



Weekly Briefing

Macedonia Economy briefing:
Adjusting the Forecasts for Macedonia's Economic Growth 2018-2020: The Future is (Not That) Bright
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Introduction

On June 7, 2018, the State Statistical Office of Macedonia published the data regarding the economic outcomes of the first trimester (January-March, hereinafter referenced as Q1 2018): Macedonia's GDP had grown by only 0.1% on a year-to-year basis. Two days before, on June 5, the World Bank Group published its Global Economic Prospects report, according to which the economic forecast for the Macedonian economy has been adjusted to reflect the new realities: the World Bank has lowered the estimate of Macedonia's expected annual GDP growth for the current year by almost 1%, from 3.2% (the estimate from the beginning of 2018) to 2.3% annual growth (adjustment made by the middle of 2018); moreover, the World Bank has also lowered their estimations about the expected growth of Macedonia's GDP in 2019 (from 3.9% to 2.7%) and 2020 (from 4% to 3%). In this report we analyze the official discourse of the government of SDSM and DUI (which is optimistic and confident despite the negative news), while also providing a critical perspective and examine the potential future developments.

The Confidence of the Government: Framing 0.1% Growth as Success

The main ruling party SDSM, which in 2016 ran on an economic platform, promised to immediately start undertaking reforms and introducing measures so as to stimulate economic activity and growth. The 1.2% GDP growth by the end of Q4 of 2017 (the previous quarters, in particular Q3 were dismal) was seen as a sign of success, and a reason for optimism entering 2018. Hence, entering 2018, government officials and pro-government voices were confident in the belief that Macedonia will at least maintain or increase the momentum from Q4 2017. They are, in fact, still optimistic when talking about economic change. On

the anniversary of the formation of the government, they published a comprehensive list of 365 achievements of the government in the first year, with the economic achievements being listed as a first section, and taking the largest share of the report (this was analyzed in detail in the last brief). In the words of Prime Minister Zoran Zaev, Vice Prime Minister Kocho Angjushev, and the Minister of Finance, Dragan Tevdovski, the SDSM-DUI government is an economic miracle maker.

The positive spirit was maintained even when the results of the subpar performance for 2018 Q1 arrived. Despite the dismal news, and the fact that the World Bank lowered Macedonia's growth forecast for the next two and a half years, the government of SDSM and DUI kept up an optimistic tone and hailed Q1 as a period of economic success, a period of growth, and a clear sign that Macedonia is finally recovering from all the economic and political crises of the past. This interpretation of the economic situation was reinforced by all pro-government media, who bombarded the public with numbers of various economic successes, while downplaying or even omitting to mention the borderline stagnation in terms of GDP growth and the lowered forecast for the next two and a half years.

According to Angjushev, the economy of Macedonia is undergoing dramatic structural changes, and this is the main reason for the apparent slowing down of the growth. This development, according to him, was a calculated risk, and a prerequisite step in the recovery of Macedonia's economy, which has to shift towards a more sustainable model. For him, the major achievements are the reduction of unemployment (from 213.000 to 206.000 unemployed individuals), and the increase in foreign direct investment (FDI) - Q1 2018 was the most successful trimester in years in terms of attracting FDI. Angjushev pointed out to increase in the output in agriculture (6.5%), industry (5.5%), trade (10%) and capital flows (4.8% on year to year basis) thanks to the unswerving efforts by the government; while at the same time, the government has significantly lowered construction, in particular civil engineering projects (decrease for

whooping 38%) – as the boost of construction was considered a bad practice of the previous government. Angjushev has indicated that the government of VMRO-DPMNE and DUI before 2017 had artificially pumped the economic growth numbers by relying on too many unnecessary and even corrupt construction projects, which were at the same time non-productive (i.e. monuments and facades of buildings); he contrasted this to the policies of the government of SDSM and DUI, which he described as responsible and feasible. He also argued that the current government tries to eradicate the practice of political protection of particular companies, which has created conditions of unfair competition.

The government of SDSM and DUI takes particular pride in the reforms in the financial sector. In this respect, the Minister of Finance Dragan Tevdovski has been outspoken on the successful reforms in the public revenue collection and allocation system, as Macedonia has managed to increase the revenue collection in Q1 2018 on a year-to-year basis. For Tevdovski, the number one priority has been reduction of the public debt and introducing budget transparency, areas in which according to the government, Macedonia has noted significant development.

Criticism, Challenges and Opportunities Ahead

Outside of the circle of government supporters, the news of the low economic growth, and Angjushev's charm offensive were not widely discussed, as the news cycle has been dominated by the name issue between Macedonia and Greece. The main criticism came from the largest opposition party, VMRO-DPMNE, which has as usual argued against the incompetence of the incumbent government and in particular its leaders.

Surprisingly, however, strong critical statements were also made by Nikola Popovski, a former Speaker of the Parliament (2002-2003) and Minister of Finance (2003-2006) during the previous terms of SDSM, known for his neoliberal approach to the economy. His main argument was that the

government of SDSM and DUI is too interventionist, and with its policies has suffocated the market. The key for achieving better results in the economy according to him is unleashing the market forces. He has argued that the government cannot afford to relativize and look for excuses for the low level of growth in Q1 2018, because if one takes in account the fact that the average growth in 2017 was 0%, which means that the average growth of Macedonia's economy in the last five trimesters is 0% as well.

Economic success was supposed to be the hallmark of Macedonia's post-Gruevski transition – yet, despite the fact that the European and Balkan economies noting (varying levels of) economic growth, Macedonia's economy as a notable exception did not grow in 2017. Given that the government of SDSM and DUI came in power in the middle of 2017, and that in the months before that the country was at the brink of collapse, it was understandable that there can be no immediate successful results in the economy. The stagnation at 0% GDP growth was blamed on the protracted political crisis, which was believed to have hurt the country's overall business climate and increased the political risk. In the subsequent instances of revising (lowering) the expectations for the future of Macedonia's economy during the past year, analysts have usually argued that the crisis will have longer lasting effects than originally planned. In that sense, there is still no widespread sense of accountability for the government of SDSM and DUI – meaning that they still have a “grace period” in which they can seek the best way forward.

Nevertheless, the news that Macedonia's economy grows much slower than expected should be a source for major concern. Earlier in 2018, a report by experts from the European Bank for Reconstruction and Development (EBRD) has hypothesized three scenarios for the lagging economies of the Western Balkan region (including Macedonia) to catch up with the rest of Europe: in case if they achieve a mini-economic miracle (prolonged growth at the pre-crisis rates), they can catch up with the advanced European economies by the middle of this century; if they grow by the average rates of the last fifteen years (2001-

2016), they can catch up with Europe by the 2070s; and if they maintain the post-crisis, sluggish growth rates, they will only converge with the rest of the continent after two hundred or more years (around the year 2220). In order for the last scenario to be averted, the Balkan economies – including Macedonia – need to return on the path of GDP growth of at least 5-6% per year as soon as possible. However, according to the latest information – Macedonia will now remain on the slow track for at least two more years, with no guarantees that it will accelerate afterwards.

The decrease in construction works, and in particular large infrastructure projects has been the major reason for the slowing down of Macedonia's economy. On one hand, this proves that without significant construction projects, Macedonia's economy cannot move forward. On the other hand, should they decide to move beyond the soft austerity approach, a potential restart of the construction activities offers SDSM and DUI an opportunity to also increase economic growth. For example, the potential restarting of the works on the highway Kichevo-Ohrid (in case issues pertaining to financing as well as implementation are solved) may have a significant effect on the economic growth. However, this could only happen in Q3 the earliest, meaning that the numbers for Q2 2018 may be also low. Another potential change may occur once the government speeds up the implementation of its plan for economic growth (critically analyzed in earlier briefs), which foresees financial assistance for the private sector, with the goal of improving the competitiveness of Macedonian companies. Finally, Zaev and Angjushev keep on promising spectacular investments by global companies, in particular in the information and communication technology, such as Microsoft, Google and Facebook. Only one major investment could be a potential game changer in Macedonia. However, to what extent these possibilities materialize – and to what extent they can contribute to acceleration of the economic growth, remains to be seen.