



COMMISSION OF THE EUROPEAN COMMUNITIES

Brussels, 30.3.2004
SEC(2004) 373

COMMISSION STAFF WORKING PAPER

Former Yugoslav Republic of Macedonia

Stabilisation and Association Report 2004

{COM(2004) 204 final}

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1. Executive Summary

While constrained by a difficult budgetary and economic situation, the former Yugoslav Republic of Macedonia has made efforts in 2003 to progress in the Stabilisation and Association process. In many areas, the reform process is still in its infancy and will need further efforts to be converted into concrete changes and bring the expected benefits.

The **political situation** has remained generally stable, building on the process initiated in 2001 at Ohrid which remains crucial to ensure the development of the former Yugoslav Republic of Macedonia as a unitary and multiethnic State. The support of the international community, in particular through the EU led military operation “*Concordia*” and the new Police Mission “*Proxima*”, has been critical in supporting gradual stabilisation. Consolidating stability calls for continued effort from the Government to implement fully the Framework Agreement and to strengthen the rule of law, as well as for commitment and sense of responsibility from all components of the population. Preparatory efforts need to be accelerated and enhanced for the implementation of the decentralisation process.

Many challenges still lie ahead, whether on decentralisation, good governance, reform in the security sector or rule of law. Implementing the reforms will also imply strengthening administrative capacity, by transforming the public administration into a modern and accountable public service. Remaining on track in facing these challenges should enable the country to shift progressively its focus from stabilisation to association.

The former Yugoslav Republic of Macedonia has been successful in maintaining a stable macro-economic framework and joined the World Trade Organisation. However, the **economic situation**, and notably serious weaknesses in the functioning of the economy, business climate, competitiveness and enforcement of property rights, is increasingly a challenge for the country’s successful transition. Foreign direct investment has been particularly low, and is likely to increase significantly only if institutional and political stability continue to improve and reforms are pushed forward. Serious progress in establishing the rule of law will also be crucial.

The **Stabilisation and Association process** has benefited from the support of all political parties and efforts have been made to make it a framework for Government actions. A National Action Plan to follow up the recommendations set in last year’s report has confirmed the will to go ahead. Further efforts and resources are needed to sustain reform. The entry into force of the Stabilisation and Association Agreement will lead to a greater co-operation between the EU and the country. The presentation by the EU of a European Partnership should provide the basis for focussing efforts to move forward on the reform agenda.

2. Political situation

2.1. Democracy and rule of law

The Government has made concrete efforts to implement the Ohrid Framework Agreement and most signatories of the Agreement have kept to their pledge to support it. Willingness to compromise on a number of sensitive issues, including on the creation of a new State University in Tetovo, has strengthened the coalition and should ease inter-ethnic mistrust. However, some opposition representatives have questioned the very principles of the Agreement. 2004 will be decisive in consolidating the return to full stability and the reform process. New legislation and action plans, especially on decentralisation and security-related reforms, now need to be followed up with implementation and enforcement. The reform of the judicial system, the rule of law and the fight against corruption remain areas where energetic measures are needed. Constructive commitment by all political parties, co-operation among the institutions, and a sense of ownership at different levels of government are needed to accelerate the pace of reform.

2.1.1. Assessment of democratic institutions and of attitudes to the state.

Implementation of the Ohrid Framework Agreement: The full implementation of the Ohrid Framework Agreement (FA) remains essential for making progress in the Stabilisation and Association process. Overall, the confidence-building process initiated by the FA is progressively taking root and has been bolstered by the personal commitment of Prime Minister B. Crvenkovski and Mr A. Ahmeti. This consensus on the principles underlying the Agreement should be sustained, and also encompass the opposition. Tangible progress has been made, in particular on the legislative component of the FA and the focus is increasingly on the two complex and far-reaching concepts of decentralisation and equitable representation of minorities in the public administration.

.The implementation of the FA has not been without tensions and difficulties. Furthermore, radical – if isolated - views expressed by some members of the opposition have advocated a reorganisation of the country along ethnic lines, which would reverse the country's course towards European integration. Activities by some extremists, often linked to criminal interests, have sought to undermine the reconciliation process. This led the EU to adopt a common position in February 2004 taking restrictive measures against extremists promoting violence and acting outside the democratic process.

The final results of the *Census* on the ethnic composition of the resident population were published on 1 December. The final data showed an increase both in the number and in the percentage of the country's ethnic Albanian population – from 22.7 % to 25.17 % – as well as a slight increase in the ethnic Macedonian population, although their percentage of the overall population decreased (to 64.18 % from 1994's tally of 66.6 %). The work done by the State Statistical Office, under the monitoring of the International Census Monitoring mission, was assessed as professional and in accordance with international standards and no substantial criticisms were raised. The completion of the Census enabled further steps in the implementation of the Framework Agreement, in particular in helping to finalise the preparation of the remaining decentralisation laws and in providing a basis for further efforts on equitable representation in public administration.

Following up the Plan adopted by the Government in spring 2003, which set intermediate objectives to ensure the *equitable representation of minorities in the public administration* as

foreseen by the FA, initial measures have been undertaken, and there has been some progress in particular in the security sector. The mid-term objectives of the Government (14 %) have not yet been met, except in specific sectors, and increased efforts will be needed. This process needs to be reconciled with the obligations to foster competence and to base careers on merit, and therefore needs to be part of a clear and comprehensive strategy. The budget 2004 has foreseen limited resources to address this issue. The strategy to be defined should include increased budgetary resources to gradually reach the objectives set by the Framework Agreement, further targeted training and changes in the regulations affecting employment in the public sector.

The use of language(s) in the public administration and the use of community symbols are two other sensitive areas where further measures need to be adopted. As regards the former, there has been some progress. Since May identity cards have been available in the Macedonian and Albanian languages upon request. This needs to be extended to all identity documents (passports, driver's licenses, travelling documents, birth certificates, etc.). At a broader level, further measures are needed to facilitate the full implementation of the FA provisions in the whole public sector.

President of the Republic: Despite occasional political confrontations with the Government, President Trajkovski has played a constructive role in building consensus on issues of national importance, including European integration and security matters, as well as the implementation of the Framework Agreement. Various initiatives in the area of regional co-operation have contributed to promoting good neighbourly relations and joint projects among the countries in South-East Europe in the economic, political and cultural field. President Trajkovski was victim on 26 February of a plane accident, leaving as one of his main legacy for the country his personal commitment to bringing it closer to the European Union family.

Anticipated presidential election will take place on 14 April. All efforts should be displayed to make the election a successful test for the country's democracy.

Parliament: After the Government's reshuffle in November, Mr. Shaqiri (Democratic Union for Integration) – a former National Liberation Army commander – was elected Vice President of the Parliament.

Parliamentary debate has to a large extent been dedicated to legislation needed to complete the implementation of the Framework Agreement. Nearly all the legislative changes related to the FA have now been adopted, except for those related to the decentralisation process submitted by the Government in December and under consideration. The Parliament has also refined its role in the debate on EU integration related issues, and outlined its role in the Stabilisation and Association Process in a declaration adopted in June.

Progressively, the structures needed to improve the capacity of the Parliament to play its role in the Stabilisation and Association process are being put in place. The Committee for Relations among the Communities, established in December 2002, started its work in September 2003. The Parliamentary Committee on EU Affairs held its constitutive session at the end of November. Whilst the actual role the Parliament will be able to play is going to depend on its capacity to make its working structures fully operational so that it can effectively contribute to the debate, it will also depend on the will of the Government to engage in a political debate on most fundamental reforms.

There have been tensions in the Parliament, especially in relation with the creation of a new State University in Tetovo and on the decentralisation laws. The boycott by the Democratic Party of Albanians of all parliamentary activities, ended in September after several months of absence from Parliament, was a blow to the functioning of the parliamentary representation. There is an open issue related to the use of language(s) which continues to impede proper working of the Parliament. While a constructive solution has been found relating to the application of the rules on language in most of the parliamentary committees, problems still occur in the work of some. The refusal by some opposition members to chair the committees of which they are in charge in the Macedonian language has been hindering the regular work of those committees for more than a year.

Executive: The Government has established itself as a functioning coalition. Relations between the two main parties in power have been strained at times by the lack of co-ordination or transparency between governmental partners, in particular during a security related crisis in September, but confidence in the coalition appears now to have been re-established.

The 2003 Government programme was ambitious. While this first year in power was marked by a number of important achievements in the security and macro-financial areas, the pressure to achieve tangible results improving the daily life of citizens is increasing. Limited resources mean the Government will have to remain attentive to setting reasonable objectives and well-defined priorities.

New advisory bodies have been set up to help the Government to take its EU objectives into account in its work. The members of the Economic and Legal Councils of the Government were appointed in August and September respectively. Some of the actions announced at the beginning of 2003 (i.e. the establishment of departments for: strategic thinking, planning and monitoring; policy analysis and co-ordination; and public administration reform, at the General Secretariat of the Government) are still in an early phase of implementation.

Public Administration: Some progress has been made since last year's report through the progressive implementation of the reform of the General Secretariat. In early 2003 and ahead of the Budget preparation, the Government prepared a document establishing strategic guidelines and setting clear expenditure ceilings for the various ministries, which were enforced by the Ministry of Finance, thus linking strategic planning and budgeting. The functional analysis of Government activities was launched in almost all ministries and should now be completed and translated into actual measures. The Agency for Civil Servants has been consolidating its structure and working on personnel management procedures. However, the full implementation of the Law on Civil Servants remains to be ensured and the Agency for Civil Servants needs to be further strengthened. The politicisation of the public administration and the changes in the administration after each election or Government reshuffle remain serious impediments to transforming the public administration into a competent, merit based, sustainable and efficient administration serving the needs of citizens. Policy formulation has to be improved and policy-related budgeting has to be systematised in all ministries. The protection of the citizen and citizens' capacity to appeal should be improved, calling for the upgrading of the Administrative Procedures and Administrative Disputes legislation.

Local government: Decentralisation is a key challenge the country must tackle to enhance the quality of its governance and its democracy. The decentralisation process has two key objectives: to bring government closer to the people and to improve the delivery of public

services. Its success depends on rationalising the size and number of municipalities in order to increase fiscal and managerial capacity and on transferring to the municipal level the competencies listed in Article 22 of the Law on Local Self-Government, passed after the signing of the Ohrid Framework Agreement. The government's Operational Programme, including the three critical laws (the Law on Territorial Organisation, the Law on the City of Skopje and the Law on Municipal Finance) is proceeding through Parliament. The decentralisation process is being co-ordinated with other reforms in the social and administrative sectors through an inter-ministry Decentralisation Working Group and a Co-ordinating Body of State Secretaries. The rationalisation and the transfer of competencies should take place so that the new decentralised set-up can begin to function on 1 January 2005. Progress is now dependent on effective co-ordination within central government, parliamentary approval of the required legislative acts, training of the municipal administrations and clarification of the situation with regard to municipal debt.

Civil society: The strengthening of civil society has been supported by the Government's efforts to favour the development of non-governmental organisations (NGO). This included a higher degree of co-operation between NGOs and Government. However, additional measures are needed to achieve the aim of a participative civil society, and the definition of a new level of decision-making in the framework of the coming decentralisation will also imply further developing NGOs and associations at local level.

The development of professional organisations and civic associations is still hampered by the lack of financial resources and remains predominantly dependant on external resources, public or foreign. Additional Government initiatives to support civil society development, such as tax incentives and better structured co-ordination remain necessary. Existing projects for the development of platforms for the latter are a step in the right direction. A higher degree of transparency in the criteria applied to the beneficiaries of public support would reduce the risk of abuse and would also improve the overall perception of their role by the wider public. This may imply the revision of the 1998 Law related to associations.

Armed Forces: Aspiration to NATO membership has led the Government to present a Security and Defence Concept which was adopted by the Parliament in June. The Law on Service in the Army was amended in October to facilitate the reduction and the reform of the structure of the army by 2007. First measures have been taken to transfer the responsibility for border control from the Ministry of Defence to the Ministry of Interior.

Developing the State's capacity to manage crises in an efficient and democratic way requires a more precise definition of the concepts and an appropriate legislative and regulatory framework. A balanced approach has to be found, aiming to strengthen security safeguards especially regarding the army's role and the preventive action of the police and law enforcement institutions. Civilian leadership must be ensured, complemented by the definition of processes that offer transparency as well as full compliance with the principles of the rule of law.

International presence: The presence of the international community has remained a guarantee for the country's continued progress towards full stabilisation. The role of the representatives of the international community in Skopje, in particular of the EU Special Representative in good coordination with the US representative, has been critical in supporting the implementation of the Ohrid Framework Agreement. The Commission Delegation is playing an increasing role in supporting the reform process.

On 15 December a significant shift took place with respect to the EU security presence in the country with the completion of the first ever EU military mission “*Concordia*” and the launching of the EU Police Mission “*Proxima*”. Since taking over from the NATO military presence in April, “*Concordia*” had been active on the ground throughout the former crisis areas, monitoring the security situation and implementing confidence building measures. Development in the security situation led to the assessment that international military presence in the field was no longer necessary but that further steps were necessary before the rule of law could be considered fully established in the former crisis areas

In order to further improve the security situation and stabilisation of the country, the General Affairs Council upon the invitation of the former Yugoslav Republic of Macedonia authorities, adopted on 29 September a Joint Action establishing a European Union Police Mission. Police officers have been deployed since December within the Ministry of Interior and in police stations throughout the country (Tetovo, Gostivar, Kumanovo, Debar, Ohrid, Kičevo and Struga).

NATO has maintained an assistance mission and continues to play an important role in security sector reform. The OSCE has also continued to play an active role to help implementing some bids of the Framework Agreement.

The presence of the International Community on the ground has also been requested by local authorities and the Government to assist in carrying out the weapons collection process from 1 November to 15 December. The fact that no incidents marked the weapons collection process and the positive involvement of the local authorities and the population have positively contributed to further stability. A rather limited number of weapons was surrendered, however, (7,571 small arms and light weapons), and the high number of small arms illegally in private hands remains an issue.

2.1.2. Assessment of judicial system, law enforcement and respect for the rule of law.

Judicial system: Reform in the judicial system is making very slow progress. Initial steps have been taken, mainly with the adoption of a law on an independent judiciary budget. The principle of equitable representation in the election of judges was also introduced. However, the serious weaknesses affecting the functioning of the judicial system stressed in last year’s report remain. There is a very low level of public confidence in the judicial system.

The weaknesses and inconsistencies of the existing system of the selection and dismissal of judges and prosecutors place severe constraints on the development of an independent judiciary and a merit-based career system. One key issue is the politicisation of the Republic Judicial Council and the politicisation of the judiciary system. This issue must be promptly addressed, including, if necessary, by amending the constitutional framework.

There were also cases of alleged corruption, conflict of interest or nepotism reported and reviewed by the State Commission for the Prevention of Corruption. Criminal actions should be taken against those for whom there is sufficient evidence of corruption.

The continuing lack of management tools, the overloading of courts with misdemeanour cases and with administrative tasks, and the resulting huge backlog of cases still hamper the efficiency of the judiciary, and the whole process needs to be rationalised. Despite the fact that the problems have been well identified, for example in the Supreme Court Report on lower Courts, recommendations have not been followed up. The working procedures of the courts lack transparency, and court decisions suffer from unjustified delays. The proper

delivery of court decisions is an elementary but major concern. The lack of efficiency and the non-application of the rules open the way to political influence and to corruption. Proper co-operation between the prosecution and the police is also failing and this has led in many cases to the incapacity to deal effectively with crime or corruption cases.

General training needs to be upgraded, notably through the setting up of a national school for judges and prosecutors. Specific training on EU law and on organised crime and new forms of crime also need to be enhanced.

Prison system: Problems persist in relation with the training of prison staff, with the material conditions in the prisons, and with the treatment and rehabilitation of various categories of inmates needing special treatment (for example specific treatment for indicted drug abusers). Although the capacity of the prison system seems to be sufficient, old buildings need to be renovated and special units to be built.

Respect for the rule of law: The former Yugoslav Republic of Macedonia has made slow progress in strengthening the rule of law, mainly due to the structural weaknesses of the law enforcement and judicial institutions, politicised and poor public administration, corruption and organised crime. The legislative, the executive and the judiciary should co-ordinate their actions in order to find solutions to bring the rule of law into line with European standards.

The high level of **corruption** and the mistrust towards institutions it generates remain a major deterrent factor to growth and investment, and beyond this, to the success of many reforms which have been initiated to accelerate the transition of the country towards a modern democracy and economy. The weaknesses of the institutions and the lack of transparency in public decisions are key issues to be addressed. In general terms the institutional capacity to investigate and prosecute corruption must be increased and the co-operation among law enforcement bodies upgraded, as committed to by the Government in the list of action-oriented measures against organised crime it adopted in November.

The Government has taken preliminary measures, in particular through supporting the State Commission for the Prevention of Corruption, which has been given a central role – despite limited resources – in defining a comprehensive approach to fighting corruption. The State Commission started its work by collecting reports on the assets of public office holders, and thirty-nine judicial procedures have been initiated for failure to report. It also presented a State Programme for Prevention and Repression of Corruption. In June the Government approved this text which should be followed up by appropriate budget allocations and a realistic implementation plan. The full co-operation of the public administration, which is sometimes problematic, will remain essential. Another weakness in the strategic approach towards an effective fight against corruption is the lack of clear concepts for co-ordination in identifying and prosecuting corruption, and failures in the exchange of intelligence between the criminal police, the financial police, the prosecution and the State Commission for the Prevention of Corruption.

2.2. Human rights and protection of minorities

The implementation of the Framework Agreement and confidence-building measures are progressively reducing ethnic tensions. The reform process has started to benefit not only minorities but society as a whole and contributes to the strengthening of democracy and better governance. Tensions have not however completely disappeared, and provocations or incidents must be kept under constant monitoring so that they do not to escalate. Effort is still needed to ensure that police misconduct is efficiently prevented or, if it occurs, duly sanctioned. In the field of higher education, the process of establishing a third State University in Tetovo has also been a highly symbolic development. Great care must be taken to ensure that this process undertaken ensures that democratic and academic standards are met. More generally education is an area where much remains to be done. The development of the country's democracy will also depend on the development of professional media. Further efforts are needed to ensure the greater independence and the upgrading of the broadcasting services. Greater professionalism in the media would also contribute to furthering democracy.

2.2.1. Civil, political, economic, social and cultural rights

Human rights: Human rights and fundamental freedoms are guaranteed by the Constitution. The European Convention on Human Rights entered into force in the former Yugoslav Republic of Macedonia in 1997. However, as underlined by the Ombudsman's reports, while the rights of citizens are in principle respected, the situation is still far from being fully satisfactory and the functioning of protective mechanisms should be improved as part of the reform of the public administration. Although citizens' awareness of their rights is increasing (60 % increase in the number of complaints to the Ombudsman in the latest period), it has not yet reached a high level.

Cases of mistreatment by the police have decreased since the 2001 crisis, but misconduct or violation of procedures remains an issue which deserves due attention . A few incidents linked to police operations have once again raised the question of the appropriate planning and training of the police forces. There have been cases of unlawful arrest or detention, violation of the custody rule and of the right of family members to be informed, or violation of the right not to be forced to make a statement during police and court procedures. These violations of due process must be dealt with. In particular, due attention should be paid to ensuring the application of procedural rules on pre-trial detention in conformity with Article 5 of the European Convention on Human Rights, which stipulates that an arrested person should be promptly brought before a judge.

Observers still express concerns on the lack of thorough investigation into serious allegations of human rights violations in past reports. The Professional Standards Unit of the Ministry of Interior has been strengthened and has improved its investigations. Twenty criminal reports have been drawn up, but only disciplinary measures have been taken so far.

Judicial and police reform, the implementation of the code of police ethics adopted in January, measures to fight corruption and organised crime, as well as the empowerment of the Ombudsman's office should, if enhanced, allow improvement of the overall situation. Continued attention must be paid to the specific measures to prevent police ill-treatment and combat impunity from disciplinary action, as identified in the January 2003 Anti-torture Committee Report of the Council of Europe which the Government has started to implement.

Freedom of expression and media: Freedom of expression is guaranteed formally and is put into practice. Some initiatives in support of reform have been undertaken in the media sector, such as the creation of a television channel broadcasting programmes in minority languages, and initial measures have been undertaken to reform the public broadcasting company.

There are however a number of problems in this sector, relating to the current legal framework, the lack of resources, the lack of professionalism and the fact that the media, being split along ethnic lines, often fail to set an agenda reflecting a collective interest. Proper mechanisms are needed to ensure the independence of the media, in particular a strengthened and independent Broadcasting Council. The law on broadcasting should be reviewed to address shortcomings in the functioning of the public broadcasting company (MRTV).

As regards the work of journalists, the absence of a proper legal framework for access to information is proving to make proper reporting more difficult. The legal definition of defamation should also be reviewed so that it is decriminalised. Professionalism in the media needs to be substantially improved through the development of training programmes and the reform of education in journalism.

Ombudsman's office: The role of the Ombudsman in the reform of the public administration and in defending citizens' rights is increasingly understood. A new law enhancing his role was enacted in September, in compliance with the Ohrid Framework Agreement and Amendment XI of the Constitution. The review and adoption of the 2002 Ombudsman's Annual Report by Parliament was a positive move. It needs to be followed up, however, starting with the full establishment of the Operational Programme for Implementation of the new law. The co-operation and assistance provided by the various administrations to the Ombudsman remains an area where improvement is needed. Non-co-operative attitudes should be tackled decisively. In particular the Parliament could, where possible, insist on the responsibility of public function holders so that they are held accountable.

Gender equality: The principle of equal salaries and of equal treatment of men and women concerning employment, training, career advancement, and working conditions has been introduced. The Government has also adopted a National Action Plan for Gender Equality. The role of NGOs is also acknowledged and should continue to be valued. Activities aiming to strengthen women's participation in the Government's decision-making structures are progressively being implemented. In addition initiatives have been undertaken to strengthen the socioeconomic position of women in society. Domestic violence remains a problem and the Criminal Code does not contain articles that relate to family violence.

Disabled persons: While the law prohibits discriminations on the basis of disability, this provision remains to be fully implemented. The Parliament has adopted a Declaration on Protection and Promotion of the Rights of Persons with Special Needs, which will have to be duly implemented.

Education: Substantial progress has been made in the reform of higher education in the Albanian language. After lengthy debate, the Government proved its capacity to compromise on a sensitive issue and succeeded in laying down the legislative conditions enabling the establishment of State University in Tetovo. However, there are open questions which need to be addressed carefully regarding the standards to be reached by the University's curricula

and the need to avoid undue duplication with curricula proposed by the South East Europe University. As regards the latter, its continuous development and wide impact across various communities has confirmed it as a viable, forward looking, and academically sound educational institution. At the end of the four year cycle this year, Albanian students will represent over 14 % of all higher education students in the country (4.8 % in 2000/2001).

Little progress has been made however on the reform of the education system which has suffered from a lack of continuity with the various plans made by successive Governments. A challenge is the lack of embeddedness of Vocational and Education Training reform elements in existing national structures and practices.

Incidents and protests with racist connotations at the reopening of schools illustrated a worrying politicisation of the education issue. In addition, there is a danger of growing separation along ethnic lines. Over-politicising the education issue may well put at risk progress in a key area for the future of the country.

Freedom of religion: Co-operation between various religious communities in the preparation of the draft Law on Churches and Religious Communities should be examined as religious dialogue can usefully contribute to the relaxation of cultural and ethnic tensions. Recent tensions between the Macedonian Orthodox Church and the Serbian Orthodox Church resulting in legal actions have raised a risk of politicising an issue which should be dealt with first at a private level and between churches.

2.2.2. Minority rights and refugees

Several incidents which occurred during 2003 showed that interethnic relations in the former crisis areas are still fragile. Even when aiming to catch well-known criminals, the actions of the security forces can easily escalate, causing interethnic tension, if not properly planned and carried out. However the completion of the implementation of the Framework Agreement, a sense of political responsibility by local authorities, including in the former crisis areas, in addition to the forthcoming implementation of the Ministry of Interior reform, should be key elements to ensure possible future incidents and provocations remain isolated. Efforts made to fully apply European standards, such as the implementation of the Framework Convention for Protection of National Minorities of the Council of Europe, would help to build further confidence and sense of loyalty to the State.

The **Law on Citizenship** was modified in December and entered into force in March. It will bring clarity to the legal status of a number of people who have thus far been residing in the country without one, following the break-up of the former Yugoslavia.

Significant progress has been made in the return of **Internally Displaced Persons (IDPs)**. There are 2.678 IDPs remaining, meaning that the reintegration of the IDPs in the villages is almost completed. This has been helped in particular by the completion of the housing reconstruction programme. However, the final phase was not without incident (burning, looting, demolishing and vandalism of houses). Local authorities have a role to play in stabilising the situation, and the police must investigate such cases thoroughly. It is expected that the reconstruction of police stations in Matejče, Aračinovo and Tearce will contribute to the sustainability of the IDPs return and promote further return. On the other hand, Unresolved property issues, problems with documentation and the poor socio-economic situation also remain obstacles to return. The Government has presented a programme on economic revitalisation in former crisis areas.

The situation of the **Roma** was highlighted when a group of Roma refugees from Kosovo who lacked proper status protested at the border with Greece from May to July, trying to obtain asylum in the EU. While the Government has shown flexibility in finding a compromise to clarify the status of these refugees, the issue of further integration of the Roma in the society and fighting against discrimination in the access to social services, education and employment will require a comprehensive approach.

The number of **refugees** has slightly decreased compared to last year, with fewer than 2.500 refugees in the country (UNHCR figures at 31 December 2003) and 1.568 in Kosovo. Most of them (2.285) are now **asylum seekers** following the adoption of the Law on Asylum and Temporary Protection in July. Activities are underway to accelerate the return of the refugees presently in Kosovo.

2.3. Regional and International Cooperation

The former Yugoslav Republic of Macedonia remains an active supporter of regional co-operation and has maintained its efforts to develop good neighbourly relations. This is based on the growing understanding of mutual dependency and the need to address common challenges, whether security-related or economic, and needs of the citizens, through co-operation and pragmatism. The Government's position towards the situation in Kosovo has been constructive and this will remain a factor in maintaining regional stability. Cross-border co-operation has also increased and is an area where practical initiatives can be further developed. At international level, the former Yugoslav Republic of Macedonia joined the World Trade Organisation. While the cooperation between the former Yugoslav Republic of Macedonia and the International Criminal Tribunal for the former Yugoslavia has not raised concern, the adoption of a legislation on cooperation would help ensuring the proper interpretation of the Amnesty Law.

2.3.1. Regional cooperation

The former Yugoslav Republic of Macedonia has remained an active participant in the **Stability Pact** and in the **South East European Cooperation Process** initiatives. In particular it has initiated the coordination of the countries participating to the SEECP in order to present joint conclusions at the Thessaloniki summit. An example of regional initiatives has also been the conference on border security and management which took place in Ohrid in May, under the auspices of the Stability Pact, the EU, the OSCE and NATO.

Relations between the former Yugoslav Republic of Macedonia and its neighbours have continued to develop. This positively reflects an increasingly well-understood mutual dependence and a shared interest in meeting common challenges. In particular the Government has been active, inter alia in the preparation of the Thessaloniki summit, in contributing to enhancing regional co-operation and co-ordination on EU integration matters. Bilateral memoranda for co-operation on EU integration-related matters, which are providing for contacts both at administrative and political level, were signed with Slovenia, Croatia and Bulgaria.

The signature of a bilateral free trade agreement with Moldova in January was a positive move which completed the network of bilateral FTAs to be established under the Stability Pact Memorandum of Understanding.

Cross-border co-operation is also increasingly on the agenda. It has been developing with Albania and Greece, through the establishment of the Euro-region Prespa-Ohrid, as well as with Bulgaria and Serbia, through the Euro-regions Sofia-Niš-Skopje and with Greece and Bulgaria through the Euro-region Belasica. An agreement was also signed with UNMIK.

An increasingly close relationship has been sought with **Albania**, as illustrated by numerous meetings taking place at high level. Significant co-operation is being developed in building reaction mechanisms to common security challenges (security, human and drug trafficking, border control and visa regime) and a friendship agreement is under preparation. Several initiatives are underway for the environmental protection of Lake Ohrid. At the same time, the bilateral free trade agreement between the two countries is progressively bringing benefits.

Bilateral relations with **Bosnia and Herzegovina** have been developing at political and technical levels, and it is likely that a bilateral agreement on economic co-operation will be signed between the two countries.

Common aspirations with **Croatia** to join the EU have been the main basis for developing co-operation between the two countries at political and technical level. A Memorandum of Co-operation was signed in March 2003, providing for the exchange of experience and expertise and the development of joint initiatives to intensify the process of preparation to future EU membership.

Contacts with **Serbia and Montenegro** at the level of the Ministries of Foreign Affairs, Defence and Interior have been developing. An agreement was signed on co-operation in the fight against terrorism, organised crime and drug trafficking. Recent tension between the Church of Serbia and the Church of Macedonia has fortunately not affected the relationship between the two countries. By refraining from interfering, both Governments will avoid feeding the religious dispute. As regards Kosovo, the Government has kept a pragmatic attitude. A solution was provided to the problem highlighted in last year's report related to the refusal of preferential status to goods coming from Kosovo. One of the two border crossing points initially planned by the authorities together with UNMIK has been opened. However the local population objected to the opening of the second crossing point. The border areas close to Kosovo remain fragile as illustrated by various security incidents at the end of the summer which stressed the need for further co-operation. After talks with Serbia and Montenegro authorities and UNMIK representatives, an agreement was signed with UNMIK on police co-operation. Meetings now regularly take place to review border security issues. In a wider approach, the direct dialogue between Belgrade and Pristina has been supported by the Government, as was the generally improved atmosphere in the region.

Relations with **Bulgaria** have also been developing on the basis of the shared objective to prepare for European integration. Two high-profile visits marked this period, with the Prime Ministers of the two countries meeting in Skopje and in Sofia and discussion taking place to adopt a memorandum of co-operation on EU integration. An agreement was signed to enhance co-operation in the area of the fight against crime.

The traditionally close relationship with **Slovenia** took on a new dimension when a Memorandum of Understanding on Co-operation for Technical Support in the area of European integration was signed in April. This memorandum, aiming to sharing Slovenia's experience in preparing itself to EU membership, is a positive example of the benefits which can be drawn by the region from the experience of the current wave of EU enlargement.

Relations with **Greece** have been developing positively in the political and economical areas. New consular sections have been opened in Thessaloniki and Bitola with the aim of enhancing co-operation and contacts across the border. The name issue remains open however with discussions have been going under the aegis of the UN.

2.3.2. International cooperation

The co-operation with the **International Criminal Tribunal for the former Yugoslavia** (ICTY) has so far met no difficulties. ICTY has taken jurisdiction over five cases, and expressly recognised domestic jurisdiction in all other circumstances. To clarify the procedural modalities of cooperation with ICTY and ensure that any domestic prosecution would not violate the Amnesty Law, it is important that appropriate legislation is adopted as soon as possible.

As regards the **International Criminal Court**, in July the former Yugoslav Republic of Macedonia ratified a bilateral immunity agreement with the USA which regrettably runs contrary to the “EU guiding principles concerning arrangements between a state party to the Rome Statute of the ICC and the United States regarding the conditions of surrender of persons to the court”¹.

Work has intensified to prepare for **NATO** membership and a national programme has been prepared. As an objective shared with other countries in the region, preparation for NATO membership has also fostered regional co-operation. A regional agreement was signed in Tirana by the former Yugoslav Republic of Macedonia, Albania, Croatia and the USA in May to promote further these efforts.

Measures have been undertaken to progress on the fate of **kidnapped and missing persons** which has still not been clarified. As recommended by the International Commission on Missing Persons (ICMP), which provided expertise and assistance in the setting of a national process, a Government-Parliament Investigation Commission was set up in December. It is important that the process does not become politicised, because it is an issue which, when solved, will contribute to healing still-open wounds.

Following the conclusion of the negotiations in 2002, the former Yugoslav Republic of Macedonia became the 146th member of the **World Trade Organisation** on 4 April 2003. This important achievement should contribute significantly to economic development.

¹ The guidelines were adopted by the Council on 30 September 2002.

3. Economic situation

3.1. Current Economic Situation

In 2003, economic growth in the former Yugoslav Republic of Macedonia recovered and inflation remained low. Monetary stability was maintained and the general government deficit was reduced by 4 percentage points compared to the previous year to a low 1.5% of GDP. The most worrying signal came from the persistently high unemployment rate. Moreover, the level of foreign direct investment was lower than the previous year's already low level, reflecting the still high perception of political risk and the difficult business environment. The agreement reached with the IMF in April 2003 on a new 14-month Stand-by Arrangement contributed to the maintenance of a stable macroeconomic and fiscal framework and allowed the release of substantial foreign financial assistance from donors.

According to official statistics, 2003 **real GDP growth** is estimated to have been around 3%, broadly in line with the initial forecasts of the authorities and the IMF. This level constitutes an improvement against 2001-2002 (-4.5% and +0.7 %, respectively), but remains insufficient to reduce unemployment and substantially improve living standards. Industrial production increased by approximately 7% in the first three quarters of 2003, thanks to the positive performance of a few important sectors, such as the steel and oil industry.

In April 2003, the **unemployment** rate, according to the Labour Force Survey using ILO standards, increased to around 37% of the labour force, up from 32% in the previous year. This was due to higher participation rates in the labour force, the absence of new job creation and the dismissal of workers linked to the restructuring of large state owned enterprises. While the large size of the grey economy may influence the reliability of the employment statistics, it is undoubtedly a reason for concern that both the percentage and the absolute number of registered unemployed have grown in the first months of 2003. The government put considerable hope in a specific measure aimed at encouraging new hirings by subsidizing payroll contributions (the so-called "Branko's Law", adopted in April 2003).

Inflation continued to be low in 2003, with consumer prices increasing by 1.2% on average, well below the projected 3.0%. Along with a drop in food prices, which had surged in 2002, the downward trend can be explained by the depreciation of the dollar, since the denar is de-facto pegged to the euro. Moreover, a reduction in average import tariffs and prices following the country's WTO accession in April 2003 also may have played a role.

In 2003, **fiscal performance** has improved very substantially. The general government deficit is estimated at around 1.5% of GDP, against a forecast of 2.7% at the beginning of the year and compared to the 5.7% deficit which was recorded in 2002. The drastic fiscal adjustment in 2003 by 4 percentage points of GDP with respect to the previous year is accounted for by the significant reduction in expenditure from 41% of GDP to 36% of GDP. This was the result of the reduction or elimination of some significant non-recurrent expenditures in 2002 - such as security-related expenditures and the one-off repayment to depositors involved in the TAT pyramid scheme – as well as the low execution of budgeted capital expenditure. As regards the latter, projects were systematically reviewed and often delayed or cancelled, because many budget users were failing to come to terms with stricter procurement procedures. Total revenues (34.5% of GDP) have been in line with the projections, thanks to the overperformance in the collection of social insurance contributions, customs duties and non-tax revenue, compensating for a lower than projected VAT revenue.

On the **external side**, in 2003 there was a slight decline in the overall trade exchange in nominal (euro) terms. Exports remained stable compared to 2002, reaching around € 1200 million, while imports decreased by 6%, totalling about € 1900 million. In 2003, the trade deficit is expected to have reached approximately € 700 million or 17.2% of GDP, lower than in 2002 in euro terms and as a share of GDP, but widening when measured in dollar terms owing to exchange rate effects.

The 2003 current account deficit is estimated at 6.2% of GDP, including significant foreign assistance amounting to around 2.1% of GDP. Total transfers, private and official, decreased from more than 13% of GDP to more than 11% of GDP. In 2003, the level of Foreign Direct Investments (FDI) was very low, amounting to around 1% of GDP, the same level as in the previous year. Additional donor support, amounting to more than € 100 million, contributed to financing the balance of payments deficit and maintain international reserves at a level corresponding to around 4 months of imports. The external debt as ratio to GDP declined by five to six percentage points in the course of 2003 reaching 33% at year-end, in part due to the weakening of the US dollar against the euro.

Over the reporting period, the authorities co-operated with the **International Monetary Fund** (IMF) and maintained a consistent macroeconomic and fiscal framework, which was a recommendation of the previous SAP report. A long overdue Stand-by Arrangement (SBA) with the IMF of SDR 20 million (around EUR 25 million) was approved on 30 April 2003, allowing the release of substantial foreign financial assistance from other donors. The first review of the SBA was successfully completed in October 2003. The second review is expected to be completed in Spring 2004 and the government has requested the IMF to start negotiations for a successor programme.

In 2003, the World Bank disbursed USD 17 million under the PSMAC (Public Sector Management Adjustment Credit) arrangement and USD 20 million for the second tranche of the FESAL 2 (Financial and Enterprise Sector Adjustment Loan) arrangement. In September, the Board of the World Bank approved a new Country Assistance Strategy. It envisages a – performance based - lending envelope of USD 90 million (base case) over three years, which could reach up to USD 165 million in a strong reform scenario.

In July 2003, the EBRD, with other international shareholders, opened a Micro-Finance Bank - *Pro Credit Bank* - typically providing loans of up to € 100,000. Its rapid procedures for examining credit applications immediately proved very popular with small businesses. In 2003, the EBRD also approved a loan of € 8 million to a marble processing company and three other regional projects – involving the former Yugoslav Republic of Macedonia - in support of the energy, transport and food processing sectors, for a total envelope of around € 105 million.

3.2. Existence of Free-market Economy and Structural Reforms

The structural reform process regained momentum in the course of 2003. The Action Plan for the restructuring, liquidation or privatisation of 40 large loss-making enterprises, which was launched in 2000, was finally completed. The authorities are now focusing on a new priority: private sector development. In September 2003, the Parliament approved a law setting up the Agency for Promotion of Entrepreneurship. However, the generally poor business environment and, in particular, the inability to enforce effectively contracts and creditors' rights hampers the lending activity of the banks, in turn affecting investment and economic development. Banking supervision in the country is improving, while banks are expected to implement a new regulation on consolidated accounting and banking supervision. The difficulties of a few, mainly small, banks in 2003 did not affect the financial stability of the whole system. Competitiveness and efficiency of the banking sector must improve in order to allow easier access to finance to SMEs. Finally, progress was made in the implementation of the pension reform program.

The **privatisation** process of small and medium size enterprises (SMEs) is almost complete. As of the end of September 2003, 1,683 enterprises had been privatised, while 81 state companies of those included in the privatisation programme that began in 1993 remained for sale. Besides having met the relevant conditions agreed with the World Bank within the FESAL2 commitments concerning large loss-making public enterprises identified in the Action Plan of 2000, the government succeeded in resolving most of the remaining cases in 2003, with a few exceptions generally due to ongoing legal disputes beyond the control of the authorities. It therefore complied with the recommendation identified in the 2003 SAP report.

In 2003, the Government started focusing on measures and activities to support the development and to enhance the competitiveness of SMEs, and more generally to improve the **business environment**. In January 2003, it adopted a programme on Small Enterprises Development Support and Entrepreneurship Encouragement and, in September, the Parliament approved a law setting up the Agency for Promotion of Entrepreneurship. The authorities also endorsed the principles of the European Charter for Small Enterprises, and set up a strategy for their implementation. A programme for attracting FDI was approved by the Government in August, and the Agency for Promotion of FDI should start its operations in early 2004. However, as regards the business environment, the inability to effectively enforce contracts and creditors' rights hampers the lending activity of the banks, in turn hampering investment and economic development. The absence of a reliable cadastre and the lack of certainty about property rights is also proving to be a serious impediment to investment. In particular, the lack of clear property rights limits the ability of firms – in particular, small and micro firms - to pledge property as collateral and obtain loans.

Over the reporting period, there have not been major structural changes in the **financial sector**, which is dominated by the banking sector, with a very limited role of non-bank financial institutions. The soundness of the banking sector has improved over recent years. The three largest banks, accounting for around two thirds of total liabilities and assets, show relatively prudent and sound banking practices. However, the IMF Financial System Stability Assessment report published in December 2003 notes that the financial system remains vulnerable to weak governance in smaller banks and also to weaknesses in the banks' balance sheet, which are reflected in the high percentage of non-performing loans (16% of total portfolio assets as of mid-2003). In 2003, six banks were under enhanced supervision by the National Bank, but the repercussions on financial stability of the whole system were relatively minor, given the small size of these banks. Banking supervision in the

country is improving, and banks are expected to implement a new regulation on consolidated accounting and banking supervision.

In 2003, banks continued to hold excessive liquidity and remained conservative in their lending activity. Notwithstanding the drop in the average interest rate on Central Bank bills – the main instrument to control liquidity – commercial banks did not fully pass this decline on to their customers. In December, average lending rates were still high at 14.6% against an average deposit rate of around 7%. The competitiveness and efficiency of the banking sector must improve in order to allow easier access to finance for SMEs. The forthcoming establishment of an independent Banking Association, supported by EU-funded technical assistance, could contribute to the latter objective, providing support for the dissemination of best practices in good governance.

As of December 2003 100 companies were listed on the first-tier market known as the "official" market of the **Macedonian Stock Exchange** (MSE). In addition, approximately 70 further companies are traded on the second-tier market known as the "unofficial" market. This dramatic change from last year (only 8 companies were listed on the "official" market) results from a decision by the Government to require all companies meeting the listing criteria actually to list their shares on the MSE and file public annual and semi-annual reports, as well as disclosing their shareholder structure. However, the Stock Exchange continues to play a marginal role in the financing of the economy. The Securities and Exchange Commission is heading a working group to draft comprehensive amendments to the securities legislation to bring it in line with principles published by the International Organisation of Securities Commissions.

During 2003, the government made significant progress in the implementation of its **pension reform** program, but much more work is needed before the new system can begin functioning. Significant accomplishments during 2003 include the creation of the Pension Supervision Agency (PSA), the adoption of key secondary regulations and the restructuring of the Pension and Disability Fund (PDF). Before the new system can begin operating, key tasks for 2004 include capacity building of the PSA, conducting the public tender to hire two Pension Companies in charge of creating pension funds and further administrative reform of the PDF. In parallel with pension reform, it is necessary to develop and support the creation of additional investment instruments that are appropriate for pension funds and possibly allow for greater international diversification. The planned introduction of a new government securities market (see below in section 3.3 'Public expenditure management') and its evolution through more frequent auctions and a wider range of maturities represents an important pre-condition for the development of pension funds.

3.3. Management of Public Finances

The authorities also made progress in public administration reform and management of public finances, initiation of the "functional" analysis in most of the administrative services, setting up a single Treasury account and preparing the establishment of a market for government securities. The decompression of the civil service salary structure, greater control of expenditure in extra-budgetary funds, the introduction of audits throughout the administration, the implementation of the fiscal decentralisation process and, in particular, the strengthening of the capacity of local entities to manage expenditure and collect revenues, remain great challenges.

The **reform of public administration**, one of the priority areas in the previous report, made some progress in 2003. The process of downsizing public administration began in 2003 with an objective of reducing the number of public employees by 4 %, while taking into account the Framework Agreement obligations (the Law on Civil Servants was amended to improve equitable representation of communities). Some preparatory work for wage decompression in the public administration (i.e. widening the difference of wages between non-qualified and qualified jobs) has been carried out but the actual implementation has been postponed to 2004 because of the extra costs associated with this reform. In spite of a number of lay-offs and early retirements in 2003, the health sector still needs considerable downsizing and other cost-saving measures in order to achieve sustainability, efficiency and effective outcomes. However, total employment showed a net increase from 70.000 to 71.800 at the end of 2003 and remains a critical structural problem, with ramifications that go beyond the public finance aspect, encompassing the commitment of having 'equitable representation' of ethnic minorities in the administration (still under 12% in spite of new hires, mostly in police and army) and capacity issues which are vital for the EU integration process.

Public expenditure management: The implementation of procedures concerning commitment registrations in the Treasury marked a significant improvements, in line with the recommendation of the 2003 SAp report. In 2003, the authorities amended the Budget Law and the Law on Public Procurement and merged separate budget users' accounts into a single account within the Treasury. The single account allows the Treasury to ensure proper supervision and control over line ministries' expenditure commitments and payments arrears. The account includes all central government revenues, without however providing a control mechanism for extra-budgetary funds. Further rationalisation should allow, as far as possible, to keep track of the financial flows connected with the several projects financed, partly or as a whole, by foreign donors. Internal controls and audit are in place in the Ministry of Finance, but must be strengthened and broadened to the whole public administration. In the Ministry of Finance, an Internal Audit Unit was established, which is expected to be further strengthened and become a separate department, with two sub-units (Audit Policy and Operational Audit).

As regards the **management of public revenues**, the authorities improved VAT administration through enhanced internal controls and more appropriate IT support. However, the level of VAT refund arrears increased in 2003 and the authorities should tackle this problem.

Financing issues are becoming an urgent priority, as two of the main sources of (mostly foreign) finance in recent years for the former Yugoslav Republic of Macedonia, donor grants and privatisation receipts, are declining. For this reason, it is now necessary to develop a reliable system of government securities in order to raise domestic financing. In the course of 2003, the Ministry of Finance and the National Bank jointly prepared the Strategy for the Development of Government Securities Market. According to the Strategy, the first issue of Treasury Bills is expected in the first half of 2004. The successful transition from exceptional foreign financing to domestic securities financing will be pivotal in the government's ability to manage public finances.

Development of a **decentralised government** still requires significant legislative reforms. The law on Local Government Financing, [still needs to be approved by the Parliament]. The implementation of the fiscal decentralisation process and, in particular, the strengthening of the capacity of local entities to manage expenditure and collect revenues, remains a great challenge in view of the Autumn 2004 local elections, as well as over the medium-term. The

authorities made provisions in the 2004 budget for the local elections, but there seem to be no other specific commitments in the budget for costs related to fiscal decentralisation. Establishing and developing a modern and unified system of financial reporting within local self-government units is needed.

4. Implementation of the Stabilisation and Association process

4.1. General evaluation

A number of measures have been taken which indicate a wish to accelerate EU oriented reforms within the Stabilisation and Association process (SAP). These measures include better co-ordination in the implementation of obligations deriving from the contractual relationship between the Former Yugoslav Republic of Macedonia and the EU, and recommendations made within the SAP. The Government's decision to solve the problem caused by infringement of the Interim Agreement in the OKTA case was welcomed. The forthcoming entry into force of the Stabilisation and Association Agreement (SAA) will substantially increase the range and level of co-operation which currently exists between the former Yugoslav Republic of Macedonia and the EU. Adaptation of the SAA should be completed before 1 May in view of upcoming EU enlargement.

Whilst work done better to comply with the obligations of the SAA can be commended, the resources, including from the national budget, devoted to the process remain insufficient. In addition the link between strategic priorities and the definition and mobilisation of resources should be clarified. Most structures, including Parliamentary ones, have been put in place too quickly to demonstrate their capacity to make a breakthrough in accelerating the reform process implied by the SAA. Further involvement and mobilisation of all ministries will be needed in order to sustain the wide range of reforms on the Government agenda.

4.1.1. Current position

The Stabilisation and Association process is going to take on a new dimension in the former Yugoslav Republic of Macedonia as a result of the ratification of the SAA, allowing for entry into force of the agreement on 1 April 2004. Negotiations started in October on a Protocol to the Agreement to take account of the upcoming accession of ten new Member States to the EU. It is now urgent that it be completed in order to not only avoid negatively affecting trade, but also to fully benefit from application of the SAA to an enlarged market.

The period since last year's report has been characterised by an intensive agenda. After the readjustment of working party structures to better reflect the requirements of the Interim Agreement agreed in April, a full cycle of meetings of the working parties took place under the Interim, Co-operation and Transport Agreements. The sixth meeting of the Co-operation Council was held in Brussels in July. In addition, technical meetings allowed for an in-depth discussion of certain Interim Agreement related issues (Internal Market related issues including competition policies, consumer protection, standardisation, metrology, accreditation, certification, and market surveillance, etc.).

Negotiations focused on greater liberalisation of trade in agricultural and fisheries products opened in December 2002 and were successfully concluded in July. In December, the results of these negotiations were adopted by a decision of the Co-operation Council.

4.1.2. General assessment of administrative capacity

Following the release of last year's Report, the Government adopted an Action Plan in June which translated SAP recommendations into 216 activities and also defined the bodies responsible for their implementation. This followed the adoption in April of the 2003

National Programme for Approximation of Legislation. A National Strategy for EU Integration is still under preparation.

A first report on implementation of the SAp Action Plan was presented at the July Co-operation Council. Reports were also produced in November and February, and all of these contributed to the elaboration of the present report.

Measures have been taken to reinforce the Government's capacity to implement the SAA and also to progress in the SAp. A new Working Committee for European Integration, chaired by Deputy Prime Minister Šekerinska was established in March 2003 in order to co-ordinate the Stabilisation and Association process and the European Integration plan. Within the framework of the Subcommittee for Approximation to EU legislation, the Government established Working Groups for Harmonisation of Legislation with the "*community acquis*" in March. After an initial delay, these groups have since become operative.

The Sector for European Integration submits quarterly reports to the Government on progress made in relation to implementation of the Interim Agreement/SAA.

The role of the Legislative Secretariat has been strengthened to provide experts' opinion on draft laws and other legal acts from the perspective of their consistency with the Constitution, other laws already in force, international agreements ratified by Parliament and with the *acquis*. Amendments to the Government's internal rules have also reinforced the role of the Government's commissions (on the political system, on the economic system, on human resources and sustainable development) with regard to the harmonisation of national policy with EU policies and the *acquis*. Since October, a Statement on Compliance with EU Legislation must accompany each draft legal text which is submitted to the Government. An Operational Plan for implementation of the 2000 Strategy on EU training for Civil Servants was adopted in October.

Whereas those instruments above have been introduced, the capacity of the various administrative bodies involved in the process has not dramatically changed, mainly due to constraints imposed by the budgetary situation as well as to a difficulty in identifying adequately trained staff. Training of civil servants involved in co-ordination of the EU integration process, including at local level, remains insufficient. Internal expertise will need to be enhanced in order to assess whether draft legislation is in line with the *acquis*.

4.1.3. Impact of the SAA/Interim Agreement on reform

The Government has confirmed its will to launch reforms required by the implementation of the Interim Agreement/SAA, as demonstrated by the various plans adopted and structures put in place in order to better co-ordinate and monitor their implementation. However, most reforms are at an initial stage and their impact cannot yet be properly evaluated. In addition, in view of the country's still limited administrative capacity and budgetary situation, the political will to make progress should not lead to an underestimation of the time needed to implement the standards aimed at. The conditions necessary to maximise impact in last year's report remain the same for the current year: enhancing co-ordination and rationalising efforts to deal with short to medium term reforms, strengthening institutions, building capacity to ensure enforcement of the new legal framework.

4.2. Internal market and trade

Some progress has been made by the former Yugoslav Republic of Macedonia in abiding by its Interim Agreement/SAA obligations. This was seen particularly by the abolition of discrimination in the import of oil and oil derivatives. In relation to internal market related legislation, the situation is mixed. Progress has been made in the areas of competition, state aid, property rights and Customs, but little change has been seen in the areas of procurement and data protection. In all areas, implementation capacity remains weak.

4.2.1. Movement of goods

The EU is the former Yugoslav Republic of Macedonia's main trade partner and accounts for 54 % of total trade. On a sectoral level, trade with the EU is dominated by manufactured products, chiefly textiles (42 % of EU imports and 20 % of EU exports). Agricultural products accounted for 14 % of EU imports. It should be noted that energy (essentially oil) accounted for about 11 % of total EU exports to the country.

After some delay since the Government's commitment was reiterated in July 2002, the abolition of the discriminatory application of different import duties for importers of oil and oil derivatives, in breach of the Interim Agreement, was notified to the European Commission in March 2003. Two other contentious issues raised by the Commission were solved: a ban on imports of certain bovine and caprine products was lifted for the EU Member States and the acceding countries in April / July, and a restrictive regulation on conditions for the import of sugar was repealed in October. Widespread concern amongst economic operators has been created by the introduction of a € 100 fee to release import licenses for tariff free quotas under a new procedure. The Commission is currently analysing whether this fee is in compliance with relevant provisions of the Interim Agreement and WTO rules.

Some progress has been achieved in the field of standardisation, metrology, accreditation, certification, and market surveillance. The three new bodies foreseen by the 2002 legislation – Standardisation Institute, Bureau for Metrology and Accreditation Institute – were officially established in 2003 but must now be properly staffed and equipped in order to operate efficiently according to their respective functions. Secondary legislation in these fields is still pending.

4.2.2. Movement of persons, services and rights of establishment

Implementation of the 2002 Company law has been put on hold and is currently under review. In the meantime however, the 1996 legislation – which is still applicable - was amended in order to prohibit the transfer of rights arising from a number of managing bodies in the shareholding companies.

The Law on Accounting for non-profit Organisations, which regulates the accounting of NGOs (including foreign and international ones), foundations, other forms of associations, religious communities and groups, the Red Cross Association of Citizens, humanitarian organisations and associations, unions and other non-profit organisations was enacted in March 2003.

Whilst both urgently needed and crucial for the establishment of a proper system of registries as well as for co-operation with EUROPOL, appropriate data protection legislation in line with EU standards has still not been adopted.

4.2.3. Movement of capital

Residents can only carry cash or cheques to the value of € 2000 when leaving the country and €10.000 when returning to the country. Any larger amounts can be brought in only in accordance with the Law against Money Laundering. A Law on Transfer of Money was enacted in November to determine the modalities followed when transferring money. Secondary legislation still has to be adopted. Since entry into force of the new foreign exchange law in autumn 2002, portfolio investment abroad by residents has been allowed under certain conditions and restrictions, while non-residents may invest freely through authorised participants. Inward direct investment is generally free (except in a few sensitive areas covered by public security) upon registration in the Ministry of Economy. Liquidation and repatriation of direct investment and of profits from these investments can be freely transferred abroad, after income tax is paid. Direct investment abroad by residents is also free upon registration.

4.2.4. Customs

With constant encouragement from the EU Customs Assistance Mission to the Former Yugoslav Republic of Macedonia (CAFAO-MAK), some steps have been taken by the authorities to enhance the Customs Service. A Strategic Plan has been prepared by the Customs Administration on activities for the period 2004-2008 which shall be a basis to carry forward the process of reform and make the Customs Administration an effective service able to ensure timely and efficient collection of customs as well as other duties such as preventing illegal goods from entering the country. It sets out and defines what the Customs Administration (MCA) should aim at over a five year period, in terms of standards of service to the business community and the general public, operational performance, infrastructure, equipment and human resource management. However, reform and modernisation efforts have been proceeding at a slow pace.

Recently, some steps have been taken to start addressing the issue of corruption and other criminal activities within the customs service. A positive step in this direction has been the creation of a Professional Standards Unit within the MCA. The number of disciplinary measures has also increased. However, substantially enhanced efforts in this area remain necessary. It is essential to ensure that customs officers involved in criminal practices are duly prosecuted, and it is also important that disciplinary measures are taken when duly justified.

The Customs Administration, with the full support of the Government, should not only be focussed on revenue collection, but should also pay further attention to areas like organised crime, drugs and smuggling. Co-ordination between the customs administration and other law enforcement bodies should be enhanced. The administration should also ensure stability and adequate human resources management, accelerate reforms, prepare for adequate implementation of SAA requirements, and achieve proper enforcement of customs procedures throughout the whole country.

4.2.5. Competition and state aids

Whilst much remains to be done, and further progress is essential, first steps have been taken to develop an EU modelled competition policy. New legislation is needed in order to cover areas such as restrictive agreements, the abuse of dominant position, merger control and practices aimed at limiting competition. To make the law an effective tool, the competition authority should be entrusted with efficient means directly to enforce the law and impose sanctions. In addition to this, the challenge is to reinforce the administrative capacity and resources (including staff) of the Competition authorities. Consultation with the competition authority on all relevant draft legislation affecting economic activity would be necessary.

As regards control of state aid, the Law on State Aid was enacted in March 2003 and implementation started in January 2004. Secondary legislation has also been adopted. The State Aid Commission is operational, and its members were appointed in June. However, the State Aid Unit remains understaffed with only two employees. Transparency would be promoted by establishing a comprehensive inventory and reporting of all aid measures in force (based on the EU state aid definition). The State Aid Commission will have a role to play in increasing awareness of the state aid control framework amongst the ministries, the public administration and the business community. Overall the country needs further to strengthen competition policy, i. e. a horizontal approach to promote competition through encouraging liberalisation, the improvement of public procurement practices, and an approach to privatisation designed to foster competition. It will also benefit from an overall strengthening of the rule of law.

4.2.6. Public procurement

In 2003, a few cases involving substantial public purchases raised questions about the effective application of existing public procurement rules: petrol reserves during the Iraq conflict (direct agreement with Makpetrol); medicaments (international tender only after strong pressure by the World Bank); and software used by public administration (direct agreement with Microsoft).

Minor changes to the Law on Procurement allowing for improvement of both the surveillance methods performed by the Ministry of Finance and the applicability of certain provisions from the Law on Obligations were enacted in March 2003. However, the current legal framework needs further improvement in order to approximate to the EU *acquis* and the administrative capacity to implement the law needs to be seriously increased. Improvements necessary include the setting up of an Agency for Public Procurement and the adoption of a new public procurement law.

4.2.7. Intellectual, Industrial and Commercial Property Rights

The Co-ordinative Body for copyrights and other related rights, established by the Ministry of Culture in May 2003, has prepared the first draft of the Programme on Promotion of the Regime of Protection of Copyrights and other Related Rights. A review of the legislation would be needed to ensure further alignment with the *acquis*. Furthermore, special departments within the Ministry of Culture remain to be established for implementation, protection, promotion and more effective surveillance of copyrights and other related rights. The applicability of the Law on Industrial Property enacted in June 2002 has been postponed from 1 July 2003 to 1 January 2004 and the deadline for preparation of the secondary legislation has been postponed until 31 December 2003.

Awareness-raising activities in this area have started and should continue.

4.3. Sectoral policies

Some steps have been taken in relation to transport and energy within regional initiatives and also to encourage SME. However, probably partly due to the difficult economic situation and fragile social context, little progress can be reported in relation to the changes that important sectors of the country's economy need to make..

4.3.1. Industry and SMEs

The industrial sector remains weak and efforts to restructure industries have been limited. The Government has not yet adopted the restructuring and conversion programme for its **steel industry**. The **textile industry** suffered considerable losses in 2003 as a result of dollar depreciation.

Some progress has been made in supporting development of **small and medium sized enterprises** (SMEs). In parallel to the adoption of the European Charter for Small Enterprise at the Thessaloniki summit, the Government adopted a programme of measures designed to support entrepreneurship and to enhance the competitiveness of SMEs. A National Competitiveness and Entrepreneurship Council was set up. A Law on Small Enterprise Development Support and the Establishment of an Agency for Supporting Entrepreneurship was adopted in September. In addition, a strategy for implementation of the principles of the European Charter for Small Enterprise was set up. Educational reform and extracurricular programmes have improved entrepreneurship education in primary and secondary education. Access to credit facilities remains weak however, and further improvement to the institutional, legal and fiscal environment of this promising sector will be needed.

4.3.2. Agriculture

The agricultural sector accounted for 10.2 % of GDP in 2003. Some steps have been taken to promote further export of key commodities such as wine and horticultural products as well as to encourage domestic production of organic produce. A significant social measure has been adopted through the leasing, free of charge, of some state land to socially vulnerable groups in rural areas. However, little has been done to address the necessary structural reforms and lack of competitiveness characterising the country's agricultural sector.

Quality standards must be improved in order to enable the country to increase exports to the EU in the medium term. Border and internal inspection services as well as practices for plant and animal health - including all corresponding legislation - should be brought gradually into line with EC standards. Policy analysis, sector information systems and statistics need to be upgraded. Further efforts are necessary in order to respond to new and more competitive market conditions and also so that the country can take full advantage of the opportunities offered by EU enlargement.

4.3.3. Environment

Some developments can be reported as far as international conventions are concerned, with the ratification of the Landscape Convention in April and the signing of both the Strategic Environmental Assessment and the Pollution Register Transfer Protocols in Kiev during the

ministerial conference in May. Amendments to the Basel Convention (hazardous waste) and the Convention on Persistent Organic Pollutants were also ratified. Significant regional developments have also occurred, in particular in the context of the REReP (more information can be found in section 4.4 “Co-operation in other sectors” of the strategy paper). Laws on the environment, waste management, water management, and protection of nature and air quality are yet to be adopted. Adoption of these laws is important because it would be a first step towards harmonising the country’s legislation with the EU *acquis*. Two monitoring stations were mounted at Taor and Demir Kapija along the bed of the Vardar River in order to monitor the quality of the water.

However, little progress has been achieved on structural reforms and capacity implementation. Plans for administrative restructuring do not seem to be advancing, and slip ups in the National Programme for Approximation of the *Acquis*, compared to the previous year’s programme, have been noted.

4.3.4. Infrastructure

Infrastructure in the former Yugoslav Republic of Macedonia remains poor. A Programme for Public Investment for 2003-2005 was approved by the Government in September 2003. This programme lists investment projects worth € 218 million in 2003. This figure includes domestic resources as well as foreign grants and loans.

The ministers of transport of Albania, the former Yugoslav Republic of Macedonia, Bulgaria, Greece, Turkey and Italy have signed a declaration for financing Trans-European **Corridor VIII**. The declaration foresees the corridor to be completed by 2020 but, if there is a higher commitment by the countries through which this corridor runs, it is also possible that the main part of it could be in place by 2013. A technical secretariat to provide co-ordination, preparation and analysis of the main projects was also set up. The road section of corridor VIII running through the former Yugoslav Republic of Macedonia is 317 km long. 84.5 km (26 %) of this has so far been constructed while 25.5 km (9 %) is in the process of construction. The development of projects for the remaining 207 km (64 %) is continuing. Work on new sections of highway along **Corridor X** continued in 2003. Significant regional developments have occurred in transport, cf. regional co-operation initiated through the SEE Transport Core Network (more information can be found in section 4.4 “Co-operation in other sectors” of the strategy paper).

First steps have been achieved with the development of the **Energy Regulatory Commission** (set up in September) and the outlining of proposals on unbundling of the integrated monopoly, *Electric Power Company of Macedonia* (ESM) in view of its privatisation. In addition, initial steps towards the liberalisation of the energy market, in compliance with the *acquis* and with the objective of integrating the Regional Electricity Market in South East Europe have also been achieved. The plan foresees the legal unbundling of ESM and the establishment of three separate entities (a generation company, a transmission company and a distribution company) which will own the assets relevant to their functions. Restructuring should be carried out during the course of 2004. Current plans are fully in line with the latest EU Electricity Directive. These developments should be followed up by progress in redrafting the Energy Law (which was drafted in 1997 and despite amendments is still not in line with the *acquis*), establishing the Transmission System Operator (without which liberalisation and the ERC’s regulation of the electricity

sector will largely remain a paper exercise) and addressing Public Service Obligations (particularly in view of the social and economic circumstances of the country).

At regional level, significant development has occurred with regard to the Regional Energy Market (cf. signature of a revised Memorandum of Understanding in December, more information can be found in section 4.4 “Co-operation in other sectors” of the strategy paper).

A new Law on **Telecommunications** was approved by Parliament in December. The European Convention on Trans-border Television and its Protocol were ratified.

4.4. Cooperation in Justice and Home Affairs

In view of the challenges posed by crime, corruption, illicit trafficking and lack of effective border management, the need for swift progress in the reform of Justice and Home Affairs related areas has been stressed in the conclusions of the Thessaloniki Summit. Some steps have been undertaken since last year's report to develop a strategic approach to areas such as integrated border management and the fight against organised crime and corruption. The regional dimension has also been developed as bilateral agreements for co-operation with Bulgaria, Albania, Serbia and Montenegro and UNMIK/Kosovo have been signed. . While it was urgent that reforms be launched, most of them will need both time and sustained efforts in order to bear fully expected fruits.

4.4.1. Visa, border control, asylum and migration

Visa : Some changes have been introduced by the former Yugoslav Republic of Macedonia in relation to its visa regime. The practice of issuing visas at the border has been abandoned since January 2004, with the exception of local traffic at the border with Albania. The additional safeguards required so that the tourist visa sticker system would meet European standards as outlined in last year's Report have also been introduced. Further concrete measures were presented at the EU-Western Balkan Justice and Home Affairs ministerial meeting in November.

Integrated Border Management : The implementation of the commitments undertaken in the regional conference on border management and control which took place in Ohrid in May is at the core of the strategy for Integrated Border Management adopted in December. Concrete measures in relation to the first implementation phases were presented at the November EU-Western Balkan Justice and Home Affairs meeting. The strategy has been positively evaluated by the EC as well as the international community. Proper care will have to be taken in relation to operational co-operation amongst all agencies involved in integrated border management, and most notably, co-operation between the Ministry of Interior and the Army.

Plans for the transfer of control of the green border from the Ministry of Defence to the Ministry of Interior and for the setting up of a Border Police are just starting. An appropriate level of coordination will have to be ensured in order to keep to the deadlines agreed.

Managing borders also requires dialogue and pragmatical solutions at regional level. Some progress was achieved when a temporary border-crossing point with Kosovo was opened in

August. There is a strong commitment to building confidence between border management services and towards border management reform in general in the region. This is seen in the Way Forward Document of the Ohrid Conference and in the conclusions of the Thessaloniki Summit. All of these conclusions and recommendation must be duly implemented.

Asylum : After a long delay, a new Law on Asylum and Temporary Protection in line with EU standards was adopted in July. The completion of this process and the flexibility shown by the authorities towards the admission of applications have both been positive developments. There is however a pressing need to bring procedures for the management of asylum seekers and refugees in line with accepted international standards. There is also a need to incorporate asylum issues into a fully integrated border management system. Training in identifying and screening asylum seekers and other migrants should be provided. There should also be a focus on refugee law and human rights training, in line with international conventions.

Important work lies ahead with the drafting and adoption of appropriate by-laws for the implementation and development of reception policies and facilities. Through a Government decision passed on 3 March 2003, Temporary Humanitarian Assisted Persons (THAP) status was extended until 28 September 2003 for those Kosovo ethnic minorities who have remained in the country since 1999. The Government then decided to terminate the THAP regime from this extended date. However, individual access to the asylum procedure will still be granted to ex-THAPs who do not repatriate, in line with the new law on asylum. A proper solution remains to be found in relation to Kosovo refugees who may not benefit from asylum but nevertheless cannot be returned forcibly to Kosovo. The Ministry for Labour and Social policy will have to take responsibility for these refugees, as stipulated in the new legislative provisions.

An Inter-Ministerial Working Group on Local Integration has been established within the framework of the Migration and Asylum Initiatives and the National Action Plan. The Ministry of Labour & Social Policy also has a section for reception and local integration. On the assumption that a substantial number of current beneficiaries under the THAP regime will be granted asylum in 2004, the number of recognised refugees in need of local integration support will increase.

There is a need to develop a concrete return policy with its own set of procedures. Those persons in need of international protection and residential permits should be separated from those illegal migrants who are not able to obtain permission to stay in the country. Voluntary return should be promoted and escorted return procedures should be introduced.

Migration: As of 31 December 2003 the Former Yugoslav Republic of Macedonia has ratified readmission agreements with France, Italy, Switzerland, Slovenia, Slovakia, Bulgaria, Croatia and Germany. The agreements with Romania and Hungary are pending ratification and further agreements with Belgium, the Netherlands,-Luxembourg, Denmark, the Ukraine, Albania and the Czech Republic are under negotiation.

Migration legislation is in need of revision. While the Law on Asylum and Temporary Protection is compatible with European standards, the Law on Movement and Residence of Aliens is not. In 2003, there were no changes to legislation with regard to legal and illegal immigration and trafficking in human beings. There is a need to establish a common strategy to fight illegal immigration and trafficking of human beings, both at the border and inside the country, including the revision of the legal framework applicable to foreigners.

4.4.2. Money laundering

The decision to strengthen further the Directorate as a functional financial intelligence unit and to avoid incorporating it into the financial police are both progressive steps. International cooperation should be supported by the agreements signed with the financial intelligence units of Slovenia, Croatia, Serbia and Montenegro and Bulgaria. As a follow up to the commitment given at the Thessaloniki summit, the government has adopted a specific action oriented measure in order to strengthen anti money laundering capacities. This includes the regional exchange of information regarding suspicious transactions.

The Directorate against Money laundering still does not meet international standards as illustrated by the failure to meet membership requirements for the Egmont Group. The exchange of intelligence with the financial police and other law enforcement and administration services will have to be strengthened in order to allow the Directorate to fulfil its role of financial intelligence unit. Understaffing of the Directorate is also an obstacle to further activities. No court case has yet been introduced. Coordination of the Financial Police with other police services should also be clarified as the current set-up allows for escape-clauses.

4.4.3. Drugs

The Police have succeeded in making a number of arrests in the field of drugs trafficking. Nonetheless drug related criminal offences increased by almost 40% in the period January-September 2003. At the same time the number of arrests and convictions has increased by 33%. An increase in the number of registered drug abusers is a matter for concern since it suggests that the former Yugoslav Republic of Macedonia is not only a transit country but is also increasingly becoming a consuming country.

These developments call for energetic action to be taken by the newly established Inter-Ministerial State Committee against illegal production, trafficking and abuse of drugs. However this committee has not yet started effective work. The lack of central strategic planning has led to a fragmented institutional and legislative framework. Proper coordination must be established amongst the authorities concerned. Setting an appropriate legal framework in relation to drugs is also needed as a precursor to preventing illicit production.

4.4.4. Police

The evolution of the country's security situation which is increasingly dependent on crime related factors has highlighted reform of the Police as a priority. The police structure is currently highly centralised and there is a failure to reach standards common to modern and democratic police services. Therefore the Police, as well as the Ministry of Interior, face comprehensive reforms. Tasked with a monitoring and advising role of the local police forces, the "*Proxima*" mission should also support progress toward a professional police operating according to EU best practices and standards.

A first step in the reform has been completed with the dismantling of the former paramilitary unit "Lions". Progressively equitable representation within the police has been promoted. At a strategic level, the main priorities were identified by the government and a Strategy was adopted in August and completed in January 2004, following EC recommendations. They have now to be converted into a concrete action plan covering all components of the Ministry of Interior, including the Directorate for State Security and Counter Intelligence

(DBK), and aiming to an effective devolution of power to local and subordinate levels of the Ministry of Interior and Police services.

Full attention should at the same time be given to equitable representation and career development of police officers, especially regarding managerial and investigative functions, in line with obligations deriving from the Framework Agreement. A new system of human resources management should aim at creating accountability and empowerment of officers in a transparent way.

The relationship between the Ministry of Interior and the Ministry of Defence in the area of security, crisis management and support to police operations needs to be clearly established.

4.4.5. Fighting organised crime and terrorism

There have been some measures taken to more efficiently tackle organised crime. The speedy implementation of the specific action-oriented measures against organised crime presented by the former Yugoslav Republic of Macedonia as a follow up to commitments taken at the London inter-ministerial Conference (November 2002) and in the context of the November ministerial meeting on Justice and Home Affairs, is important. The Constitution was amended to enable the use of special investigative techniques. Law enforcement activities against trafficking in human beings have been more effective even if a low conviction rate relative to arrests has however emerged as an area of concern. In this respect the development of witness protection programmes and the provision of specific training for Police and prosecutors are steps in the right direction. The possibilities raised by the action oriented measures against organised crime for cooperation in the region in relation to witness protection should be utilised. Temporary residency status for victims of human trafficking should be considered.

Still, more needs to be done. Changes in the legal framework (in the criminal procedure, the criminal code, and in the protection of witnesses and victims legislation in particular) will be needed to allow for the implementation of the Constitutional amendment. The UN Convention against transnational organised crime has been signed but not yet ratified (subject to the prior adoption of a series of measures necessary to make the national legal framework compatible with the UN Convention and its protocols). Legislative changes will have to be introduced in order to implement the ratified international conventions properly. The necessary reform of law enforcement bodies and the Judiciary in order to allow them deal effectively with organised crime is only commencing. The planned establishment of a separate section within the office of the Public Prosecutor devoted to the fight against organised crime is a positive step. However, little has been done to upgrade coordination between prosecution and police, which would be needed to strengthen all phases of criminal investigation.

The capacity to gather and analyse criminal intelligence must be enhanced. A central criminal intelligence unit would upgrade the current capacity and should be established in coordination between Police, other law enforcement bodies and the Judiciary.

More generally, resources used for the fight against organised crime should be upgraded and training as regards new forms of criminality and the methods necessary to fight these new crimes should be provided. As in other areas, there is a need to increase the national capacity not only to manage the process of reforms, but also to coordinate actions amongst the ministries themselves and with the EU (especially Commission services, but also the

Member States), within a clear and realistic framework. The cost of the various institutional reforms should not constitute a deterrent to implementation of the various measures. At the same time the existence of various strategic documents provides for proper coordination in the implementation of priorities.

As regards the fight against terrorism, the former Yugoslav Republic of Macedonia has adopted eight of the twelve UN Conventions against terrorism. Progress has been slow however on the adoption of the terrorist financing and terrorism bombing Conventions.

5. EC Financial Assistance

Between 1992 and 2003 the former Yugoslav Republic of Macedonia benefited from total European Community assistance of approximately € 677 million. In 2003, € 43.5 million was allocated to the country under the CARDS Programme, on the basis of the priorities set out in the Country Strategy Paper for the former Yugoslav Republic of Macedonia covering the period 2002-2006 and the Multi-annual indicative Programme for the period 2002-2004, adopted by the European Commission in December 2001.

Assistance has focused on institutional reform and development in order to favour the gradual integration of the country into European structures while also taking into account the needs arising from the implementation of the Framework Agreement.

As in previous years, the 2003 CARDS Programme (€ 43.5 million) has been based on the principles and priorities of the SAp and is therefore aimed at helping the country prepare for full and effective implementation of the SAA. It also addresses some of the country's needs related to implementation of the Ohrid Framework Agreement such as the strengthening of inter-ethnic relations and the strengthening of the administrative capacity of local municipalities. The main focus of the 2003 programme was on the following sectors: Democracy and Rule of Law (inter-ethnic relations and support to civil society), Economic and Social Development (private and financial sector development, trade, local infrastructure development, social cohesion and education), Justice and home Affairs (integrated border management, immigration and asylum, fight against crime) and the Environment.

In October, € 2 million was allocated from the 2002 CARDS National Programme Reserve in order to develop a project designed to facilitate the process of achieving equitable representation of non-majority community representatives in the public administration. The funds are enabling the training of some 600 trainee civil servants from non-majority ethnic communities.

The CARDS Programme 2004 (€ 51 million) reflects the main priorities set out in the Multi-annual Indicative programme. The original annual allocation of € 45.5 million has been increased by € 5.5 million in accordance with the Council conclusions of 16 June 2003. These conclusions were successively endorsed by the Thessaloniki European Council of 19 June and by the Declaration adopted by the EU-Western Balkans Summit of 21 June (in conjunction with the "Thessaloniki Agenda"). Added importance will be given to selected key projects designed to help the country progress in the implementation of the Framework Agreement and in particular, in the sector of equitable representation of non-majority ethnic communities in the public administration, especially during decentralisation.

In addition, the former Yugoslav Republic of Macedonia benefits from the CARDS Regional Programme. Besides this, the EC has continued to provide funding under specific budget lines in the fields of environment, Justice and Home Affairs, and the 6th Framework Programme in Research under which the country can benefit from funding for indirect actions within all thematic priorities of the Programme and from funding for complementary activities of the INCO part of the 6th Framework Programme.

The Commission has completed the implementation of the EC macro-financial assistance decided by the Council in November 1999 (€ 80 million) and increased by € 18 million in December 2001. The third *tranche* (€ 10 million grant and € 10 million loan) was released in May-June 2003 following approval by the IMF Board of a new stand-by-arrangement with

the authorities of the former Yugoslav Republic of Macedonia. The fourth and last *tranche* (€ 18 million loan and € 8 million grant) was released in December upon fulfilment of the economic policy conditions set in the Supplemental Memorandum of Understanding (SMoU) signed in September 2002 by the European Community and the former Yugoslav Republic of Macedonia.

EC **humanitarian assistance** (ECHO) was progressively phased out in 2002 due to an overall improvement in the humanitarian situation in the country. ECHO activities were eventually terminated in March 2003.

As of 31 December 2003, the **European Investment Bank** had supported projects in the former Yugoslav Republic of Macedonia with funds totalling € 163 million. These funds were concentrated in the area of transport – in particular road construction (€ 130 million) – and small and medium enterprise financing (€ 20 million). In 2003 a project was approved to support the energy sector (€ 13 million).

Implementation of assistance has been taken over by the European Agency for Reconstruction whose mandate was extended to the former Yugoslav Republic of Macedonia with effect from 1 January 2002 for the management of emergency assistance provided in 2001, and from 1 March 2002 with respect to the implementation of past and future programmes/projects.

In March 2002 the EAR took control over a total of € 105 million of financial assistance committed under PHARE/CARDS annual programmes between 1997 and 2001. It has made good progress in implementing this backlog which has now significantly decreased, with over 80% of the € 71 million in uncontracted funds now contracted.

CARDS funds allocated to the customs sector, to the TEMPUS programme, as well as those allocated through the Regional Programmes have remained centralised at Commission Headquarters. Deconcentrated implementation by the EC Delegation applies to any funds allocated through the EIDHR budget line (€ 0.5 million in 2003).

6. Perception of the EU

The close relationship between the EU and the former Yugoslav Republic of Macedonia has been made highly visible during the course of 2003 through the activities of the large EU presence in the country (Delegation of the European Commission, EU Special Representative, European Agency for Reconstruction), and the “*Concordia*” and “*Proxima*” Operations. The EU’s continued support of the political stabilisation process has contributed to the maintenance of a generally positive image in the country. The rapprochement between the country and the EU is also perceived to be a guarantee of economic development and further political stabilisation. More than 90% of the population support membership of the EU². Further efforts are needed to improve the understanding of the Stabilisation and Association process.

The commitment of the Government to move forward in the process of European integration has contributed to heightened public awareness of the challenges ahead and also of the benefits it can engender for the country. However, there is still a need to explain what the SAA means for relations between the EU and the former Yugoslav Republic of Macedonia and for the reform process.

Newly planned communication efforts by the Government, through the Sector for European Integration, on the challenge of European integration are likely to be a positive catalyst for further improvement of the general perception of the EU in the country. In March 2003, the Government adopted a Strategy on Communication with the Public in relation to the processes involved in EU integration as well as an Operational Plan for its implementation. The adoption of a national strategy for EU integration should also put in clear terms the European ambitions of the country. In addition, several NGOs emerged with programmes aimed at active participation in the EU integration process.

In this context the importance of the development of adequate information and communication tools, including appropriate opinion polls, is strongly encouraged.

² Based on results obtained from the most recent opinion polls carried out: 1) the Institute for Democracy, Solidarity and Civil Society carried out a public opinion poll under the project financed by the Government "Public Opinion in Macedonia on EU integration and the EU" in December 2003; and 2) the International Republican Institute carried out a Survey "Macedonia in 2003" in September 2003.

7. Annex ³

³ Eurostat data may be different from figures in other sections of the report, where recent updates have been provided by the national authorities and the International Monetary Fund but have not been elaborated and processed by Eurostat.

STATISTICAL DATA AS OF <JANUARY 2004>					
<Former Yugoslav Republic of Macedonia>					
	1998	1999	2000	2001	2002
Basic data	in 1000				
Population (as of 30th June)	200 7.5	2017.1	2025.4	2035.0	2043.0
	in km²				
Total area	257 13	25713	25713	25713	25713
National accounts	1000 Mio Denars				
Gross domestic product at current prices	194 979	209010	236389	233841	
	Mio ECU/euro				
Gross domestic product at current prices	319 3	3448	3893	3839	
	ECU/euro				
Gross domestic product per capita at current prices	159 0	1709	1921	1887	
	% change over the previous year				
Gross domestic product at constant prices (nat. currency)	3.4	4.3	4.5	-4.5	
Employment growth					
Labour productivity growth					
	in Purchasing Power Standards				
Gross domestic product per capita at current prices		6137			
Structure of production	% of Gross Value Added b)				
- Agriculture	13.2	12.9	12.0	11.7	
- Industry (excluding construction)	27.2	26.5	26.9	26.1	
- Construction	6.7	6.1	6.8	6.0	
- Services	52.9	54.5	54.2	56.1	
Structure of expenditure	as % of Gross Domestic Product				
- Final consumption expenditure	92.6 2	90.28	92.64	94.84	
- household and NPISH	72.3 6	69.71	74.44	70.04	
- general government	20.2 6	20.58	18.20	24.80	
- Gross fixed capital formation	17.4 3	16.61	16.22	14.85	
- Stock variation	4.83	3.09	5.22	3.44	
- Exports of goods and services	41.2 1	42.17	48.31	42.38	
- Imports of goods and services	56.0 9	52.15	62.39	55.50	
Inflation rate	% change over the previous year				
Consumer price index	-0.1	-0.7	5.8	5.5	1.8
Balance of payments	Mio USA\$				
-Current account	-270	-32	-72	-244	-325
-Trade balance	-515	-496	-690	-526	-768
<i>Exports of goods</i>	129 2	1190	1321	115	1110
<i>Imports of goods</i>	- 180 7	-1686	-2011	-1682	-1878

-Net services	-60	42	49	-19	-25
-Net income	-45	-42	-46	-41	-31
-Net current transfers	350	464	615	343	498
-of which: government transfers					
- FDI (net) inflows	128	33	175	442	77
Public finance	in % of Gross Domestic Product				
General government deficit/surplus	0.0	0.3	2.3	-2.5	
General government debt					
Financial indicators	in % of Gross Domestic Product				
Gross foreign debt of the whole economy	41.0	40.0	38.2	39.8	
	as % of exports				
Gross foreign debt of the whole economy					
Monetary aggregates	Mio denars-status as December				
- M1	151 78	19694	22388	25324	26406
- M2	260 03	33720	41957	69785	64222
- M3	272 03	35065	43663	71617	64956
Total credit					
Average short-term interest rates	% per annum-status as December				
- Day-to-day money rate					
	17.0				
- Lending rate	- 26.7	18.0-26.0	18.0-25.0	9.0-32.0	10.0-32.0
- Deposit rate	2.5- 8.0	2.5-7.0	3.0-7.0	3.0-7.5	2.0-7.5
ECU/EUR exchange rates	(1ECU/euro=..XX)				
- Average of period					
- End of period			60.7250	60.9133	60.9783
	1995=100				
- Effective exchange rate index					
Reserve assets	Mio denars-status as December				
-Reserve assets	190 32	30136	48015	55103	45923
External trade e)	Mio ECU/euro				
Trade balance	322 534 2	2967416	3416489	2851107	3110683
Exports	131 067 9	1191266	1322617	1157507	1115527
Imports	191 466 3	1776151	2093872	1693601	1995156
	previous year=100				
Terms of trade					
	as % of total				
Exports with EU-15	44.1	45.3	42.8	48.9	51.1
Imports with EU-15	36.3	40.7	38.2	42.5	44.9
Demography	per 1000 of population				
Natural growth rate	6.2	5.2	6	5	5
Net migration rate (including corrections)					

	per 1000 live-births				
Infant mortality rate	16.3	14.9	11.8	11.9	9.2
Life expectancy :	at birth				
Males:	74.8	74.8	75.2	75.2	
Females:	70.3	70.5	70.7	70.7	
Labour market (Labour Force Survey)	% of population				
Economic activity rate (15 - 64)	54.8	53.1	52.9	55.5	52.6
Employment rate (15-64), total	35.9	35.9	35.8	38.6	35.8
Employment rate (15-64), male	45.4	44.6	44.7	46.3	43.5
Employment rate (15-64), female	26.3	27.2	27.1	30.9	28.1
Average employment by NACE branches	in % of total				
- Agriculture and forestry				24.9	23.8
- Industry (excluding construction)				29.3	27.4
- Construction				5.9	5.8
- Services				39.9	42.8
	% of labour force				
Unemployment rate, total	34.5	32.4	32.2	30.5	31.9
Unemployment rate, males	32.5	31.9	30.5	29.5	31.7
Unemployment rate, females	37.6	33.3	34.9	32.0	32.3
Unemployment rate of persons < 25 years	70.8*	62.9*	59.8*	56.1*	58.4*
	as % of all unemployed				
Long-term unemployment share					
Infrastructure	in km per 1000 km²				
Railway network	27.1	27.1	27.1	27.1	27.1
	km				
Length of motorways					
Industry and agriculture	previous year = 100				
Industrial production volume indices	104.5	97.4	103.5	96.9	94.7
Gross agricultural production volume indices	104.2	101.1	101.0	90.2	97.5
Standard of living	per 1000 inhabitants				
Number of cars	14.4	14.4	14.8	15.2	15.1
Main telephone lines	-	38.9	39.8	38.9	38.8
Number of subscriptions to cellular mobile services	-	2.4	4.9	10.9	17.9
Number of Internet subscriptions	-	0.3	0.5	1.1	1.8
P=provisional figures					
E=estimate					
Source: State Statistical office of Republic of Macedonia					
<i>CAVEAT: It should be noted that due to a variety of data collection methods, survey and calculation techniques, data presented in this Statistical Annex are not always fully comparable.</i>					