

BTI 2008 | Macedonia Country Report

Status Index	1-10	7.52	# 22 of 125	
Democracy	1-10	7.75	# 29 of 125	➔
Market Economy	1-10	7.29	# 24 of 125	↗
Management Index	1-10	6.52	# 21 of 125	

scale: 1 (lowest) to 10 (highest) score rank trend

This report is part of the Bertelsmann Transformation Index (BTI) 2008. The BTI is a global ranking of transition processes in which the state of democracy and market economic systems as well as the quality of political management in 125 transformation and developing countries are evaluated.

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Key Indicators

Population	mn.	2.0	HDI	0.80	GDP p.c.	\$	6,405
Pop. growth ¹	% p.a.	0.2	HDI rank of 177	66	Gini Index		39.0
Life expectancy	years	74	UN Education Index	0.87	Poverty ³	%	<2
Urban population	%	68.9	Gender equality ²	0.55	Aid per capita	\$	113.2

Sources: UNDP, Human Development Report 2006 | The World Bank, World Development Indicators 2007 | OECD Development Assistance Committee 2006. Footnotes: (1) Average annual growth rate 1990-2005. (2) Gender Empowerment Measure (GEM). (3) Percentage of population living on less than \$2 a day.

Executive Summary

Three major events characterized the period under review: the local government elections in 2005, the granting of candidate status to Macedonia by the European Union in December 2005 and the national elections in July 2006. The national elections led to a change in government, bringing the center-right VMRO-DPMNE (Internal Macedonian Revolutionary Organization – Democratic Party for Macedonian National Unity) back into power. The VMRO and its coalition partner, the ethnic Albanian Democratic Party of Albanians (DPA), replaced the government led by the Social Democratic Alliance of Macedonia (SDSM).

According to international observers, the national election held on 5 July 2006 largely met international standards and 56.1% of registered voters turned out for the election. After the elections, however, the ethnic Albanian party (DUI) refused to accept that it would not be a party in government for weeks and even hinted at the possibility that it would resort to its former rebellious tactics. The decline of voter turnout from 73.4 % in 2002 to 56.1% was considerable, affecting the ethnic Albanian vote as well.

The 2005 local elections were won by the SDSM coalition. Although the Social Democratic Alliance of Macedonia received more votes and had more of their mayoral candidates elected over all, the opposition was successful in the capital city of Skopje. The new mayor of Skopje was an independent candidate supported by the opposition. Among Macedonian Albanians, the ruling DUI (Democratic Union for Integration) won over the opposition DPA. Although local elections were marred by a number of irregularities, the EU Commission gave Macedonia a positive recommendation. On 17 December 2005, the European Council granted Macedonia the status of a “candidate country.” The government adopted the draft National Program for the Adoption of the Acquis in March 2006 and focused on the implementation of the Ohrid Framework Agreement. Steps were taken to decentralize public administration when a new law on

the territorial organization of local government was adopted. To ensure an equitable representation of national minorities in public administration, members of these groups were increasingly recruited as public employees.

History and Characteristics of Transformation

Modern Macedonia emerged in 1945 as one of the six constituent republics of the Socialist Federated Republic of Yugoslavia (SFRY). Constitutional changes in 1989 and 1990 paved the way for the first multi-party elections in November 1990. With the exception of an expert government holding office between March and July 1992, all governments until 1998 were led by the SDSM (Social Democratic Alliance of Macedonia), the successor party to the Macedonian communists. A new constitution was adopted on 17 November 1991. When Yugoslavia disintegrated in the second half of 1991, Macedonia chose to assert its own independence rather than remain in a truncated Yugoslav state likely to be dominated by Serbia without the counterbalancing influences of Croatia and Slovenia. Macedonia declared independence on 8 September 1991, and is a democratic multiparty state today. The political system is a parliamentary democracy with a directly elected president who may not appoint members of government without the approval of the legislature. In practice, Macedonian presidents have been able and have tended to exert more influence than envisaged by their constitutional role.

Macedonia's peaceful transformation in the early 1990s was preceded by an uneasy period of democratic consolidation. The combination of Greek diplomatic pressure, the economic embargo imposed on Macedonia (1992 – 1995) and the difficulties stemming from taking part in UN sanctions against the Federal Republic of Yugoslavia significantly impaired Macedonian democratic stabilization efforts. Due to Greek objections, the admission of Macedonia to the United Nations in April 1993 required the new member to be “provisionally referred to for all purposes within the United Nations as ‘the former Yugoslav Republic of Macedonia’ pending settlement of the difference that has arisen over the name of the state.” Although the reference to the Yugoslav past was to be used within the United Nations as a result of Greek pressure, other international institutions have continued referring to Macedonia as a “former Yugoslav republic.” Despite the recent warming of relations between Skopje and Athens, Greece has yet to grant Macedonia its approval.

Besides the issue of Macedonia's formal name, interethnic relations and the question of minority rights were at the forefront of the domestic political agenda during the democratization period. Macedonia's political elites established a practice of power sharing, involving representatives of Macedonia's ethnic Albanian community (25.2 % of the population) in successive governments. Following an armed conflict in early and

mid 2001 involving unrest among ethnic Albanians, the Ohrid Framework Agreement was signed. The agreement envisaged a restructuring of the political system to allow greater use of the Albanian language, ensure equitable ethnic Albanian representation in government institutions and decentralize powers from the central state to the municipal level. Macedonia amended its constitution and initiated a process of decentralization in order to implement the agreement.

Transformation Status

I. Democracy

Starting in 1991, Macedonia has slowly transformed its political order from Yugoslav-style communism to multiparty democracy. The outstanding questions regarding ethnic relations and regarding the status of the Albanian minority in particular were settled in 2001 to a great extent as part of the Ohrid Framework Agreement. Transformation shortcomings still remain, especially regarding corrupt practices regarding the rule of law. Furthermore, full democratic consolidation is somewhat impaired by a weak civil society and an economy unable to alleviate significant unemployment rates.

1 | Stateness

Since the constitutional and legal reforms linked to the Ohrid Framework Agreement, stateness-related problems have been diminishing. In principle, the state monopoly on the use of force is in place. In September 2004, a group of ethnic Albanian paramilitaries occupied a rural suburb of the capital Skopje for two months. However, no similar case has occurred since then. Certain villages inhabited by ethnic Albanians are controlled by the state in theory. In practice, however, local leaders control business and social life.

Monopoly on the use of force

Following the breakup of federal Yugoslavia, there was confusion regarding a number of individuals who did not acquire Macedonian citizenship due to failure to meet citizenship requirements established by the new Macedonian republic. Most of these persons were ethnic Albanians who migrated to Macedonia from Kosovo during socialist times. Since the introduction of legislative changes easing the requirements to acquire Macedonian citizenship, this issue has not been on the political agenda. By law, all citizens have the same civic rights; the nation-state is accepted as legitimate even if ethnic loyalties are still strong

State identity

Church and state are separated by law; the political process is generally secularized. However, preferential treatment is given to the major Orthodox Christian and Islamic denominations. New denominations within these faiths cannot officially register under the same name nor operate in the country. The present government is considering the idea of introducing religious teaching in the public education system. A draft law on religious communities and churches

No interference of religious dogmas

is in progress. Legal experts are working together with the Inter Religious Council in Macedonia (all five churches and religious communities mentioned in the constitution on both issues.

A basically functioning administrative system and public security and order are assured throughout the country, albeit with some limitations. These institutions suffer from widespread corruption and a lack of technical skills. Many public institutions lack essential equipment like computers or printers. More importantly, there is a lack of knowledge and skills to cope with the reform process and new responsibilities, especially within local self-government.

Basic
administration

2 | Political Participation

In general, elections in Macedonia are free and fair. The new electoral laws adopted in March 2006 (the Law on Election of Members of Parliament, the Law on the Voter List and the Law on Election Districts) inter alia established a fully professional state election commission and restricted the influence of political parties over electoral administration by involving civil servants in electoral administration. Parliamentarians are elected for a four-year term in six electoral districts. Each district has about 275,000 voters and elects 20 members. The unicameral assembly (Sobranie) is comprised of 120 members elected according to a proportional formula without a minimum threshold. Manipulations of the vote have occurred in certain areas of the country, including during local elections in 2005. Ballot-box stuffing, family voting, voter intimidation on election day and the breaking of electoral boxes by armed individuals have all occurred in past local and national elections, most of the incidents occurring in rural regions populated by ethnic Albanians. The EU has made further progress in the integration process conditional on the regular conduct of parliamentary elections. While the 2006 parliamentary elections were generally conducted in an orderly and peaceful manner, isolated cases of serious irregularities were reported from a number of municipalities. The OSCE/ODIHR report on the 2006 elections noted that the first half of the election campaign was overshadowed by numerous violent incidents, including attacks on campaign offices, fights among party activists and non-fatal shooting incidents. Most of these incidents “occurred in the north-west of the country and involved the ethnic Albanian parties Democratic Union for Integration (DUI) and the Democratic Party of Albanians (DPA).” Clashes between party members or supporters during the election campaign provoked the European Union and United States to intervene again and to call on the party leaderships to send a clear signal to their supporters to refrain from the use of force.

Free and fair
elections

The military and the intelligence services are under full civilian control. Further reforms aimed at reforming the Macedonian military to meet NATO standards have strengthened the democratic control of the military by the government. There is consolidated civilian rule of the military and intelligence service. At the moment, there are no veto powers in the hands of the military.

Effective power
to govern

The rights to politically organize and form civic groups are respected. Newly proposed legislation on founding and registering political parties, however, is likely to pose obstacles to political organization as it requires parties to (re-)submit a list of members, who in turn have to sign their membership cards at the office of the Ministry of Justice. The creation and activities of non-governmental organizations are regulated by the 1998 Law on Citizen Associations and Foundations. In principle, the legal framework for the functioning of civil society is free of excessive state pressures and bureaucracy. The law prohibits NGOs as well as trade and professional organizations, employer and employee unions, interest groups and foundations from being involved in direct economic activities. While the state imposes no impediments to civic organizations, neither does it provide tax breaks or other forms of legal assistance for them. For a long period of time since independence, trade unions have been under political influence, as a large portion of their income has come from the state budget.

Association /
assembly rights

The state-run and private media are mostly free of government influence. Yet commercial electronic media has links to political parties and often influence on editorial politics. Corporations owning print media are also alleged to have links to political leaders, and the editorial independence of various newspapers is doubtful.

Freedom of
expression

3 | Rule of Law

The rule of law in Macedonia has been deteriorating for a while. Corruption has been growing, especially within the judiciary. Reforms have been slow and ineffective. The system of checks and balances was inefficient, allowing the executive to dominate the political system. Since 2002, reforms have been made, and the government elected in 2006 continues the trend. The judiciary remains the most precarious of democratic institutions in Macedonia. Macedonia's political system emphasizes the separation of powers between the executive, legislature and judiciary. Yet in practice, political parties in power have often attempted to influence the judiciary. The legislature has been and is still influenced by the government, sometimes to the extent that it ceases to propose any new laws, leaving the initiative to the executive. The control function of the parliament is also not very strong. There are several reasons for this, including a lack of competence and lack of administrative capacity to support the deputies. On the other hand, the strong office of the president works to balance the

Separation of
powers

premier's dominating tendency. Presidents have used their influence particularly in foreign affairs. The countervailing role of the president is especially successful when the president and the premier do not belong to the same party (as in the periods 1998-2002 and 2006-present). In recent years, Macedonia has thoroughly decentralized its political system. Sub-national governments now enjoy a number of competencies and fixed sources of funding, making them more independent of the central government. The system of checks and balances, however, suffers from the low degree of professionalism in all branches of government. The executive dominates the parliament ; formative decisions in Macedonian history (the retreat of the Yugoslav army, Ohrid, the decentralization laws) were not made or shaped by parliament, but rather by various other actors.

The independence of the judiciary is formally guaranteed by the legal framework. Yet in practice, judges are politically appointed to all courts from the lowest to the highest. Professionalism among personnel is low and salaries are even lower. There are thousands of pending cases. Recent reforms of the judiciary aimed at improving the selection mechanisms of judges and prosecutors. The constitution was amended in December 2005 to reform the court system, immunity rules, the administrative sanction system, the selection and training system for judges and prosecutors, the Judicial Council and the Public Prosecutor's Office and to allow administrative bodies to impose sanctions. In May 2006, a new judicial council was formed consisting of senior judges who monitor the independence of judges and courts and review court procedures and decisions. In January 2007, a new law was adopted on state prosecution.

Independent
judiciary

There are a number of legal mechanisms that should prevent officeholders from abusing their positions. Corruption has been the most important issue for the public in recent years as it has reached very high levels. Together with eliminating poverty and unemployment, the public views fighting corruption as the most urgent problem related to good governance. Since 2002, the issue has also ranked high on the political agenda. Various civic organizations, such as Transparency International's Macedonian office, also try to monitor the work of public officials. The results are still pending. A number of high-ranking officials were investigated for corruption following the change of government in 2006. However, as the previous government also initiated anti-corruption measures when it entered office, observers have cautioned that these campaigns may be driven by partisan political motives. It remains to be seen whether the new coalition government is more committed to the fight against corruption than previous governments.

Prosecution of
office abuse

Civil liberties are respected in principle, but especially volatile segments of the population are often denied their basic civil liberties. The authorities' selective application of established law especially harms Roma and the poor. Both individuals and non-governmental organizations have complained of instances of

Civil rights

torture and abuse at the hands of the state security forces. Women are often victims of domestic violence, sexual trafficking, rape etc. Unfortunately, society is male-dominated, the police are mostly male and there has consequently not been much sensitivity to the abuses suffered by wives or victims of sexual trafficking. The police have improved operational capacity and are increasingly trusted by the various ethnic communities. An ombudsman is collecting complaints and publishes reports on breaches of civil and human rights. Special administrative courts aimed at improved protection against violations of civil rights have yet to be established.

4 | Stability of Democratic Institutions

Democratic state institutions perform their functions without major inter-institutional conflict. The main opposition Albanian political party, the Democratic Union for Integration, has withdrawn from parliament, protesting against its exclusion from government despite the fact that it had won a majority of the votes within the ethnic Albanian community. Under the previous government, the other Albanian party DPA also boycotted parliamentary sessions for nine months after having been defeated by the DUI in the 2005 local elections. Since March 2005, local government has gained new, extended powers free from the threat of meddling by central authorities. Relations between the central government and the president are complicated whenever the president is not a member of the ruling party. Institutions that monitor, evaluate and audit the work of the government have not been very effective. Parliamentary committees have been especially weak in this regard, since their monitoring function has been hampered by partisan politics.

Performance of democratic institutions

Following the improvement of inter-ethnic relations thanks to the implementation of the Ohrid Framework Agreement and legislative reforms, all influential political actors accept democratic institutions in principle and regard them as legitimate. However, the ruling party questions the electoral victory of the current president. Citizens have become alienated by the political process and their electoral participation has decreased – even in voting districts where ethnic Albanians are a majority. In 2006 voter turnout was about 10% lower in districts with an ethnic Albanian majority.

Commitment to democratic institutions

5 | Political and Social Integration

Parliamentary elections in 2006 increased fragmentation in parliament. The electoral coalition led by the VMRO-DPMNE (Internal Macedonian Revolutionary Organization – Democratic Party for Macedonian National Unity) secured 32.3% of the vote and 45 seats in the new parliament. On the other hand,

Party system

the “Together for Macedonia” coalition led by the Social Democratic Alliance of Macedonia (SDSM) won just 23.2% of the vote and 32 seats. The coalition of the Democratic Union for Integration (DUI) and the PDP won 12.2% of the vote and 16 seats in the new parliament. The opposition Democratic Party of Albanians (DPA) won 11 seats with 7.5% of the vote. Four other parties entered parliament: the New Social Democratic Party (NSDP), led by Tito Petkovski, who was formerly with the SDSM, winning seven seats; VMRO-Narodna, led by Ljubcho Georgievski, winning six seats; and DOM and PEI, each with one seat. The Macedonian party system reflects historical tendencies, as the main political parties, the Social Democratic Alliance of Macedonia (SDSM) and VMRO-DPMNE, were founded on the traditions of the former League of Communists, a historic organization linked with the Macedonian revolutionary/liberation/nationalist movement of the early 20th Century. The VMRO-DPMNE became an observer to the European Peoples Party in May 2007. The leading political parties among the Macedonian Albanians were founded around different ideas on how best to achieve political reforms to improve the status of this community. Among the parties of ethnic Albanians, ideological differences do not play an important role. SDSM and VMRO-DPMNE have followed their respective ideological stance more in recent years than in the early 1990s. Since 1990, the party system has been dominated by these two main parties who have changed power with no new major players appearing on the scene. Polarization has been high among the parties representing the ethnic Albanian population, although relations between SDSM and VMRO-DPMNE have also been strained at times. It is difficult to see how the main political parties, Macedonian or Albanian, articulate and aggregate societal interests and mediate between society and state. On the contrary, the main political parties represent narrow interests with hardly any reflection on the welfare of the societal groups they supposedly represent.

Macedonia’s civil society is relatively well differentiated but weak and highly fragmented. The voices of interest groups are hardly heard. The unions, once the major player and partner in the tripartite social dialogue, have lost much of their influence, and their recent fragmentation has made this worse. Particular economic reforms, such as the liberalization of the telecommunication market or the sale of the Electric Distribution Company, have drawn great public interest, even political protests.

Interest groups

Surveys by the UNDP, the Institute for Sociological, Juridical and Political Research, and the Institute for Democracy do not question support for democracy in Macedonia, assuming that it is high. Yet citizens’ trust in the institutional underpinnings of democracy has been very low. The low voter turnout (around 50% in the 2006 parliamentary elections and the 2004 presidential election) indicates disappointment with the way democratic norms are put into practice.

Consent to
democratic
norms

A big part of Macedonian society functions by the use of social capital. Networking or using “connections” (vrski) is often necessary in order to complete even the simplest assignment or job. The level of interpersonal trust is much higher among ethnic Albanians than among Macedonians. This has been largely a result of the urbanization process that Macedonians have gone through since the late 1950s.

Associational
activities

The development of NGO activities is hampered mainly by a lack of resources. Since 1999, there has been a boom in the sector due to the increased availability of funds. An estimated 5,500 NGOs were thought to be present in the country. Various international donors, each with its own agenda, supported the NGO sector in Macedonia, frequently not coordinating with local needs and NGO demands. Major donors take a top-down approach, offering funding to local organizations only if their programs and projects match the priorities established by the foreign sponsor. Very few well-organized and professionally working NGOs have established partnerships with international organizations or donors in which their assessments of local needs are seriously taken into account. These international actors are increasingly leaving the Western Balkan region and Macedonia, leaving many NGOs in peril. The remaining large grants by the rapidly retreating donors are left to be managed by the largest local organizations. To a certain extent, fundraising is difficult for local NGOs that do not have good relations to such local organizations that are now in the position to provide grants. Key NGOs, such as the Open Society Institute Foundation and the Macedonian Center for Intercultural Cooperation, dominate the activities and the funding of the local civil society organizations. Few civil society groups will be financially viable in the long term. Although a new law on sponsorship and donations was enacted in April 2006, providing tax incentives for donations and sponsorship by local or foreign legal or physical entities, local philanthropy and volunteerism are almost nonexistent, and the participation of religious groups in charitable activities is minimal.

Macedonian civil society has yet to attain the critical mass needed to become a serious actor at either the national or the local level. Instead of relying on funds on a per-project basis, local NGOs would be better served if core funding were available in key sectors. Macedonian civil society groups also lack sufficient organizational capacity to sustain their work. Most NGOs are poorly managed, lack professionalism and communication skills, and have few experienced practitioners or trainers.

II. Market Economy

Macedonia is the new business heaven in Europe according to the government's latest slogan in its campaign to attract foreign direct investment. Since independence, Macedonia has maintained macroeconomic stability with low inflation, but it has lagged behind the region in attracting foreign investment, and job growth has been anemic. Per-capita GDP is low; the government estimated it to be some \$2,783 in 2006, and the CIA estimates it to be \$8,600 when adjusted for PPP. Yet a very large portion of the working age population is unemployed or engaged in low productivity or occasional work. The State Statistical Office estimates unemployment to be hovering around 35%. Many of the unemployed are young and without good education. There is a large gray sector (estimated by CIA at no less than 20% of GDP) and a strong remittances factor (estimated by the World Bank at 5% of GDP). The most recent published results on poverty are from 2001, at which time 24.6% of the population lived below the national poverty line of €2.50 a day. Many Macedonians survive on the remittances (totaling approximately one billion U.S. dollars per year) sent by relatives working abroad.

6 | Level of Socioeconomic Development

Macedonia's Human Development Index value is 0.797, its rank, 60th – five ranks lower than its neighbor, EU-member Bulgaria. This indicator shows a medium level of development for Macedonia. Yet segments of the population live a miserable life, socially excluded and marginalized. This in particular applies to Roma and inhabitants of rural areas. The GDI value for Macedonia ranks 49th, with a value of 0.794. Women hold 29.1% of parliamentary seats and make up 51% of professional and technical workers. 27% of administrators and managers are women. Social disparities are high between regions, with the capital Skopje by far exceeding the rest of the country. Macedonia's economic development since independence has been hampered by various factors, both internal and external. Only since the end of the conflict in 2001 and the implementation of the Ohrid Framework Agreement has the economic agenda received due government attention. Economic performance has improved since then but has not lead to a significant increase in the number of jobs.

Socioeconomic
barriers

Economic indicators		2002	2003	2004	2005
GDP	\$ mn.	3,791	4,630	5,368	5,766
Growth of GDP	%	0.9	2.8	4.1	4.0
Inflation (CPI)	%	1.8	1.2	0.9	0
Unemployment	%	31.9	36.7	37.2	-
Foreign direct investment	% of GDP	2.1	2.1	2.9	1.7
Export growth	%	-5.1	-5.7	12.9	8.5
Import growth	%	9.8	-15.2	16.7	2.4
Current account balance	\$ mn.	-357.9	-149.0	-414.8	-81.4
Public debt	\$ mn.	1,264.6	1,437.7	1,536.8	1,613.2
External debt	\$ mn.	1,662.6	1,865.4	2,055.2	2,242.8
External debt service	% of GNI	6.3	5.3	4.6	4.2
Cash surplus or deficit	% of GDP	-	-	-	-
Tax Revenue	% of GDP	-	-	-	-
Government consumption	% of GDP	22.4	20.7	20.0	19.0
Public expnd. on edu.	% of GDP	3.5	3.4	-	-
Public expnd. on health	% of GDP	5.7	5.9	5.7	-
R&D expenditure	% of GDP	0.3	-	-	-
Military expenditure	% of GDP	2.8	2.5	2.6	2.2

Sources: The World Bank, World Development Indicators 2007 | UNESCO Institute for Statistics | Stockholm International Peace Research Institute (SIPRI), Yearbook: Armaments, Disarmament and International Security

7 | Organization of the Market and Competition

Although the foundations of a competitive market economy are by and large assured, Macedonia has problems in implementing laws regulating the freedom of the market. Recent new developments have seen the liberalization of Macedonia's telecommunications market. Since new laws must be adjusted to EU legislation, law-making is and will be aiding the market-based forces. Reforms of the judiciary are aimed at filling the gap between the regulations and their implementation. Public institutions suffer from a number of deficiencies, including widespread corruption and deficient rule of law. Macedonia has

Market-based
competition

become a member of CEFTA as it now has a very liberal trade environment, and it has EU candidate status since 2005.

There is a state anti-monopoly commission especially designed to tackle this issue. Yet in practice, certain sectors have remained under the power of monopolies and public enterprises owned by central and/or local authorities for a long time. The laws are applied only sporadically, leaving bureaucratic corruption to take its toll.

Anti-monopoly
policy

Foreign trade has been extensively deregulated, and there is no fundamental state intervention in free trade. This particularly applies to the treatment of foreign investments and stockholding. There are no restrictions or controls on payments, transactions, transfers or the repatriation of profits.

Liberalization of
foreign trade

The banking sector remains underdeveloped, especially in comparison with neighboring countries such as Serbia or Albania, not to mention EU members Bulgaria and Greece. Changes in banking sector laws envision easier access to the local market for foreign banks. At least one big player in the European banking business is negotiating a takeover of a local Macedonian bank. So far, local banks have been bought by Bulgarian, Slovenian and Greek investors. At the moment, the banking sector remains highly concentrated, with four banks holding about three quarters of total deposits. High credit costs for small and medium-sized firms remains a main problem for Macedonia's economic development. The government has tried to ease access to capital for small and medium-sized enterprises, which comprise 99% of the economy, by setting up the State Guarantee Fund. Capital markets are still weakly developed.

Banking system

8 | Currency and Price Stability

The rate of inflation, which was in double digits in the early 1990s, has remained very low ever since. The Macedonian central bank NBRM is an independent institution with a strong governor. The head of the central bank's prerogatives would even be strengthened if the new draft law on banks passes. Since the mid 1990s, monetary policy continues to be based on a de facto near-peg of the denar to the euro. The peg has been maintained at approximately the same rate for nearly eight years, only shaken temporarily during the recession of 2001-2002. Foreign reserves grew in 2006, reaching record levels in early 2007.

Anti-inflation /
forex policy

Over the past decade, different governments have generally adhered to strict monetary and fiscal policies as advised by the IMF. Macedonia's debt is regularly serviced, and the debt to the Paris and London Clubs of Loaners has already been paid back in full. It is not clear how the government's new tax policies and especially the introduction of the flat tax will affect government revenues for 2007.

Macrostability

9 | Private Property

In general, property rights and property acquisition in Macedonia are adequately defined with regard to the acquisition, use, benefits and sale of property. Yet exceptions occur, especially in cases when restituted land or buildings are being acquired. Huge chunks of cities and towns without urban plans have no defined land titles. The main problem lies in the fact that property rights are not adequately protected in practice because the judicial and administrative systems are still flawed. For example, the national office of the Cadastre is remarkably poorly managed and corrupt.

Property rights

The legal framework for a functional private sector exists in Macedonia. But to make laws fully effective, the court system needs to be strengthened. A company can be registered in just three days. Although private enterprises form the backbone of the national economy, only a few public companies remain. New tenders for the privatization of public companies continue. The privatization of an electricity-producing plant in Negotino was opened recently. The new government plans to undertake further privatizations.

Private enterprise

10 | Welfare Regime

Macedonia's public social safety nets exist but are not sufficient to compensate for poverty or other risks, such as old age, illness, unemployment or disability. The expansion of informal employment has further eroded the effectiveness of the social insurance system. Poverty is widespread among the unemployed, who are often poorly educated as well. Roma are particularly disadvantaged. Although healthcare services are available to all citizens in theory, this sector is underfunded and in a serious crisis. The crisis reflects the level of services offered; patients often asked to pay even for most basic medications or treatments themselves. Macedonia introduced a two-pillar pension system in January 2006, but the results are still not conclusive.

Social safety nets

In theory, equality of opportunity exists for all citizens. Yet the uneducated, Roma and women are faced with more obstacles to success in life. A special program has been envisioned since 2001 to tackle the low participation of ethnic minorities, especially Albanians, in public administration. The program has been quite successful in raising the number of minority members in public service. Besides the electoral requirement to have at least 30% of women on party nomination lists, there are hardly any mechanisms to promote the advancement of women. Persons with disabilities and the socially disadvantaged have even fewer chances for advancement. Nepotism is a widespread phenomenon undermining the equality of opportunity.

Equal opportunity

11 | Economic Performance

Following the war-like crisis in 2001, the Macedonian economy has slowly but surely picked up pace, GDP growing by 0.9% in 2002, 3.2% in 2003, 4.1% in 2004, 4% in 2005 and 4.3% in 2006. In the same period, exports doubled from \$1.1 billion in 2002 to 2.3 billion in 2006. Foreign direct investment has also grown, from \$82 million in 2002 to 320 million in 2006. There is a growing trade deficit of \$1.2 billion. Macedonia's current account balance is \$-0.2 billion. Attracting foreign direct investment is key to creating new jobs as the local private sector has been unable to do so on its own. The government has realized this and put FDI high on the agenda.

Output strength

12 | Sustainability

Waste management, deforestation and air and water pollution are Macedonia's primary environmental problems. Only one regional waste management facility exists (JP Drisla), and it is located near the capital. In the rest of the country, garbage is not properly collected or processed. Environmental awareness in society at large and among lawmakers has grown in recent years, but it is still very low. Environmental concerns tend to take a back seat to growth considerations. Macedonian civic organizations have recently been able to successfully lobby for a reassessment of a proposed highway route around the capital city due to ecological concerns for the inhabitants of a nearby village. Ecologically sustainable growth gets only scant attention and is not reflected in the institutional framework. Wastewater treatment plants do not exist. Although sewage networks exist in the cities, wastewater is merely collected and then released into rivers. There are rare examples of projects supported by a donor community, such as the Lake Ohrid environment protection project.

Environmental policy

Education and training facilities are of very poor quality. Government spending on research and development is minimal. Education is a priority of the new government, which aims to open a new public university and make secondary education mandatory for all citizens. Nevertheless, the Macedonian education sector is underdeveloped. The sector's lagging behind is a significant obstacle to Macedonia's further development in all areas considered here. Quantitatively and qualitatively, investment in education, training, research and development is rather low. State expenditures on education are also remarkably low.

Education policy / R&D

Transformation Management

I. Level of Difficulty

The level of difficulty of Macedonia's transformation to a consolidated democracy is high. Not only has the country had problems being internationally recognized due to Greek objections to the name, but Macedonia has also gone through painful economic adjustments, both in terms of transformation to a market-based economy and losing traditional trade links with former Yugoslav republics. Inter-ethnic issues have strained the political leadership's governance capacity for about a decade. Much needed economic structural reforms have been met with fierce resistance from workers and managers alike. The existence of a weak civil society vulnerable to an external donor agenda has contributed to difficulties. Macedonians lack quality education, and although social tensions have not dramatically escalated yet, they have posed additional problems to the political leadership's governance capacity on occasion.

Structural
constraints

The country's civil society was suppressed during the communist era, when Macedonia was part of the Yugoslav federation. Established citizens' institutions, like the Association of Women of Macedonia or the Association of Youth of Macedonia, could not in fact be characterized as non-governmental institutions. In the 1980s, during the period of liberalization from communist rule, Macedonia witnessed the rise of a plethora of civic groups, movements and associations. Following independence, opportunities for the development of civil society became real. In the last 16 years, the number and scope of NGOs in Macedonia have risen dramatically. Many deal with significant societal, political and economic issues.

Civil society
traditions

Although Macedonian society is still split along ethnic lines, conflicts have been reduced through the implementation of the Ohrid Agreement. Today, Macedonian society is free of excessive influence by extremist and intolerant nongovernmental institutions and organizations. In fact, there are no visibly active organizations, private militias, or vigilante groups advocating racist or xenophobic agendas or threatening political and social stability or the country's transition to democracy. Religious conflicts have occurred only within denominations, not between them. The Islamic and Orthodox communities have

Conflict intensity

both witnessed internal conflicts in recent times. Although the societal groups most hit by the economic transition have occasionally protested against government policies, these protests have been peaceful.

II. Management Performance

14 | Steering Capability

Since the beginning of democratic transition, Macedonian political leaders have struggled to achieve an elite consensus on the question of political governance. In the first decade since independence, elite dialogue did not attain sustainable any arrangements to control inter-ethnic conflicts. While the Ohrid Agreement established such arrangements in 2001, party relations and cooperation within public institutions have remained strained. The idea that the government is elected to serve the people is slowly taking root among the current government's political leadership. Yet dialogue with opposition parties and firmly established rules of the game remain elusive. In the period under review, the government led by the Social Democratic Alliance of Macedonia (SDSM) focused on the implementation of the Ohrid Framework Agreement and the reforms required for EU and NATO accession. These efforts were rewarded by the EU, which declared Macedonia a candidate country in December 2005. However, the 2002-2006 government failed to deliver on its promises to provide more jobs and to fight corruption. Only to a certain extent was the political leadership able to prioritize and organize its policies according to strategic aims beyond the immediate concerns of political competition. The government increasingly lost sight of the main transformation goals — tackling the issues of unemployment and creating new jobs, eliminating corruption, strengthening the rule of law and the state. These problems and internal conflicts within the SDSM contributed to its defeat in the 2006 national elections. The new government coalition is led by VMRO-DPMNE (Internal Macedonian Revolutionary Organization – Democratic Party for Macedonian National Unity) and includes the Democratic Party of Albanians as the main coalition partner together with a number of smaller parties. This coalition holds 65 seats in the 120-seat national parliament. Although the new government is reform-oriented, it lacks tact and skills in diplomatic maneuvering in its relations with opposition parties, especially the Democratic Union for Integration (DUI). DUI and the Social Democrats have both criticized the government for not having enough “political will” to communicate, even when this was the government's clear intention. Only

Prioritization

pressure from the international community has forced elites to talk to each other. Due to parliament's weak control capacity, the government has dominated the assembly by introducing laws to be adopted or amended. This governmental dominance has been limited by the cohabitation between the social democratic president and the center-right government. In addition, the Macedonian political system features an informal rule according to which the government is composed of a multiethnic coalition. Governing such a coalition requires advanced political skills and accommodation, which in turn necessitates much political maneuvering and compromise, making the concentration of power unfeasible. The pursuit of the long-term aim of European Union and NATO accession are two main priorities of the Macedonian political leadership. Another strategic aim is adherence to the Ohrid Framework Agreement, especially regarding the measures to increase ethnic minorities' participation in public administration and the decentralization process. As with a number of other countries in Eastern Europe, Macedonia's reforms have been focused on two issues simultaneously in the last 16 years — state-building and setting up the legal base for a functioning market economy.

The new government has picked up the pace of the reforms. The adoption of a new police law in October 2006 represented a major step in the reform of the police and a key priority of the European Partnership. The delayed adoption of this framework law had impeded the decentralization of the police as stipulated by the Ohrid agreement and the creation of a new appointment system for police chiefs. Many bylaws, ordinances and administrative rules currently being prepared need to be adopted before the new police law can actually be implemented. The most urgent bylaws are those regulating the election of the municipal police commanders by local government. Employees in the ministry of interior will also need to be trained. Both policemen and civil servants will have to get familiar with the competencies this law grants them. In 2006, reforms continued in the ministry of defense and in the army, driven by the prospect of Macedonia's membership in NATO. As part of the reforms needed to prepare for NATO membership, the law on defense was amended in May 2006 to allow for establishing a professional army. The entire process of transformation is due to be completed by the end of 2007. In September 2006, the new government adopted a national program for NATO membership. The reform also takes the objectives of the Ohrid Framework Agreement into account in terms of achieving equitable minority representation in the civil service. According to the constitution, the commander in chief of the armed forces is the president, while a civilian minister of defense oversees all security- and defense-related activities. In 2006, Macedonia made progress in the implementation of the Stabilization and Association Agreement, although it did not meet all of its obligations. The two main exceptions are the issue of telecom liberalization and the protection of the intellectual property. Improvements are in sight. The new government has

Implementation

made a public tender for a third mobile operator and has announced that it will liberalize the telecommunications market. Functioning institutions and administrative procedures are crucial for reform implementation. Serious shortcomings are still obvious in these areas. Prior to the 2005 municipal elections, a new law was adopted on territorial organization of local government. The law was very important for the decentralization reform process, which is one of the key results of the Ohrid Framework agreement. Before the Ohrid accords were implemented, minorities and ethnic Albanians in particular were underrepresented in the public sector. In particular, the number of Albanians had been low throughout the 1990s in sensitive areas of public administration, such as the police. According to available data, Albanians only filled some 7% of positions in the public, mixed and cooperative employment sectors. In 2006, the process of recruiting qualified minority members continued, with the new government pledging €2.5 million for this purpose for 2007, three times more than the money spent in 2005 and 2006. The numbers are steadily improving. In all state institutions 81% of employees are Macedonians, 13% Albanians, 2% Serbs, 1.4% Turks, 0.6% Roma and Vlachs. In some institutions, like the ministries of education, economy and local government, the percentage of ethnic Albanian employees corresponds to proportional representation. All these ministries were led by ethnic Albanian ministers from 2002 to 2006.

The new government has promoted a new approach to policy-making that includes thorough reliance on policy analysis, including monitoring and evaluation. Reforms have been enacted in various sectors to foster pro-market solutions. Health care reforms, reforms in the educational sector and telecommunications, and the introduction of the lowest flat-tax rate in Europe coupled with an excellent public relations campaign are clear signs that the new government is innovative. Yet the crucial test for the new government to show flexibility and innovation will be the continuation of reforms in the judiciary, since improving the independence and the efficiency of the judiciary remains a major challenge for Macedonia. So far, the government has demonstrated its capacity to push through this reform. In 2005, the constitution and legal framework were amended to allow for the implementation of judiciary reform. In 2006, the government continued the reforms of the judiciary. Thus, the budgetary resources allocated in 2006 to the judiciary have increased slightly compared to 2005. A law was passed to found an academy for training judges and prosecutors, but the academy is not yet operational and the selection of its director and executive director has been delayed. Candidates for a basic court will have to complete a training course at the new academy. Admission will be based on an anonymous examination. A law on mediation was adopted in May 2006 with the intention of reducing the backlog of unresolved cases (assuming people will use the services of mediators). Sixty mediators have been appointed. New laws on courts, the Judicial Council, misdemeanors and administrative

Policy learning

disputes were passed in May 2006. Apart from the law on the Judicial Council, however, which entered into force in September 2006, the other laws will not enter into force until 2007.

15 | Resource Efficiency

The new government has already made attempts to make use of the available economic, cultural and human resources to pursue its transformation policy. It brought a number of young successful Macedonians living in the United States back to the country. Their experiences are important for promoting Macedonia to foreign investors and undertaking economic reforms. In April 2006, the government amended its rules of procedure to further improve its strategic planning and decision-making. As far as other human resources are concerned, government efficiency suffers from a poorly paid huge public administration that often lacks the skills necessary to implement the reforms. The European Union criticized the administrative staff changes made by the new government partly because many discharged personnel had passed intensive long-term training financed by the European Union. One serious issue is the lack of knowledge and skills to cope with the reform process and the new responsibilities given to local self-government.

Efficient use of assets

The government coalition is comprised of political forces that have different ideological standpoints. While the VMRO-DPMNE (Internal Macedonian Revolutionary Organization – Democratic Party for Macedonian National Unity) is a right wing Christian democratic party, one of its key junior partners, the New Social Democratic Party (NSDP), is self-proclaimed social democratic (although the leader of the so-called New Social Democratic Party claimed to be much closer to the political program of the conservative VMRO-DPMNE than to the Social Democrats) while the DPA caters to the interests of the Albanian electorate in Macedonia, which is not very interested in left- and right-wing ideologies. Therefore, government policies are difficult to coordinate at times, especially since the minister of economy belongs to the NSDP. To limit the powers of this ministry, the coalition agreement delegated the basic department and other fundamental departments to the ministry of finance, led by a VMRO-DPMNE politician. Coordination between central and local government is often poor. Although the central government announced it would take action against owners of illegally constructed buildings, few local governments responded to the call to demolish such objects since this is costly and not very popular. Moreover, while the central government plans to increase investment levels, municipalities complain that it refuses to amend the law so that state-owned land can be given to local government. Local authorities claim that they can bring in investors more easily if they can negotiate the sale of land in their municipality

Policy coordination

directly with interested parties instead of waiting for the central government to approve such deals. Finally, the coordination between the president and government regarding foreign affairs has often been poor, even on important issues such as Macedonia's relations with Kosovo.

One of the main policies of the government has been to tackle corruption. The prime minister even reported that he turned down a Serbian company's attempt to bribe him for \$3 million. The company threatened the prime minister with a slander lawsuit because there is no proof of the attempted bribe so far. A new law forbids doctors working in public hospitals to be simultaneously employed by private medical institutions. Since corruption in the health sector has been staggering, this measure is clearly aimed to prevent it. The State Commission on Anticorruption was established in November 2002. A law permitting citizens to not pay for goods and services if they are not given a VAT receipt upon payment is another measure aimed at preventing corrupt behavior. Traders and service providers often avoid paying taxes or agree with customers to record transactions incorrectly. This law directly aids law-abiding citizens in the fight against corruption.

Anti-corruption
policy

16 | Consensus-Building

Compared to the SDSM-led (Social Democratic Alliance of Macedonia) government, the new government has not made many improvements in the process of consensus-building. EU-Enlargement Commissioner Rehn criticized the government's lack of dialogue and consensus-building. He advised Macedonia's politicians to replace confrontation with dialogue and obstruction with constructive criticism. In Macedonia, all significant political and social actors agree on a stable market-based democracy as a long-term strategic aim. All parties agree that Macedonia should become a member of the EU and NATO, although their ideas of how to reach that goal vary considerably.

Consensus on goals

There are no clearly antidemocratic veto powers in Macedonia. Yet the Democratic Union for Integration's (DUI) behavior following the elections as well as the continuing speculations by DPA (Democratic Party of Albanians) leader Arben Xhaferi about the creation of Greater Albania indicate possible dangers for the democratic system.

Anti-democratic veto
actors

Macedonia's political leadership's record in managing the main political cleavage has been positive since the Ohrid Framework Agreement. Slowly but surely, Macedonia's key political actors have learned the blessings of consociational democracy and how to mitigate ethnic divisions. Political decentralization has helped the process as ethnic minorities now have a greater say in local matters. The winner-take-all attitude of new governments provokes

Cleavage / conflict
management

conflicts between democratic parties. This is not necessarily based on political cleavages, but on the exercise of power.

The Macedonian political leadership has generally ignored civil society actors. The rise of the think-tank sector has proven difficult to ignore as numerous analyses, surveys and commentaries are produced by experts in such civic organizations. In 2006, the active involvement of NGOs in public policy-making and reforms has grown. A number of think tanks are being noticed due to their offering policy analyses and making proposals for new and amended legislation. The government adopted a strategy for cooperation with civil society in June 2006. Following a long period of discussion, amendments to the 1998 law on citizen associations and foundations were debated in parliament in February 2007. Yet not all the changes are supported by the civil sector as the new government has altered the proposed amendments significantly. As reported by the media and the representatives of FOSIM, some of the amendments to the law would allow “concerned citizens” or the public prosecutor to intervene in the work of NGOs if a complaint is made that a given NGO does not follow its own bylaws. A shutdown of the NGO is envisioned in this case. Another problematic amendment to the law prohibits NGO employees to be part of the executive organs of the given citizens’ association. These and other similar amendments to the law would further complicate the development of the NGO sector in Macedonia. Although the government respects the right to form and join civil society organizations, including free trade unions, it is hardly receptive to policy advocacy by interest groups, policy research centers and other nonprofit organizations. Government officials rarely engage civil society groups by inviting them to comment on and influence pending policies or legislation. The media, on the other hand, are more accessible to civil society groups and serve as independent sources of information and commentary, thus contributing positively to the country’s civic life.

Civil society
participation

Lustration has only recently been put on the agenda in Macedonia. Other Central European countries went through this process immediately after the collapse of the communist system or soon thereafter. In Macedonia, however, it was not until early 2007 that a draft law on lustration was discussed in parliament. It is not clear at this stage whether there will be sufficient data to identify perpetrators of past injustices in the communist system. On the other hand, a number of crimes were committed during the war-like crisis in 2001 that merit the public’s attention. At least three of the four cases involving Macedonia investigated by the Hague War Crimes Tribunal fall into this category. It is difficult to imagine a reconciliation between the perpetrators and victims of past injustices that goes beyond the Macedonian amnesty law, which pardoned all members of the National Liberation Army for all deeds except those that fall under the jurisdiction of the Hague Tribunal.

Reconciliation

17 | International Cooperation

The Macedonian political leadership works with bilateral or multilateral international donors and makes use of international assistance. In the past, however, cooperation with international agencies such as the World Bank has not always facilitated significant policy learning and improvement. World Bank aid in the reform of the health sector is a prime example of the failure to transfer policy knowledge to local institutions. Expert help is provided by various EU agencies and programs as well as by partner countries such as Slovenia. The EU accession process has provided a strong impetus for reforming Macedonia's public administration.

Effective use of support

The new government promotes Macedonia as a hot place to invest and as a reliable international partner in the Balkan region. Recognizing the progress of democratic and economic reforms in Macedonia, the EU concluded its Stabilization and Association Agreement with Macedonia. In general, both the SDSM-led (Social Democratic Alliance of Macedonia) government and the current one act as credible and reliable partners in Macedonia's relations with the international community.

Credibility

Macedonia's willingness to cooperate with neighboring countries in regional and international organizations is hindered by persistent Greek nationalistic objections to the country's official name as used in international forums. Even this obstacle does not prevent the Macedonian leadership from pursuing a cooperative relationship with Greece in various spheres and especially with regard to the economy. Similarly, despite Bulgaria's illiberal treatment of its Macedonian minority, the leaders of the two countries have developed cordial relations. Macedonian political leaders cooperate well with Albania in their shared goal of joining NATO. Starting this year, Macedonia and its Western Balkan neighbors are members of CEFTA. On the whole, political actors actively strive to build and expand cooperative international relationships. In the recent past, Macedonia was very active in the so-called Adria Group (Albania, Croatia and Macedonia), whose members aspire to become NATO members. Macedonia also took a very constructive approach in the regional SEECP process and the Stability Pact for SEE.

Regional cooperation

Strategic Outlook

Macedonia's new government has introduced a number of policy measures aimed at improving the economy through reducing bureaucratic obstacles to doing business, liberalizing telecommunications markets, attracting foreign direct investment by lowering taxes, a public relation campaign in Western countries and introducing a regulatory guillotine to lower the number of unnecessary laws and regulations. The reform process is expected to continue throughout 2007. Further harmonizing of Macedonian legislation with EU law is expected. As soon as the new government and the opposition address the EU Commission's criticism regarding the lack of political dialogue, and if there is a notable will for consensus, a date will likely be set for the beginning of negotiations with the European Union at the end of the Slovenian EU presidency in mid-2008.

Ethnic relations are not supposed to be affected by the upcoming solution to the status of Kosovo. Even if there are political complications concerning Kosovo, Macedonia has few reasons to worry. All political elites accept the political system despite occasional dissatisfaction with electoral results or the way in which specific governments function. Notwithstanding European enlargement fatigue, Macedonia is firmly committed to EU integration, having been granted candidate status in the winter of 2005. As it awaits a date for the beginning of negotiations, Macedonia has the support of the whole international community.

Finally, prospects for Kosovo's independence will likely hinge upon responsible policy-making on the part of local elites. These factors will reduce the possibility of new violent outbursts if Kosovo gains the status of a sovereign state. Indeed, Macedonia will continue implementing the Ohrid Framework Agreement agenda and the affirmative action program aimed at increasing the representation of ethnic minorities in public administration. In the spring of 2007, Macedonia reached an agreement with the European Union on the liberalization of the visa regime. This measure was expected to boost the mood among regular citizens and elites who travel frequently. The European Union and other Western states and organizations should continue to provide political support and financial assistance to Macedonia until economic recovery picks up in pace. Giving Macedonia a date for the start of EU negotiations will not only help the government's reform agenda, but will also be a stabilizing sign for the region itself.