

## EXECUTIVE SUMMARY

i. **It has been nearly two decades since FYR Macedonia’s 1991 independence. The country has made important progress in many areas of social and economic development.** Under the 2001 Ohrid Agreement, the Government chose a peaceful solution to ethnic conflict and, notwithstanding periods of tension, has maintained constructive political dialogue and social stability. Successive governments of differing political parties have largely pursued prudent macroeconomic management, which has contributed to gradually accelerating economic growth and helped the country weather the 2008-2009 global economic crisis. FYR Macedonia performs well on indices of business climate and, most promising, is nearing European Union (EU) accession. Improvements in social and human development have been less consistent, but people are living longer, fewer infants are dying, more children are going to school, and women are taking their rightful place in social and political life.

ii. **There are, however, enduring and emerging challenges.** First, economic growth in FYR Macedonia picked-up later than in much of South East Europe and only reached regional averages at the outset of the 2008 economic and financial crisis. Second, while growth in output accelerated in the pre-crisis years, it did not significantly improve living standards. Unemployment is notably high and falling slowly, and poverty remains persistently high. In this context, establishing faster, more inclusive growth remains the preeminent challenge. Turbulence in Greece and the eurozone underscores this point. Third, evidence is mounting that South East Europe—and FYR Macedonia specifically—confronts growing climate pressures that could fundamentally affect its economic development. Growth, therefore, needs to be “greener” as well as faster and more inclusive.

iii. **The authorities are committed to meeting these challenges.** The Government has established clear goals beginning with, above all, faster economic growth and job creation. The authorities have also defined a roadmap for swift EU accession, continued “social harmony,” transformation into a knowledge economy, and, ultimately, a higher quality of life for all citizens, including a focus on the response to climate change.

iv. **The World Bank Group’s objective over the FY 2011-2014 is to provide selective and targeted financing and knowledge advisory services in support of faster, more inclusive and greener economic growth.** Because FYR Macedonia’s future growth and development will depend fundamentally on the pace of EU accession, virtually every intervention in this CPS has been identified and will be designed to help prepare for EU membership.

- ***Faster growth by improving competitiveness.*** FYR Macedonia can build on improvements in the business climate through continued sound macroeconomic management, further efforts to reduce bottlenecks in the business environment and infrastructure, and stepped-up investments in education, including higher education.
- ***More inclusive growth by strengthening employability and social protection.*** The CPS will emphasize continued improvement of social programs amid growing fiscal constraints.
- ***Greener growth through more sustainable resource use.*** Key Bank Group interventions will include “win-win” investments in clean and efficient energy. As this is an emerging area of knowledge and new subject of dialogue with the Government, the Bank will also collaborate with selected partners of FYR Macedonia on analysis on “green growth” and climate change to support adaptation and other climate sensitive policymaking.

- v. **World Bank Group support will be guided by three principles of engagement.**
- Assistance will be directed to support EU accession;
  - Interventions will seek to leverage financing and expertise from within the World Bank Group and across FYR Macedonia's development partners;
  - CPS implementation will be flexible, reflecting the pace of economic recovery and the external environment; emerging development challenges, including evolving knowledge on the impacts of global climate change; and the demand of government authorities.
- vi. **The CPS is consistent with the Bank Group's regional strategy for Europe and Central Asia (ECA).** It identifies the challenges and priorities in the ECA Strategy and adapts them to the circumstances in FYR Macedonia; and it supports expanding regional and sub-regional approaches, deepening the partnership with the EU, and aligning knowledge services to support country priorities.
- vii. **The Bank will accelerate consolidation of the portfolio to achieve a lending program of fewer, larger projects.** This will help free budget resources to identify and carry out timely, demand driven analytical products that influence policy and leverage results. The Bank Group has engaged closely with the authorities to identify sectors where it can concentrate its assistance and maximize impact. This will be especially important given that International Bank for Reconstruction and Development (IBRD) lending is relatively small and increasingly selective.
- viii. **The total volume of new IBRD commitments under the CPS over FY11 and FY12 is expected to amount to a little over US\$100 million.** The Government has asked for a total envelope that would imply lending of similar amounts over FY13 and FY14. Overall lending amounts will depend on the IBRD's lending capacity and demand by other borrowers as well as Government demand and performance in the course of the CPS period. The lending program for the last two years of the CPS will be discussed with the authorities closer to the time of the CPS mid-term Review. The CPS includes US\$30 million for the second operation of a Programmatic Development Policy Lending (DPL). Additional policy based budget support may follow during the CPS period depending upon Government priorities and a continued satisfactory macroeconomic framework. Investment operations are planned initially in the energy sector and toward catastrophic risk mitigation. The International Finance Corporation (IFC) expects to provide financing to the private sector of up to US\$100 million. IFC's investments will aim to improve competitiveness, address climate change issues, and facilitate intermediation in the country. IFC will use its Public-Private Partnership Transaction Advisory to facilitate private financing for public private partnerships (PPP) transactions for new hydro power generation facilities, road operation and maintenance, water supply, and solid waste management. In addition, IFC will provide its advisory support to further improve the investment climate in line with country's overall EU accession aspirations.
- ix. **The CPS program is subject to four principal risks.** Prolonged financial turbulence in neighboring Greece—and the eurozone more broadly—could restrain economic growth, which could in turn impact debt sustainability in the absence of further policy adjustment. This could lead the authorities to delay scheduled investment operations and demand more policy lending, which would be subject to a continued sound macroeconomic framework. Two, the pace of EU accession will be accelerated by resolution of negotiations with Greece over FYR Macedonia's "name issue." An interruption in progress toward membership could weaken public support for reforms. Three, failure to create jobs could undermine Government support and increase social tensions. Four, FYR Macedonia is vulnerable to natural disasters, including earthquakes, and, increasingly, severe climate related events such as draughts and floods, which could affect Government investment priorities.