

The Economical Reforms of The Republic of Macedonia after The Independence

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ABSTRACT

After the independence of Republic of Macedonia in 1991 the Macedonian government had to undertake arduous economical reforms in order to fulfill the European Union economical criteria's given in Copenhagen to the countries that wish to become full member states of European Union. The reforms were made in macro economical policies and some structural changes were made in the economy. The new laws of central Bank in 2002 and 2003 had provided legal background for the monetary policy. However some of the remaining problems are high unemployment rate, high rate of grey economy, low level of foreign direct investments.

1. Introduction

Republic of Macedonia got the independence in 1991 after the dissolution of the Socialist Federal Republic of Yugoslavia. Since the independence, the governments of Macedonia included as their top priorities the entrance in NATO and entrance in the European Union. Since the independence the country had to undertake strenuous reforms in order to restructure the communist centralized economy into an open market economy tailored according to the European Copenhagen criteria's for new members.

Macedonia is a small open economy in southeastern Europe. As a landlocked country with a population of only 2 million, Macedonia was the third poorest country in all the countries in South Eastern Europe in 2013. Trade is an important part of the economy compared to other countries in the region, the share of trade to GDP ratio of 112 percent in the past decade. Since 1995, the exchange rate of the national currency is pegged to the euro, which successfully supports price stability. Inflation, on average, was 2.5 percent in the past 10 years. National Bank of Macedonia (Central Bank) reacts quickly and decisively to any possible threats for exchange rate. Moreover, the government implemented important structural reforms in the past few years, including reducing the regulatory burden and red tape, improve customs administration and introduction of a flat tax on personal income and corporate profit.

The transition in the country is characterized by achieved strong macroeconomic stability. By 1995 was successfully implemented an economic stabilization program, which resulted in the reduction of inflation and ever since it has been continuously maintained at a low level. Basic macroeconomic forecasts in the medium term move in the following framework: GDP growth of 4-5% per year inflation of 2.5% budget deficit, lower than 1% and the current account deficit of the balance of payments of 0.8%. Priority objectives of macroeconomic policy remain maintaining macroeconomic stability, stabilize the budget deficit to a sustainable level (within the Maastricht criteria) and creating a favorable environment for interest rate cut.

1.1. Macroeconomic Policies and Structural Reforms

During the first years of transition after 1990, the Macedonian economy is faced with extremely high inflation at the time of independence, it was 1,700% back in 1992. Moreover, early transition was characterized by a sharp drop in gross domestic product (GDP). Cumulative decline in real GDP over the period 1992 - 1995 year was about 20%, driven largely by the significant decline in industrial production by 42% due to the loss of markets in the former Yugoslavia after its breakup (Petrevski, 2005).²

Therefore, the Government wrote the program for economic stabilization which resulted in a significant reduction of inflation in a relatively short period of time, which successfully maintained a stable single-digit level, from the beginning of 1995 until today. Monetary policy and its coordination with fiscal policy and

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²Petrevski G, (2005) Macedonia: a decade of stabilisation policy, SEER SouthEast Europe Review for Labour and Social Affairs, issue: 01 / 2005, pages: 97115, on www.ceeol.com.

wage policy, greatly contributed to the achievement and maintenance of price stability and the coordination proved particularly successful during the Kosovo crisis in 1999 and in 2001 military crisis in the country. As a result of establishing and maintaining price stability, from the beginning in 1996 until today (with the exception of 2001, due to the negative effect of military crisis), the GDP of the Republic of Macedonia has continued rising, although the rate of growth is varying.

Structural change - after the independence of the Republic of Macedonia, the structure of the economy largely reflected the specific features of the economic and social system of Federal Socialist Republic of Yugoslavia, in whose structure was Macedonia integrated for almost five decades from 1944 to 1991. Social Federal Republic of Yugoslavia has developed a very specific economic model, where much of the means of production were "socially owned" (i.e. not owned by the state, but owned by the employees), with a relatively high degree of local self-autonomy. As a result of this, economic operators have had a comparatively high level of freedom and independence. Private ownership of the means of production was possible, and prices are largely determined by market processes. However, one important feature of this system is de facto liberal budget constraint for social enterprises that enables politically well-connected companies easy access to credit from the banking sector and the opportunity to accumulate vast arrears of taxes, social contributions or commitments to other companies. This practice allowed unviable enterprises to survive, even at the expense of deterioration in the financial sector and price stability.

During the five decades when Macedonia was part of Yugoslavia, its economic structure undergoes significant reorientation and modernization, especially on transport infrastructure and industrialization. Agriculture has become semindustrialized and gained in importance, while manufacturing and mining declined because many loss-making firms were closed. Because of all this in the service sector began to employ more people. The restructuring began in production 48% of value added in 1990, including mining. The share of the trade sector was relatively high (almost 20% of total value added), while agriculture accounted for about 10% (European Commission, 2005).³ Tourism accounted for only 2% (European Commission, 2005).⁴ The share of agriculture in total employment is of great importance to the participation of people in the agricultural sector accounted for about 22% in 2003 (European Commission, 2005).⁵

The transformation of ownership was recognized as crucial for the transition to a free market economy and privatization became a priority of the newly independent state. In fact, privatization in Macedonia was originally introduced in 1989, the Law on the social capital of the former Yugoslav federation when over 600 companies in Macedonia have been transformed into joint-stock companies or limited liability companies. However, the real impetus to the privatization process was given by the new Law on Transformation of Enterprises with Social Capital in June 1993. Under the Act, 1200 companies from the commercial sector were subject to privatization.⁶

In 1996 began the privatization of the agricultural sector, including companies operating in the insurance sector and companies that organize games of chance or a total of about 1600 entities. During that time, from privatization were excluded companies that have special national interest like utilities, forests, land and social public goods. Banks are transformed as part of a wider reform of the financial sector. However, for full capitalization, number of Macedonian banks found foreign investors, backed by the European Bank for Reconstruction and Development and International Finance Corporation. Meanwhile, infrastructure companies and utility companies, like for example Macedonian Electrical Power Company, and the Macedonian Telecom, were later privatized and sold.⁷ The data show that most of the privatized companies

³European Commission, (2005), Analytical report for the opinion of the application from the Former Yugoslav Republic of Macedonia for EU membership, {COM (2005) 562 крајна верзија}. Retrieved from [http://www.sobranie.mk/WBStorage/Files/Analiticki_izvestaj_COM\(2005\)562%2009.11.2005.pdf](http://www.sobranie.mk/WBStorage/Files/Analiticki_izvestaj_COM(2005)562%2009.11.2005.pdf)

⁴European Commission, (2005), Analytical report for the opinion of the application from the Former Yugoslav Republic of Macedonia for EU membership, {COM (2005) 562 крајна верзија}. Retrieved from [http://www.sobranie.mk/WBStorage/Files/Analiticki_izvestaj_COM\(2005\)562%2009.11.2005.pdf](http://www.sobranie.mk/WBStorage/Files/Analiticki_izvestaj_COM(2005)562%2009.11.2005.pdf)

⁵European Commission, (2005), Analytical report for the opinion of the application from the Former Yugoslav Republic of Macedonia for EU membership, {COM (2005) 562 крајна верзија}. Retrieved from [http://www.sobranie.mk/WBStorage/Files/Analiticki_izvestaj_COM\(2005\)562%2009.11.2005.pdf](http://www.sobranie.mk/WBStorage/Files/Analiticki_izvestaj_COM(2005)562%2009.11.2005.pdf)

⁶Privatization Agency of Republic of Macedonia, (2005), Jovanovska M., Belogaska E., Sajnoski S, Privatization and restructuring of the of the socially and state owned companies in Republic of Macedonia and its implications on corporate governance, Retrieved from OECD site <http://www.oecd.org/daf/ca/corporategovernanceprinciples/2394769.pdf>

⁷Agency for Privatization, (2005)

were bought by the Macedonian citizens, especially by former employees of companies (Arsov).⁸ However, privatization with foreign capital amounted to about 185 million Germanmarks, which was an important impetus for the Macedonian economy.

The loss-making companies were put into a program for restructuring which was prescribing liquidation of the loss making companies, budget limitations and privatizations. The results of this was increased number of the unemployed people that were waiting for a solution from the government for many years. Out of 125 loss making companies some were liquidated, other privatized, or waited a few appropriate solutions for many years. In many of them, the state became a major shareholder for debts that are not shown as the final solution, as 52 companies were found to further loss and their situation was resolved in 1999 (Jovanovska M., Belogaska E., Sajnoski S, 2005). In fact the privatization process was criticized a lot by the experts because it provided possibility for the insider workers mostly coming from the highest management to depreciate the value of the company and to buy the majority of shares for a very low price. In comparison the privatization made in Republic of Slovenia, a country that also was part of the Yugoslav Federation was done gradually and in major enterprises majority shareholder was the government of the Republic of Slovenia. This ensured a safer and more transparent transfer of the capital.

Another major change which has undergone the Macedonian economic system after the disintegration of Yugoslavia was a process of restitution of property and land. After the change of political and economic system, and following the example of other countries in the so-called Communist bloc, the Republic of Macedonia in 1998 passed the Restitution Act (published in "Official Gazette" nr.20/98), which has undergone several amendments. The purpose of the enactment of this law was to correct an historical and ideological injustice to owners or their heirs of the property, which was seized in the previous system and enable them to re-exercise the right of ownership over it. The adoption of the law was aimed at respecting the constitutional right of ownership of property as one of the fundamental rights. Thus, under Article 30 of the Constitution "guarantees the right to property and inheritance. No person may be deprived of property or rights deriving from it, except for the public interest, as specified by law."⁹

The bigger problems identified in this process are the are long procedures and slowness of government bodies, disappearance of documents, issuing governmental bonds instead of returning the real property and usually for very low value (Mihajlova, 2010).¹⁰ According to the Ombudsman, the largest numbers of complaints over the years were concerning the restitution proceedings: "As of November 2007, there were 109 complaints. Citizens often complain of long duration procedures, non execution of the decisions for restitution, non-implementation of the guidelines in the decisions of the Supreme Court of the first instance and appeal committees."¹¹ The process ended in March 2012 rather than in 2008, as was the original plan of the Macedonian government, the Ministry of Finance has decided the last of a total of 30,744 cases of first instance in restitution.

In terms of macroeconomic indicators, it is important to note that the Republic of Macedonia has already met some of the EU criteria defined in the Maastricht meeting: criteria for exchange rate and public debt are fully met (expressed as a percentage of GDP), while the inflation rate criterion was reached in 2002. At the same time, it is close to meeting the criteria for the budget deficit despite the budget deficit limit was exceeded during the last few years as a result of the exceptional situation in the country. Generally, the interest rates are too high compared to European level, although from 2003 there is a trend of decreasing.¹²

1.2. Monetary Policy

The Law on the National Bank of the Republic of Macedonia from 2002 and 2003, is largely harmonized with EU requirements. It strengthens the position of the Bank as the Central Bank, as well as its

⁸Arsov Sašo, (2012), Post-privatisation retrospective of Macedonia – could we have done it better?, Faculty of Economics University "Ss.Cyril and Methodius" – Skopje, Republic of Macedonia.

⁹Constitution of Republic of Macedonia, Article 30. Retrieved from Parliament webpage <http://www.sobranie.mk/ustav-na-rm.nspk>

¹⁰Mihajlova, (2010) Процесот на денационализација - од декларativност до realност, Правен Дијалог Број 1, 2010, <http://www.ihr.org.mk/praven-dijalog/praven-dijalog-br1/102-proces-na-denacionalizacija.html>,

¹¹Ombudsman, Annual report, 2012. Retrieved from the Ombudsman website: <http://www.ombudsman.mk/upload/documents/2013/GI-2012.pdf>

¹²Government of Republic of Macedonia, Sector for European Integration, National Strategy of RM for European integration, 2004, http://www.sobranie.mk/WBStorage/Files/Nacionalna_strategija%2006.09.04.PDF

independence in carrying out its legally defined functions. The main objective of monetary policy, contained in the Act, is the maintenance of price stability as a necessary precondition for sustainable economic development. In order to achieve this ultimate goal, the Central Bank identified intermediate targets of monetary policy. After independence until 1995, interim monetary policy objective was the achievement of M1 money supply and a stable demand for money in order to maintain exchange rate stability and price stability. Therefore, by the end of 1995, the Central Bank started implementing monetary strategy of pegging the exchange rate against the German mark and since 2002 against the euro. The implementation of such a strategy gave positive results, which are reflected by maintenance of the low rate of inflation in the country.

Employment and unemployment-employment rate in Macedonia in 1997 was 38.1% and in 2014 is 41%, which is low by international standards, and the rate of participation in the labour force is 57.3%, which is equal to the other countries in the region, but is low compared with European countries.¹³ Unemployment rates for men and women are very similar, they are higher for the younger age groups from 20 to 29 years, as well as minorities, especially minority women. The unemployment rate in 2014 is about 28.8%, reaching the highest level of 37.3% in the 2005¹⁴. Unemployment rates are also high for the workforce with lower levels of education, where 61.5 percent are men and 38.5 percent are women. Furthermore the biggest rate of unemployment is among the people who have only secondary education.

Additionally, the government started reforms of the labor market, including measures that aim to reduce employment in the informal sector the so-called "gray economy". The objectives of these reforms are to reduce the official rate of unemployment. This is important for monitoring of the future policy measures for the labor market, aimed at job creation and increase the quality of human capital. In this context, one of the priorities was reducing regulatory barriers to formal employment such as lower costs to meet various requirements in recruitment, application and firing workers, reducing the fees that are associated with wages and social charges, especially for SMEs, and registration of enterprises operating in the informal sector.

Conclusion

In 1993, the Copenhagen European Council defined the following economic criteria for EU accession: The existence of a functioning market economy and the capacity to cope with competitive pressure and market forces within the Union.¹⁵ These criteria are related. Firstly, a functioning market economy can better deal with the pressure of competition. Second, in the context of Union membership, functioning market is the domestic market. Without integration in the internal market, the EU will lose its economic importance as the Republic of Macedonia and its partners. Since the independence Macedonian government was working to change the economy from centralized economy to market oriented economy with quite a success. It has come long way and for this was rewarded with status of candidate country of the EU in 2005. This path was hard and strenuous. Today Macedonia has preserved the macro economical stability, the inflation rates are relatively low, and many companies were restructured and are fighting to be competitive in the European market. All the new laws are harmonized with the acqui of the European Union. Macedonia was in the group of top 10 reformers according to the Doing Business report of the World Bank.¹⁶ The 2013 Pre-accession Economic Programme (PEP) for the period 2013-2015 outlines key economic, fiscal and structural policies and planned reform measures. The key objectives remain promotion of growth and employment. However many problems remain like high unemployment rate, high rate of the grey economy, the general qualification of the workforce remains low, and matching the skills of graduates with the needs of potential employers remains a major challenge.

¹³State Statistical Office of Republic of Macedonia, (2011), Report for 20 years independence of Republic of Macedonia. Retrieved at the website State Statistical Office of Republic of Macedonia <http://www.stat.gov.mk/Publikacii/20GodiniRM.pdf>

¹⁴State Statistical Office of Republic of Macedonia, (2011), Report for 20 years independence of Republic of Macedonia. Retrieved at the website State Statistical Office of Republic of Macedonia <http://www.stat.gov.mk/Publikacii/20GodiniRM.pdf>

¹⁵European Council in Copenhagen, (1993), Conclusions of the Presidency, (21-22 June 1993, SN180/1/93) 12. Retrieved at the website of European Commission: http://ec.europa.eu/bulgaria/documents/abc/72921_en.pdf

¹⁶World Bank, (2013), Doing business report, Retrieved from the website: <http://www.doingbusiness.org/~media/GIAWB/Doing%20Business/Documents/Annual-Reports/English/DB13-full-report.pdf>

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