

**DOCUMENT OF THE EUROPEAN BANK
FOR RECONSTRUCTION AND DEVELOPMENT**

**STRATEGY FOR THE FORMER YUGOSLAV
REPUBLIC OF MACEDONIA**

**REPORT ON THE INVITATION TO THE PUBLIC
TO COMMENT**

Strategy for FYR Macedonia: Report on the invitation to the public to comment

1. Invitation to the public to comment on the Bank's Country Strategy for the Former Yugoslav Republic of Macedonia

In accordance with the EBRD Public Information Policy (PIP), an invitation to comment on the new Strategy for FYR Macedonia, along with a Management Note on the issues to be addressed in the strategy, were posted on the Web page on 6 April 2006. The public was invited to submit comments, based on the Note and the previous strategy already on the Web site no later than 2 June 2006.

Up to 2 June 2006 comments were received on the strategy from one NGO and two research institutions in the country.

As required by the Public Information Policy (PIP), these comments were examined by the relevant teams (including Banking teams, Office of Chief Economist, Evaluation Department, Office of General Counsel, Environment Department, Official Co-financing, and NGO/Outreach Relations Unit) and Management. Responses have been provided in *Staff Responses to Public Comments*, which becomes an addendum to the Country Strategy for FYR Macedonia. The addendum will be discussed along with the strategy at a Board Workshop in advance of the Board discussion scheduled for 11 July 2006.

2. EBRD Management Note

Invitation to comment on the Bank's Country Strategy Review for the Former Yugoslav Republic of Macedonia

The EBRD has started work on the revision of its Strategy for Former Yugoslav Republic of Macedonia ("FYR Macedonia"). Comments are invited to help the Bank in revising its Strategy. Any comments should be submitted to the Bank no later than **2 June 2006**, so that they can be taken into account. The current Strategy - which has been available on the EBRD Web site since August 2004 - is attached as a basis on which to comment.

The first Article of the *Agreement Establishing the Bank* states that "the purpose of the Bank shall be to foster the transition towards open market-oriented economies and to promote private and entrepreneurial initiative in the Central and Eastern European countries committed to and applying the principles of multiparty democracy, pluralism and market economics."

In order to achieve these objectives, the Bank primarily provides finance for investment projects, with a special focus on the private sector, carefully selecting projects that promote transition, by:

- creating, expanding and improving markets;
- establishing and strengthening of institutions, laws and policies that support markets; and;
- facilitating the adoption of market-oriented skills and sound business practices.

In addition, every Bank project is examined for its environmental impact and the EBRD lays special emphasis on projects that are oriented directly towards environmental improvements and energy efficiency.

In the last country Strategy, the Bank noted that the Government elected in September 2002 continued the implementation of the Ohrid Framework Agreement. Political stability and military security had been restored since the security crisis in 2001. The economy was continuing to recover after the severe negative shock of the security crisis in 2001. Overall progress in transition was steady but slow, with the pace of structural reforms in the preceding two years affected by political uncertainty and changes.

The perceived transition challenges for the country's authorities, as identified at the time of the Bank's strategy, were to:

- Improve the business environment, particularly for SMEs, reducing bureaucracy, improve corporate governance standards, and improve SME access to financing.
- Reform the judiciary and step-up the fight against corruption.
- Improve governance and strengthen the banking sector, including through consolidation.
- Implement further regulatory reform and commercialisation in key utilities to attract strong investment flows to modernise relevant infrastructure.

The strategic priorities for the Bank were to:

- Support strategic foreign investors and local export-oriented companies showing good corporate governance.
- Channel more funding to SMEs through commercial banks and micro-lending institutions, including through the implementation of an EU/EBRD Western Balkans SME framework; (ii) Support for the strengthening and consolidation of the banking sector, and (iii) Expand the range of financial instruments offered to banks.

- Support utility restructuring and privatisation through the implementation of the pre-privatisation agreement for the electricity company, (ii) support energy projects that fit the regional energy market development such as regional electricity and gas interconnections, (iii) promote road network rehabilitation in conjunction with restructuring of the road maintenance sector, and (iv) develop, where possible, municipal guaranteed water sector investments.

During the current strategy period, the EBRD signed the following projects. In 2004, the EBRD signed Migros Foodstores Skopje project (EUR 8.6 million) and signed a syndicated loan to Tutunska Banka (the total syndication of EUR 20 million including EUR 7 million from the EBRD) in the private sector and the ESM Pre-Privatisation Support Share Purchase Project (EUR 45 million) in the public sector. In 2005, the EBRD financed Mittal Steel Skopje Project (EUR 25 million) and opened another SME credit line with Investbanka (EUR 5 million) under the an EU/EBRD Western Balkans SME framework. Eurostandard Bank and Investbanka became new partner banks under the existing regional Trade Facilitation Program in 2005.

To prepare the new Strategy for FYR Macedonia, it would be useful for the Bank to receive comments on the business and economic environment, as it substantially affects the Bank's operational policies and activities, particularly in the following areas:

1. Issues related to the investment climate

This would include issues concerning (i) the legal environment (the implementation and enforcement of laws), (ii) the regulatory environment for enterprises (such as issues related to taxation, trade protection, price-setting mechanisms, etc.), (iii) the functioning of public administration, and (iv) corporate governance and integrity. We seek your views on how serious these issues are for businesses and how you think the EBRD could help to overcome them.

2. Issues related to access to finance

This would include comments on the ease of access to funding by small and medium scale enterprises in particular, given the current state of development of the banking sector and the low level of financial intermediation. What are the main obstacles? What measures should be taken to enhance the banking sector? What type of projects should be supported by the EBRD?

3. Issues related to the social impact of EBRD investments

This would include issues concerning (i) micro, small and medium scale enterprises that enhance opportunities for entrepreneurship, job creation and social flexibility; (ii) investment in public utilities, with particular attention given to issues relating to social impact, tariff reform and affordability.

4. Issues related to the environmental impact of EBRD activities

This would include issues concerning environmental improvements and energy efficiency.

The Strategy provides guidance for EBRD activities in a country, identifying the main challenges which the Bank is best placed to confront. As such, the Strategy cannot address all of the development issues a country faces and necessarily must be selective in identifying issues where the Bank has the experience and ability to play a constructive role.

The Bank will take into account all comments received. A summary of these, with staff responses, will be posted on the Web site following the Board approval of the revised Strategy. The Country Strategy is, however, a Bank document and the responsibility for its contents remains with the Bank.

3. Staff Responses to Public Comments

Issues related to the investment climate

3-1 Public Comment:

Donor co-operation with NGOs and independent research institutions should improve in the country. We really appreciate this initiative to give comments to help in development of the EBRD Strategy for the country. The EBRD NGO Newsletter is a good example.

Staff Response:

Consultation with local communities has been a key element of EBRD operations. A delegation from the EBRD's Board of Directors undertook fact-finding mission to the country from 29 to 31 March 2006. During the visit, the directors had meetings with senior government officials, members of civil society and various representatives of the business community in the country. A meeting with seven NGOs was also organised on 31 March 2006. The meeting was chaired by Mr. Zoran Cali, Director of Foundation Open Society Institute of Macedonia (FOSIM), and Mr Scott Clark, Director for Canada and Morocco. As a follow up to this meeting, EBRD Resident Office in Skopje joined a series of meetings that were organised by FOSIM in April and May 2006.

The EBRD welcomes suggestions and ideas from NGOs and research institutions on how to further improve the EBRD NGO Newsletter so that it responds to your need of information regarding the Bank's operation and activities in the region. Please send your comments to ngo@ebrd.com. You can either subscribe to the newsletter at www.ebrd.com/oppo/ngo or forward your specific queries to ngo@ebrd.com. The NGO Team at the EBRD will continue to help you receive timely and well-documented responses to these.

3-2 Public Comment:

How the Bank is trying to develop the policy dialogue with government bodies. In what form this dialogue takes places? How often and through which channels? EBRD took initiative with the establishment of Investors Advisory Council (IAC). (Section 1.3.2) There are a lot of similar organisations including International Council of Investors, etc. Support to existing ones should be enhanced in a sustainable manner.

Staff Response:

Bi-lateral dialogue: The EBRD is very actively trying to develop policy dialogue with the government through various opportunities, including the EBRD-organised Skopje Seminar for Private Sector Development (March 2005), dialogues at EBRD Annual Meetings (May 2005 and 2006), EBRD Transition Report Presentation (January 2005, November 2005), Country Strategy Review Mission (March 2006) and the Board Consultation Visit (March 2006). The EBRD is also actively discussing with the government, on a regular basis, the status of implementation of various sector reforms that have been agreed under key infrastructure projects. Showcase examples are presented in Section 3-18 of this paper.

Multi-lateral dialogue: IAC was established in March 2005. There are many other forums for dialogues between the government, international organisations, and private investors. In reality there are many forums and mechanisms that are not fully co-ordinated, while participants (the government, international organisations, private investors) are almost same despite the different name of each forum. The EBRD is constantly participating in all the forums of policy dialogue, including various investment forums (including the recent FYR Macedonia Investment Forum of April 2006), and EAR-supported monthly government-donor co-ordination meetings.

3-3 Public Comment:

The previous strategy discussed very important issues: “FYR Macedonia is not the only transition country where *management/employee buy-outs* (MEBO), the dominant form of privatisation, have not proved to be a success for company turn-around. Foreign investor interest in the country has been low and the few that have tried to approach local privatized companies for potential acquisition have often found that the management of these companies has an unrealistic valuation for their companies, which are typically characterized by stagnating or declining sales, over-employment and overvalued but decaying assets.” (Section 1.3.2) How the Bank, by investing in projects, will address these post privatization issues and the problem of collateral lending approach of the banks?

Staff Response:

The Bank will continue to focus on new companies with strategic investors or newly created entrepreneurial businesses to encourage competition in the economy. The Bank will enhance its support towards smaller-scale local export-oriented companies showing good corporate governance, by providing loans, guarantees and making equity investments in the range of EUR 1-4 million through the newly established EBRD-Italy Western Balkans Local Enterprise Facility. The Facility will target local private enterprises, with growth and export potentials in all sectors, from agribusiness to metal-related industries which are currently not properly supported by local banks, equity funds or the Bank. Many of these enterprises are with high growth rates, entrepreneurial approach and good opportunities to expand regionally.

Through its investments in local banks as well as through SME credit lines supplemented with a TC component, the Bank is supporting its partner banks to adopt cash flow based lending approach.

3-4 Public Comment:

What is the Bank’s methodology in making an assessment about the flexibility of the labour market? (Section 2.1.5). The high unemployment rate itself cannot be indicator for inflexible labour market. CEA have done research on the topic and find that other reasons are determinants of the high unemployment rate in the country. ([http://www.cea.org.mk/Documents/First USAID report labor final 4.pdf](http://www.cea.org.mk/Documents/First_USAID_report_labor_final_4.pdf)).

Staff Response:

The assessment of the labour market flexibility is made on the basis of the comparison of the country’s labour market legislation to other countries in the region both by the EBRD and in consultation with other international bodies such as the European Commission (see e.g., Analytical Report for the Opinion on the application from the FYR Macedonia for EU membership). This assessment is further supported by the Business Environment and Enterprise Performance Survey undertaken by the

EBRD and the World Bank in 2005. Labour regulations are seen by managers as a bigger obstacle in doing business in FYR Macedonia compared to other SEE countries as well as compared to more advanced transition countries in Central Europe.

3-5 Public Comment:

How can steel and textile sectors' development be addressed with the Bank's goals. (Section 2.2.1). The country's export sector is highly concentrated one. Steel sector was benefiting the fluctuations of the world market prices. How the China WTO relationship will affect the textile industry in the country? How the Bank will respond to this environment within its operations?

Staff Response:

Industrial production has recovered from a contraction in 2004 and grew an estimated 6.7 per cent in 2005, driven by the strong performance of the steel, textile and chemical industries. The entry in 2004 of a strong strategic investor – Mittal Steel – to the metal processing sector has led to a sharp rise in base metal production in 2005. It is expected that Mittal Steel will continue to perform strongly as the further restructuring measures, including skill and technology transfers, are implemented and the Mittal regional network of companies is fully integrated. The stable growth performance at around 4 per cent per year should be sustained in the medium term, supported by progress in negotiations for EU accession and progress in reform of the business environment.

3-6 Public Comment:

The previous strategy made assessment that “the country has made major progress in areas such as privatization (which is now close to completion)” (Section 3). It is not consistent with its more negative assessment in Section 1.3.2. I use opportunity here to show that the speed toward functional capitalist society in the country was and still is very slow, given the initial endowment (see the figure at the end of this document) and compared to other countries.

Staff Response:

Despite the good progress that the country has achieved since its independence, it is also clear that the country is facing many remaining challenges. Improving the business environment, particularly for SMEs - speeding up the ongoing judiciary reforms, stepping-up the fight against corruption, reducing bureaucracy (long administrative procedures with unpredictable outcomes, and unequal treatment of licence applications), and reducing ambiguities over property rights, is remaining one of the key transition challenges for FYR Macedonia.

3-7 Public Comment:

The Bank should pay attention that establishing organization and passing laws in a country is necessary but not sufficient condition for a functional market economy. (Section 3.1). The case of the Anticorruption commission having no instruments to finish cases and given no political will in the country is a dead end in fighting corruption, providing business climate, boosting private sector investment and economic growth.

Staff Response:

FYR Macedonia is continuing to make progress in implementing the legal reforms necessary for a free market economy. As regards the “quality” of FYR Macedonia’s laws, many of FYR Macedonia’s laws fare well when compared with other countries, or when tested against international benchmarks. For example, both the country’s capital markets and company law legislation are considered to be in “high compliance” with the relevant international benchmarks. But, and as has been pointed out in previous country strategies, there remains a significant “implementation gap” between the “quality” of such laws, and their implementation. This implementation gap can have the dual effect of undermining the utility of the specific laws in issue and diminishing the confidence that both local and foreign investors and traders have in the legal system as a whole. However, here too, it appears that FYR Macedonia is taking important steps to make improvements, with a case in point being the recent reform efforts under way in connection with the country’s judiciary.

3-8 Public Comment:

The Strategy should address tax policy reforms and institutional credibility in order to foster foreign investments.

Staff Response:

The EBRD is involved in an active policy dialogue regarding business environment improvements, including the tax reform and the institutional framework that fosters foreign direct investments. The business environment remains challenging for domestic and foreign investors. Enterprises see corruption and judicial shortcomings as major constraints on their activities, according to the Business Environment and Enterprise Performance Survey undertaken by the EBRD and the World Bank in 2005. Business environment is further complicated by the ambiguities over property rights, hindering foreign direct investment. Policy dialog on these issues with the authorities will continue to be an important complement to EBRD investment activities in the country.

3-9 Public Comment:

In the area of donor coordination, what is the success and achievements that have been made so far? (Section 5).

Staff Response:

Co-ordination with international financial institutions and donors as well as TC and official co-financing will remain crucial for project preparation and institution building, particularly promoting smaller scale local enterprises and for public sector operations. In this respect, a decision to create **the new Western Balkans Multi-Donor Fund** was made at the EBRD Annual General Meeting in London (21-22 May 2006). Eleven countries agreed to provide a total EUR 10 million in donor funds towards a new EBRD-driven initiative to boost private business investment and infrastructure development in the Western Balkan countries, including FYR Macedonia. The new multi-donor fund will strengthen EBRD – donor coordination in FYR Macedonia and expand the resources available to support economic growth and regional cooperation.

The Bank has mobilised EUR 12.7 million in technical assistance to FYR Macedonia, with 72 technical co-operation (TC) projects, mainly in the banking,

telecommunications, transport and municipal sectors. Disbursement of TC funds as of May 2006 stood at EUR 11.1 million, reflecting the fact that projects are still ongoing in the small business finance and infrastructure (transport, municipal) sectors.

3-10 Public Comment:

The Bank should stress more the monopoly and the captured regulators problem in the country related to the telecommunications and in future possible the energy sector.

Staff Response:

Liberalisation of public fixed communications networks and services was scheduled for January 2005, but has been delayed pending adoption of the secondary legislation required under the Electronic Communications Law. While the authorities appear to be aiming for liberalisation in 2006, there is no clear indication when this will actually take place. The Bank will look for opportunities to support or participate as a co-investor in the sale of state shares in telecommunications and to encourage the faster growth and consolidation of the existing small telecoms/cable TV alternative operators in order to enhance the competition on the market.

The Bank will continue to support the privatisation of the newly unbundled power companies through transparent and competitive tender process, supported by electricity sector regulatory reforms.

Issues related to access to finance

3-11 Public Comment:

The Bank's efforts in the country's banking sector maybe is not so successful. Despite the legal requirements for the banks to have risk management departments, they do not have good risk management departments. They still use the collateral based approach. The new banking law has not been passed.

Staff Response:

The Bank has contributed to the development of the banking sector since 1994. At present, the risk management function exists in most of the banks and it is continuously being improved and strengthened. Through its investments in local banks as well as through SME credit lines supplemented with a TC component, the Bank is supporting its partner banks to adopt cash flow based lending approach.

While the Bank is not involved in the preparation and or adoption process of the new Banking Law, new banking legislation and supervision development plan are expected to be adopted within the next 12 months, strengthening the stability of the financial sector. The central bank is required by the IMF to apply a number of measures to improve banking supervision, including tighter prudential regulations, provisioning and reporting requirements. By the end of 2006 the central bank is expected to issue accounting guidelines for banking sector, require banks to publish their annual audited accounts on central bank homepage, and require bank auditors to comment on adequacy and quality of lending policies, risk management and internal controls.

3-12 Public Comment:

The previous strategy states that the National Bank of Greece, as a strategic investor of Stopanska Banka, “has accomplished tremendous work since then, cleaning up the inherited portfolio substantially, introducing excellent new MIS and expanding substantially into retail banking.” (Section 1.3.1). Please explain about the new MIS.

Staff Response:

Stopanska Banka implemented a new modern management information system (MIS) which was an important step in the modernisation and enhanced efficiency of its operations. Further details on the new MIS is commercial information of the Stopanska Banka.

3-13 Public Comment:

How the Bank exactly will increase competition in the country’s banking sector? (Section 4.2).

Staff Response:

The Bank endeavours to increase the competition in the banking sector by:

- Supporting its existing investee banks in attracting strategic investors;
- Facilitating the sector consolidation by taking participation in the mergers of local banks;
- Strengthening the corporate governance through its representation in the Board of Directors of its current and future investee banks; and
- Providing technical expertise to support the institution building and new product development to its partner banks.

3-14 Public Comment:

The Bank should also focus its attention to the non-banking sectors that could provide financial means for the country’s private sector. The non-banking sector is rather underdeveloped.

Staff Response:

The Bank will look to develop business opportunities in the developing leasing sector, which may include the provision of training for leasing companies. The mandatory pension reforms were introduced in 2005 with the establishment of just two mandatory pension funds. Despite efforts by the Bank following support given for the implementation of the reforms, a suitable opportunity to invest in either of the two pension consortia did not materialise. The Bank is also reviewing opportunities in the insurance sector and has provided TC for strengthening the role of the insurance supervisory office. The consumer finance industry is developing - mainly through the commercial banks - which is an area where the Bank may look to be involved. The local capital market is underdeveloped and the bank will closely monitor developments as the pools of assets eligible for refinancing in a secondary market grow.

The Bank will pursue establishing credit lines with micro-finance institutions to enhance their lending capacity to SMEs and micro businesses under the newly established MSME Finance Framework for Western Balkans and Croatia.

Issues related to transition impact of EBRD investments

3-15 Public Comment:

The previous strategy states that “all new projects have good or excellent transition impact potential and are already under implementation.” (Section 1.2). There should be some information on who has made the impact evaluation. How is the impact measured?

Staff Response:

The impact evaluation is a combined effort of Banking, Chief Economist Office and Evaluation Department staff. The transition impact is mostly qualitative and measured through performance indicators defined in the annual transition reports of EBRD. Since EBRD is mostly a project Bank, the policy evaluation is closely linked to the project evaluation and is found mostly in Project and technical assistance evaluations.

3-16 Public Comment:

The previous strategy says that “in the private sector, good transition results have been achieved in general by enhancing the companies’ competitiveness and export potential.” (Section 1.3.1). Is the assessment related to 5 companies only? They do not make the whole private sector of the country.

Staff Response:

The Bank is trying to reach a critical level of presence in key sectors in each country of operation not only through the growth of its client base, but also through demonstration effects achieved through project implementation and project impact

3-17 Public Comment:

“The Bank is financing a considerable number of projects in public infrastructure and the preparation and implementation of these projects brought about significant institutional reforms in the areas of sector restructuring and commercialization as well as financial management and procurement.” (Section 1.3.1). Which are the significant institutional reforms that have been brought forward?

Staff Response:

The Bank has been very proactive in supporting initial stages towards more private sector involvement in the development and management of public infrastructure. Usually these are the most difficult stages since they imply a change of management culture and business practice in the public sector. The following are the show case examples of such reforms:

Air navigation sector: The Bank signed the loan agreement for the Civil Aviation Upgrading Project with the government in 2002. Under the project, the Bank arranged technical assistance financed by Swedish and Italian governments to support the government with the establishment of an independent and financially autonomous air navigation service provider. In addition, GTZ provided the government with technical assistance financed by the German government. This requires the reorganisation of the Civil Aviation Administration, which currently functions as a regulator and a service provider. In February 2006, the Parliament approved the new Aviation Act, which requires formal separation of these two

functions. The reform process is expected to be completed in the coming months. The Government is reviewing legal documents for the establishment of the two new entities. This separation will lead to the full corporatization of the new air navigation services provider.

Power and energy utilities sector: The Bank signed the ESM Power Pre-Privatisation Share Purchase project with the government in October 2004 with the aim to help promote the privatisation of Elektrostopanstvo na Makedonija (ESM), the state-owned electric power company. The former vertically integrated state-owned utility was unbundled into 4 major companies in the sector: AD ESM (distribution), MEPSO (transmission system operator), AD ELEM (generation and major hydropower plants) and AD TEC Negotino (generation) in 2005. The regulatory framework was enhanced with the establishment of the Energy Regulatory Commission in January 2004. It oversees the wholesale market operations and the electricity tariff setting. The EBRD pre-privatisation project supported the privatisation process giving strong incentives to accelerate the process in accordance with internationally accepted practise. The privatisation of AD ESM was completed in a fair and transparent manner in March 2006.

3-18 Public Comment:

The previous strategy states that “despite the steady progress in the banking sector reform especially in the area of privatisation (direct and indirect state ownership of banks’ capital has fallen to 13 per cent), the country’s banking sector remains highly concentrated and is still not competitive enough.” (Section 3.2). Although this has been generally accepted as true, comparative data should be added to support the assessment.

Staff Response:

As at 31 December 2005, the degree of banking sector privatisation (excluding the state-owned Macedonian Bank for Development Promotion) was 97% (increased from 87% as of December 2003). The three largest banks account for 68% of the total banking sector assets as at December 2005 (increased from 55% as at December 2003). The annual EBRD Transition Report also provides a regular update of the progress and remaining challenges per country and provide substantive background information for a good understanding of the country context in which EBRD strategies are developed.

Issues related to the social impact of EBRD investments

3-19 Public Comment:

The government has requested from the Bank a study on energy affordability, including recommendations for a social safety net (Section 1.3.1). What are the results of this study?

Staff Response:

In November 2003 the Bank concluded a regional study on Power Sector Affordability in South East Europe, funded by the UK Department for International Development (the “Regional Study”). The Regional Study covered eight countries – Albania, Bosnia and Herzegovina, Bulgaria, Croatia, FYR Macedonia, Moldova, Romania and Serbia and Montenegro. The result of the study was presented at a regional conference on Energy Reform and Social Safety Nets in Sofia, organised by

USAID. The Regional Study confirmed that power affordability was a problem for many consumer groups in South East Europe (e.g. pensioners, unemployed, low income households). At the same time many of the South East European countries have not yet developed adequate social safety mechanisms to protect energy poor consumers. FYR Macedonia is no exception in this respect.

Recognising the need to improve the country's social safety net, the government of FYR Macedonia asked the EBRD to assist it in reforming its approach to social protection against energy poverty. The request is in line with the government's efforts to reform its power sector and to integrate it into the proposed South East European Regional Energy Market and meet EU Directives. EBRD secured grant funds from Danish Government for preparation of the energy affordability study. The purpose of the assignment is to advise the GOM on ways to improve their social safety net with respect to energy poverty (covering heat and power, but taking into account linkages with other sectors such as gas). The Qualified Consultant will focus on three areas of work (i) Review the current social safety net and specific provisions, if any, for dealing with energy poverty; (ii) Recommend change, taking into account institutional, technical financial and legal constraints and (iii) Develop implementation plan, with key milestones. The assignment is expected to start in August 2006 and to last 3 months.

3-20 Public Comment:

The previous strategy states that “in the 1980s, the state provided a guaranteed and comprehensive healthcare service, which on paper still remains intact but in practice suffers from acute lack of funds, resulting in scaled back health and related social benefits.” (Section 2.1.4). CRPM is currently preparing a policy study on the state of affairs in four medical centers around the country and would be happy to share the results once the analysis is published. Until our studies are publicly available, the comparative analysis of the salaries in the public sector would confirm the very opposite (the salaries in the public health sector are competitive), though de-compression is needed.

Staff Response:

The quality of healthcare has deteriorated since independence due to an acute lack of funds and shortages of medical supplies. Compared with the private sector, the medical service is seriously underpaid. The situation is made more difficult by the unclear division between military and civilian health structures. Most of the funding for the state healthcare system comes from employers' payroll contributions to the Health Insurance Fund. The balance comes from transfers from the state budget and from user fees. The IMF is pressing the authorities to strengthen financial controls in the healthcare sector. Its concern is that wage pressure and unfunded spending commitments will increase arrears.

3-21 Public Comment:

The previous strategy states that “The educational system has been drained of resources since independence. At the primary and secondary level, parents have had to make the shortfall in resources and teaching materials. Postgraduate students have fewer opportunities to study.” (Section 2.1.4). The government is responsible to provide free primary education but has never provided text books, which always has been covered with out of pocket payments. But parents do not participate with financial means to the primary education in the country. A CRPM recent overview of

the tertiary education sector depicted that at postgraduate level the opportunities are growing immensely with introduction of many interdisciplinary studies and private university programs. Therefore we are wondering in what sense postgraduates have fewer opportunities to study? Have some of the postgraduate programs been closed down?

Staff Response:

FYR Macedonia inherited from Yugoslavia two universities, one in Skopje and one in Bitola, both with a wide range of departments. The overall literacy was 94%. Since independence, the number of children completing primary education each year has remained unchanged: it was 29,697 in 1990/91 and 29,939 in 2003/04, according to the State Statistical Office. The number of those completing secondary education fell from 21,102 in 1990/91 to 15,704 in 1992/93 but recovered to 23,621 in 2003/04. The number of university graduates fell from 2,500 in 1990/91 to 2,150 in 1994/95, but then rose to 4,178 in 2002/03.

The controversial issue in education is that of the right of ethnic Albanians to education in their own language. At primary level 32.7% were taught in Albanian in 2003/04, an adequate provision. At the secondary level the number of those taught in Albanian more than doubled from 7,128 in 1994/95 to 18,361 in 2003/04, still representing only 19.6% of the total number of students enrolled. In February 2004 the Tetovo University was legalised, which means that the university which offers tuition exclusively in the Albanian language now receives state funding along with the Macedonian-language universities in Skopje and Bitola.

3-22 Public Comment:

The previous strategy states that “The Confederation of Trade Unions (SSM) encompasses 17 separate unions organised according to the industry sectors. More than 50 per cent of the legal workforce is unionised. Unions are particularly strong in the garment industry.” (Section 2.1.4). As the CRPM policy study on the economy of Shtip and the garment industry in general shows, trade unions are a rarity in this sector. The claim that unions are particularly strong in the garment industry is false. See CRPM’s *MACEDONIAN CLOTHES FOR EUROPE* at http://www.crpm.org.mk/Papers/Macedonian%20clothes%20for%20Europe_PolicyStudy1.htm

Staff Response:

The information that the over 50 per cent of the legal workforce was unionised and that trade unions were particularly strong in the garments industry was taken from the US State Department 2003 country report on human rights practices in FYR Macedonia prepared by the Bureau For Democracy, Human Rights and Labor published on 28 February 2004, page 18.

Issues related to the environmental impact of EBRD activities

3-23 Public Comment:

Environmental issues will be more and more an important issue in the country. The National Environmental Action Plan (NEAP) 2 has been prepared. Integrated Prevention Pollution and Control (IPPC) units should be established within the ministry and the local government. What is the EBRD’s activities in this area.

Staff Response:

The Bank encourages the government's effort in harmonising national environmental legislation with the current EU's. Establishment of IPPC units is a part of this process and the government is following it accordingly. The Bank will continue to promote private sector development of SMEs through the Turnaround Management (TAM) and Business Advisory Services (BAS) Programmes. BAS Programme also provides local companies with support in complying with Environmental legislation such as Environmental Impact Assessments (EIA), IPPC, Energy Efficiency issues.

3-24 Public Comment:

The previous strategy states that the Thessaloniki-Skopje Pipeline "is state of the art at a technical level and has brought new standards of engineering to the country, while significantly reducing the risk of environmental hazard linked to oil transportation." How did the building of the pipeline bring new standards of engineering to the country?

Staff Response:

The pipeline has reduced transport costs by more than 40% and, on the basis of a risk assessment, significantly reduced the risk of a major hazard accident from the previous rail transportation of petroleum products. Moreover, the previous system of top loading and unloading of rail wagons lead to significant hydrocarbon vapour losses, particularly in summer months, and represented a major fire and explosion risk at both the Thessaloniki and Skopje Oil Refineries.

The routing originally passed alongside sensitive ecological areas and in the proximity of the Vardar River, the main river of FYR Macedonia and Greece. As a result of the EIA Study, and the Bank's involvement, the pipeline was re-routed to take account of all sensitive environmental and ecological issues. In particular the pipeline is no longer routed alongside the Vardar and its nearby riparian (wetland wildlife) ecosystems with the majority of the route now passing through agricultural land of limited ecological importance. A detailed environmental management plan, including an emergency response plan, has been developed to ensure that any unforeseen or unidentified impacts of the development are minimised. The pipeline's state-of-the-art technical engineering standards, particularly the monitoring capability, will ensure that in the event of a drop in pressure as a result of an oil leak, block valves will close down the flow of oil throughout the pipeline system.