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BUSINESS CLIMATE LEGAL AND INSTITUTIONAL REFORM  
DIAGNOSTIC:

# MACEDONIA'S AGENDA FOR ACTION

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**Executive Summary**

**March 2009**

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**DISCLAIMER**

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## Macedonia at a Critical Juncture

Macedonia, or the Former Yugoslav Macedonia (FYROM) as it is officially known by the United Nations for the moment, seems to have come through the catastrophes of the Yugoslav collapse a stronger, prouder and more resilient country that is ready to do business with the region, Europe and the rest of the world.

In spite of continued domestic political tensions, the lingering vestiges of a weak socialist economy, and some difficulties finding its *place in the world* – including the latest round of debate with Greece over just what the Macedonians may call themselves – the country is moving forward with increased political and economic reform.

The assessments of the business environment conducted by USAID in 2000, 2003, and 2005 provide a moving picture of Macedonia's business environment reform since Independence in 1991, but in order to continue working toward a common set of goals, this reform must be reexamined on a regular basis. The purpose of this assessment is to build on previous reports and provide the public and private sectors, civil society, and the donor community with an intuitive guide to the current state of business environment reform in Macedonia as well as recommendations to improve currently existing weaknesses. With this purpose in mind, the report should be used as a unique addition to the collection of tools available to assist in programming donor funding, informing policy, educating investors, and aiding research and analysis.

## The Diagnostic Process

The in-country portion of this diagnostic took place from October 5 to 17, 2008, when a team of consultants traveled to Macedonia to study the country's business environment. The team conducted over 150 interviews across the business environment, including national and local officials, multi-national and SME owners/directors, agricultural enterprises, business associations, representatives from the banking and lending sector, and many others.

### USAID/BizCLIR Diagnostic Team Local Team

Samir Latif	Local Team Senior Advisor
Kiril Minoski	Employing Workers
Marija Ignatova	Registering Property
Voislav Ilievski	Starting a Business

### Traveling Team

Mark Walter	Trading Across Borders, Enforcing Contracts
Judge Charles Case	Closing a Business, Getting Credit
Laura Jones	Team Lead, Protecting Investors

Interviews and observations took place in Skopje, Tetovo, Bitola and Stip. The team's objective was to obtain a broader picture of Macedonia's enabling environment for business and trade than in the previous reports, which were based solely on interviews in Skopje. Questions elicited a variety of perspectives and viewpoints, and sought explanations for how a certain subject works in all pertinent communities, whether urban, suburban, or rural.

The diagnostic culminated in a roundtable presentation and discussion on October 17, attended by representatives from throughout Macedonia's public and private sector. At the roundtable, team members introduced their preliminary observations, which were then subjected to feedback and elaboration from more than 50 participants. Electronic audience voting technology also permitted some unique data to be gathered anonymously, and motivated full audience participation.

**Recommendations.** Each chapter offers a set of recommendations drawn from the key findings in each chapter, taking into account current reform capacities, opportunities, and evident will to reform. In light of Macedonia's commitment to boosting its Doing Business scores, the recommendations are divided into those that relate directly to the areas of the Doing Business inquiry, and those that are less directly related, but concern other key aspects of the business environment. In addition, as this assessment was conducted under USAID's

Macedonia Business Environment Activity, recommendations falling under the mandate of the project have been marked with an asterisk in the Appendix to the full report.<sup>1</sup>

## Main Findings

The 2005 report found that Macedonia's legal framework was already relatively well harmonized with international standards at the time of that report's publication, leaving little room for improvement in that area. At the same time, that report noted a need for improvement in the implementation and enforcement of the legal framework, as well as in the social dynamics hindering reform.

With respect to implementation, the 2008 assessment team found five findings that cut across the 8 BizCLIR categories described in detail in the full report:

- Lack of consistent dialogue between public and private sector institutions
- Slow development of a culture of private sector competitiveness
- Low institutional capacity overall to implement legal framework
- Inadequate and non demand-driven Workforce Development
- Inefficient judicial dispute resolution system

A brief explanation of each finding is provided below including a summary of the team's recommendations to target these obstacles.

### **I. Dialogue among and between various public and private sector actors needs to be improved before meaningful economic growth can advance—**

There is a burdensome multi-level communication breakdown in Macedonia: within the public sector, between the public and private sectors, and within the private sector.

Without these three types of dialogue, private sector firms are like small islands in a fog. They cannot effectively advocate for the reforms that

will most help them compete, and they cannot take advantage of the natural synergies available through cooperation with related firms, both horizontally and vertically.

Likewise, government is unable to create a united front in facilitating economic growth, and cannot be responsive to the needs of the private sector.

Mistrust seems to be one of the common threads in the failure of dialogue. The private sector still mistrusts a government that is new and still somewhat infirm, and government, whether this one or its predecessor, shows troubling signs of viewing the private sector as a *burden* to policy development.

In order to build trust within the public sector, within the private sector, and between the two sectors, dialogue must be facilitated by external organizations such as donors and associations. Training must be provided to associations and members of each sector on how to effectively carry out these dialogues and these external organizations must be acquainted with scenarios in which this dialogue has functioned properly elsewhere in the world.

### **2. Private Sector Competitiveness is severely lacking and would benefit from focused, sector specific, demand-driven assistance –**

This crosscutting area follows directly from the discussion on dialogue. What little attention has been given to the private sector has had limited effect partly because it has been too focused on broad swaths of the private sector via the national Economic Chamber. Further, competitiveness programming has been channeled through those whose entrenched interests run counter to the growth of a vibrant new cadre of entrepreneurs.

For government, donors, and civil society to be effective in developing a competitive private sector, they must become more focused on sector-specific, demand-driven assistance. This includes first actively seeking out the sectors where competition is lacking, and then ensuring that government, civil society, and donors work together to improve competitiveness in these areas.

<sup>1</sup> USAID's Macedonia Business Environment Activity aims to improve the environment for conducting business in Macedonia and accelerate economic growth. The Project accomplishes this by facilitating public-private dialogue on economic policy issues, promoting legal and regulatory reform, improving the fiscal capacity of local government, and advancing labor policies.

### **3. With all the development of complex new EU and WTO compliant legal frameworks, capacity for implementing them remains low–**

Macedonia has expended considerable resources in adopting the new and revised legislation necessary to comply with the EU integration process and its WTO accession commitments. Attendant to the adoption of the rules, however, Macedonia needs to be able to implement and enforce them as well. Macedonia lags well behind in this area. The net effect is that business is now often bound by the new rules; but, with no facility for implementation, business cannot comply. In some cases this results in non-compliance. In others, it means that business simply doesn't get done because in order to trade abroad, especially in the EU, companies need to be able to comply with the rules.

Proper implementation requires the addition and retention of qualified staff in both government and non-governmental institutions. Appropriate incentives must be put in place to make these positions attractive relative to alternatives outside of Macedonia. In addition, ongoing training must be provided to current employees in order to ensure that they understand, and are qualified to carry out, new directives.

### **4. Workforce Development lags well behind Macedonia's desire to participate in the global economy –**

One of the root causes of Macedonia's lack of competitiveness is the absence, in most sectors, of a well-trained workforce. A common thread through most interviews with the private sector and business associations was that business owners in Macedonia rarely rely on managers to direct segments of their businesses. In fact, it is very common that owners are performing *all* the skilled labor in a firm that would otherwise be readily expandable if trustworthy skilled labor could be found.

As in many Eastern and Southeastern European countries, education is focused on increasing enrollment in liberal arts and professional programming, rather than in labor market-driven vocational education and lifetime trade training. In order to improve this situation, a flexible demand-driven approach must be agreed upon by all entities conducting workforce development activities.

### **5. Macedonia needs to renovate the judicial dispute resolution system by creating a commercial court or through the use of dedicated commercial judges and staff –**

All assessment team members recognized the need for reform of the judicial system. Though significant improvement of the existing system's ability to clear cases has taken place, the quality of the outcomes has been called into question in many of the BizCLIR categories.

Two options have been proposed: the first is the establishment of a dedicated commercial court entirely separate from the existing structure. In this case, rules more conducive to the commercial environment can be established, and the likelihood that the system would be co-opted by the larger judicial system would be decreased. The second option is the establishment, within the existing structure, of a group of judges and staff dedicated to the resolution of commercial cases. Here, the advantages are lower cost, potentially better possibilities for oversight by the Ministry of Justice, and fewer backlogged cases during the transition period.

## **Next Steps**

This report concludes that, since 2005, Macedonia has continued to close in on international standards such as EU and WTO regulations, however much work remains to be done. At this time, Macedonia's goals must be reexamined and a well-coordinated strategy for how to target them must be identified. The recommendations in this report provide the building blocks for a comprehensive business environment strategy, however in order to be effective, it must be agreed upon by all donors, government agencies, and civil society actors working to mold the business environment.

The assessment team recommends that a series of working sessions be convened between the major players described above in order to jointly agree to a business environment reform road map for Macedonia over the next three years. Activities should be divided between donors based on currently existing projects and relative funding levels. After three years, an update to this assessment should be conducted in order to monitor progress, review goals and readjust activities based on the needs of the business environment at that time.