project for technical assistance for developing of software and preparation of technical specification for hardware for establishing of the System will be implemented. In 2016 and 2017, supply of the needed hardware, testing and operationalizing of the hardware is envisaged.

Contribution to SEE 2020 Strategy: Contribution in implementation of the measures in the Sustainable Growth pillar, Dimension K. Competitiveness.

Potential implementation challenges and risks: Delays in tendering procedures, aversion to using the electronic system by the users, poor cooperation with institutions which issue licenses and permits.

Budgetary implications: The funds for the design of software, technical specification and procurement of software (about 1.1 million euros) are allocated under IPA Component 1-TAIB, Sector fiche for Private sector development.

Foreseen impact of the measure: This system will enable all licenses and permits necessary for starting and running a business to be issued at one place which will decrease the time and costs for the business in the country.

Measure: Development and implementation of Master plan for improvement of the competitiveness

Type of measure: Programme

Description of how the measure contributes to national economic policy objectives: Set of measures for encouraging and enhancing the competitiveness of the Macedonian economy will be created through dialogue with the business sector and in cooperation with NECC. The measures are aimed at improving the business environment, which will result in improving the competitiveness of the Macedonian companies and the economy in general.

Current status of preparation/implementation: The preparation of the Master Plan in cooperation with the business community through NECC is on going.

Timetable of implementation: 2015 - adoption of the Master Plan, establishing working groups for implementation of measures, implementation of first measures. In 2016-2017 implementation of measures from the Master Plan continues.

Contribution to SEE 2020 Strategy: Contributing to the implementation of measures for Sustainable growth pillar, Dimension K. Competitiveness, and Integrated Growth and Smart Growth Pillars, Dimension E. R & D and innovation.

Potential implementation challenges and risks: Commitment to implementation of the measures by the responsible institutions, timely implementation of tendering procedures, awareness of the business community on the measures which need to be implemented by the business sector.

Budgetary implications: Projects financed under IPA Component 1-TAIB, Sector fiche for Private sector development will be implemented so as to realize measures from the Action plan for competitiveness.

Foreseen impact of the measure: Increasing the competitiveness of the Macedonian economy based on innovation, increased exports, developing a functioning market economy, reducing unemployment and increased GDP growth.

Flagship measure: IMPROVING THE SUPPLY CHAIN LINKAGES BETWEEN FOREIGN INVESTORSAND LOCAL COMPANIES

Measure: Preparatory activities for Macedonia Automotive Backward Linkages - MABL Program – MABL Program

Type of measure: Programme

Description of how the measure contributes to national economic policy objectives: The focus of the program will be implementation of activities for inclusion of domestic companies in the supply chain of foreign companies, with an overall aim to increase employment and introduction of new technologies. This program will be implemented by a team from the WB and IFC in coordination with the Multi-institutional Working Group responsible for the inclusion of domestic companies as suppliers of foreign companies that invest and produce in the Republic of Macedonia. Main activities of the program are: 1/ Increased availability of information about opportunities for linkages between domestic and foreign companies, 2/ Improved supply chain enabling regulatory environment, 3/ Strengthened linkages between local suppliers and foreign investors through technical assistance for upgrading existing and potential local suppliers' capacities and 4/ Enhanced access to finance.

As part of the MABL program, preparatory activities are foreseen, which are elaborated in detail in the Supplier Development Pilot Program, comprising four components:

- Supplier information collection and dissemination
- Capacity building and training of the Multi-institutional Working Group and other relevant institutions
- Provision of expertise for companies – potential suppliers
- Assistance accessing financing sources.

Current status of preparation/implementation: Draft pilot programme for preparatory activities for the MABL programme is prepared.

Timetable of implementation: The Pilot proggrame will be implemented in the first half of 2015.

Contribution to SEE 2020 Strategy: Contributes towards realisation of measures from the pillar Sustainable growth, Dimension K. Competitiveness.

Potential implementation challenges and risks: Short time period, securing funds for full implementation of activities after the preparatory stage, untimely engagement of experts, lack of interest from companies.

Budgetary implications: Activities will be implemented under the WB's MCIISP grant - Macedonia Competitive Industries and Innovation Support Program amounting to 300,000 dollars.

Foreseen impact of the measure: Strengthening the capacity of domestic companies so as to be easily included in the supply chain of foreign investors and strengthen the capacity of institutions in the country involved in the implementation of this program.

3.5. TRADE INTEGRATION

Republic of Macedonia outlines key objectives for trade integration in a way that covers the key dimensions in the "Integrated growth" pillar, so that link between CEFTA and SEE 2020 priorities is established, given that they are connected with each other. An important benefit is to ensure consistency and cohesion in interactive enhancement of CEFTA Agreement / PEM Convention and Strategy in practice by all SEE 2020stakeholders. This approach will enable the facilitation of trade in all CEFTA structures, applying the methodology for systemic measuring of integration in the global economy and the creation of multi-dimensional synergy between trade policies of CEFTA Parties.

Flagship measure: ENCOURAGING THE REGIONAL TRADE OF GOODS AND SERVICES

Measure: Establishing free trade area within CEFTA

Type of measure: Administrative measure

Description of how the measure contributes to national economic policy objectives: Based on the obligation according to Article 27 of the CEFTA Agreement, CEFTA parties shall gradually approach towards achieving progressive liberalization in trade of services and mutual opening of services market, in context of European integration, bearing the provisions of the GATS within WTO.

The opening of the services market should be on a higher level than the liberalization the countries' committed within their membership or potential membership in WTO, as well strengthening of intra-regional trade with services.

Current status of preparation/implementation: In 2014, two rounds of negotiations were held. Further progress in the process of negotiations shall continue in the next period and should result by concluding a Regional Protocol of trade in services by the end of 2016.

Timetable of implementation: During 2015 и 2016 six rounds of negotiations will follow concerning the level of liberalization of sectors and sub-sectors of services (business and professional services, tourism services, environmental services, communication and construction services, distribution, education and health services, financial, transport and audio-visual services). The implementation will follow after completing the ratification of the Protocol by CEFTA Parties during 2017.

Contribution to SEE 2020 Strategy: Contributes to the Pillar "Integrated Growth" where new development model is created in Dimension A "Free trade area". The Dimension is directed towards facilitating trade and liberalizing trade in services, in order to reduce any restriction in exporting of services that currently exists in the region.

Potential implementation challenges and risks: Untimely ratification process by CEFTA Parties of the concluded Protocol of trade in services.

Budgetary implications: Experts' working meetings during negotiations will be financed from IPA2 2015-2017. The total IPA contribution is 3.412.500 euros, out of which 10% is allocated for this measure.

Foreseen impact of the measure: Increase the scope of trade in services among CEFTA Parties and equal opening of the CEFTA markets is expected in the next period.

Measure: Application of the Regional Convention on Pan-Euro Mediterranean rules of origin

Type of measure: Administrative measure

Description of how the measure contributes to national economic policy objectives: For further integration in the global economy Republic of Macedonia approached towards harmonization of the Protocols for rules of origins for application of diagonal cumulation according to the Free Trade Agreements of the Republic of Macedonia with EU, EFTA, CEFTA and Turkey, in line with the rules of the Regional Convention. The goal is to apply unified rules of origin.

Current status of preparation/implementation: Republic of Macedonia ratified the Protocol for rules of origin according to the CEFTA Agreement on August 27th 2014. Thus four countries out of seven (Republic of Macedonia, Albania, Serbia and Montenegro) are applying the Convention's Protocol of origin in its mutual trading starting from September 12th 2014.

European Commission prepared Decision for amendment of Protocol 4 for rules of origin within the Stabilization and Association Agreement, published in Official Journal of EU L304/91 on October 23rd 2014. The Decision is the basic document for mutual harmonisation of the text, which should than be adopted by the Macedonia-EC Council for Stabilization and Association in mid 2015.

Republic of Macedonia has already initiated modification of the Protocols for rules of origin with EFTA States and Turkey, and mutual consent is expected to be reached by the end of 2015.

Timetable of implementation: Harmonisation of Protocols for rules of origin with EU, Turkey and EFTA States is expected to finish during 2015 and their ratification to be done in 2016.

Contribution to SEE 2020 Strategy: In the Pillar "Integrated Growth" new development model in Dimension C "integration into global economy" is created. The Dimension is directly aimed at creating preferential access, not only to the existing export destinations but also to other markets in the so called PEM Region. Application of the Convention in full is an opportunity to participate in the global supply chain.

Potential implementation challenges and risks: untimely harmonization of Protocols for rules of origins according arising from the Free Trade Agreements with the Protocol of the Regional Convention.

Budgetary implications: There are no financial implication since this is a legal document that needs to be ratified.

Foreseen impact of the measure: Diagonal cumulation is expected to be equally applied in the PEM Region according to unified rules of origin. 47 countries are signatories of the Regional Convention, out of which Republic of Macedonia together with 40 countries applies Free Trade Agreements (3 multilateral agreements and 1 bilateral). Application of diagonal cumulation among 40 countries creates greater opportunities to utilize the preferential treatment in trade of goods.

Measure: Facilitation and acceleration of the transit procedure through implementation of the New Computerised Transit System in the Customs Administration of the Republic of Macedonia

Type of measure: Administrative measure

Description of how the measure contributes to national economic policy objectives:

- Establishing interconnection between the customs transit system of the Republic of Macedonia and the EU transit systems and provide its maintenance,
- The present activities of alignment of the customs legislation with the Acquis will be continued in the period 2015 - 2017, particularly in area of further operationalisation of the common procedures, focused on the implementation of the Convention on a Common Transit Procedure and the Convention on the simplification of formalities in trade in goods,
- Ratification of the Convention on a Common Transit Procedure and the Convention for simplification of formalities in trade in goods,
-The accession to the EU system is expected to be realised in the middle of 2015,
-The implementation activities will be continued in the period 2015 -2016 through realisation of the Twinning Project "Finalization of the preparation for the accession to the Convention on a common transit procedure (CTC) and to the Convention on the simplification of formalities in trade in goods" funded under the EU Instrument for Pre-Accession Assistance (IPA TAIB 2010).

Current status of preparation/implementation:

- The New Computerised Transit System, which implementation is a pre-condition for accession to the Convention on a Common Transit Procedure, was put in function at national level on March 1st 2014,
- Pre-monitoring Mission for assessment of the progress made in implementation of the system was held in June 2014 and recommendations regarding the future activities were given,
- Connection with the DG TAXUD was established in November 2014, through the Common Communication Network/Common System Interface (CCN/CSI),

- Two exceptionally important meetings of the EU-EFTA Working Group on "Common Transit" and the EU-EFTA Joint Committee on "Common Transit" were held in December 2014 in Brussels, at which the decisions to invite the Republic of Macedonia to accede to the Common Transit System were adopted,
-Monitoring Mission for assessment of the preparedness for accession to the Convention on a Common Transit procedure will take place in January 2015, after which an invitation for full membership will be expected.

Timeframe for implementation: Determination of the need for preparation of guidelines and instructions for operational application of the provisions of the conventions concerning the common transit and preparation of proposals – planned activity covered by the matrix of activities for reinforcement of the administrative capacities (activity C4/A1 with defined deadline for realisation 30.06.2015).

- Preparation of proposals for adoption of Amendments to the Customs Law and Customs Law Implementing Regulation - planned activity covered by the matrix of activities for reinforcement of the administrative capacities (activity C4/A2 with defined deadline for realisation 30.09.2015).
- Analysis of the need for passing guidelines and instructions concerning the operational application of the Amended Customs Law and preparation of proposals - planned activity covered by the matrix of activities for reinforcement of the administrative capacities (activity C4/A3 with defined deadline for realisation 30.09.2015).
- Analysis of the need for introducing procedures in accordance with the Amended Customs Law - planned activity covered by the matrix of activities for reinforcement of the administrative capacities (activity C4/A4 with defined deadline for realisation 31.10.2015).
- Establishment of corresponding organizational structure and system and sub-systems for management and control of customs procedures, in conformity with the Amended Customs Law - planned activity covered by the matrix of activities for reinforcement of the administrative capacities (activity C4/A5 with defined deadline for realisation 31.10.2015).
- Realisation of specialised trainings concerning the application of the amended customs legislation, intended for the customs officers and economic operators - planned activity covered by the matrix of activities for reinforcement of the administrative capacities (activity C4/A6 with defined deadline for realisation 30.11.2015).
- Law on Ratification of the Convention on a Common Transit Procedure – planned activity covered by the legislation matrix (activity C1/A12 with defined deadline for realisation 31.12.2015).
- Operational preparation of the NCTS for accession to the Convention – testing (in cooperation with the DG TAXUD and the Customs Service of Slovenia (IPA 2010)) – planned activity covered by the matrix of activities for reinforcement of the administrative capacities (activity C1/A1 with defined deadline for realisation 30.09.2015).
- Implementation and maintenance of the CCN/CSI (Common Communication Network/Common System Interface) - planned activity covered by the matrix of activities for reinforcement of the administrative capacities (activity C10/A1 with defined deadline for realisation 31.12.2020).

Effects that this measure has on the objectives defined by the Strategy SEE 2020: The implementation of these measures will provide more competitive business climate and integration into the global economy through introduction of processes in the customs working that meet the international standards.

Potential implementation challenges and risks: The maintenance of the system shall be assured and further training for the employees shall be provided.

Budgetary implications: Previous activities covered by the IPA 2008 (in a total amount of about 3 mil. euros) and future activities covered by the IPA 2010 (in a total amount of 0,947 mil. euros).

Foreseen impact of the measure: The system via which the transit documents are submitted only in electronic form, provides for further acceleration and facilitation of the customs procedures; the connection with the EU systems planned for the next year will enable to avoid the border customs formalities, in paper form, when exchanging goods with the EU Member States and additional benefit for the economic operators.

Measure: Reinforcement of the operational capacities of the Customs Administration through implementation of an infrastructure project for improvement of the capacities at the Tabanovce border crossing point (IPA 2012)

Type of measure: Investment

Description of how the measure contributes to national economic policy objectives:

- The benefits from the implementation of the project are the following: increased capacity of the border crossing for the flow of shipments of goods, reduced time for the border formalities, improved infrastructure enabling use of modern methods for inspection, which will result in accelerated and facilitated exchange through one of the most frequented border crossing points in the Republic of Macedonia, facilitation and acceleration of the transport along the Pan-European Corridor 10.
- The project includes an extension of the present terminal for import and export of goods for additional 4.000 м2, as well as building of accompanying facilities.

Current status of preparation/implementation: The project is planned to be realised in the period 2015-2017.

Timeframe for implementation: Preparation of tender documentation - planned activity covered by the matrix of activities for reinforcement of the administrative capacities (activity C6/A1 with defined deadline for realisation 30.09.2015).
- Publication of an invitation to bids - planned activity covered by the matrix of activities for reinforcement of the administrative capacities (activity C6/A2 with defined deadline for realisation 31.12.2015).

Potential implementation challenges and risks: To be assessed additionally at the beginning of the implementation.

Budgetary implications: available 1,89 million euros funded under IPA 2012.

Foreseen impact of the measure: Acceleration and facilitation of the exchange realized through one of the most frequent border crossing points in the Republic of Macedonia and facilitation and acceleration of the transport along the Pan-European Corridor 10 after 2018.

4. Institutional issues and stakeholder involvement

The institutions in charge, the academic community, social partners and civil society were involved in the preparation of the National economic reform program. The program was adopted by the Government in January 2015.

The program was prepared by Ministry of Finance, coordinated by the Vice President of the Government of the Republic of Macedonia, in cooperation with the following institutions:

- Cabinet of the Deputy Prime Minister in-charge of economic affairs;
- Ministry of Economy of the Republic of Macedonia;
- Ministry of Labour and Social Policy of the Republic of Macedonia;
- Ministry of Education and Science of the Republic of Macedonia;
- Ministry of Transport and Communication of the Republic of Macedonia;

- National Bank of the Republic of Macedonia;
- Commission for Protection of Competition of the Republic of Macedonia;
- Agency for Supervision of Insurance of the Republic of Macedonia;
- Employment Service Agency of the Republic of Macedonia;
- Securities and Exchange Commission of the Republic of Macedonia;
- Agency for Supervision of Fully Funded Pension Insurance of the Republic of Macedonia;
- Agency for Foreign Investment and Export Promotion;
- Directorate for Technological Industrial Development Zones;
- Ministry of Finance - Customs Administration;
- Fund for Innovation and Technical Development;
- Macedonian Bank for Development Promotion;
- Ministry of Finance – Public Revenue Office;
- Agency for Real Estate Cadastre.

Below are the institutions, organizations and associations from which an official opinion for `the National economic reform program for 2015 - 2017 year was requested:

- General Secretariat of the Government of the Republic of Macedonia;
- Secretariat for European Affairs;
- Ministry of Foreign Affairs;
- Ministry of Information Society and Administration of the Republic of Macedonia;
- Ministry of Agriculture, Forestry and Water Economy of the Republic of Macedonia;
- Ministry of Justice of the Republic of Macedonia;
- State Statistical Office of the Republic of Macedonia;
- Macedonian Academy for Science and Arts;
- "Ss. Cyril and Methodius" University, Faculty of Economics – Skopje;
- "Ss. Cyril and Methodius" University, Faculty of Agricultural Sciences and Food – Skopje;
- "Ss. Cyril and Methodius" University, Faculty of law "Iustinianus I" – Skopje;
- University American College, Faculty of Business Economics and Organisational Sciences;
- South –East European University, Faculty of Business and Economics - Tetovo;
- State University of Tetovo, Faculty of Economics – Tetovo;
- "Goce Delcev" University, Faculty of Economics – Stip;
- "Goce Delcev" University, Faculty of Agriculture – Stip;
- "St. Clement Ohridski" University, Faculty of Economics – Prilep;
- FON University, Faculty of Economics - Skopje;
- European University, Faculty of Economics – Skopje;
- "Ss. Cyril and Methodius" University, Economic Institute – Skopje;
- Association of Local Government Units;
- Federation of Trade Unions of the Republic of Macedonia;
- Independent Trade Union of Education, Science and Culture of the Republic of Macedonia;
- Union of Independent and Autonomous Trade Unions of the Republic of Macedonia;
- Association of Chambers of Commerce of the Republic of Macedonia;
- Chamber of Commerce of the Republic of Macedonia;
- American Chamber of Commerce in the Republic of Macedonia;
- Chamber of Commerce of the North-West Region in the Republic of Macedonia
- Federation of Farmers of the Republic of Macedonia;
- Centre for Research and Policy Making - Skopje;
- Institute for Democracy, Solidarity and Civil Society - Skopje;
- Centre for Economic Analyses – Skopje;
- CeProSARD Centre for promotion of sustainable agricultural policies and rural development;
- Macedonian Centre for International Cooperation – Skopje.

Table 1: Reporting table on sectoral structural reform measures

Recommendation / country-specific policy guidance (1)	Number and title of the measure and the sector (2)	Description of main measures of direct relevance to support competitiveness and growth, and to address country-specific policy guidance (if applicable)					Link to SEE2020 targets	Challenges/ Risks	Budgetary implications/ including committed IPA funds	Qualitative elements
		Main policy objectives and relevance for competitiveness and growth (3)	Description of the measure (4)	Legal/ Administrative instruments (5)	Timetable on progress achieved in the last 12 months (6)	Timetable on upcoming steps (up to three years) (7)	Estimated contribution to SEE2020 national action plan (8)	Specific challenges/ risks in implementing the measures (9)	Overall and yearly change in government revenue and expenditure (reported in mln. national currency) Contribution of IPA (source and amounts) (10)	Qualitative description of foreseen impacts and their timing (11)
Physical capital										
	Transport – Project for preparation of a Study and an Action Plan for improvement of the safety along the SEETO overall network (Corridor X, X-d, VIII, route 6 and route 8)	Improvement of the standards during designing of the new road systems, reduction of the road accidents risk in the Republic of Macedonia and significant reduction of casualties	The preparation of the Study and the Action Plan shall provide recommendations for improvement of the standards	/	/	The Study shall be prepared in the second half of 2015	The measure contributes to the pillar Sustainable growth, Dimension I, Transport	Poor quality of the Study and the Action Plan	The contract value is 145.271 euros, of which 85% shall be secured from IPA, and 15% from the national Budget. In 2015, 58.108 euros are foreseen for preparation of a Study and an Action Plan for improvement of the safety along the SEETO overall network (Corridor X, X-d, VIII, route 6 and route 8).	The aim of this project is to prepare Study and Action Plan for improvement of safety along the SEETO network (Corridor X, X-d, VIII, route 6 and route 8)

Recommendation / country-specific policy guidance (1)	Number and title of the measure and the sector (2)	Description of main measures of direct relevance to support competitiveness and growth, and to address country-specific policy guidance (if applicable)					Link to SEE2020 targets	Challenges/ Risks	Budgetary implications/ including committed IPA funds	Qualitative elements
		Main policy objectives and relevance for competitiveness and growth (3)	Description of the measure (4)	Legal/ Administrative instruments (5)	Timetable on progress achieved in the last 12 months (6)	Timetable on upcoming steps (up to three years) (7)	Estimated contribution to SEE2020 national action plan (8)	Specific challenges/ risks in implementing the measures (9)	Overall and yearly change in government revenue and expenditure (reported in mln. national currency) Contribution of IPA (source and amounts) (10)	Qualitative description of foreseen impacts and their timing (11)
	Transport – Investment in the railway infrastructure –Corridor 10	Reduction of the travel time Modernised railway station in Skopje in accordance with the best European practices	Reconstruction of the railway Corridor 10 – section Negotivno – Nogaevce (30 km). Rehabilitation and upgrading of the Railway Station Skopje in accordance with the best EU practices	/	In the previous period, the reconstruction of the sections from Tabanovce – Kumanovo (12 km) and Miravci – Smokvica (12 km) was realised.	2015	The measure contributes to the pillar Sustainable Growth, Dimension I, Transport.	Not completing construction activities on time and poor performance quality.	- Loan from EBRD in amount of 17.600.000 euros (of which 4 million euros in 2015) – IPA component 3 - Regional development 2.091.074 euros. For modernisation of railway station in Skopje in accordance with the best EU practices: Project works in 2015 - 869.084 euros; Procurements in 2015 - 662.908 euros	Implementation of the projects will ensure stronger integration with regional markets and connecting with the common EU market.

Recommendation / country-specific policy guidance (1)	Number and title of the measure and the sector (2)	Description of main measures of direct relevance to support competitiveness and growth, and to address country-specific policy guidance (if applicable)					Link to SEE2020 targets	Challenges/ Risks	Budgetary implications/ including committed IPA funds	Qualitative elements
		Main policy objectives and relevance for competitiveness and growth (3)	Description of the measure (4)	Legal/ Administrative instruments (5)	Timetable on progress achieved in the last 12 months (6)	Timetable on upcoming steps (up to three years) (7)	Estimated contribution to SEE2020 national action plan (8)	Specific challenges/ risks in implementing the measures (9)	Overall and yearly change in government revenue and expenditure (reported in mln. national currency) Contribution of IPA (source and amounts) (10)	Qualitative description of foreseen impacts and their timing (11)
	Transport – Investments in the road infrastructure – Corridor 10	By completing the road Corridor X at a motorway level, the capacity and the overall efficiency of the route E-75 North – South shall improve, thus obtaining safe and faster transport.	- Construction of the section Demir Kapija – Smokvica (28.3 km). Rehabilitation of the motorway section Veles – Katlanovo. Rehabilitation of bridges with grant from NATO. Rehabilitation and upgrading of the motorway section Smokvica – Gevgelija – road A1 and Pan-European Corridor Xd Gradsko – Prilep (10.2 km)	/	By October 2014, 50,6% of the construction activities on the section Demir Kapija – Smokvica have been completed, For the section Veles – Katlanovo and the rehabilitation of bridges, the activities are ongoing, for Smokvica – Gevgelija, the tenders are currently being reviewed.	- 2016 - 2015 - 31.08.2015 - 18 months as of the contract signing	The measure contributes to the pillar Sustainable Growth, Dimension I, Transport.	Not completing of the construction activities on time and poor performance quality.	219.125.677 euros of which IPA funds 45.000.000 euros; the rest is budget funds secured from EIB 89.947.799 euros, and from EBRD 84.177.878 euros - 5.674.232 euros IPA – grant from NATO 8.5 million euros - 8.971.170 euros IPA In 2015: Demir Kapija – Smokvica 40.000.000 euros Veles – Katlanovo 3.934.329 euros. Smokvica – Gevgelija 1.500.000 euros	Implementation of the projects will ensure stronger integration with regional markets and connecting with the common EU market.

Recommendation / country-specific policy guidance (1)	Number and title of the measure and the sector (2)	Description of main measures of direct relevance to support competitiveness and growth, and to address country-specific policy guidance (if applicable)					Link to SEE2020 targets	Challenges/ Risks	Budgetary implications/ including committed IPA funds	Qualitative elements
		Main policy objectives and relevance for competitiveness and growth (3)	Description of the measure (4)	Legal/ Administrative instruments (5)	Timetable on progress achieved in the last 12 months (6)	Timetable on upcoming steps (up to three years) (7)	Estimated contribution to SEE2020 national action plan (8)	Specific challenges/ risks in implementing the measures (9)	Overall and yearly change in government revenue and expenditure (reported in mln. national currency) Contribution of IPA (source and amounts) (10)	Qualitative description of foreseen impacts and their timing (11)
	Transport – investments in the railway infrastructure – Corridor 8	The objective of the construction of Corridor 8 is the connection of the Black Sea with the Ionian Sea; hence the significant strategic and economic importance of this project.	Reconstruction of the railway section from Kumanovo to Beljakovce (1) - Construction of new and reconstruction of the existing railway section Beljakovce – Kriva Palanka (2)	/	- first section - in March 2014, the construction activities have commenced - second section - in December 2014, the EBRD loan was secured	- third quarter of 2016 - fourth quarter of 2015 contract conclusion and completion of the activities in the period of 48 months	The measure contributes to the pillar Sustainable Growth, Dimension I, Transport.	Not completing of the construction activities on time and poor performance quality.	-46.400.000 euros loan from EBRD (of which 9.1 million for 2015) - of 145.000.000 euros loan from EBRD (of which 5 million for 2015).	Implementation of the projects will ensure stronger integration with regional markets and connecting with the common EU market.
	Transport – investments in the road infrastructure – Corridor 8	Improvement of the country's competitiveness – increased traffic, increased transport safety and reduced travel time.	- Construction of the motorway A2, section Kichevo – Ohrid (57 km).	/	The project is being realised in accordance with the envisaged dynamics	February 2018	The measure contributes to the pillar Sustainable Growth, Dimension I, Transport.	Not completing of the construction activities on time and poor performance quality.	USD 505 million loan from the China Exim Bank	Implementation of the projects will ensure stronger integration with regional markets and connecting with the common EU market.

Recommendation / country-specific policy guidance (1)	Number and title of the measure and the sector (2)	Description of main measures of direct relevance to support competitiveness and growth, and to address country-specific policy guidance (if applicable)					Link to SEE2020 targets	Challenges/ Risks	Budgetary implications/ including committed IPA funds	Qualitative elements
		Main policy objectives and relevance for competitiveness and growth (3)	Description of the measure (4)	Legal/ Administrative instruments (5)	Timetable on progress achieved in the last 12 months (6)	Timetable on upcoming steps (up to three years) (7)	Estimated contribution to SEE2020 national action plan (8)	Specific challenges/ risks in implementing the measures (9)	Overall and yearly change in government revenue and expenditure (reported in mln. national currency) Contribution of IPA (source and amounts) (10)	Qualitative description of foreseen impacts and their timing (11)
	Transport – construction and rehabilitation of the local and regional road infrastructure	Improvement of the country's competitiveness – increased traffic, increased transport safety and reduced travel time.	- Construction of the motorway A4, section Miladinovci – Sv. Nikole – Shtip (47 km). - Project for construction, reconstruction and rehabilitation of national and regional roads (246.8 km)	/	-by November 2014, 7% of the contract were realised (A) all sections are in the design phase (b) the tender documentation for 4 road routes is in the preparation phase, and the others are in the design phase.	- May 2017 - 2015-2019	The measure contributes to the pillar Sustainable Growth, Dimension I, Transport.	Not completing of the construction activities on time and poor performance quality.	-USD 278 million loan from the China Exim Bank (of which USD 70 million for 2015) -160.000.000 euros loan from EBRD (of which 16 million for 2015) -157.000.000 euros loan from the World Bank (of which 7 million for 2015)	These investments will significantly improve the competitiveness of the country in terms of increase in traffic, increased traffic safety and reduced transport time

Recommendation / country-specific policy guidance (1)	Number and title of the measure and the sector (2)	Description of main measures of direct relevance to support competitiveness and growth, and to address country-specific policy guidance (if applicable)					Link to SEE2020 targets	Challenges/ Risks	Budgetary implications/ including committed IPA funds	Qualitative elements
		Main policy objectives and relevance for competitiveness and growth (3)	Description of the measure (4)	Legal/ Administrative instruments (5)	Timetable on progress achieved in the last 12 months (6)	Timetable on upcoming steps (up to three years) (7)	Estimated contribution to SEE2020 national action plan (8)	Specific challenges/ risks in implementing the measures (9)	Overall and yearly change in government revenue and expenditure (reported in mln. national currency) Contribution of IPA (source and amounts) (10)	Qualitative description of foreseen impacts and their timing (11)
	Energy-Energy Development strategy until 2035	Improving the security of energy supply	Defines measures and activities for security of energy supply improving and they are related to infrastructure development , integration of regional markets	Energy Development Strategy of the Republic of Macedonia until 2035	Several scenarios for the strategy are already developed and are presented in front of the Advisory Body	It is expected this Strategy to be adopted in the first half of 2015 after the public consultation and debates	The measure contributes to the pillar 1b, Dimension H. Energy	Influence on safety, quality and security of energy supply foe consumers	It is prepared in the framework of bilateral technical assistance from USAID	Decrease of the energy dependency of the country

Recommendation / country-specific policy guidance (1)	Number and title of the measure and the sector (2)	Description of main measures of direct relevance to support competitiveness and growth, and to address country-specific policy guidance (if applicable)					Link to SEE2020 targets	Challenges/ Risks	Budgetary implications/ including committed IPA funds	Qualitative elements
		Main policy objectives and relevance for competitiveness and growth (3)	Description of the measure (4)	Legal/ Administrative instruments (5)	Timetable on progress achieved in the last 12 months (6)	Timetable on upcoming steps (up to three years) (7)	Estimated contribution to SEE2020 national action plan (8)	Specific challenges/ risks in implementing the measures (9)	Overall and yearly change in government revenue and expenditure (reported in mln. national currency) Contribution of IPA (source and amounts) (10)	Qualitative description of foreseen impacts and their timing (11)
	Energy-Construction of 400 kV Interconnection overhead line TS Stip-Macedonian Serbian border	Improving the security of energy supply	Investment measure-construction of Interconnection	/	Investor has Approval for construction, has completed delivery of conductors and OPGW, has completed test of towers, supervisor of construction is selected, the delivery of the towers is ongoing	Construction of 400 kV Interconnection overhead line TS Stip-is ongoing and it is planned to be ended at the end of 2015	The measure contributes to the pillar 1b, Dimension - Energy	Untimely implementation of the activities because of the difficult weather conditions.	10 million euro loan from the World Bank (out of which 4.5 in 2015) and 5.15 million euros MEPSO's own funds	Increased reliability of the power supply system removes the risk of insecure regimes and partial collapse of systems of southeastern Europe

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	Energy-Construction of 400 kV Interconnection overhead line TS Bitola 2-Macedonian Albanian border and 400/110 KV Ohrid	Improving the security of energy supply	Investment measure-construction of Interconnection	/	Preparation of final EIA and obtain a decision on approval from the Ministry of environmental. Preparation of tender documents for selecting the best bidder who will developed the overall technical documentation .	In 2015 are expected the most suitable designer who will develop the overall technical documentation to be chosen and negotiations with the financial institution for approval of a loan to start It is expected that by the end of 2019 construction will be completed.	The measure contributes to the pillar 1b, Dimension-Energy	Starting of construction will depend on timely prepare of the technical documentation, expropriation of land and obtaining the permission to build as well as negotiations with the financial institution providing the loan	Preparation of the feasibility study and EIA grant from WBIF 800,000 euros. For the preparation of technical documentation grant from WBIF of 900,000 euros is approved. Total estimated value is 43.5 million, with proposal 37.3 million euros to be obtained by loan, and 6.2 million euros to be provided by MEPSO's own funds .	Creating 400 kV contour Albania - Macedonia - Greece, improve reliability of the regional network security of supply and stability of the transmission system, reduction of technical losses in electricity transmission system.

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	Energy-Rehabilitation and modernization of the transmission network and power system	Improving the security of energy supply	Investment measure	/	The tender procedure for selecting the best consultant is completed , and signing of the contract is ongoing . Preparation of necessary technical documentation is ongoing.	Projects of the four components should be e implemented by the end of 2017 . In 2015 the tender will be published.	The measure contributes to the pillar 1b, Dimension - Energy	Start of the implementation will depend on the timely preparation of the technical documentation , expropriation of land where it will be necessary , and the reconstruction of existing interconnection over head line and replacement of equipment in existing TC - and also will depend on the possibility of their exclusion from the transmission network to work under voltage.	25 million euros loan from the EBRD (of which 7 million for 2015) and 15.5 million euros MEPSO's own funds	Stability of the transmission network

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	Energy- Construction of small hydro power plants (SHPP) based on granting water concession for produce electricity	Greater utilization of RES in the final energy consumption and improving the security of energy supply	Investment measure- construction of energy facilities – in total 41 SHPP	/	Currently 25 SHPP with investment over 30 million euros are already constructed	During 2015 and 2016 is expected to be construct 21 SHPP that are currently under construction , while the remaining 20 SHPP is expected to be built by 2017.	The measure contributes to the pillar 1b, Dimension - Energy	Untimely providing technical documentation and construction of SHPP under the terms specified in the concession agreement , a lack of interest by private investors , risk in terms of the impact on the environment etc	/	Reduced energy dependency of the country, greater utilization of RES in the final energy consumption

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Human capital										
	Improving the transparency of higher education in the country by providing quality higher education	Enhancing the quality of higher education	This measure covers the provision of training to improve the administrative capacity of the Board for Accreditation and Evaluation in Higher Education and other persons responsible for quality management activities. It will be implemented through funding of external evaluation of the higher education sector.	/	The project started in March 2014	The activities of this component is expected to be realized within the period 2015-2017	Link to the goal - Connecting the education with the labor market needs - Dimension D.	Delayed implementation of the project activities.	There has been provided funds in the amount of 4.000.000 US dollars, for implementation of the activities under this component, provided through a loan from the World Bank.	Enhancing the quality of higher education

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	Modernization of secondary technical vocational education and training	Modernization of the system for secondary technical vocational education and training	The measure covers support to the development of a model for transformation of this system, development of standards for occupations and curricula according to the labor market needs, assessment of the degree of cooperation and networking of technical secondary schools, as well as the development of training programs for teachers.	/	The project started in March 2014	The activities of this component is expected to be realized within the period 2015-2017	Link to the goal - Connecting the education with the labor market needs - Dimension D.	Delayed implementation of the project activities.	There has been provided funds in the amount of 4.500.000 US dollars, for implementation of the activities under this component, provided through a loan from the World Bank.	Meeting the labor market needs with adequate labor force.

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	Promoting Lifelong Learning and Modernizing the Vocational Education and Training and Adult Education	Enhancing Lifelong Learning through Modernizing the Vocational Education and Training and Adult Education	The activities are focused towards modernizing the VET and AE systems	Preparation of a strategy for lifelong learning and strategy for adult education	The project start is foreseen for May 2015.	It is planned for the activities to be implemented in the course of May 2015-2017	Link to the goal - Connecting the education with the labor market needs - Dimension D.	Inadequate quality of documents.	The amount of 2,300,000 euros is provided form IPA funds (85%) and national co-financing of 15%	Increased competitiveness of the labor force in the labor market.
	Provision of financial instruments aimed at improving innovation capacity of enterprises and cooperation with research organisations	Strengthening the administrative and institutional capacities for innovation	Activities are aimed at strengthening the capacities of FITD, through staff training as well as planning and designing strategic documents, plans, programs and procedures.	/	The project started in March 2014	The activities of this component is expected to be realized within the period 2015-2017	Link to the goal - Connecting the education with the labor market needs - Dimension D.	Delayed implementation of the project activities.	470,000 euros in 2015 provided by a World Bank loan	Increasing the enterprises' capacities for research and innovation.

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Better industrial structures										
	-Better industrial structure - Implementation of annual programmes for SMEs and clusters support	In order to further implement activities for improvement of competitiveness and enterprises growth of, the Ministry of Economy and APPRM will continue to implement annual programs for supporting competitiveness, innovation and entrepreneurship	Supporting SMEs infrastructure, support of implementation of quality standards, support women's entrepreneurship, promotion of craftsmanship, increased productivity and diversification of production etc	Strategy for industrial policy, Strategy for export promotion, Strategy for innovation, Strategy for development of craftsmenship 2011-2020	/	Publishing public calls in 2015	Contributes to realisation of measures from the Sustainable growth pillar, Dimension I. Competitiveness , as well as pillars Integrated Growth and Smart Growth	Great interest from companies for the provided measures, planned funds are not sufficient	15,970,000 denars from the Budget (Competitiveness, Innovation and Entrepreneurship Programme 2015, implemented by ME Denar 12.07 million; Entrepreneurship, innovation and competitiveness of SMEs support programme 2015 APPRM, Denar 3.9 million).	Strengthening the capacity and competitiveness of companies, increased exports, increased number of employees in SMEs, increased number of SMEs.

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	Better industrial structure- Stimulation and support of innovation activities among SMEs	Stimulation and support of innovation activities in small and medium sized enterprises and stimulation of rapid technological development. The aim is to improve the capacity of companies through the transfer of knowledge and technology, research development and innovation.	The Fund for Innovation and Technology Development has developed four instruments (grant schemes) to finance projects:	Innovation Strategy, Law on innovation activity	At the moment, the preparation for the first public call for the instrument co- financing grants for start ups, spin off companies and innovation is in progress.	It is foreseen that instruments will be piloted during 2015. According to the implementation schedule till 2017 it is planned to publish at least one public call per instrument annually.	Contributes to the implementation of measures in pillar Sustainable growth, Dimension K. Competitiveness, and pillars Integrated Growth and Smart Growth, Dimension E. R & D and innovation	Insufficient institutional/ human resources, Lack of interest among potential applicants for the instruments of the Fund; Lack of business readiness (and knowledge) between potential applicants for project development (business plans)	9.159.750 euros from WB loan for realisation of activities in the period 2015-2019. In 2015 - 10.375.000 denars (from WB loan), 514.000 denars from FITD budget and 18.005.000 denars from IPARD after signing a memorandum between FITD and AFSARD	Established new businesses, new jobs created (especially for young qualified people), connecting research with entrepreneurship and development of products and services that would be competitive on the global market.

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	Better industrial structure – Financial support to SMEs through the MBDP instruments	Investment support in fixed assets and working capital, priority projects, decrease in unemployment, increase in exports and liquidity improvement	Access of SMEs to quality credit line under favourable conditions	Law on MBDP and financial contracts between EIB and MBDP	Up till now EUR 282 mil were withdrawn from the EIB credit line to finance 1,378 projects, thus creating 5,868 new jobs.	Continually, activities have been carried out for withdrawal of new funds/tranches or for improvement of credit line conditions and the rest of the products.	It contributes to the realization of the measures in the pillar Sustainable Growth, Dimension K, Competitiveness.	High liquidity of the commercial banks may reduce the interest for using funds from the EIB credit line and the future movement of the rate of risk placements.	The Budget of the Republic of Macedonia provides between EUR 200-350 thousand on annual basis to subsidize the interest rate of the EIB credit line depending on the movement of EURIBOR	Easier access to finance for SMEs, attractive interest rate, favourable credit conditions to improve competitiveness, increase in exports, development of undeveloped areas and creation of new jobs. It is expected that EIB IV credit line will support close to 480 projects and around 2080 new jobs.

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Business environment										
Economic criteria, Functional market economy	Implementation of measures for improvement of the business environment	The implementation of the proposed measures and activities will contribute to further facilitate the conditions for doing business in the country, both domestic and foreign companies	Measures are aimed at improving conditions in the following areas: Starting a business, Dealing with construction permits, Registration of property, Paying taxes and Resolving insolvency	/	Measures are based of inter-ministerial coordination of several institutions in charge and are adopted by the Government	Most of the activities are planned to be implemented in 2015, while longer-term measures will be implemented in 2016 and 2017.	Contributes to realisation of measures from the pillar Sustainable growth, Dimension K. Competitiveness	Commitment to the implementation of measures by the institutions in charge.	Additional funds from the budget are not necessary for implementation of the activities, the measures are aimed at improving working processes in institutions	Implementation of the measures will improve the business climate in the country.

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2014 Progress Report, part: Economic criteria	One stop shop system for foreign and domestic investors, Economic criteria	- Improving business environment - improving competitiveness of Macedonian companies and the economy in general	This system will ensure all needed licenses and permits for starting and running of business to be issued on one place which will decrease the time and costs for the business in the country. The establishment of the system will be carried out in phases.	/	- 2014, revision of the programming document-Sector fiche Private sector development - 2014 , finalization of the operational plan for establishing of the OSS	- Q4 2014 and Q1 and 2 2015-starting tender procedure for the implementation of the activities envisaged in the Sectoral fiche for private sector development - 2015-2017-implementation activities for the first phase of the process of establishing a One stop shop System	Contributes in implementation of the measures in the Sustainable Growth pillar, Dimension K. Competitiveness	- Delays in tendering procedures, - Commitment to implementation of the activities of the institutions in charge	IPA Budget (including National contribution) around 65 millions denars	- Easier access, decreased time and costs for the business in the country - increased level of foreign investments - improved business environment and competitiveness of the Macedonian economy

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Economic criteria, Functional market economy	Development and implementation of Master plan for improvement of the competitiveness	- Ensuring competitive functional market economy - improving of the business environment Improving of the competitiveness of Macedonian companies and the economy in general - decreasing of the unemployment in the country	The Master plan covers measures created by NECC members. Some of the measures will be financed under IPA Component 1- TAIB, Sector fiche for Private sector development	/	- Ongoing is the implementation of Action plan with measures for competitiveness adopted in may 2012 - On going is the preparation of the Master Plan for competitiveness	2015- Implementation of the Master plan for competitiveness and monitoring its realisation	Contributes to Dimension K. Competitiveness	- Providing financial recourses - Commitment in the implementation of the measures by the responsible institutions	National Budget: 450.000 denars every year (1.350.000 for 3 years period) IPA Budget: around 215 millions denars	- Increased competitiveness of the Macedonian economy based on innovation, - increased exports, - developed a functioning market economy, - reduced unemployment, - increased GDP growth

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Progress report for 2014: Market entry and exit	Preparatory activities for Macedonia Automotive Backward Linkages - MABL Program – MABL Program	The focus of the program will be implementation of activities for inclusion of domestic companies in the supply chain of foreign companies, with an overall aim to increase employment and introduction of new technologies.	As part of the MABL program, preparatory activities are foreseen, which are elaborated in detail in the Supplier Development Pilot Program, comprising four components .	/	Draft pilot programme for preparation activities for the MABL programme is prepared.	The Pilot proggrame will be implemented in the first half of 2015.	Contributes in implementation of the measures in the Sustainable Growth pillar, Dimension I. Competitiveness	Short time period, securing funds for full implementation of activities after the preparatory stage, untimely engagement of experts, lack of interest from companies..	Activities will be implemented under the World bank's MCIISP grant - Macedonia Competitive Industries and Innovation Support Program amounting to 300.000 dollars.	Strengthening the capacity of domestic companies so as to be easily included in the supply chain of foreign investors and strengthen the capacity of institutions in the country involved in the implementation of this program.

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Trade integration										
	Establishing free trade area within CEFTA	Higher level of liberalization and strengthening of the intra-regional trade with services.	According to the obligation of CEFTA Parties, they will gradually approach towards achieving progressive liberalization in trade of services and mutual opening of the market with services, in context of European integration, bearing the provisions of the GATS within WTO.	/	In 2014, two rounds of negotiations were held. Negotiation shall continue in the next period and should result in concluding a Regional Protocol of trade in services by the end of 2016.	During 2015 и 2016 will follow six rounds of negotiations concerning the level of liberalization of sectors and sub-sectors. The implementation will follow after completing the ratification of the Protocol by CEFTA Parties during 2017.	Contributes to the Pillar "Integrated Growth" Dimension A Free trade area	Unduly providing the ratification processes of the concluded Protocol of trade in services by CEFTA Parties.	The experts' working meetings concerning the processes of negotiation will be financed from IPA 2015-2017. Total IPA contribution is 3.412.500 Euros, out of which 10% is allocated for this measure.	Increased scope of trade in services among CEFTA Parties and equal opening of the CEFTA markets, etc.

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	Application of the Regional Convention on Pan-Euro Mediterranean rules of origin	The goal of the measure is to apply unified rules of origin.	In integration of the Republic of Macedonia in the global economy, the approach is towards harmonization of the Protocols for rules of origins for application of diagonal cumulation according to the Free Trade Agreements of the Republic of Macedonia with EU, EFTA States, CEFTA Parties and the Republic of Turkey, in line with the rules of the Regional Convention.	/	Republic of Macedonia ratified the Protocol for rules of origin according to the CEFTA Agreement on 27 August 2014, thus four countries out of seven countries are applying the Convention’s Protocol of origin in its mutual trading starting from 12 September 2014.	It is expected during 2015 to finish the consent of Protocols for rules of origin with EU, Turkey and EFTA States and in 2016 to provide the process of ratification.	Pillar „Integrated Growth„ Dimension C "Integration into global economy"	Unduly harmonization of the Protocols for rules of origins according to the Free trade Agreements with the Protocol of the Regional Convention.	It is a legal document to be ratified and has no financial implication.	It is expected the diagonal cumulation to be equally applied in the PEM Region according to unified rules of origin. Signatories of the Regional Convention are 47 countries, out of which Republic of Macedonia with 40 countries applies Free Trade Agreements (three multilateral agreements and one bilateral). By applying diagonal cumulation among 40 countries gives a greater opportunity to utilize the preferential treatment in trade of goods.

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	Facilitation and acceleration of the transit procedure through implementation of the New Computerised Transit System at the Customs Administration of the Republic of Macedonia	Connection of the customs transit system of the Republic of Macedonia with the EU transit systems. The implementation of these measures will provide more competitive business climate and integration into the global economy through introduction of processes in the customs working that meet the international standards.	The present activities of alignment of the customs legislation with the Acquis will be continued in the period 2015 - 2017, particularly in area of further operationalisation of the common procedures, focused on the implementation of the Convention on a Common Transit Procedure and the Convention on the simplification of formalities in trade in goods	Ratification of the Convention on a Common Transit Procedure and the Convention on the simplification of formalities in trade in goods	The New Computerised Transit System, which implementation is a pre-condition for accession to the Convention on a Common Transit Procedure, was put in function on 1st March 2014	Accession to the EU system in the middle of 2015. The implementation will be continued in the period 2015 -2016 through realisation of the Twinning Project "Finalization of the preparation for the accession to the Conventions" funded under IPA TAIB 2010	Contribution to the measure a3 Dimension A – Free trade area	It is necessary to provide maintenance of the system and further training for the employees	Previous activities covered by the IPA 2008 (total amount of about 3 mil. Eur) and future activities covered by the IPA 2010 (total amount of 0,947 mil. Eur)	The system via which the transit documents are submitted only in electronic form, provides for further acceleration and facilitation of the customs procedures; the connection with the EU systems planned for 2015 will enable to avoid the border customs formalities in paper form, when exchanging goods with the EU Member States and additional benefit for the economic operators

Recommendation / country-specific policy guidance (1)	Number and title of the measure and the sector (2)	Description of main measures of direct relevance to support competitiveness and growth, and to address country-specific policy guidance (if applicable)					Link to SEE2020 targets	Challenges/ Risks	Budgetary implications/ including committed IPA funds	Qualitative elements
		Main policy objectives and relevance for competitiveness and growth (3)	Description of the measure (4)	Legal/ Administrative instruments (5)	Timetable on progress achieved in the last 12 months (6)	Timetable on upcoming steps (up to three years) (7)	Estimated contribution to SEE2020 national action plan (8)	Specific challenges/ risks in implementing the measures (9)	Overall and yearly change in government revenue and expenditure (reported in mln. national currency) Contribution of IPA (source and amounts) (10)	Qualitative description of foreseen impacts and their timing (11)
	Improvement of the operational capacities of the Customs Administration through implementation of an infrastructure project for reinforcement of the capacities of the Tabanovce border crossing point (IPA 2012)	- Increased border crossing capacity for goods shipments -Reduced time for the border formalities and -Improved infrastructure enabling use of modern methods for inspection, which will accelerate exchange through the most frequent border crossing and facilitate transport along the pan-European Corridor 10	The project includes an extension of the present terminal for import and export of goods for additional 4.000 м2, as well as building of accompanying facilities	/	/	The Project is expected to be realized in the period 2015 - 2017	Contribution to implementaion of the measure a2 Dimension A –Free trade area	To be assessed additionally at the beginning of the implementation	Future activities of IPA 2012 (available 1,89 million euros)	Acceleration and facilitation of the exchange realized through one of the most frequent border crossings; Facilitation of the transport along the Pan-European Corridor 10 after 2018