

Review of the Measures of the Macedonian Government against the Global Economic Crisis

Center for Economic Analyses (CEA)

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1. Introduction

Due to the global financial and economic crisis the world's economy and each national economy, is currently faced with serious challenges. What are the necessary steps to be undertaken in order to answer the crisis, when there is not enough knowledge about its dimension; what are the consequences on the monetary and the real sector; what should the governments and the central banks undertake as direct and indirect measures to help the economies overcome this period, etc. are some of the questions that need answers in order for each country to protect their national economy from the consequences of the widely spread financial and economic crisis. For this purpose each country is undertaking different measures, compatible with their unique situation.

With the aim to prevent the domestic economy from the influence of the global crisis, the governments have two options when considering implementation of plans. One is to boost the fiscal spending and generate GDP growth and new employments; and the other is to liberate the monetary policy, supporting lower interest rates to help the households and the companies secure finances.

In this situation the Macedonian Government is no exception. In order to help the real sector in overcoming the crisis and stop the influence of the ongoing financial shock on the Macedonian economy, the government undertook several measures mainly based on writing-off some type of liabilities.

In this sense the main goal of this paper is to elaborate the main measures undertaken by the Macedonian Government in order to protect the real sector from the widely spread economic crisis. First of all we will make a short review on the historical background on the financial crises, where did it start and what was the impact on the global economy. After that a short analysis on the measures undertaken by the Macedonian Government will be presented together with some of the plans undertaken by the other countries in the region and the USA. At the end we discuss on the recent global developments and the relevance to Macedonia. We end with conclusions and recommendations to the Macedonian government.

2. Background

The explicit phase of the financial crisis started in the second half of 2007 in the USA. The financial markets were struggling with liquidity issues, reduced asset prices and investment withdrawals. This was the beginning of a financial crisis which was spread all over the world in a short period and forced the governments to face the biggest challenges since the last big Economic Depression in 1929-1933.

The crisis started with the mortgage crisis in the USA which spread onto the banking sector. Namely, in order to create higher profit for themselves and their companies, the

investors were trying to find various instruments that will create and earn higher profits. For that purpose, the USA bankers created instruments which are based on the mortgage loans and the small spending loans and started to sell these as securities. At that point of time a huge number of banks and investment funds from all over the world thought that this type of securities were very attractive, as they were offering high rates of returns for a small amount of risk, and started to trade these “bad” loan based securities creating a bubble that was obvious that in some point of time will blow.

In 2008 we saw the first negative results of the financial crisis in USA. The Lehman Brother Bank started the vicious circle of inverse order and instead of the higher returns from the mortgage securities the investors had a worthless piece of paper. Then the US Government with the president Gorge Bush, prepared a bail-out plan worth 700 billion \$, and repurchased all the bad debts from the banks and started the nationalization process of some of the largest investments banks in USA.

Banks Affected by the Global Crises in 2008

Bank	Date	Status	Website
Fannie Mae	07 Sep	Nationalized	<u>Fannie Mae</u>
Freddie Mac	07 Sep	Nationalized	<u>Freddie Mac</u>
Lehman Bros	15 Sep	Collapsed	<u>Lehman Bros</u>
Merrill Lynch	15 Sep	Taken over	<u>Merrill Lynch</u>
AIG	16 Sep	Part-nationalized	<u>AIG</u>
HBOS	17 Sep	Taken over	<u>HBOS</u>
WaMu	25 Sep	Collapsed and sold	<u>WaMu</u>
Fortis	28 Sep	Nationalized	<u>Fortis</u>
Bradford & Bingley	29 Sep	Nationalized	<u>Bradford & Bingley</u>
Wachovia	29 Sep	Taken over	<u>Wachovia</u>
Glitnir	29 Sep	Nationalized	<u>Glitnir</u>
Hypo Real Estate	06 Oct	Rescue package	<u>Hypo Real Estate</u>
RBS	13 Oct	Part-nationalized	<u>RBS</u>
Lloyds TSB	13 Oct	Part-nationalized	<u>Lloyds TSB</u>

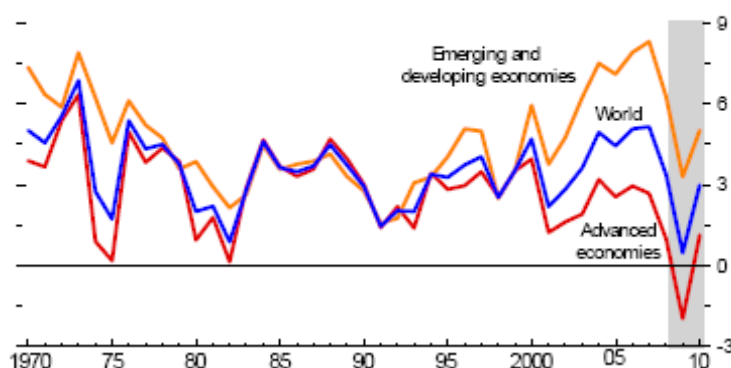
Source: <http://news.bbc.co.uk/2/hi/business/7644238.stm>

Through the market channels of the globalized world the crisis started to take its course into the European and the Asian markets and economies. As the global economic crisis

continues to unfold, spreading from financial markets into the real economy, the economies found themselves struck.

The external demand had collapsed, driven by the recession of Europe's main trading partners. Foreign capital inflows are drying up, especially intra bank lending (between EU15 parents and EU10 subsidiaries) and foreign borrowing by companies. A credit crunch has further undermined the production, as banks weather a crisis of confidence of lending to each other and to the private sector. As a result of sharply decreasing of the demand in advanced countries and worsening of credit conditions of the emerging countries, in January 2009, IMF produced new numbers for the global growth. According to IMF the world's global growth in 2009 is estimated at 3,0% and it is 0,8% smaller then the predictions made in November 2008¹.

Figure 1. GDP Growth
(Percent change)



Source: World Economic Outlook Update, IMF, January 2009

A lot of the developed countries are already in recession and they are struggling with the increasing number of unemployment and decreasing public consumption. On the other hand, the emerging countries will have higher growth from the developed countries but they will be confronted with reduced Foreign Direct Investments (FDI), the net export of the produced goods and services will have a high decrease and the interest rates will go much higher.

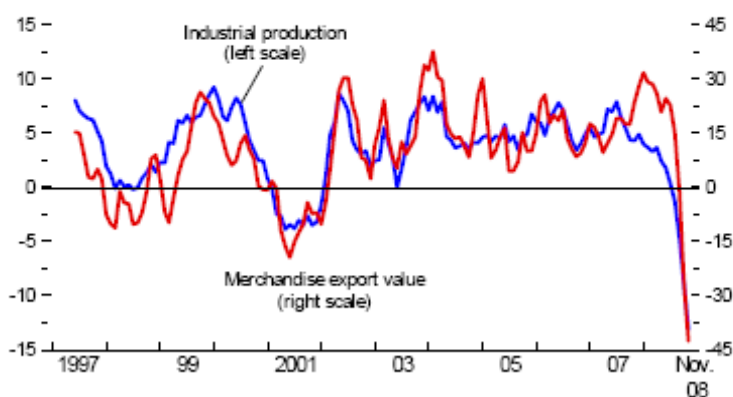
The recession spillover from the old to the new EU member states, already visible last year, will further cut the EU10 average growth rate in 2009. With another downward revision for the euro zone countries in the wake of data on the unprecedented fall in industrial production in the last two months of 2008, projected 2009 growth for the EU10 dropped to below 0,3 percent. A combination of rapidly weakening domestic demand and a deteriorating external environment already pushed two Baltic countries (Estonia and Latvia) into recession in the third quarter, a state last observed in the late 1990s. In

¹ World Economic Outlook Update, IMF, January 2009

Lithuania and Hungary, growth rates turned negative in the 4th quarter of 2008. The slowdown in the 3rd quarter was relatively broad based across countries. Agriculture registered positive growth due to last year's good weather and low base from 2007 (and Bulgaria, Hungary, Romania displaying exceptional growth rates due to a particularly low base in 2007). Moreover, high frequency indicators such as industrial production suggest more countries in the region may enter a technical recession by early 2009.²

Figure 2. Growth in Global Industrial Production and Merchandise Trade

(Annualized three-month percent change)



Source: World Economic Outlook Update, IMF, January 2009

2.1. The Macedonian economy & the crisis

The above given short review indicated that the crisis is spread all over the globe and we can freely say that the Macedonian economy was not spared from the negative flows as well. The global financial crisis had partial impact on the real and the external sector in Macedonia. The main reason for this is the dependence of the production of the Macedonian companies on the European market where in this last months the market demand is on a very low level. The financial crisis had an impact on the financial sector as well which can be seen through the measures undertaken by the National Bank of the Republic of Macedonia, in order to protect the banking sector from the ongoing crisis.

2.1.1. Macedonian financial sector

The Macedonian financial system is characterized by a relatively simple structure and dominated by the banking segment. It is composed of banks, insurance companies, investment funds and the stock exchange. However, the largest share of the financial

² EU 10 Regular Economic Report – World Bank

sector belongs to the banking sector and therefore, the banking sector has the most important role in the stability of the overall financial system.

The banking sector of Macedonia is recognized to be a solid financial system and well capitalized sector (the average capital adequacy ratio was 15% in September 2008³). The Macedonian banks are not relying on foreign credit needs, and therefore they are not largely exposed to the foreign financial markets. In fact, only 2,8% of the total liabilities are based on borrowings from foreign banks. The main source of financing of the Macedonian banks is the household and company deposits. It is important to mention that the saving deposits are insured under the Deposit Insurance fund, which in the case of possible problems will indemnify the savers.

The strict criteria for granting credits enable the Macedonian banks to have quality credit portfolio. Only 7,5% of total granted credits are considered to be non-performing credits. The share of issued credit which are classified in higher categories of risk is 5,5% and in comparison with 2007 it has been improved by 0,2%.

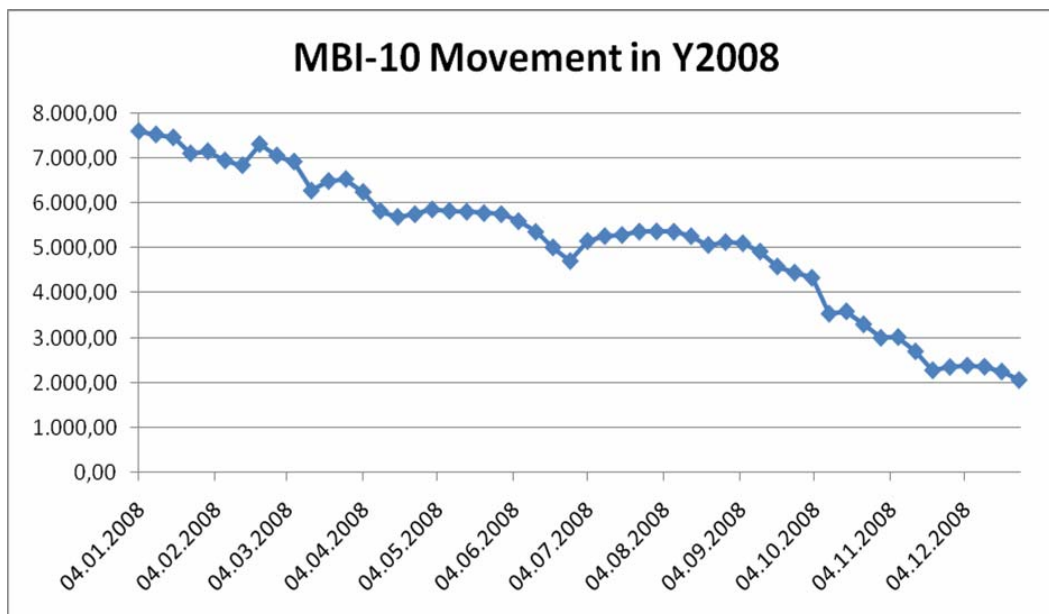
However, we should mention that there are some indirect effects on the banking sector in Macedonia caused by the global financial crisis felt by the increased interest rates of the credits on one hand, and the increased interest rate of the savings deposits on the other hand. It is much easier for the banks to gather Euros through the domestic deposits than to take credits from foreign banks where the financial crisis is ongoing. In addition, in order to limit the possible risk within the banking sector, the National Bank of the Republic of Macedonia (NBRM) has already undertaken preventive measures such as:

- Obligations for the banks to maintain a certain minimum level of liquid assets for covering their liabilities;
- Obligation for allocation of the mandatory deposit at the NBRM if the stock of credit to households exceeds the projected growth rate for each separate month;
- Determination of the type of securities which the authorized banks may purchase and sell abroad etc.⁴

Despite the solid structure of the banking sector, the situation on the Macedonian Stock Exchange (MSE) was different. The negative trends from the financial crisis were firstly anticipated by the foreign investors trading on the Macedonian Stock Exchange (MSE) as they were selling off their share investments within the Macedonian companies in order to protect their investments in their home countries. This created a large disparity in the supply and demand on the Macedonian capital market affecting the share market prices by moving it downwards. As an illustration if we compare the value of the Macedonian Stocks Index - MBI-10, have lost 73,3% from its value in about just one year (01.01.2008 – 31.12.2008).

³ NBRM – National Bank of the Republic of Macedonia

⁴ Dimitar Bogov – Vice Governor of National Bank of the Republic of Macedonia



Source: MSE –Macedonian Securities Exchange

2.1.2. Macedonian real sector

After three consecutive quarters of high growth, the industrial production decreased by 7,6% in the fourth quarter. This led to a GDP decline since the industrial production is participating with 22% within the GDP. The processing industry and the energy sector also decreased, by 8,8% and 21,8% respectively.

That was the first indicator that showed that something is happening and was about to happen within the Macedonian economy. The textile industry and the metal processing industry were the first sectors affected by the ongoing economic crisis. In December 2008, the prices of the raw metals on the world stock markets decreased for more than a half of their value (copper and zinc decreased by 53%, nickel decreased by 63%) compared to the same month last year⁵. Thus, the Macedonian metal processing industry companies were confronted with serious problems. The global market demand for their products was dropping and they were confronted with the decision of permanent or temporary workers' layoffs.

According to the State Statistical Office data, the industrial production index in the Republic of Macedonia in January 2009 in comparison with January 2008 is 83,3. The industrial production in the section Mining and quarrying in January 2009 in comparison with average production in 2005 is decreased by 3,0%, in the section Manufacturing industry is decreased by 24,9% and in the section Electricity, gas and water supply is increased by 17,7%. The industrial production by Main Industrial Groups in January

⁵ www.bloomberg.com

2009 in comparison with average production in 2005 is lower in Intermediate goods industries, except energy by 40,1%, Capital goods industries by 7,7% and in Non-Durable consumer goods industries by 22,1%.⁶

The situation with the present production orders supplying is also unsatisfactory compared to the previous months. In the past three-four months the volume of production of the enterprises is decreasing and it also decreases in the current month. The assessment for the expected production volume is noted to be unsatisfactory. The expectation of the number of the employees is also more unsatisfactory. The stocks of the raw materials and intermediate goods, present supplies of the production with raw materials and intermediate goods, in January 2009 are under normal level, and the present stocks of finished products are above the normal level. In the next period the average purchasing prices of the inputs will increase and decrease of the average selling prices of the finished goods is expected. The enterprises average capacity utilization level in January 2009 is decreased compared to the previous month by 56,3% of normal utilization. The most important influence, limiting the production development in January 2009 refers to the following factors: insufficient foreign demand with 26,0%, insufficient domestic demand with 17,6%, uncertainty of the economic environment with 13,5% and financial problems with 12,1%.⁷

Also, the managers of the enterprises evaluated that the current business situation in the fourth quarter of 2008 is less satisfactory compared to the same quarter of the previous year. The assessment of the present financial situation of their enterprises is much more unsatisfactory than in the same quarter previous year. The expectations for the number of employees in the next period are very pessimistic, and the assessment of the present orders is considered as the most unsatisfactory compared to any other quarters of the previous two years including the three ones of the current one, and the assessment of the present quantity and quality of the enterprise's mechanization and equipment is far under normal level. In the next period an increase of the selling prices is expected, and the total orders (agreements) will decrease. The most important influence, limiting the improvement of the present construction activity are the following factors: shortage of equipment with 20,5%, no demand with 13,6%, shortage of materials with 13,3% and increased financial expenditures (interests) with 11,0%.⁸

Despite this, textile industry was complaining on orders cancelations from their buyers in Europe and USA for 2009. The companies from the construction sector started to publish information on the loss they are generating from currency devaluations in other countries where they have branches. Granit AD Skopje gave information that it has loss from the

⁶ http://www.stat.gov.mk/english/glavna_eng.asp - State Statistical Office

⁷ Ibid.

⁸ Ibid.

currency devaluation in Ukraine for about 3.400.000 EUR.⁹ Beton, AD Skopje also published that some of their largest foreign projects were postponed.¹⁰

3. Measures undertaken by the Macedonian Government

Due to some of the above events, at the end of December 2008, the Macedonian Government, decided to undertake measures that will protect the real economy from the economic and financial crisis already spread all over the world. As all institutions agreed that the crisis will have higher implications on the real sector, it was decided to implement several measures that will have impact to the real economy through aiding the economic entities to get over the widely spread economic crisis.

Our goal in this analysis will be to review and describe what might be the impact on the real economy by these measures and to make a comparison with other measures undertaken by other governments.

The ten governmental measures for protection of the real sector against the implications from the global crisis are:

1. Writing-off the outstanding current liabilities for health insurance, if in the next four years the companies regularly and on time pay the employee's health insurance benefits.
2. Writing-off all accumulated interest payables on the liabilities for social care insurance benefits if the company pays the principal debt;
3. Writing-off all the accumulated interest payables on the unpaid tax liabilities if the company pays the principal debt (VAT, Income tax, Property tax, PIT).
4. Opportunity for the company for postponed payment to the main tax liability if the company secures the debt with banking guarantee of 100% or if the company offers mortgage with a value of 250% of the main liability.
5. Discharging of the companies from the obligation of income tax payment if the total annual profit is retained within the companies (if no dividends are paid).
6. Reduction of the custom taxes (for 498 items)
7. Lower personal incomes taxation rates for the individual farmers.
8. Postponing of the payment operations law for a period of one year, for the companies which have blocked accounts.
9. Transformation of the tax receivables of the government into a permanent share in some companies where the government is already the major shareholder/owner.
10. Reduction the Governmental New Year's spending (2008).

The total package of the measures is estimated to have a value of around 330 million Euros, however it should be stressed that there are no specific information regarding each

⁹ <http://www.seinet.com.mk/Default.aspx?MK&docID=19148>

¹⁰ <http://www.total.com.mk/default.aspx?mId=16&eventId=15442>

single measure's value and the effects of the 2009 national budget. Nonetheless, the review will try to consider and explain the possible positive and/or negative effects on the business sector for every measure separately.

In our review we won't discuss all the measures undertaken by GoM. Measure 8 and measure 10 won't be included in our review due to lack of proper information.

Measure 1: Writing-off the outstanding current liabilities for health insurance, if in the next four years the companies regularly and on time pay the employee's health insurance benefits.

There are a significant number of entities within Macedonia that have an outstanding debt for health insurance benefits. This is one of the obligatory employment benefits which are paid by the employer for the employee that enter the state budget through the Health Insurance Fund. In order to assist the business sector the GoM decided that the entities should be relieved from this outstanding debt for past years as long in the future (four years) these benefits are regularly paid.

According to the GoM the expected value of this measure is about 50 million EUR indicating that this is the amount of the liability of the business sector towards the state budget generated throughout the years.

Since the measure puts a condition for the entities which are liable it automatically indicated that the liabilities are not to be written off immediately from the books of the enterprises and the debt is still outstanding for the next four years. The actual writing-off of the liabilities will occur in 2012 until when the liabilities balance on the company's accounts will stay as such if the condition is fulfilled.

In order for this measure to be understood it should be mentioned the latest change in the payment of the employees' salary with which the employer pays the net salary and all the benefits through one account not allowing the employee to make a selective payments for the benefits and disabling the possibility for receiving net salary if all the benefits and taxes are not previously paid. The implementation of this reform of payment of gross salary will disable creation of such liabilities in the future as it is not possible to pay part of the benefits or just the net salary.

As the first measure considers indirect assistance though "forgiveness of debt" and not a injection of direct funds it can be easily concluded that the companies which are currently liquid enough and will be able to "survive" the implications of the economic crises, will be the only companies taking advantage of this measure.

In a moment of crisis triggered by the financial sector it can be expected that more stringent conditions will reduce the possibilities of the entities to take loans for increasing

their liquidity on one hand, and the measure on the other hand demands significant outflow of cash from the companies again reducing the liquidity of the entities.

At the same time it is more significant to mention that the measure no matter the intention has a negative impact on the other companies which have been regularly paying their liabilities and benefits for the employees. There is a feeling of dissatisfaction and discrimination as they feel punished for paying their obligations.

The writing-off of the liabilities is a measure which is not practiced for the first time and in the past had no significant effects except for creation of double standards-moral hazard (past experience City of Skopje 2007 wrote off 205 mil MKD¹¹ on the basis of old debt for property tax; in 1997 and 2003¹² the GoM at that time undertook similar measures).

Measure 2: Writing-off all accumulated interest payables on the liabilities for social care insurance benefits if the company pays the principal debt and Measure 3: Writing-off all the accumulated interest payables on the unpaid tax liabilities if the company pays the principal debt (VAT, Income tax, Property tax, PIT).

The first measure for writing off the liabilities for health insurance benefits including the writing-off the interest payables as well. The measure 2 & 3 are considering writing of the accumulated interest payables on the pension obligatory benefits and the tax interest payables but not the principal liabilities.

As the measures are similar we will consider them both together. This measure also goes with a condition for writing-off and that is if the main debt is paid by a certain date the interests will be “forgiven” to a specific percentage (100% if paid until 30/04/2009; 75% until 31/08/2009 and 50% until 31/12/2009).

The companies which have earned significant earnings for Y2008 and have a level of liquidity will be able to pay the principal debt, however the liquidity of the companies which are able to pay the principal debt will be reduced depending on the size of the principal debt. The potentially significant outflow of cash for the debt payment may cause reduction of the number of the employees and creation of other liabilities due to reduced liquidity.

It can be expected and assumed that those companies which are not paying their liabilities and taxes way past the due dates are the companies which are facing financial problems including liquidity problems. These companies most likely are possibly not well managed or working with loss and the writing off the tax and other interest payables will have no significant effect on their success as it can be assumed that the companies cannot pay the

¹¹ <http://www.utrinski.com.mk/?ItemID=FE4DFCDBDD0AA8418041B2F06F7772B2>

¹² <http://www.novamakedonija.com.mk/DesktopDefault.aspx?tabindex=0&tabid=2&fCat=1&top=1&Editio nID=257&ArticleID=13056>

principal debt. On the other hand, the successful and export oriented sector companies which have already paid their tax liabilities will have no relieve measures at their assistance but are struck by the crisis.

As the state budget will give up around 50 million by the measure 1, the measures 2 is going to cover this gap in the budget as an immediate cash inflow which with a simple calculation can be expected to be larger than the 50 million as the pension benefits are larger percentage compared to the health benefit insurance (assumption that those who are not paying health insurance are also not paying the pension benefits). At the same time as the principal debt from some of the companies will be paid the state's balance of bad and risky receivables will be reduced.

Measure 4: Opportunity for the company for postponed payment to the main tax liability if the company secures the debt with banking guarantee of 100% or if the company offers mortgage with a value of 250% of the main liability

This measure is comparable with the impact that is expected from the previously analyses two measures. As for the other measures this measures gives the companies the ability to postpone their liabilities by securing the liabilities with a bank guarantee or mortgage.

This measure may be implemented by the companies whose creditworthiness is on a level which enables them to ensure bank guarantees and mortgage for the liabilities and it will aid the companies which need liquid assets by retaining the cash planned for the tax liabilities and use it for other operating or investment purposes to boost development or reduce the risk of the crises.

Measure 5: Relieving of the companies from the obligation of income tax payment if the total annual profit is retained within the companies

The relieving for the companies from the net income tax liability if the net income is retained within the companies will assist the companies which have the capacities for investments assuming that the crisis will not cause distress high enough leading to a net loss. The measure will have a practical impact in 2010 since it refers to the net income liability for the fiscal 2009 while the net income tax liabilities for this year (2008) remain to be paid according to the existing net income tax law. According to GoM the expected savings from this measure are to be around 100 million EUR.

On the other hand practicing this measure may cause distrust in the already weak capital market. The external investors such as the shareholders within the companies are expecting reward for their investment i.e. dividend distribution. The retained net income may positively impact the companies through stimulating investments and potential increase of employment however the companies will reduce the dividend payments. Except for the domestic investors the dividend payments in foreign currency to the foreign investors will also be limited reducing the deficit in the balance of payments.

The changes of the Net Income tax law (for 2009) will enable the companies to pay the tax advances not based on the net income from the previous year but on the unrecognized expenses within the tax balance. This measure will have a positive effect on the companies with positive net income and low unrecognized expenses but will impose additional payments on the companies with net loss and higher unrecognized expenses.

Measure 6: Reduction of the custom taxes (for 498 items)

The reduction of the import custom taxes will have an overall positive effect if the imported goods for which the customs are reduced are raw materials which are scarce in the country and will achieve higher value added with increased exports of finished products.

On the other hand import of goods which are available on the Macedonian market will cause higher competition, reduced demand for the domestic products which may cause an opposite effect for the domestic companies.

The GoM expects decreased revenues of 3 million EUR which are expected to be retained in the real economy.

Measure 7: Lower personal incomes taxation rates for the individual farmers

The farmers within Macedonia are group of individuals which has been hard to control for a very long time when it comes to PIT payment. In line with this in several occasions there have been several ad hoc measures undertaken in this direction. The registered individual farmers who are recorded within the PIT system are paying the tax is very small (around 1.500) compared to the agricultural households within Macedonia which is estimated to be around 90.000.

Most of the farmers have not paid any PIT in the last decade due to the cadastral income tax basis relieve for the period 2002-2008. There are no specific value publicly stated by the GoM however if we suppose that these 90.000 households are earning total average annual revenues from agricultural activities of 8.500 EUR then with a 2% PIT on the gross amount the expected inflow within the budget are approximately around 15,5 million EUR. On the other hand the GoM subsidies and other support programs for the agriculture will amount around 70 million EUR.

According to *James Maxwell – Chief of Party of the USAID’s AgBiz Program* in Macedonia, this measure and the impact that this measure has under the current law regulation, in 2010 will be under revision and it is possible that flat taxation will be implemented as a model for all individual farmers.¹³

¹³ Comments received on the presentation held on 17.03.2009 in USAID’s offices in Skopje

Measure 9: Transformation of the tax receivables of the government into a permanent share in some companies where the government is already the major shareholder/owner

This measure concerns four specific companies: *OHIS*, *EMO*, *Tutunski Kombinat-Prilep* and *Eurokompoziti*. The state's receivables in these companies are much higher than the market capitalization of these entities which will cause double loss for the state as the GoM will gain ownership over entities which are worth much less and as the aim is to make the companies more appealing for sales will receive lower price than the paid share gained through the liabilities.

According to the relevant Audit reports for 2007, for three¹⁴ of four companies, Ohis, Emo and Tutunski Kombinat-Prilep, the total state's receivables and the total market capitalization are given in the table below:

Emo AD	Ohis AD	Tutunski Kombinat Prilep AD
Total State's Receivables		
3.330.504 Euro	22.814.504 Euro	24.391.984 Euro
Total Market Capitalization ¹⁵		
1.219.492 Euro	2.716.021 Euro	3.310.894 Euro

As we can see the total state's receivables in these three companies are 50,5 million Euro, and the total market capitalization is 7,25 million Euro. It is obvious that the GoM by "buying" these receivables from these companies will create budget loss for more than 43 million Euros.

4. Summary

	<i>Measure</i>	<i>Pros</i>	<i>Cons</i>	<i>Amount</i>
1	Writing-off the outstanding current liabilities for health insurance, if in the next four years the companies regularly and on time pay the employee's health insurance benefits.	*"cleaning" of the Balance Sheets *Insurance that the budget will receive the benefits inflows in the next four years	* the liabilities will be written-off in 2012 *not a direct injection of cash *double standard (moral hazard) punishing the regular benefit payers	50 million EUR
2	Writing-off all accumulated interest payables on the liabilities for social care insurance benefits if the company pays the principal	* reduction of bad debt liabilities of the companies	* reduce the liquidity of the companies with significant cash outflows *double standard (moral hazard) punishing the regular benefit	N.A.

¹⁴ Eurokompoziti AD is not included in these calculation since there are no publicly available Audit Reports for 2007

¹⁵ The total market capitalization (TMC) is calculated using the number of shares of the company (NS) and the last average price (AP) on the MSE. $TMC = NS \times AP$

	dept		payers	
3	Writing-off all the accumulated interest payables on the unpaid tax liabilities if the company pays the principal debt (VAT, Income tax, Property tax, PIT).	*reduction of bad debt liabilities of the companies	* reduce the liquidity of the companies with significant outflows for the principal debt *double standard (moral hazard) punishing the regular tax payers *writing off revenues of the state budget	N.A.
4	Opportunity for the company for postponed payment to the main tax liability if the company secures the debt with banking guarantee of 100% or if the company offers mortgage with a value of 250% of the main liability	* increase the liquidity of the companies by postponing the cash payment for the liabilities * substitution for bank loans for liquidity and working capital	* can be used only by companies with satisfactory creditworthiness	N.A.
5	Relieving of the companies from the obligation of income tax payment if the total annual profit is retained within the companies	* incentive for increased investments within the companies *potentially new employments or reduced layoffs *reduced national cash outflow outside the country	* investors will be de-motivated to invest in securities * increased fragility of the Macedonian capital market	100 million EUR
6	Reduction of the custom taxes (for 498 items)	* lower input costs *in creased price competitiveness * increased competitiveness if the inputs are exported as finished products	*potential threat for the domestic production	3 million EUR
7	Lower personal income taxation rates for the individual farmers	*improved control of group so far evading tax *reduced tax rate for the existing registered payers	* increased costs for producers not paying tax until now *potentially more expensive exports and reduced international competitiveness	N.A.
9	Transformation of the tax receivables of the government into a permanent share in some companies where the government is already the major shareholder/owner	* the liabilities turned into capital may increase the value for future company sales	* concerns 4 specific companies with already questionable future *the state will generate double loss (will not collect the receivables and will become owner of questionable companies) *the state becomes owner in low quality companies	N.A.
TOTAL EXPECTED VALUE FROM THE MEASURES				330 million EUR

5. Suggested measures by the businesses in Macedonia

In Macedonia there are two organized chambers of commerce, one is the Chamber of commerce in Macedonia and the other is the Association of chambers of commerce in Macedonia. Both seems to have enhanced their cooperation with the GoM recently however, the packages of the three subject differ from each other.

In December 2008 the Chamber of Commerce in Macedonia presented measures in order to improve the business environment in Macedonia. These measures were suggested to the Macedonian Government in order to help the real sector in the battle with the ongoing economic crisis. The suggested measures were:

1. Regulation on the receivables and the payables between the Government and the companies on every basis;
2. Priority to the Macedonian companies instead of foreign companies within equal condition on the announced tenders;
3. Shortening, or practicing of the legally determined time frame for returning the VAT liabilities to the private sector;
4. Opportunity for the companies to reinvest their earnings in new investments and in such cases those retained earnings to be exempt from taxation of the income;
5. Simulation of the investment activities with equal systematic treatment to the domestic and to the foreign investments;
6. Enforcement of the National Program for reconstruction of the steel industry in Republic of Macedonia;
7. Reform of the Macedonian Bank for Support the Development by adding and improving the offered variety of services;
8. Enforcement of the Gross Salaries reform.

Some of these measures were accepted by the GoM and implemented such as the measure number 4 - Opportunity for the companies to reinvest their earnings in new investments and in such cases those retained earnings to be exempt from taxation of the income and the measure number 8 - Enforcement of the Gross Salaries reform.

The measures suggested by the Chamber of Commerce in Macedonia (CCM) are different from the measures suggested and undertaken by the GoM. The measures of the CCM are more oriented to help all the companies that are hit by the ongoing economic crisis and to reduce the time for recovering the tax liabilities of the GoM to the private sector. On the other hand the governmental measures are more oriented towards assisting the companies which are already in trouble without the ongoing financial crisis. In addition, the CCM measure number 7 is suggesting to the GoM to reform the already existing Macedonian Bank for Support the Development in order to secure funds to the SMEs with lower interest rates.¹⁶

¹⁶ According to CCM.

At the same time, the Macedonian Association of Chambers of Commerce has also suggested some measures to the GoM and according to them four of the undertaken measures by GoM are part of their suggestion. We have to mention that the Macedonian Association of Chambers of Commerce is preparing another package of measures and as they say will announced it after the presidential and local elections in Macedonia.

6. Measures undertaken by other Governments

In order to compare the measures undertaken by the Macedonian Government and the other countries in the region, USA and Europe, we will give a short review. We will start with measures undertaken by the Governments and National banks in the region and what are the expected effects.

In the section below the measures of the Croatian and the Slovenian government are presented. The other countries in the region are also undertaking similar measures aimed at the increase of the personal spending of the population, increase the availability of the loans through subsidizing these and reduction of the budgets and the state's spending.

6.1. Croatian Government Measures

The Financial and Economic crises in the Balkan countries are mainly seen through the decline in the national GDPs caused by the decline of the personal consumption and the reduced external demand for their products as well as through the decreased number of Foreign Direct Investments (FDI). The number and the value of the Foreign Direct Investments in this region are expected to decrease even further. The effect the global crisis which makes the borrowing from the banks and from the Capital markets more expensive. Thus the international companies will postpone their new investments planned for the Balkan region and will concentrate on the improvement of the investments in the existing businesses and countries in order to achieve their already adjusted returns for the nearest future.

In order to protect the Croatian economy from the global crisis the Croatian Government decided to undertake measures based on several factors. According to the Economic Institute in Zagreb, the planned measures will require rebalance of the state's budget to fulfill the projected results. According to the same source, due to the high foreign debts, the large debt payment, the current account deficit, the limited availability and high costs of capital, the threat of possible worsening of the credit rating of the country and the orientation towards the euro-zone, the measures undertaken by the Croatian Government cannot be based on the antirecession models for increasing the investments in infrastructure and giving incentive for personal spending through decreased taxes. The measures are aimed at:

- Amendment to the budget to unburden the economy with non-taxable contributions

- Securing the liquidity of public companies and the private sector by saving around 273 million EUR through reductions of the due dates of the debts to the Croatian Bank for Reconstruction and Development.
- The public companies will not employ any more workers and managers' salaries will be determined by the success of their business.
- Increased government financial support to the companies to receive from 200.000 to 500.000 Euros in the next three years for small and middle-scale companies.
- Strengthening the financial position of the Croatian Bank for Reconstruction and Development, for which 400 million Euros are requested from the European and World Investment Bank, in accordance with the assessment that it needed five billion Kuna (676 million EUR) for small and middle-scale entrepreneurship in 2009.
- Tourism boosting through amendments to the law on public procurement the companies using government subsidies to use Croatian products.
- Speeding up the process of giving permits to foreign and domestic investors with investments exceeding ten million Euros.
- Support to the real-estate market by allowing 13.000 unsold flats to be sold under reduced interest rates and reduced prices to initiate a new construction cycle, and production in cement and brick companies.
- The government is considering subsidizing of the loan interest rates for the purchase of people's first flats.
- Boosted customs inspection controls to prevent import of goods with low quality¹⁷.

6.2. Slovenian Government Measures

The Slovenian government has undertaken several measures to face the global crisis to prevent further budget deficits and maintain it within the allowed 3% of the GDP (the Euro zone limit) and prevent reduction of the employment.

The measures that were undertaken by the Slovenian government were aimed at increasing of the liquidity of the banking sector, reduction of the public spending and job maintenance though financing of the liquidity of companies; labor market, life-long learning and social security; infrastructure, energy, environment - for sustainable development; better drawing of cohesion funds. Some of the most important measures are:

- Subsidizing of the companies which have shortened working hours due to lower demand for their products
- Eased the tax burden and made available state guarantees for bank loans in a total amount of 12 billion Euros.
- Issued a one billion euro syndicated bond, to help the economy, cover budget needs and repurchase old bonds.

¹⁷ http://www.javno.com/en-croatia/croatian-government-to-urgently-amend-budget_237991

Bailout Plan for Eastern EU Rejected, 1/3/2009

(http://www.huffingtonpost.com/2009/03/01/angela-merkel-rejects-bai_n_170860.html)

“BRUSSELS — German Chancellor Angela Merkel and other EU leaders flatly rejected a new multibillion euro (dollar) bailout for eastern Europe on Sunday, suggesting that additional aid be given to struggling nations only on a case-by-case basis...”

“...Chancellor Angela Merkel insisted a one-size-fits-all bailout was unwise."Saying that the situation is the same for all central and eastern European states, I don't see that," said Merkel, adding "you cannot compare" the dire situation in Hungary with that of other countries.

That tough stance came even as Hungarian Prime Minister Ferenc Gyurcsany warned that the global credit crunch was creating a widening economic chasm in the 27-nation bloc which threatened to rend Europe.

Noting that eastern members were being hit the hardest, he suggested setting up an EU fund of up to euro190 billion (\$241 billion) to help restore trust and solvency in eastern members.

"We should not allow that a new Iron Curtain should be set up and divide Europe," Gyurcsany told reporters...”

“...EU Commission President Jose Manuel Barroso said eastern European countries already were getting billions in emergency rescue funds and loans from the EU, the World Bank and other financial institutions and did not need a sweeping new bailout plan.

He said the EU has euro25 billion (\$32 billion) in reserve to help member nations. It already gave euro9.6 billion of that to Hungary and Latvia, the first EU government to fail because of the global economic turmoil.

“..."If you are speaking about Europe and you are facing this type of complicated challenge, you have to respond in a way not just concentrating on independent nations, but some regions as well," he [Gyurcsany] said...”

6.3. USA Government Measures

The USA Government was the first one to take actions against the financial crisis. The first package of measures of the so called bailout program with a total cost of 700 billion dollars was with an aim to purchase bad debts, to reduce the uncertainty of the value of the remaining debts and to restore confidence in the credit markets. 250 billion dollars were spent on the purchasing of bank stock, giving the infusion of cash to the financial institutions and 40\$ billion dollars as an investment in the troubled insurance giant American International Group¹⁸.

Another measure to help market participants meet the credit needs of households and small businesses was supported by issuance of financial instruments backed by assets. Other funds were used for injecting cash within other commercial and investment banks in order to retain the jobs and save them though which process these were nationalized or partly nationalized.

The election of the new president in 2009, the USA Government undertook another package for helping the USA economy from the crisis. The first \$350 billion in the program committed by the Bush administration is believed by many that it failed to impose enough restrictions on banks to make sure they used the billions of dollars they were receiving to boost lending and keep the country from toppling into an even deeper recession.

Obama administration decided against seeking any additional money however many economists believe that it will eventually reach to the rescue to \$1 trillion or more. The new government intends to provide support through government-private sector partnership although details are still being worked out. The new plan includes the following most important elements¹⁹:

- Continued government purchases of stock in banks as a way to support the banks and increase the lending intended for the banks which have not received assistance so far;
- Government-private sector partnership aimed at encouraging private investors to buy the bad debts of the banks.
- To assist the homeowners better manage the mortgages and the related foreclosures.

¹⁸ http://www.cea.org.mk/Documents/CEA_Journal_VI.pdf

¹⁹ http://www.nola.com/news/index.ssf/2009/02/obama_administration_readies_o.html

7. The confidence in the worldwide effort to fight the Global economic crisis

It is our opinion that there are few disappointing global indications that might affect for the global economic recovery to be prolonged.

First is that the IMF's call for three main measures (cleaning bank's balance sheets, boosting global trade and open economies instead of economic nationalism) are not on the agenda in the world economies and even more there is no proper focus that the global economic crisis is asking for. For example, beside the G20 communiqué²⁰, in a separate communiqué, four major emerging market economies—Brazil, China, India, and Russia—called for a bigger voice on international bodies, and backed a large increase in IMF resources.

“We draw our special attention to the reform of international financial institutions. We stand for reviewing the IMF role and mandate so as to adapt it to a new global monetary and financial architecture. We emphasize the importance of a strong commitment to governance reform with a clear timetable and roadmap,” BRIC said.

Further, BRIC said the crisis has demonstrated that the IMF must strengthen its capability to monitor and give policy advice on the global economy. *“To achieve this goal, we emphasize the importance of better-focused even-handed surveillance across all IMF members, especially in respect to advanced economies with major international financial centers and large cross-border capital flows.”*

Thus, the old division and problems are still in focus beside the need for unite coordination.

Second, the IMF in its web page says: *“The International Monetary Fund (IMF) is an organization of 185 countries, working to foster global monetary cooperation, secure financial stability, facilitate international trade, promote high employment and sustainable economic growth, and reduce poverty around the world”*. Thus, it should provide economic surveillance and: *“The IMF oversees the international monetary system and monitors the financial and economic policies of its members. It keeps track of economic developments on a national, regional, and global basis, consulting regularly with member countries and providing them with macroeconomic and financial policy advice”* as IMF says.

Thus, there is nothing there mentioned about strong and weak countries but only generally about financial sound countries. We want to call to mind on the IMF's critics of

²⁰ <http://www.imf.org/external/pubs/ft/survey/so/2009/NEW031409A.htm>.

the Macedonian government's policy for fiscal expansion and expansionary policies even though the G20 communiqué literary says²¹ for restoring global growth:

“3. Fiscal expansion is providing vital support for growth and jobs. Acting together strengthens the impact and the exceptional policy actions announced so far must be implemented without delay. We are committed to deliver the scale of sustained effort necessary to restore growth, and call on the International Monetary Fund (IMF) to assess the actions taken and the actions required. We will ensure the restoration of growth and long-run fiscal sustainability.

4. Interest rates have been cut aggressively in most countries, and G20 central banks will maintain expansionary policies as long as needed, using the full range of monetary policy instruments including unconventional policy instruments, consistent with price stability.”

We also want to mention here that in the IMF's staff position note²² it is literarily said: *“Global fiscal stimulus is essential now to support aggregate demand and restore economic growth. The International Monetary Fund has called for fiscal stimulus in as many countries as possible, including emerging market and advanced economies.*

Thus, we believe that the Macedonian government is on the right track with its fiscal expansion and its expansionary policies and thus it is hard to understand the IMF's critics to Macedonian policy to fight crisis. The problem with Macedonia is the capacity of its administration to cope with fiscal expansion of relatively large scale and this risk should be addressed as priority by the government and we need more engagement from the IMF in the area of fiscal transparency.

Thus, beside the inconsistency of the IMF in its critics to the GoM we want to suggest that IMF and the GoM go for a Stand-by arrangement²³ where the budget targets (conditionality) can be relaxed for the capital expenditures but can be more tight for some current expenditures of the GoM. The timing is perfect, given that we are expecting supplementary budget immediately after the elections. The arrangement with the IMF will open the door for other FDI and IFIs. These capital inflows will ease the pressure to the fixed exchange regime even within a fiscal expansion²⁴.

²¹ http://www.g20.org/Documents/2009_communique_horsham_uk.pdf.

²² <http://www.imf.org/external/pubs/ft/spn/2009/spn0903.pdf>.

²³ Since its independence and membership renewal, Macedonia has undergone 124 months (or roughly 10 years) in formal arrangements with the Fund. See more at: <http://www.cea.org.mk/Documents/Third%20USAID%20report%20on%20IMF.pdf>.

²⁴ See more at:

http://www.cea.org.mk/Nikolov/MEASURING_OPENNESS_CAPITAL_MARKET_MACEDONIA.pdf. Also there: *“From the above figures we can see that the capital account is closed in Macedonia with small changes across time. The relatively closed capital account has implications that the fixed exchange rate can still be a beneficial regime for the case of Macedonia if the economic agents have adaptive expectations. If the economic agents in Macedonia have adaptive expectations, the monetary policy in Macedonia still have relatively more powerful effect compared to the fiscal policy on the domestic demand and the trade balance. The NBRM should take this argument into account to further investigate the possible*

Third, we want to note to Professor's Dani Rodriks from the Harvard University argument that the world needs national and financial regulation as the widely held notion of global regulation will be difficult to implement have its point. He argues that there is risk in putting all of our eggs into one regulatory basket and that different level of risk and regulation are appropriate to different countries²⁵. Thus, the recent debate (more debate than really coordinative effort so far) about coordination is impotent so far and the "old way" of national and financial regulation might be more efficient as the crisis is asking for quick short run measures instead of impotent debates.

Fourth, we want to stress that the Global Economic nationalism is taking place possible resulting with inefficient global coordination for overcoming the crisis (France about its automobile industry, USA about buying their own goods).

Given such an environment we would like to stress that in Macedonia fighting crisis will be fighting rising unemployment (the number of unemployed have risen by 2,3% in February 2009 compared to December 2008²⁶) and poverty (income based poverty headcount is 26% in March 2008 as per the UNDP's PCA report). The mechanism is one of less foreign demand thus, lower export and possible less remittances (in Macedonia however, there is a steady growth of remittances through official financial channels up to 2008). Also, as Macedonia benefits a lot of donor aid the possible aid fall might worsen the situation.

8. Conclusion

Many of the countries are taking measures for protecting their economies from collapsing. Even though it was initially announced that Macedonian as a country which is not developed may be circumvented by the effects of the financial crisis it can be seen that the real sector is facing serious challenges from the global crisis.

Many of the programs undertaken by the neighboring countries and other countries are aimed at increasing of the personal spending of the population, boosting the real sector, protection from job loss, increasing the possibility for loans etc.

The Macedonian government on the other hand has undertook several measures which are based on a writing off liabilities and tax reduction rather than assistance through injection of money within the economy or relieve measures for loans with better or subsidized interest rates in order to initiate spending of the population and the operations of the businesses which are the main generator for the GDP growth. Many of the

exchange rate misalignment (especially in the light of the new SBA with the IMF and the liability to keep the regime status quo) since the monetary policy has been shown as more important compared to the fiscal policy at the moment."

²⁵ See more at: www.economist.com/freexchange and The Economist for March 14th-20th.

²⁶ See: <http://www.avrm.gov.mk/>.

countries have completed their supplementary budgets and it is a step necessary to be undertaken by the GoM as soon as possible.

At the same time it is more significant to mention that the measures undertaken by the Macedonian Government will have impact only on companies which are already in trouble regardless of the ongoing financial crisis and will have a negative impact on the other companies which have been regularly paying their liabilities and benefits for the employees. There is a feeling of dissatisfaction and discrimination as they feel punished for paying their obligations (a typical moral hazard problem).

In order to undertake measure that will assist the real sector we recommend additional steps including:

- The 10 Measures of the GoM are not the right package for the targeted objective
- The business representatives and GoM should coordinate themselves before any new package
- Macedonian government to be prepared for the effects of the “economic nationalism” globally²⁷
- Macedonian government should go with possible Stand-by arrangement with the IMF with relaxed budget targets on the capital expenditures but with tight budget targets on the current expenditures. This should go step by step with supplementary budget with proper roll over assumptions of the PEP, fiscal strategy and strategy for managing the public debt
- Fiscal expansion and expansionary policies should be accompanied with fiscal transparency enhanced
- Short term policies targeting the real sector to keep jobs are needed
- Policies should be focused on securing financing and know-how for the small and medium enterprises
- GoM announcement about the arrangement with EIB for 50 million EUR with lower interest rates to SMEs in Macedonia needs a follow up immediately²⁸
- Aggressive search for the FDI should continue

²⁷ Recently we’ve read that in France there were complaining about the aggressive Macedonian campaign presenting competitive price (wages and salaries) for the labor factor input (Macedonian labor force).

²⁸ <http://www.cea.org.mk/Documents/CEA%20February%20presentation.pdf>

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