MACEDONIAN COMPETITIVENESS PORTRAIT: STRENGTHS AND WEAKNESSES

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Economic developments in Macedonia

- **Growth** has been subdued in the post-crisis period, then recovered more strongly for a few years and recently was constrained again due to the political instability in the country.
- **Inflation** has been low and stable.
- **Unemployment** remains high, but declined substantially during the recent years.
- The government implemented a countercyclical policy in the wake of the crisis, increasing the **budget deficit** and **public debt** as percentage of GDP.
- **Current account** deficit widened dramatically during the crises, but then reversed to more sustainable levels.
- **FDI** flows registered decline since the start of the crises, but still sufficient to cover the CA gap and support de facto pegged ER regime.
Global Competitiveness Ranking

- Macedonia registered a significant competitiveness improvement during the last decade and has the best rank among the SEE countries (rank of 68 according to GCR 2016-17 vis-à-vis rank of 89 in GCR 2008-09)

- In terms of stage of development, Macedonia belongs to the group of efficiency driven economies (Stage 2) as all of the SEE countries
Global Competitiveness Ranking

- In comparative context with SEE countries, Macedonia has better macroeconomic environment and institutions as well as more efficient goods market.
- On the other hand, developments in health and education are lagging behind the SEE region.
Global Competitiveness Ranking

• **Improvements** are driven by better ranking on institutions, goods market efficiency, financial market developments and innovations.
Yet, there are many **problematic factors for doing business** in Macedonia.

- **Access to finance** is constantly the most emphasized challenge for the corporate sector, accompanied by **labor market imperfections**.
Focus on specific issues

• Our further elaboration focuses on the government role as well as the existing weaknesses in five areas relevant for improving competitiveness of the country:
  • Investment policy
  • SME and access to finance
  • Education
  • Innovation
  • Labor market efficiency
Investment policy

The role of the government

- Macedonia has undertook plenty of measures to improve the climate for doing business and thus, attract FDI
  - This has been evidenced in the WB Doing Business Report (rank of 11 in DBR 2018 vis-à-vis 75 in DBR 2008)
- Macedonia has operational investment policy focusing on the protection of foreign investors’ rights (equal treatment of foreign investors and the protection of their ownership rights)
- It has also developed and implemented a strategy to promote and facilitate investments, including a set up of investment promotion agency
  - investment promotion and matchmaking events targeting specific countries or sectors
  - establishment of the Technological Industrial Development Zones offering incentives for foreign investors (tax holidays for up to 10 years, for both profit tax and personal income tax, VAT and custom duties exemptions etc.)
    - empirical studies suggest that the benefits outweigh the costs of financial incentives (NBRM, 2017; Finance Think, 2016)
Investment policy

- FDI inward flows in Macedonia were usually higher than in the EU, but underperformed the flows in SEE
- The FDI flows after the crisis caused a structural change in terms of:
  - increasing the export/import coverage ratio
  - Improving the export structure in favor of medium- and high-tech goods
Investment policy

Major Weaknesses

• Existence of administrative ports of call
  • moving towards a one-stop shop
• Uneven treatment of domestic investors
• Transparency vs flexibility in offering financial incentives
• Weak FDI-SME linkage practices
  • support foreign investors in building local supplier bases with domestic SMEs
SME development

• The SME sector is an important driving force of overall economic activity
  • represent 99% of all businesses in Macedonia (similar in the EU).
  • provide three fourths of all private-sector employment (two thirds in the EU)
  • generate two thirds of value added (three fifths in the EU)
SME development

Small Business Act Profile Score for Macedonia and SEE

Source: EBRD, ETF, SEECEL, EU, OECD 2016
SME development

Small Business Act Profile Score for Macedonia over time

Source: EBRD, ETF, SEECEL, EU, OECD 2016
SME development

The role of the government in SME promotion

• A regulatory guillotine has been regularly applied since 2006.

• **Company registration** process currently takes one day and a single procedure.

• A **cadastre** is available online, covering 99% of the country’s territory.

• Broad **e-governance system** established in recent years.

• A national **strategy for innovation** was adopted, which has established a range of support services for SME.
SME development

Major Weaknesses

• SME perceive access to finance as a major challenge to their operations – why?
  • Around 80% of businesses cover their financing needs with internal funds and retained earnings
  • Bank-centric model dominates – only around one third of total private-sector lending goes to SME
    • high collateral requirements (in a range 150-250%) combined with banks’ heavy reliance on (immovable) collateral
    • higher cost of borrowing that that in the euro area
    • Lack of investment readiness (SME’ poor skills in business planning and financial management) vis-à-vis underdeveloped investment banking
    • High level of grey economy (around one third of GDP according to some studies) which constraints further the reliance on bank financing
  • Absent SME integration into global value chains
Education

• The educational system of Macedonia has undergone a **series of reforms**, at all levels
  • With positive intentions, but frequently ad-hoc solutions
  • Resulting in underperformance of students
    • E.g. PISA rankings
Education

- **Challenges**
  - Improve the quality of education at all levels, rather than quantity (access to)
  - Make VET more attractive
  - Develop career guidance and profiling, as a key link between the educational system and the labor market
    - Hence, key for competitiveness
Innovation

• The only country in the region with dedicated innovation strategy
  • Fund of innovation and technological development
    • Funding innovative projects
    • Supporting start-ups and spin-offs
  • Lately, the government introduced the support for start-ups directly in their Plan for economic growth

• Still, investment in R&D comparatively low
  • 0.44% of GDP, as compared to 2% of the EU
  • Cooperation between the Ministry in charge of science and economic ministries still very weak
  • The Ministry of Science ceased its program for academic excellence in 2010
  • Limited business-academia cooperation
Score of R&D in Macedonia (max 5)

- RDI policy governance: 3
- Research base: 2
- Private sector RDI activities: 1.5
- Business-Academia Collaboration: 1.5
Labor market

- Comprehensive strategy for **fight against unemployment**
  - The core of government economic policy for a decade (2006-2017)
  - Special consideration of **youth and women** (also addressed in other related strategies)
- Instruments
  - The core job-generating activity has been the attraction and setting up of **foreign companies** in the country
  - **ALMPs** (though the spending comparatively lower than on passive measures)
  - “**Macedonia employs**” as a special type of employment policy – providing new employees tax and contribution holidays
- Technically
  - The role of **PES** has been significantly strengthened and modernized
  - The labor market has been **flexibilized** in a multitude of venues (e.g. hiring and firing procedures)
  - The role of **social enterprises** is emerging in the national legislation
Unemployment rates

- Unemployment rate
- Youth unemployment rate (15-24)

Employment and participation

- Female participation rate
- Employment rate
- Female employment rate
Conclusion

- Macedonia has made steady progress during the last decade. In global terms, it has registered significant competitiveness improvement.
- Better macroeconomic environment and institutions as well as more efficient goods market are our main strengths in the regional context.
- However, our competitors are not standing still. They are actively reducing business costs, building infrastructure and stimulating entrepreneurial spirit.
- Therefore, Macedonia has to rapidly improve its weaknesses related to SME access to finance and integration into global value chains, quality of education, R&D investments and labour market imperfections.
- These will lay ground for changing the competitiveness model over the long-term – from the current low cost wages approach to enhancing competitiveness through greater entrepreneurship, value added and productivity.
Thank you for your attention!

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