



EUROPEAN COMMISSION
EXTERNAL RELATIONS DIRECTORATE GENERAL

DIRECTORATE Western Balkans

CARDS ASSISTANCE PROGRAMME

FORMER YUGOSLAV REPUBLIC OF MACEDONIA

2002-2006

Including Multi-annual Indicative Programme 2002-2004

FOREWORD

This Country Strategy Paper has been drafted against the background of the deep political and military crisis into which the former Yugoslav Republic of Macedonia plunged in March 2001 following the uprising of ethnic Albanian armed groups. The internal conflict harbours severe threats to the reform process and the implementation of the Stabilisation and Association Agreement and the Interim Agreement on trade and trade-related matters signed on 9 April 2001. Both its short-term effects and its potential long-term consequences have been analysed and fully taken into account when drafting this document and have significantly contributed to determining the choice of the sectors and priorities for assistance.

However, the purpose of this document is that of setting a strategic framework for the period 2002-2006, which shall serve to set long-term objectives and priority fields of action for the provision of CARDS assistance in the former Yugoslav Republic of Macedonia. CARDS is a financial instrument firmly inserted into a well defined political context, the Stabilisation and Association Process, designed to favour the gradual integration of the countries of South East Europe into the structures of the European Union. Central to this strategy are the Stabilisation and Association Agreements.

The SAA and the IA set the agenda of the relationship between the EU and the former Yugoslav Republic of Macedonia for the years to come and as a consequence this Country Strategy Paper has largely been directed at supporting the efforts required for their full implementation.

Nevertheless, it is evident that no long-term strategy can be successfully developed and implemented in the absence of a stable and conflict-free political and economic environment. The security crisis of the first half of 2001 brought the country to the brink of civil war. The European Union has taken a leading role in helping the former Yugoslav Republic of Macedonia to overcome the crisis. The European Commission both before and after the signature by all main political parties of the country of the Framework Agreement which marked the end of the hostilities, has specifically designed a set of exceptional assistance programmes.

However, the European Commission had already in past years addressed its assistance to tackling some major structural constraints of the country. Support to the reform of the judiciary, to the creation of the South East Europe University in Tetovo, to the definition of an integrated border management strategy and to the process of administrative decentralisation are only some of the measures undertaken which directly address issues which lie at the roots of the recent crisis.

While addressing the immediate consequences of the recent crisis through its emergency assistance, the European Commission believes that the full implementation of the SAA and the IA and the accomplishment of the objectives of the SAP are the best means to ensure the long-term stability and the prosperity of the former Yugoslav Republic of Macedonia. It is therefore on those objectives that this Country Strategy Paper and the Multi-annual Indicative Programme are focused.

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COUNTRY STRATEGY PAPER FORMER YUGOSLAV REPUBLIC OF MACEDONIA (FYROM)

EXECUTIVE SUMMARY

As provided in the CARDS Regulation (Council Regulation (EC) 2666/2000), the Country Strategy Paper (CSP) provides a strategic framework in which EC assistance will be provided in the period 2000-2006. It sets out EU co-operation objectives, policy response and priority fields of co-operation based on a thorough assessment of the partner country's policy agenda and political socio-economic situation. The Multi-annual Indicative Programme (MIP) attached to the strategy and forming an integral part thereof sets out the EU response in more detail, highlighting programme objectives, expected results and conditionality in the priority fields of co-operation for the period 2002-2004.

The former Yugoslav Republic of Macedonia is a full participant in the Stabilisation and Association Process. After almost a decade of relative political stability the country was plunged to the brink of civil war in March 2001 when ethnic Albanian armed groups, claiming improved civil and political rights for the ethnic Albanian minority, took up arms against the Macedonian security forces. The security crisis produced severe economic consequences halting the economic growth registered in 1999 and 2000 and endangering the macroeconomic stability of the country. The main challenges facing the former Yugoslav Republic of Macedonia over the medium term are:

- a) Maintaining peace and stability and easing inter-ethnic tensions;
- b) Enhancing the efficiency of the state;
- c) Alleviating poverty and developing human capital;
- d) Promoting private sector growth and job creation;
- e) Implementing the Stabilisation and Association Agreement signed with the European Union in April 2001.

Within that context and taking into account the objectives of the Stabilisation and Association Process, the EC CARDS programme can most effectively assist the partner country in meeting those challenges by focusing on four main priority sectors: democracy and the rule of law, economic and social development, justice and home affairs, and the environment and natural resources.

1. EU CO-OPERATION OBJECTIVES IN THE FORMER YUGOSLAV REPUBLIC OF MACEDONIA

The EU's co-operation objectives with the former Yugoslav Republic of Macedonia are anchored in the Stabilisation and Association Process, a proximity policy which reflects the political and strategic importance of the Balkans to the EU. The Stabilisation and Association Process is a framework in which a new contractual relationship (Stabilisation and Association Agreements) and an assistance programme (CARDS) help each country to progress, at its own pace, towards EU membership.

The crisis in 2001 added a further emphasis, within this overall objective, on the need for EU support to conflict resolution and prevention that will help FYROM pass through its current period of instability.

The European Commission set out this ambitious vision for the region's development in May 1999. This is based on:

- (1) A recognition that one of the main motivations for the reforms relating to respect for the rule of law, democratic and stable institutions and development of a market economy is a relationship with the EU that is based on a credible prospect of membership once the relevant conditions have been met.
- (2) The need for the countries to develop bilateral relationships between themselves as a basis for greater economic and political stability in the region.
- (3) The need for assistance programmes and contractual relations, which although anchored to a common set of political and economic conditions, are flexible enough to allow each country to move ahead at its own pace, to accommodate a range of situations from post-conflict reconstruction and stabilisation to technical help with matters such as the approximation of legislation to the core elements of the EU "acquis".

Following the Feira Council of June 2000, which confirmed that the EU's goal is the fullest possible integration of these countries into the economic and political mainstream of Europe, the 24 November 2000 Zagreb Summit set the seal on the Stabilisation and Association Process by gaining the region's agreement to a clear set of objectives and conditions. In return for the EU's offer of a prospect of accession on the basis of the Treaty on European Union (TEU) and the 1993 Copenhagen criteria, and an assistance programme to support the ambition, the countries of the region undertook to abide by the EU's conditionality and participate fully in the Stabilisation and Association Process.

They also accepted that the Stabilisation and Association Agreements, when signed, would be the principal means to begin to prepare themselves for the demands that the perspective of accession to the EU naturally entails. The SAAs focus on respect for democratic principles and integration of the countries of the region into the EU single market. They foresee the establishment of a free trade area with the EU and set out rights and obligations in areas such as competition and state aid rules, intellectual property and rights of establishment, which will allow the economies of the region to begin to integrate with the EU's. The conclusion of such Agreements represents the signatories' commitment to complete over a transition period a formal association with the EU, tailored to the circumstances of each country but based on the implementation of the same core obligations.

The EU's political strategy towards the region relies on a realistic expectation that the contract it enters into with individual countries will be fulfilled satisfactorily. Careful preparation with each country before the EU offers such a contract has been and remains a vital component of the Stabilisation and Association Process. The agreements contribute to the EU's objectives in the following way:

- (1) They are a tool which provides, much as the Europe Agreements did for the candidate countries in Central Europe, the formal mechanisms and agreed benchmarks which allow the EU to work with each country to bring them closer to the standards which apply in the EU.
- (2) They are a means to focus attention on respect for key democratic principles – human and minority rights, stable democratic institutions, standards of political behaviour and the independence of the media.
- (3) They include the core elements which are at the heart of the EU single market. Through free trade with the EU and the associated disciplines (competition and state aid rules, intellectual property, etc) and rights (e.g. establishment), this process will allow the economies of the region to begin to integrate with the EU's.

Effective implementation of the Stabilisation and Association Agreements is a prerequisite for any further assessment by the EU of a country's prospects of accession. Each country will need time, help and encouragement to implement such obligations properly.

The Stabilisation and Association Agreements is not simply a bilateral process with each country: the Zagreb Summit placed considerable emphasis on the need for regional co-operation. Similarly the Stabilisation Agreements include a clear commitment to regional co-operation, which is reflected both by the funding of a regional CARDS programme and the shared objectives of national CARDS programmes.

The CARDS programme underpins the objectives and mechanisms of the Stabilisation and Association Process and as each country moves deeper into that process, assistance will focus increasingly on support for the reforms and institution building necessary to implement the obligations in the Stabilisation and Association Agreements. A precondition for receiving assistance under CARDS is compliance with Article 5 of the CARDS Regulation (Council Regulation 2666/2000 of 5 December 2000) covering conditionality issues. The indicative financial allocation for CARDS assistance for the former Yugoslav Republic of Macedonia for the period 2002-2004 is € 110.5 under the National Programme and € 20 million under the Regional Programme for measures which will be implemented in the former Yugoslav Republic of Macedonia. In addition, the former Yugoslav Republic of Macedonia will also participate in other measures under the Regional Programme.

On 9 April 2001 the former Yugoslav Republic of Macedonia became the first country of the region to sign a Stabilisation and Association Agreement. This was an event of major symbolic and practical significance which marked an important step in the establishment of ever-closer relations with the country. However, if the SAA offers major incentives and opportunities to the country it also sets political and economic conditions which will have to be fully implemented if the desired progress towards integration is to be made.

2. THE FORMER YUGOSLAV REPUBLIC OF MACEDONIA'S POLICY AGENDA

Since 1991 the country has embarked upon a process of transition from socialism and a centrally managed economy towards the establishment of a free civil society, fully functioning democratic institutions and a market economy. Although the priorities and policies adopted by the Government have brought good results, development has been limited by continued regional instability and by internal structural constraints at the political and economic level.

A centre of right government took office in December 1998; it adopted an ambitious programme to boost the economy, reform legislation and the public administration, reduce unemployment, increase foreign direct investment and to improve inter-ethnic relations as well as relations with neighbouring countries. A central plank of the Government's policy was the integration of the country into Euro-Atlantic structures.

The Government's efforts to progress have been hampered by a series of unfavourable events such as the political crisis which prompted a cabinet reshuffle in December 1999, the 1999 Kosovo crisis, and the internal crisis started in March 2001 and provoked by an outbreak of violence caused by ethnic Albanian armed groups (the so called NLA or National Liberation Army). This led to the creation of a Government of National Unity, representing all major political parties, which should steer the country out of the crisis and leave the stage to a newly elected government following elections scheduled for the end of January 2002.

The policy agenda of the Government is currently two-fold: on one side lies the implementation of the Framework Agreement, the accord between the main political parties which brought hostilities to an end; on the other side lies the continuation of the agenda for socio-economic development set in 1998 and the process of institutional reforms which should gradually move the country into the economic and political mainstream of Europe. The main elements of the Government's policy agenda therefore are: (i) the strengthening of inter-ethnic relations; (ii) fostering efficient democratic institutions and the rule of law; (iii) deepening economic reforms and creating the conditions for self-sustaining market-driven economic reform; (iv) promoting the country's integration into Euro-Atlantic structures.

The former Yugoslav Republic of Macedonia's diverse and complex ethnic composition means that inter-ethnic relations are a long-standing issue upon which its stability, and possibly that of the entire region, depend. The political and military crisis of 2001 has highlighted the necessity to rekindle and upgrade inter-ethnic dialogue. The Framework Agreement largely sets the agenda of the reform process needed to bring back stability to the country. In particular, the proportional representation of ethnic minorities in the sector of Public Administration and the police services will have to be ensured and the use of minority languages introduced in the Public Administration as well as for primary, secondary and university education. The Framework Agreement will also produce important consequences for the process of administrative decentralisation; the Government has pledged in fact to develop a stronger and more efficient local government endowed with the necessary financial means to carry out its new powers and tasks. The process, which had already started before the security crisis of 2001, has become one of the cornerstones around which the renewed stability of the country is to be built and will have to be brought forward with new vigour and speed to meet the terms of the Agreement.

In terms of practical policies the action of the Government is mainly oriented towards ensuring the country's integration into the structures and institutions of the European Union. The implementation of the Stabilisation and Association Agreement requires that important legislative and institutional reforms are undertaken over the next few years. In this context the reform of the judiciary, already underway, is designed to enhance the effectiveness of the judicial system, reduce the significant backlog of cases in the courts and ensure the respect of the rule of law through a thorough restructuring of the court system. The reform of the Public Administration directed to improve the structure and the efficiency of the state administration and the process of institution capacity building designed to build an institutional set up enabling the country to enact, implement and enforce the legislative reforms needed "on the road to Europe", are necessary steps the Government will have to take forward with renewed intensity.

In terms of economic policy the Government has set a comprehensive programme intended to lead the country to the establishment of a fully-fledged market-based economy. For the purpose, fiscal policy will be used to tackle the current imbalances and weaknesses in the budget structure whilst on the financial side reforms of the enterprise and banking sectors will be pushed forward. The development of a buoyant, efficient and competitive private sector is crucial for the success of the whole process of reform. The focus here will primarily be on strengthening the legal framework, in particular with regard to the rights of trustees and shareholders, increasing investors' confidence thus creating an appropriate environment for direct investments, and favouring entrepreneurship. Particular emphasis is placed on SMEs development, a largely underdeveloped sector in the country and on the development of corporate management. Completing the privatisation process, one of the major tasks of the process of transition, remains a central element of the agenda of the Government. The process, which began in 1989 and was speeded up after 1993, is to be carried forward and completed. By the end of 2000, more than 1,600 (mostly small) enterprises had been privatised, with a further 126 companies in the process of privatisation. However, the privatisation of big loss-making enterprises has met with significant delays and the envisaged targets for selling or closing them, as agreed with the World Bank and the IMF, have not been met. The completion of the privatisation process remains an important element on the agenda of the Government.

Social sector policies are centred around the development of an active policy directed at accelerating growth and job creation through greater investment in human capital development, the financing of programmes to help the unemployed find employment, the stimulus of entrepreneurship and self-employment. In this framework the general modernisation of all levels of education is seen as a crucial investment in human capital; reforms are designed to adjust curricula to meet the needs of a market-oriented economy as well as to raise enrolment rates and to reduce dropout levels.

The Government's agenda for socio-economic development had been set in accordance with the IMF and World Bank's conditionality requirements imposed as a precondition for the conclusion of crucial three-year arrangements¹. In this context the Government of the former

¹ On 29 November 2000, the board of directors of IMF approved a three-year PRGF/RFF arrangement with the former Yugoslav Republic of Macedonia worth US \$ 45.9 million and designed to reduce poverty growth, keep macroeconomic stability and stimulate development. On 14 December 2000, the Board of Directors of the World Bank approved a FESAL II arrangement for financial and enterprise sector restructuring worth US \$50.3 million.

Yugoslav Republic of Macedonia prepared an Interim Poverty Reduction Strategy Paper (IPRSP) in November 2000 which is supposed to lead to the definition of a final strategy in the year 2002. However, the IMF programme has been off-track since December 2000 and its resumption appears unrealistic following the security crisis of 2001. At the time of writing the IMF is negotiating with the Government a new short-term arrangement in the form of a Staff-Monitored Programme, which should then lead to the conclusion of a Stand-by Agreement in the first half of 2002.

The external dimension of the economic policy agenda includes the integration into regional, European and global markets, including WTO membership for which a memorandum on the foreign trade regime has already been submitted and negotiations are ongoing. The former Yugoslav Republic of Macedonia is committed to a policy of liberalisation of foreign trade and a low level of tariff protection while promoting an export strategy designed to limit chronic balance of payments imbalances, which the recent crisis has significantly deepened.

2.1. European integration and the Stabilisation and Association Agreement

On 9 April 2001 the former Yugoslav Republic of Macedonia became the first country of the Western Balkans region to sign a Stabilisation and Association Agreement with the European Community and its Member States..

The agreement covers a wide range of sectors in which the co-operation with the EU will be developed over the transitional period of ten years following its entry into force. It is a comprehensive agreement which forms an agenda *per se* and it is around its requirements and provisions that the co-operation between the former Yugoslav Republic of Macedonia and the EU will revolve in the years to come. An Interim Agreement (IA) covering the trade and trade-related matters of the SAA entered into force on 1 June.

In order to meet the demanding requirements of the SAA the government has developed a National Action Plan which should set the strategic priorities guiding medium to long-term actions and has prepared a National Law Approximation Programme which will steer the process of approximation of legislation with that of the EU.

3. THE POLITICAL, ECONOMIC AND SOCIAL SITUATION IN THE FORMER YUGOSLAV REPUBLIC OF MACEDONIA

3.1. Political situation

The former Yugoslav Republic of Macedonia is a parliamentary republic and has existed as an independent state since September 1991 when it declared independence from the former Yugoslavia following a referendum. The President represents the Republic and is the

commander-in-chief of the armed forces. He is elected through general and direct elections for a five-year term and appoints the Prime Minister who exercises executive power jointly with his cabinet. According to the Constitution the Assembly of the Republic is composed of 120 to 140 Representatives directly elected by the people. Ten main parties differentiated along political and ethnic lines contest the elections. Representatives are elected by universal suffrage for a four-year term.

The Constitution protects individual freedoms as well as fundamental civil and human rights. It sanctions the autonomy and independence of the judiciary whose functioning has so far been characterised by a marked procedural slowness causing a significant backlog of cases. Full achievement of the respect for the rule of law requires a streamlined and more efficient judicial system.

Democratic principles are deemed to have been generally respected; however, allegations of fraud and election rigging have been advanced in several occasions. In particular during the 1999 Presidential elections and the 2000 local elections widespread irregularities were reported by international observers, although they were not considered to be of such proportions as to affect the final outcome of the elections.

The country enjoyed relative political stability in the early years of transition with the same coalition government, led by the Socialist Party (SDSM), staying in power from 1992 to 1998. A coalition Government led by the centre-of-right VMRO-DPMNE party took office in December 1998 and had undergone a series of reshuffles until the creation of the government of National Unity in April 2001 as a consequence of the political and military crisis in the country.

Since March 2001 this relative political stability has been shattered by the deterioration of the inter-ethnic situation with ethnic Albanian extremists fighting the Macedonian security forces. Corruption in the public service is a thorny issue which mars the credibility of the political and administrative institutions. The politicisation of the administration, through appointment based on party affiliation, continues to pose a major constraint on the development of a modern professional civil service.

Reports of human rights violations have been generally limited but have increased in the aftermath of the political crisis of March 2001. Reports of police brutality towards ethnic Albanians are a cause of major concern.

Freedom of expression is enshrined in law and practice but the quality of information produced by the public and private media is generally biased by political control. The lack of a libel law is often the source of vicious and unsubstantiated allegations and accusations which contribute to embitter the political climate.

The country's population is ethnically diverse; according to the last census carried out in 1994 66.6 percent of the population is composed of ethnic Macedonians, 22.7 percent of Albanians, 4 percent of Turkish, 2.2 percent of Roma, 2.1 percent of Serbs while other groups make up for the remaining 2.4 percent. The Constitution of the Republic declares the former Yugoslav Republic of Macedonia to be the country of the Macedonians while granting full equality to the other 'nationalities' as they are defined in the text of the Preamble.

Inter-ethnic relations are the most relevant and at the same time most sensitive political issue the current and future governments will have to deal with if the stability of the country and the progress of the reform process are to be ensured. Successive governments since 1991 have managed to control ethnic tensions but they have not been able to deal effectively with the most contentious issues at stake. Relations between the Slav majority and the large Albanian community in particular have been strained with the latter constantly pressing for the uplifting of their status as citizens of the Republic and for increased participation of Albanians in public administration offices. The Roma community, whilst more settled than in neighbouring countries and represented by active NGOs, is subject to constant discrimination. In the provision of housing, education, health and welfare services, living conditions are well below those of ethnic Slavs or ethnic Albanians. Repeated allegations of police brutality and systematic prejudice are a cause for concern.

The government has renewed its commitment to advancing inter-ethnic dialogue and easing tensions and some tangible progress has been made in meeting the expectations of the Albanian community, especially on the issue of higher education in the Albanian language. In spite of this, the situation has rapidly degenerated in March 2001 with an escalation of violence perpetrated by groups of armed Albanian rebels, a good number of whom apparently coming from neighbouring Kosovo, who attacked some positions of the Macedonian Army and occupied some areas bordering Kosovo. After the reaction of the Macedonian Army managed to disperse the rebels, talks started among the political forces of the country. Negotiations for the formation of a new broad coalition government including all major parties were started but proceeded with difficulty. The resumption of the hostilities at the beginning of May 2001 with renewed attacks by the armed rebels and the occupation of numerous villages in the northern area of the country has shown once again the potentially devastating consequences that inter-ethnic confrontations may have for the country.

The conflict also harbours severe dangers for the stability of the entire region due to its obvious possible implications in neighbouring countries. The restoration of a climate favourable to political dialogue and to the solution of long-standing and most contentious inter-ethnic issues is the most immediate priority upon whose favourable solution the whole political agenda of the government depends. The Signature of a Framework Agreement on 13 August 2001, aptly brokered by the Special Envoys of the European Union and of the US administration, can be seen as a the first step in the direction of a lasting solution to the conflict. The Agreement sets out a complex agenda including *inter alia* the complete cessation of hostilities and the complete voluntary disarmament and disbandment of the ethnic Albanian armed groups, the strengthening of the process of decentralisation, the achievement of equitable representation of the different ethnic groups in public administration and public enterprises, important reforms in the education sector, the use of minority languages, and the introduction of special parliamentary procedures for all constitutional amendments concerning minority and local self-government issues. The full implementation of the Agreement requires a series of constitutional amendments and legislative changes and will be supported by the International Community through the development of an articulated package of assistance including reconstruction works in the areas worst affected by the conflict, the development of confidence building measures designed to ease ethnic tensions and rebuild mutual trust among the different ethnic communities and support for the return of refugees and internally displaced people. Macro-financial assistance is also envisaged after the Government reaches a new agreement with the IMF. As the necessary complement to the above described measures a

NATO mission was deployed to supervise the disarmament of the ethnic Albanian armed groups and restore conditions of security throughout the country.

The former Yugoslav Republic of Macedonia seems to be at a crossroads. In spite of the signature of the Framework Agreement the political and security situation remains extremely unstable and the risk of full-blown civil war, which appeared ever so real at some stages during the crisis, is still a possibility to be reckoned with. Six months of conflict have contributed to the further polarisation of society and significantly deepened feelings of mutual distrust and resentment between ethnic Macedonians and ethnic Albanians. The road to peace is still paved with difficulties and can be run to the end only with the total commitment of the country's political *élite* to the full and correct implementation of the recently signed Framework Agreement.

3.2. Economic and social situation

3.2.1. Economic situation, structure and performance

In 2000, strong economic activity was driven by domestic demand, both in terms of investment and consumption. Linked to this was the reconstruction of neighbouring Kosovo, which also contributed to boosting economic growth in the former Yugoslav Republic of Macedonia. Real GDP growth stood at 5.1%, the highest rate of growth since the beginning of economic transition, despite a sharp deceleration in the second half of the year. The security crisis in the country makes the economic outlook quite uncertain and in view of the growth profile in 2000 earlier expectations of growth of around 6% per year over the medium term will not be fulfilled. The 2001 economic performance is adversely affected by the current crisis and this can only be reversed in the presence of normal political conditions.

During 2000, the very high unemployment rate remained virtually unchanged at 32.2%, in spite of rather buoyant economic growth. Moreover it is expected that even real GDP growth of some 6% per year over the medium term would not in itself lead to a significantly lower unemployment rate. Structural reforms, including a lowering of the replacement rate for low wage earners and strengthening of benefit eligibility criteria, are indispensable to achieve significantly lower unemployment rates.

At 5.8% the inflation rate remained rather moderate in 2000, despite a one-off effect due to the introduction of VAT in April. The policy mix appears suitable for maintaining low inflation rates over the short to medium term. Inflation does not seem to be a concern at the present stage although inflationary expectations appear to be consolidating, partly as a result of the security crisis.

The monetary policy of the authorities remains oriented towards the maintenance of the *de facto* exchange rate anchor. The effective Denar peg to the Euro was successfully maintained in the course of 2000, but came under some pressure in the first half of 2001 due to the security crisis. The exchange rate was defended by the National Bank, implying a significant loss of reserves. At the end of 2000 reserves amounted to nearly 4 months of imports. The discount rate was lowered in 2000 and the inter-bank interest rates fell from about 12% to around 7% by the end of the year. Likewise, lending and borrowing rates of banks fell during the year. Yet, the spread between lending and deposit rates remained above 8 percentage points, signalling structural problems (too many banks, non-performing loans, and lack of

competitiveness and low efficiency) in the banking sector. Albeit falling, high nominal and real interest rates remain an important obstacle to SME development and economic activity in general. However, SME development requires progress with the financial sector reform.

The performance of the external sector remains fragile. In the course of 2000, imports grew by 17.4% while exports grew by 10.7%, implying a considerable widening of the trade balance deficit. The surge in imports was mostly driven by increased domestic consumption and the sharp rise in the oil price in the international market. As a result, the trade deficit widened considerably to US\$ 760 million in 2000 from US\$ 410 million in 1999. Due to significant transfers, the current account deficit did not rise as much as the trade-balance deficit in 2000; at 3.1% of GDP it remained broadly unchanged with respect to the 3.% level of the previous year.

Since 1997 the external debt level has been increasing rather rapidly and at the end of 2000 total external debt amounted to some 43% of GDP. Total debt service was about 13% in terms of exports of goods and services. Official reserves increased significantly in 2000, in part due to privatisation revenue, and reached the equivalent of almost 4 months of imports at the end of the year. The economic programme foresees that reserves would stabilise at around 3-1/2% of imports.

3.2.2. Social developments

About 20 percent of the total population in the former Yugoslav Republic of Macedonia live under the official poverty line with minimum resources for living. The poor in the country are households with less than 60 percent of median household income (the official poverty line of about US\$75 per month in 1996 prices). Poverty is most widespread in rural areas and in larger households with more members unemployed or with low education. As noted in the Poverty Reduction Strategy Paper (Interim Version) produced by the Government of the country in November 2000, poverty in the former Yugoslav Republic of Macedonia is the result of two factors: the fall in aggregate consumption during the 1990s and the rise in inequality in its distribution. A drastic decrease in economic activity, the fall in real wages, pensions and other social incomes of the population, the increase in income differences among different groups of the population and the unemployment generated by the process of privatisation seem to be the factors that have contributed most to the creation of poverty during the last decade. Regional inequalities remain marked with two-thirds of poor households living in rural areas.

The quality of health services as well as the level of accessibility to those services are strictly related to income levels. There are still illnesses associated with poor living conditions and illnesses that remain typical of certain groups of the population (i.e. the unemployed, the elderly, the disabled, and the rural population).

Education levels are reasonably high, 95 percent of the population is literate and primary school enrolment rates are close to universal. However, gross enrolment rates are lower at all levels of the education system than in other countries of the region and participation in education has declined since independence. Drop out levels are comparatively high, especially at secondary school level.

Population	2.0 million
Population per Sq. Km. (1997)	78.5
Population growth	0.5 %
Life expectancy	73 years
GNP per capita	US \$ 1690
GDP (2000)	US \$ 3.4 billion
Unemployment (2000)	32.2 %
Inflation (2000)	5.8 %
External debt as % of GDP	43%
Trade deficit	US \$ 760 m. (3.1%)
Literacy	95%
Population living in poverty	20%

3.2.3. *Assessing the process of reforms*

In the recent past the process of structural reform has gone through a period of slow pace followed by some acceleration. The Kosovo crisis and the need to address some of the problems related to the refugees and to the negative economic consequences of the crisis detracted policy makers' attention from the reform agenda. After the resolution of the Kosovo crisis, the process of structural reform gained some momentum again, but suffered another setback due to the crisis in the first half of 2001. In the course of 2000, significant progress was achieved in tax reform, including the successful introduction of VAT. Moreover, there were reforms in the financial system, including new Banking, Security and Collateral Laws, as well as significant amendments to the Law on Bankruptcy. According to the authorities, the 2001 crisis is likely to imply a delay in the implementation of the planned reforms. While the Government claims to remain committed to reforms some slippage not directly related to the crisis has occurred. In view of the country's poor track record, particularly with regard to privatisation, keeping up the pace of structural reforms will be a crucial and difficult challenge for the authorities.

With regard to public sector reform, the action of the authorities during the year 2000 broadly followed the guiding principles agreed with the IFIs for a medium-term transformation of the fiscal domain. Those principles include improved fiscal transparency, budget design and preparation, shifting the taxation burden from direct to indirect taxes, reform of public administration and rationalisation of expenditure, integration of core off-budget special revenue into central government accounts and the improvement of debt management. Several important actions were undertaken in 2000, notably the introduction of VAT in April. Among other measures, the authorities established a Treasury Department at the Ministry of Finance, issued negotiable government bonds in exchange for frozen foreign currency deposits and established a debt-monitoring unit in the Ministry of Finance. However, it is to be noted that a major risk for public sector reform is posed by the political and security crisis.

Despite those improvements, government finances still suffer from a number of structural shortcomings, especially regarding the composition of the budget. Within the central government budget, transfers and wages account for close to 80% of total government expenditure, leaving little room in the budget for investment and other activities supporting growth over the medium term. The authorities have made attempts, *inter alia* by preparing a comprehensive plan for civil service reform, at reducing employment in the public sector, thus also making room for increases of wages in this sector. However, the envisaged downsizing of the civil service through early retirement was not achieved, due first to a ruling of the

Constitutional Court against the envisaged scheme and subsequently to the difficult political situation in connection with the crisis in early 2001.

Rapid progress in the privatisation process, especially of small enterprises, had been made by the end of 2000. However, the process has encountered problems. In particular, privatisation of large, loss-making firms has proven a difficult task, and privatisation has not been paralleled by an improvement of corporate governance. The privatisation methods (mostly management-employees buy-outs), the weakness of bankruptcy procedures and the difficulty in enforcing them, as well as the absence of an effective hard budget constraint (particularly for large companies) has represented a major obstacle to enterprise restructuring and is hampering enterprise performance. Thus, nearly half of the privatised companies remain loss-makers. A reluctance to face the social and political costs of restructuring, closing or privatising loss-making enterprises is the most important underlying reason for the disappointing progress in this area.

The banking sector is mostly private (80%), and the privatisation of the largest commercial bank (through sale to foreign investors), Stopanska Banka, was completed in April 2000. This sale, as well as the previous one of Kreditna Banka, the closure of Almako Banka and the announcement for the sale of the third largest bank are major steps for the restructuring of the sector. Those steps have been reinforced by a new Banking Law in June 2000, which is in line with EU legislation and BIS principles. The legislation strengthened the legal framework of bank supervision and enhanced the monitoring ability of the Central Bank. The sector, however, continues to suffer some structural problems, such as a large number of banks, many non-performing loans, lack of competitiveness and efficiency in the banking sector, etc., which the authorities aim at addressing in the medium term. While financial sector reform is making good progress, the sector remains weak, not least due to a weak loan portfolio.

It may be concluded that the country has made quite substantial progress with macroeconomic stabilisation policies and that an adequate and ambitious policy agenda for the medium term has been established. However, in view of past experience and in view of the current security and political crisis the commitment and willingness to quickly implement the reform agenda needs to be upheld and the international community should underpin this through applying suitable conditionality, wherever appropriate.

3.2.4. Structure of public sector finances and main sectoral policies

As regards public sector finances, during 2000 fiscal performance was particularly strong but this has been greatly and adversely affected by the current crisis in the country. The rebound of economic activity and especially the better-than-expected results in VAT collection resulted in a surplus of about 3.5% of GDP in the general government accounts. Following a major slippage in the wage bill of the central government, the authorities introduced direct control of the Prime Minister's office on recruitment and wage level of line ministries, but were not successful in achieving the planned reductions in the Government staff. The security crisis in the country seriously questions the envisaged fiscal strategy of lowering income taxes and expenditures, as increased military and other expenditure in combination with a shortfall in revenues and incomplete reductions in Government staff could endanger the foreseen manageable deficits expected over the medium term. Slippage in the conduct of economic and budgetary policies started ahead of the crisis in early 2001 and were aggravated by the crisis. At the time of writing severe difficulties are being experienced in the negotiations with the IMF on a Staff Monitored Programme which should pave the way for the successive

conclusion of a Stand-by Agreement. In particular, the unwillingness of the Government to reduce the programmed expenditures in sectors that have a direct relevance to the crisis is proving a major stumbling block. Such measures will be needed to get the former Yugoslav Republic of Macedonia back on track compared to its previous relatively good economic performance.

The implementation of the Framework Agreement will imply additional one-off as well as recurrent budgetary expenditures. As for one-off expenditures it is expected that the greater use of the Albanian language will imply capital costs for media and translations. Other types of one-off costs are also expected and will be subject to the implementation of the agreement. Regarding recurrent costs it is expected that the number of ethnic Albanians in the state administration and the police force will increase, which will imply a higher wage bill. Other types of recurrent costs are expected for translators and more generally for the wider use of the Albanian language. Very preliminary estimates of the recurrent costs suggest that they might be in the order of one per cent of GDP. A more detailed assessment of the budgetary implications of the Framework Agreement is being prepared by the authorities.

3.2.5. External environment

Since 1994 the country has been experiencing high balance of payments deficits due to a deteriorating trade balance, a trend confirmed by the data for the year 2000 when exports covered 63.3 percent of imports and the negative exchange balance amounted to US \$765.7 million. The bulk of the exports concern reproduction products (54.4%) whilst consumer goods account for 42.8% of the total. Imports of reproduction products increased to 67.7% of the total with consumer goods declining to 19.5%. The 2001 crisis produced dire consequences on the balance of payments especially due to its negative effects on trade and foreign investment. A marked deterioration is expected with respect to 2000 and a significant gap is expected in 2002 as well.

The EU and the former Yugoslav republics constitute the main trading partners: they absorb the bulk of the country's exports and provide a large chunk of the imports. The former Yugoslav Republic of Macedonia has applied for WTO membership and has submitted its Memorandum for accession to all Member States. Furthermore, it has concluded Free Trade Agreements with Croatia, Slovenia, Yugoslavia and Bulgaria. A Free Trade Agreement has been signed with Turkey whilst negotiations are being held with Albania, Bosnia and Herzegovina, and Romania. On 27 June 2001 the former Yugoslav Republic of Macedonia signed a Memorandum of Understanding with Albania, Bosnia Herzegovina, Bulgaria, Croatia, Romania and the Federal Republic of Yugoslavia aimed at liberalising trade and lowering tariff barriers. The MoU provides for the establishment of a network of Free Trade Agreements for Southeast Europe by the end of 2002. This will enlarge the regional market size considerably to 55 million consumers, creating better conditions for private investment and economic growth.

In 1996 the country undertook liberalising steps by decreasing the average custom rate, eliminating all quantitative restrictions and decreasing the number of customs rates. The commitments imposed by WTO membership as well as the obligations imposed by the SAA with the EU will require further reductions in the level of trade protection. They will have to be accompanied by deep structural reforms fostering an increase in competitiveness and productivity if international competition is to be withstood effectively and the beneficial effects of trade liberalisation enjoyed.

The legal and structural conditions for pursuing an active trade-promotion strategy will have to be gradually but rapidly introduced.

The country's external debt has continued to grow in the course of the year 2000 reaching the overall amount of US \$1,463.3 million for a debt to GDP ratio of 43%. In the past the former Yugoslav Republic of Macedonia used to honour its Paris Club obligations. The exceptional situation in the context of the Kosovo crisis gave rise to a temporary and agreed memorandum. Crucial arrangements were agreed both with the IMF and the World Bank at the end of 2000. Complementary macro-financial assistance has been provided by the EC. Failure to comply with the terms of the PRGF/EFF agreements with the IMF renders a new agreement with the IMF currently under negotiation crucial for the disbursement of any further or new *tranches* of the Community's Macro-Financial Assistance

Strict adherence to IMF and EU conditionality is a necessary step towards the desired macro-economic stability.

		1997	1998	1999	2000	2001
Real GDP Growth	Percent	1.4	2.9	2.7	5.1	-5.0 ¹
Inflation	Average	2.6	-0.1	-0.7	5.8	6.0 ²
	End-of-period	3.2	-2.4	2.6	6.1	6.9 ³
Unemployment rate	Percent of labour force	36.0	34.5	32.4	32.2	na
General government budget balance (% of GDP)		-0.4	-1.7	0.0	3.5	-0.7 ⁴
Current account balance	Percent of GDP	-7.4	-8.8	-3.3	-3.4	-11 ⁴
Foreign debt	Percent of GDP	30.4	37.9	42.1	43.6	39.4 ⁵
Debt-export ratio	Percent	94.5	111.5	124.7	108.9	120.9 ⁶
Gross foreign debt	Billion €	1.04	1.30	1.39	1.56	1.52 ⁵
Foreign direct investment	Percent of GDP	0.4	4.8	0.7	4.7	10.3 ⁴
	Million €	13	151	23	160	408

Sources: National sources, OECD external debt statistics, IMF Government Finance Statistics, World Bank

¹ World Bank estimate for Q1 2001; ² January-June, National Bank CPI data; ³ June, National Bank CPI data; ⁴ January-June/January-June GDP; ⁵ June 2001; ⁶ June 2001 debt/twice January-June exports.

3.3. Capacity for European integration

Several years of continued relations with the European Union, culminating in the recent signature of the Stabilisation and Association Agreement, clearly demonstrate the capability of the country to engage at a political level with the European Union and its Member States. However, a smooth implementation of the SAA is likely to be hampered by the constraints placed by an overbloated, highly centralised and politicised public administration. The lack of a modern administrative culture, a legacy of the previous government-system, coupled with a lack of the necessary skills and flexibility will undoubtedly pose a major hurdle on the way to the effective implementation of the commitments undertaken in the framework of the SAA. This is most immediately reflected in a clear difficulty on the part of the government to think strategically and identify medium to long-term policy objectives to be supported through the CARDS assistance. An excessive focus on the process of legal harmonisation risks to lose sight of the necessary structural reforms needed in order to ensure the effective implementation and enforcement of the enacted legislation.

One of the cornerstones around which the process of European integration revolves as well as one of the benchmarks indicating the country's capacity to progress along that path is the sector of justice and home affairs. The judicial sector is characterised by a significant backlog of cases which inevitably reduce the credibility of both the system and the citizens' faith in it; illegal trafficking of people, goods and drugs has assumed alarming proportions with the country being one of the preferential routes for the smuggling of tobacco, arms, drugs and illegal immigrants coming from within the region and from the Middle East. Porous and insecure borders significantly increase the difficulty of controlling illegal trafficking and fostering legalised trade.

3.4.Sustainability of current policies

Ten years into the transition from the socialist system of the former Yugoslavia to democracy and a market economy and the former Yugoslav Republic of Macedonia still has significant hurdles to overcome before a stable and sustainable political and economic environment can be established. The complete restructuring of the economic environment and negative short-term developments, such as the 1999 Kosovo crisis, have produced some undesired side effects which bear a distinctive mark on the current situation of the country. Rising poverty and falling employment have reached significant proportions (20 and 32 percent respectively) and have had severe repercussions at the social level. A scarcely efficient, overbloaded and largely corrupt public administration puts a break on the dynamic changes needed for the rapid development of the country and keeps citizens' confidence in the system at alarmingly low levels. A high correlation exists between lack of education and unemployment and between the latter and poverty. Regional inequalities persist and particularly affect rural areas, which suffer from growing depopulation.

The required progress with legislative approximation and structural reforms will pose very high demands on the public administration, as witnessed by the preparatory work already undertaken with a view to complying with the requirements arising from the SAA and the Interim Agreement. The authorities appear to accept and to draw operational conclusions from this but have still to prove that they will be capable of performing the enormous task of implementing the required reforms and changes.

The country seems to have partially lost the momentum that had characterised its reform process in recent times, a trend which goes beyond the negative repercussions produced by the recent crises. This is a concerning deviation from a necessary process which is to be corrected as rapidly as possible.

The reform agenda must be brought forward with renewed intensity in order to foster economic growth, job creation and the streamlining of state institutions.

3.5.Medium-term challenges

As it is apparent from the preceding analysis, the former Yugoslav Republic of Macedonia faces a number of major challenges in the medium-term, which, if successfully met, may significantly improve long-term perspectives.

In order to progress effectively on the reform path the country requires a stable and conflict-free civil and political environment. Inter-ethnic tensions which have been contained for a number of years dramatically exploded in February 2001 and brought the country to the brink of civil war. Political dialogue must be sustained and the concrete measures to ensure increased integration of the different nationalities are to be carried forward. In this respect the full implementation of the Framework Agreement will be a decisive factor for the restoration of stability.

The 1999 Kosovo crisis and the outbreaks of violence of the first half of 2001 have placed some significant constraints on the prospects for economic growth. Apart from these external constraints, the government's determination to carry out the planned reforms appears to be flagging. Painful and perhaps unpopular measures are needed to carry out the much-needed reform of the public administration and complete the privatisation process. Improved corporate management, SME development, promotion of entrepreneurship and self-employment and a restructuring of the agricultural sector in order to improve its efficiency and the quality of products should be promoted. Efforts towards the alleviation of poverty and the promotion of human development are to be intensified. Adequate consideration of environmental matters will contribute to ensure that sustainable economic development is achieved.

The Stabilisation and Association Agreement provides major opportunities but poses also significant challenges to the country by setting a wide and complex agenda. In order to make the most of the opportunities offered by the Autonomous Trade Measures and the Interim Agreement, the focus should be laid on the development and implementation of a trade strategy. Free access of national production to the EU market can only be enjoyed if appropriate technical and quality standards make the country's products suitable to distribution and consumption in the European internal market.

The reform process can only be successfully advanced if boosted and directed by a streamlined, leaner and more effective public administration. A widespread lack of strategic thinking and the consequent limited ability to project and implement medium to long-term policies has to be urgently addressed. Institutional capacity building remains a major priority of EU co-operation with the former Yugoslav Republic of Macedonia.

In the field of Justice and Home Affairs co-operation should focus on the reinforcement of institutions at all levels, law enforcement and consolidation of the rule of law. The development of an integrated border management strategy will have to be carried forward and a comprehensive strategy to combat organised crime appears to be a necessary element in the democratic and economic development of the country.

4. OVERVIEW OF PAST AND ONGOING CO-OPERATION

4.1. EC co-operation: past and present

The former Yugoslav Republic of Macedonia became a PHARE partner-country in March 1996, having previously benefited from the PHARE Critical Aid Programme (€85 million) between 1992 and 1996. The first Multi-annual Indicative Programmes (MIP) for both the

Country Operational Programme (COP) and the Cross-Border Co-operation Programme (CBC) with Greece covered the period 1996-1999. The total funds allocated to the country over this period under both programmes amount to €105 million, €68 million under the COP and €37 million under the CBC Programme. The CBC Programme with Greece has been primarily focused on mature infrastructure projects concerning the north-south Pan-European Corridor X and specifically on the up grading of the E75 road.

The implementation of the first series of PHARE projects began in the first half of 1997 with the process continuing in 1998 and 1999. A considerable number of the projects experienced common implementation difficulties stemming from limited absorption capacity and inexperience on the part of the beneficiary in relation to international funded assistance projects. The Government has been making concerted efforts to address these difficulties.

The PHARE National Programme 2000 and the CARDS programme for 2001 were moulded around the priorities identified by the Stabilisation and Association Agreement. They form a bridge between past assistance objectives and future support to the Stabilisation and Association Process to be defined in the present Country Strategy Paper, with the aim of bringing the country closer to EU standards and principles and to prepare the country for gradual integration into EU structures in the framework of the SAA process.

In 2001, the European Commission has also adopted a set of exceptional assistance programmes aimed at helping the country to overcome the security crisis and implement the Framework Agreement. On 4 May 2001 it adopted a programme worth €2.5 million under the Rapid Reaction Mechanism, the first ever use of such new financial instrument, to address reconstruction needs in conflict-torn areas. On 3 October 2001 a new RRM package worth € 10.3 million was adopted; the measures envisaged include reconstruction/rehabilitation of local infrastructure and public utilities, confidence-building measures including an assessment of the budgetary impact of the implementation of the FA and support to the process of reform of the police services. Finally, an additional emergency CARDS package of € 13.7 million covers housing and local infrastructure reconstruction/rehabilitation needs, financial assistance to families hosting internally displaced persons and measures to complete the work undertaken under the RRM on the reform of police services.

Furthermore, macro-financial assistance was provided in 1997 in the form of a loan facility of €40 million, subject to economic policy conditions. The conditions included satisfactory performance under the IMF programme, clearance of all arrears due to the Community and to the EIB, and a number of measures in the areas of trade (trade liberalisation, customs code), private sector development (promotion of foreign direct investment, bankruptcy legislation) and banking sector supervision and reform (lending exposure of banks, privatisation). The Commission released the first *tranche* of € 25 million on 30 September 1997 and following the fulfilment of the relevant conditions, the second *tranche* (€ 15 million) on 13 February 1998. A second assistance package of up to €80 million (of which up to 30 million in grants and up to €50 million in loans) was decided in 1999, of which a first tranche of €30 million (€20 million of grants and €10 million in loans) has been disbursed. It is expected that a second *tranche* of € 22 million (including € 10 million grants) will be disbursed as soon as the IMF and the authorities will have agreed on a revised macro-economic framework.

Since 1999, following the Kosovo crisis, the European Commission through the humanitarian office has provided over € 50 million of humanitarian assistance to the former Yugoslav Republic of Macedonia. This assistance addressed the needs of over 350 000 refugees who

fled neighbouring Kosovo and helped the local population to cope with the influx and after the return of most refugees, with its human consequences. In 2001, ECHO's operation in the country was expanded to address the basic humanitarian needs of the internally displaced persons and vulnerable local population and of the refugees that fled to Kosovo as a result of the crisis.

Previously, between 1992 and 1996, the Commission allocated over € 45 million of humanitarian assistance to the country to alleviate the humanitarian consequences of the war in the region (assistance to Bosnian refugees, support to local vulnerable population, provision of fuel to public institutions).

4.2. Assessment of past EC assistance

The delivery of past EC assistance has encountered some significant difficulties which can be re-conducted to two main principal causes: a limited absorption capacity of the partner country mainly due to an inefficient and badly structured administrative sector and a limited ability of the European Commission in delivering promptly the programmed assistance. The latter cause has been in turn partly due to a sometimes overambitious approach in the programming of the assistance. A comprehensive assessment of the main lessons learned from past EC support to the country are set out in Annex 4.

4.3. EU Member States' Programmes

Co-ordination of donor activities by EU member states is beginning to improve with the introduction of regular meetings of diplomatic missions and representative offices in the country. A further exchange of information takes place through the Delegation of the European Commission.

Although no individual donor emerges as an obvious leader in any single sector, the contribution by EU member states in assistance to the country has been considerable. All EU Member States have been present, and assistance has been provided in almost all sectors.

A significant part of the assistance has been under the heading of budgetary support and humanitarian aid, partly due to the alleviation of the serious consequences of the Kosovo crisis.

The private sector and SME development received an important support in the form of loans for the SMEs, as well as technical assistance targeting services to SMEs; assistance was provided by a number of donors, but major contributions were provided by Italy and Germany. The assistance in the environment sector focused on protection programmes for the lakes Ohrid and Prespa, as well as on local (municipal) environment action plans, with a major presence of German bilateral aid. In the water supply/waste water sector, again dominated by German bilateral aid, activities targeted water supply projects and wastewater treatment stations for less developed regions. The agricultural sector received a significant input (especially by the Netherlands and Germany) in developing and modernising various production sectors, irrigation, and food control.

Donor activity in the sector of democracy, human rights and civic society was characterised by a larger number of smaller projects on promotion of multi-ethnicity, minority rights, civic society education, and support to NGOs.

In the sector of public administration reform, British bilateral aid (DFID) is providing bridging support to the PAR Permanent Unit, the Civil Service Agency and in strengthening negotiation and management capacity, while France is involved in university education for officials and there are plans for major support to the establishment of a School for Public Administration Reform.

Assistance was provided also in the social sector (social institutions, social partners, and disabled), while a significant social infrastructure programme by the German bilateral co-operation is under preparation. In the education sector, activities focused on the rehabilitation of schools, education reform and training of specific target groups. Several EU Member States contributed to the five-year financing plan prepared by the OSCE for the creation of the South East Europe University in Tetovo.

The financial sector received assistance in auditing of loss-making enterprises and technical assistance in the reform process, while a significant programme is under preparation by the Dutch bilateral aid, mainly for the Ministry of Finance.

In the legal sector, British and German bilateral aid provided support in consumer protection, while French aid focused on permanent training for judges. Germany will provide assistance to the Monopoly Agency, and Sweden to the Macedonian Bar Association.

In the period 1997-2001 Greece has provided humanitarian assistance and investments in infrastructure whilst for the period 2001-2006 it will be mainly directed to improve social infrastructure and to provide technical co-operation to the economic sector.

4.4. Other Donors'² programmes

Efforts to improve the co-ordination of various donor activities in the country have been consistently made over the last years. Some progress was made through the EC PHARE funded assistance to the Government's Aid Co-ordination Unit (ACU), later transformed into the European Integration Office (EIO) and now into the Sector for European Integration (SEI). Further progress was achieved with the introduction of UNDP software at the end of 1999. However, not all donors report their activities to the EIO, and there is an incomplete flow of information from the various Government ministries and institutions to the EIO. All data on other donors need therefore to be considered as indicative.

A significant level of co-ordination has now been achieved between the Delegation of the European Commission and various donors present in the country in spite of the general absence of a systematic approach in donors' co-ordination.

² For a breakdown of figures on other donors' assistance see Annex 3.

The main donor is the United States Agency for International Development (USAID) whose activities stepped up during and after the Kosovo crisis, and have been marked by a two- to three-fold increase in funding. Activities are concentrated in the accelerated development and growth of the private sector (including support to enterprises, legal reform and rule of law, and agriculture), increased, better informed citizen participation in political and economic decision-making (political and civic participation, democracy network, civic education, child education and community self-help initiatives), more effective, responsive and accountable local government (environment action programme and local government reform), and cross-cutting and special initiatives (pension sector reform, tax administration and participant training).

The World Bank provides loans and some technical assistance in public administration reform, enterprise support and restructuring, school reconstruction, culture, social sector reform and support to social cases, health, agriculture, environment, transport, and border crossings infrastructure. EBRD provides loans for support to enterprises, the establishment of business advisory services and development/modernisation of infrastructure. The EIB has to date authorised loans worth € 150 million for road rehabilitation and construction and support to the SME sector. Finally, UNDP activities support local governance and environmental development.

Swiss bilateral aid focuses on support to enterprises, environmental protection and more recently on support to families hosting internally displaced persons as a consequence of the crisis.

5. THE EC RESPONSE STRATEGY

5.1. Principles and objectives for co-operation

Based on the above analysis, the EC response strategy has two main pillars – firstly, supporting the former Yugoslav Republic of Macedonia's participation and progression in the SAP which, through political and economic stabilisation and increasing association to the EU, are the keys to the country's long-term prosperity while, secondly, continuing the conflict prevention and rehabilitation support that is key to enabling it to pass through its current period of instability.

This dual focus reflects the need to focus limited budgets on areas where the Community has a clear comparative advantage, thereby ensuring an impact with its funds, while also helping the country to maintain its course through current crises.

Careful co-ordination and repartition of tasks with other international community donors and IFI's will ensure that support is directed to other areas that may clearly also be priorities, as shown by above analysis but which, due to budget limitations and lack of comparative advantage, the Commission cannot finance.

In spite of the good progress made since the beginning of the transition, the process of reforms in the former Yugoslav Republic of Macedonia has to be brought forward with sustained intensity over the years to come. The slowing down of the process of economic reform, partly imputable to the effects of the 1999 Kosovo crisis and the internal crisis of 2001 resulting in a serious threat to its stability, are warning beacons that clearly indicate the scope of the challenges ahead. The country needs to take concrete and sustained action if the objectives of sustainable economic growth, easing of ethnic tensions, poverty reduction, reform of state institutions and integration into the European Union's structures are to be achieved.

EC assistance will have to stimulate, support and intensify the ongoing reform process in the country, in particular in areas where further progress is most needed.

The main purposes of EC assistance are to support the participation of the former Yugoslav Republic of Macedonia in the Stabilisation and Association Process and concretely help the country to overcome the consequences of the political and security crisis that erupted in the first half of 2001. The signature of the Stabilisation and Association Agreement in April 2001 marked a very important step in the process of integration into the European Union and set the agenda for future co-operation between the European Community and the former Yugoslav Republic of Macedonia. The European Commission's response strategy is largely based on the priorities and the objectives set by the agreement and most importantly on fostering political dialogue and regional co-operation, sustaining democratisation and the rule of law, the promotion of economic development and trade facilitation, enhancing co-operation in the field of justice and home affairs, and increasing environmental protection standards. Sustained assistance in these priority sectors is also designed to sustain the process of ethnic reconciliation and set the conditions to ensure the long-term stability of the country.

The specific objectives are the consolidation of democratic institutions and the rule of law, the easing of inter-ethnic tensions, the support of the transition to a functioning market economy

capable of delivering economic growth and of raising standards of living and the support to the maintenance of peace and regional co-operation.

Moreover, in cases of exceptional financing need, the European Commission may consider the possibility of providing macro-financial assistance based on an ad-hoc Council Decision as stipulated in the Stabilisation and Association Agreement (Art. 106).

The EC Response Strategy serves not only the direct policy goals of the SAP as required by the CARDS regulation but also two critical objectives underpinning all EC support, namely conflict prevention and poverty reduction. The Stabilisation and Association Process is a regional conflict prevention strategy and the EC Response Strategy will address fundamental weaknesses and tensions which may contribute to or trigger conflict within the country and the region and their economies. Sustainable economic development is central to the SAP. All of the measures supported will contribute directly or indirectly to this goal. It is only through sustainable development that poverty reduction can be effectively addressed. This is an approach which is shared with the World Bank.

It is important to note that EC assistance to the former Yugoslav Republic of Macedonia must not be seen as a one way process but it is rather intended to be based on increased level of responsibility or ‘ownership’ of the process by the partner country which will be increasingly requested to provide solutions to its own difficulties. EC assistance is therefore designed to assist and support this approach to the greatest possible extent.

The European Commission will concentrate the assistance on a limited number of priorities in order to maximise the impact of its programmes. Concentration will be sought compatibly with the overall objectives of the SAP and of the implementation of the SAA and the IA. This approach will allow the European Commission to focus on those sectors and priorities in which it has a comparative advantage with respect to other donors such as the building of institutional capacity, the gradual harmonisation of the country’s legislation with the European Community’s “acquis” and justice and home affairs.

5.2. Priorities for co-operation

5.2.1. Democracy and the rule of law

Respect for democratic principles, human rights and the rule of law is a specific requirement of the SAP and according to article 2 of the SAA “shall form the basis of the domestic and external policies of the Parties and constitute essential elements of this agreement”. The European Commission’s response strategy is designed to help the country establish solid democratic institutions and develop a climate favourable to increased political stability and inter-ethnic integration.

Inter-ethnic relations are a long-standing issue in the former Yugoslav Republic of Macedonia whose solution is paramount for the future stability of the country and for its very existence. The analysis of the preceding chapters has underlined how the 2001 crisis strengthened the already existing polarisation of society along ethnic lines. The process of reforms the country has embarked upon requires a stable and conflict-free civil and political environment in order to be brought forward successfully. The EC wants to favour the creation of mechanisms that

can improve inter-ethnic dialogue and effectively contribute to socio-economic development which cuts across ethnic lines.

A well-developed civil society is one of the cornerstones of a fully functioning democratic system. Assistance will support NGOs development and in particular those active promoting inter-ethnic dialogue. Support will also be provided to the gradual development of an active third sector which is able to complement effectively the public and private sectors.

5.2.2. Administrative capacity building

Institutional capacity building is the cornerstone around which the whole process of European integration revolves. One of the priorities identified for EC assistance by the CARDS Regulation is “the creation of an institutional and legislative framework to underpin democracy, the rule of law and human and minority rights, reconciliation and the consolidation of civil society, the independence of the media and the strengthening of legality and of measures to combat organised crime”. The EC believes it enjoys a comparative advantage in this institution-building process which aims at establishing an institutional framework responsive to the needs of a fully-fledged democratic country with a functioning market economy. This will be primarily done through a series of punctual interventions in those sectors where the needs are most apparent and will be directed at creating the institutional capacity needed to implement and enforce the legislative changes related to the “acquis” and to the development of a modern system of administration. Actions in this field will be closely co-ordinated with the requirements of the World Bank’s public sector management loan providing the framework for the public sector reform.

5.2.3. Economic and social development

5.2.3.1. Private and financial sector development

The process of harmonisation of legislation with the EU ‘acquis’ will be primarily targeted to facilitate the free movement of capital, the creation of banking and insurance sectors which are fully in line with EC standards and the development of accounting principles compatible with the EC’s.

A buoyant and productive private sector characterised by a high degree of legal certainty favouring foreign investment and entrepreneurial initiatives, effective corporate management and highly developed entrepreneurial skills are necessary requirements to ensuring the achievement of sustainable economic growth. For this purpose the improvement of corporate management and training for enterprise development will be addressed. The process of legal harmonisation in the sectors of public procurement, intellectual property rights and company law will also be supported.

Efforts will be made to sustain the completion of the privatisation process and help the restructuring of the major industrial sectors.

The creation of an effective system to ensure full respect of fair competition principles in the business environment is a major priority. Assistance will target both the process of legal approximation and the setting up of the appropriate authorities designed to monitor the implementation of the relevant legislation.

5.2.3.2.Trade

The former Yugoslav Republic of Macedonia has been progressively opening its markets over the years and has undertaken to make further liberalisation efforts by entering the SAA with the EC. The most immediate objective of EC assistance is to ensure that the country is able to fully enjoy the benefits that free access to the EC market can bring. In this view it will support an effective trade-development strategy and it will provide the necessary technical and legal assistance to ensure that the partner country's products meet the EC's technical and quality standards. Technical and legal assistance will also be provided to ensure the country develops the necessary institutional capacity to implement its commitments under the SAA and the IA and to favour its accession to the WTO.

Trade facilitation is also dependent on the existence of an integrated and efficient transport system. Efforts will concentrate on the development of transport safety standards and the needs of rail, road and air transport systems will be addressed.

Support will be provided to raise quality standards of agricultural products. The improvement of veterinary and phytosanitary controls will be supported as well as the overall process of harmonisation with EU standards and legislation. Particular attention will be devoted to the food-safety sector.

5.2.3.3.Economic and Social Cohesion

With official unemployment at 32 percent the country is in dire need of a major restructuring of its labour market. EC assistance will focus on improving job information networks, helping the country develop a national plan for employment and transform the plan into concrete actions.

Compulsory elementary education has resulted in a very high degree of basic education and literacy. However, the structure of secondary education is not in tune with the needs of the emerging market economy due to its specialisation in the provision of highly technical skills. The higher education system also needs to be streamlined and improved. The EC will continue to provide assistance under the Tempus III programme in order to support the reform of higher education and will continue to provide support to the process of modernisation of Vocational Education and Training. Assistance will also be directed to the establishment of a training fund for enterprise development.

Regional imbalances are marked in the former Yugoslav Republic of Macedonia. Assistance will be directed at promoting development and conditions for growth in the least developed areas of the country. Development of entrepreneurial skills, conditions for self-employment, creation of SMEs and increased access to education will be specifically targeted. On top of that, assistance will be directed at supporting the reform of Local Self-government currently underway. Support to fiscal decentralisation and the creation of mechanisms enabling municipalities to achieve a sustainable degree of financial autonomy will be provided. The streamlining of local structures of government will also be targeted.

5.2.4. *Justice and home affairs*

5.2.4.1.Reform of the judiciary

The process of reform of the judicial system is already underway but continued support is needed in order to develop a strong, independent and efficient judicial system. Assistance will

be directed to strengthening the independence and increasing the effectiveness of the judiciary and to restructuring the court system. The specific measures foreseen include training of legal professions and the increase of the effectiveness of court procedures including the computerisation of the Courts.

5.2.4.2. Integrated border management

Border management problems in the former Yugoslav Republic of Macedonia are inter-linked and only a comprehensive solution that addresses all the various problems will be effective. For this reason, an overall integrated border management approach is proposed that strengthens controls at the border, facilitates trade across the border and meets the particular needs of the regions spanning the border:

- (1) Alongside other linked support (e.g. standards and norms), facilitating trade will involve the improvement to border crossings, strengthening of national institutions and procedures (e.g. customs, veterinary agencies) and improving infrastructure within the country (e.g. multi-agency information systems).
- (2) Enhanced border control will involve not only strengthening the capacities and the infrastructure of border guard agencies and promoting inter-agency co-operation with customs but also actions on border demarcation and regional crime fighting.
- (3) Particular needs of border regions will be addressed through regional development programmes.

The Regional Strategy Paper, which complements the national strategic papers, sets out priorities which will be addressed in a regional context. Although included in the Regional Strategy and funded from the regional envelope, measures to address the Integrated Border Management priority will, for reasons of efficiency, be implemented as part of the national programmes and for that reason are described in this paper.

The EC will support an integrated approach to border management in the former Yugoslav Republic of Macedonia and the other countries covered by the SAP. The interlinkage of border management problems justifies this approach. In fact, only a comprehensive approach addressing all the various problems will be effective. The specific problems which this approach is designed to address are the low levels of regional and international trade and the threat posed by increasing levels of organised crime and corruption, including trafficking and illegal migration to the EU transiting through the former Yugoslav Republic of Macedonia. The objective is to strengthen controls at the border and to facilitate cross-border trade.

5.2.4.3. Immigration and asylum

Illegal immigration is often the source of profound social tensions and a rise in criminal activities. Co-operation on the prevention and control of illegal immigration will be fostered. Training of public officials and improved communications systems will be given priority assistance. Standards and methods for controls on persons and the development of rules concerning visas will also be targeted.

5.2.4.4. Fight against crime

The European Commission is working jointly with the OSCE on a 12-month programme designed to implement the reform of the police services required by the Framework Agreement. CARDS will build on that programme to fund a more extensive approach to the reform of policing. A competent and corruption-free police will be a key step on the road to a

stable and secure society. The priorities will be to support the effectiveness and the democratisation of the police and assist the training of police officers, in particular in anti-corruption matters. Training to address issues like respect of ethnic minorities and human rights will also be provided.

Illegal trafficking of people, cigarettes and goods has become an increasingly serious problem in the former Yugoslav Republic of Macedonia. Tackling all these forms of crime is a major priority which EC assistance will support. The priority will be placed on increasing expertise and on training. Assistance will be provided for the development of a comprehensive strategy designed to reduce the supply, trafficking and demand of illicit drugs and psychotropic substances. The strategy will be based on the lines and principles of the EU co-ordinated strategy on drugs. Assistance will be provided to the development of the strategy and to the implementation of concrete measures for its implementation.

The establishment of a set of anti-money-laundering legislation and enforcement measures compatible with EU standards will also be targeted.

5.2.5. Environment and natural resources

Support will be directed to the creation of strong and independent national authorities for the protection of the environment. Legal approximation to the Community 'acquis' and the capacity to ensure enforcement of environmental rules and regulations will also be targeted. In order to increase health protection levels support will be given to water quality, air pollution and waste management programmes. Efforts will also be made to raise public awareness of environmental issues and strengthen public access to environmental information and decision-making.

5.3. Coherence

EC assistance is focused on advancing the SAP and in particular on assisting the former Yugoslav Republic of Macedonia to implement the Stabilisation and Association Agreement signed in April 2001. The agreement is designed to bring the country closer to and favour its gradual integration into the European Union. The SAA sets forward a series of specific objectives to be achieved within precise deadlines with the aim of making the partner country's policies and legal framework fully compatible with the EU's. Moreover, in preparing this strategy paper EU policies have been taken as a reference and in particular the external dimensions of policy sectors like Trade, Justice and Home Affairs and the Environment have been fully assessed. When the assistance will not be strictly related to the obligations of the SAA, EC policies will be invariably taken as the reference upon which objectives are defined and achievements measured. The EC Trade policy in particular represents a key facet of the overall strategy for South East Europe, as trade development is seen as a catalyst for economic transformation and for integrating the region with the rest of Europe and of global markets at large. It is in this perspective that the countries of the region are requested, as part of the SAP, to establish a free trade area between themselves which is consistent with relevant WTO provisions. Free trade is an advantage but also represents a major challenge since it requires that minimum standards of quality and safety be met thus providing a stimulus to increasing competitiveness, lowering production costs and raising quality standards. Free trade and economic growth necessitate a secure civil and economic environment in order to thrive. Support to the sector of Justice and Home Affairs becomes

paramount then in order to ensure a stable environment conducive to human and economic development. This is all the more true in the former Yugoslav Republic of Macedonia which is a crucible of illegal trafficking in the region and is going through a most sensitive time of its history.

Coherence with CARDS regional programmes: the bulk of CARDS support to the countries is being financed through national CARDS support programmes. Experience from PHARE and other Community programmes has shown that this subsidiarity ensure greater levels of national commitment and ownership, better targeting and impact of projects and greater efficiency in implementation.

However the European Commission has concluded that complementing this basic national approach with a small regional CARDS programme will ensure its objectives are achieved and complement the activities of the CARDS national programmes because either: (i) the problem addressed is truly cross-border and requires active regional co-operation between the SAP governments if it is to be corrected; or, (ii) there are significant gains to be obtained in terms of efficiency or enhanced impact by implementing through one regional programme instead of five national ones.

To this end, some 10% of the available funds will be allocated through the CARDS regional programme to help countries achieve the regional co-operation objectives of the SAP. These will be focused on three priorities: (a) supporting democratic stabilisation, including minority rights, media and good governance; (b) building the capacities of state institutions; and (c) reinforcing regional infrastructure and environmental development. These priorities are outlined in greater detail in the CARDS Regional Strategy Paper.

When the priorities of the CARDS programme contain a cross border co-operation character, complementarity with the INTERREG programme III A will be ensured to the greatest extent possible. This is particularly the case in the Integrated Border Management, Environment and Local Infrastructure programmes. To this end, close co-operation will be developed between the country concerned, the CARDS and INTERREG programmes and the concerned EU Member States and candidate countries, including as appropriate the identification of relevant projects in the priority areas of the Multi-annual Indicative Programme and regular reporting of progress.

Coherence with ECHO assistance will also be sought. In conformity with its humanitarian mandate ECHO will phase out from the country provided the situation stabilises. In the implementation of the measures planned in this strategy an effective linkage with previous and current humanitarian actions funded by the European Commission will be sought, in particular in the local infrastructure and social sectors.

5.4.Complementarity with the EU Member States and other donors

The country strategy results in a clear focus of CARDS' limited resources on a limited number of priorities where the European Community's funds will have a clear impact. When coupled with the Community's other support, notably in macro-financial assistance and emergency support, the programme provides an effective tool to support the country's implementation of the SAP and to promote stability.

However, the focus of CARDS resources requires there to be a clear complementarity not only with the governments' actions but also with the actions of other donors.

Close co-operation will be sought with Member States' planned assistance particularly for sectors like education, health-care, media, communications networks, major infrastructure development, culture and civil-society development and public administration reform.

In this way, the CARDS strategies will be part of a coherent international community response to help the former Yugoslav Republic of Macedonia meet its substantial development and SAP challenges.

The mechanisms for this co-ordination effort – on the overall strategy, on annual programming and on implementation of specific programmes and projects - are already in place. And the Commission gives its full commitment to working through these mechanisms not only to co-ordinate its support and share information but also to ensure complementarity by promoting other donor support in areas where budget constraints and comparative advantages preclude Community action.

First, the Commission co-chairs and is guided by the High Level Steering Group for Southeast Europe that provides overall guidance on donor co-ordination. Second, the Commission maintains a Joint Office with the World Bank to help co-ordinate and develop support to the region (e.g. the Regional Conference in October 2001). Third, the Commission plays an active and leading role with the countries and international community in the three tables of the Stability Pact for Southeast Europe.

Fourth, the Commission maintains relations with governments to ensure its actions complement and build on national efforts, organised directly by headquarters or through its Delegations in each country. These discussions range from detailed trade negotiations through to implementing CARDS support alongside national authorities.

Fifth, the Commission delegations organise regular meetings in-country through the year with Member states, national authorities and other involved organisations (such as International Financial Institutions) to ensure monitoring and co-ordination on an on-going basis throughout the programme cycle. An annual meeting reviews progress over the year and identifies any substantive issues on co-ordination. The Commission is fully aware of the extreme importance of effective co-ordination with the Member States and makes a priority of reinforcing and improving existing co-ordination mechanisms so that possible overlaps/discrepancies are avoided and resources are effectively pooled or managed.

It is obviously paramount that the different donors' programmes are designed to assist the partner country's progress in its reform process in a consistent and uniform manner. The World Bank appears to be increasingly taking into consideration the former Yugoslav Republic of Macedonia's European integration objectives when devising sector reform programmes. Complementarity of the Poverty Reduction Strategy currently under preparation with EC assistance seems to be assured in that it aims at establishing administrative, economic and social conditions which can set the basis for sustained economic growth and equitable distribution of wealth, conditions which a successful process towards European integration inevitably require. The IMF and World Bank's loans agreed on at the end of the year 2000 are

fully complementary to the Commission's macro-financial assistance and based on a similar set of conditionalities.

USAID's growing involvement in the former Yugoslav Republic of Macedonia and the significant increase in the amount of its assistance require improved co-ordination and co-operation in particular with reference to support for local government, political, economic, financial and legislative reforms.

5.5. Risks and assumptions

The underlying assumption of the CSP is that the former Yugoslav Republic of Macedonia will progressively regain its political and economic stability and will be back on the track towards European integration. This is assumed to happen in a regional context which should also become increasingly stable in the coming years. Any deterioration of the regional environment might produce important negative consequences for the country and rekindle the internal security crisis that has affected it in 2001. The international community will play an important role in ensuring and advancing stability by fostering the consolidation of the regional dialogue and economic ties and by promoting the economic and institutional development of the country.

There is however the risk that a deadlock in the political dialogue plunges the country back into a dangerous spiral of conflict. This would obviously produce direct negative consequences for the delivery of the EC assistance which is made conditional to the restoration of a stable political climate and the full implementation of the Framework Agreement.

It is assumed that the country will fully implement the Interim Agreement on trade-related matters signed with the EU, sign further free-trade agreements and become a member of the WTO. The risk remains however, that the country's industry will not be able to take full advantage of the opportunities which these developments will offer.

There is a relevant risk that the country's lack of absorption capacity will pose constraints on the delivery of the assistance. This has been carefully taken into consideration when identifying sectors and programmes for the assistance; on its part the European Commission is determined to and is examining all ways to improve its ability to deliver the programmed assistance, and is already gradually catching up with the backlog accumulated in past years.

In implementing EC assistance careful attention will be paid to changes in the assumptions underlying the CSP and project identification will take account of the new circumstances. In some cases the situation may require that a particular programme is postponed or not undertaken. The MIP takes account of this possibility by setting out programmes with a total value of 15 percent more than the indicative allocation for the former Yugoslav Republic of Macedonia. Where appropriate a revision of the CSP may be undertaken in accordance with the CARDS Regulation.

ANNEX TO THE COUNTRY STRATEGY PAPER

6. MULTI-ANNUAL INDICATIVE PROGRAMME (MIP) 2002-2004

INTRODUCTION

The Multi-annual Indicative Programme (MIP) describes the sectors and the planned interventions to which Community assistance for the former Yugoslav Republic of Macedonia in the period 2002-2004 will be directed as well as the expected results and indicators of achievement. The assistance will be delivered through a number of sectoral interventions in support of the four priority areas identified in Section Five of the Country Strategy Paper:

- Democracy and the Rule of Law
- Economic and Social Development
- Justice and Home Affairs
- Environment and Natural Resources

The overall objectives of the National Indicative Programme are to support the participation of the former Yugoslav Republic of Macedonia in the Stabilisation and Association Process and to assist the country in its efforts to overcome the consequences of the political and security crisis erupted in the first half of 2001.

The immediate objectives of the assistance are to:

- Support the process of integration of the former Yugoslav Republic of Macedonia into EU and other international structures;
- Consolidate democratic institutions and democratic principles and promote the application of the rule of law and good governance;
- Support the establishment of a functioning market economy which is capable of delivering sustainable economic growth, fostering trade and generating employment;
- Support the development of social cohesion and social justice while promoting inter-ethnic integration;
- Encourage regional co-operation.

6.1. Democracy and the rule of law

6.1.1. *Inter-ethnic relations and civil society*

Background: Democratic stabilisation of the countries of Southeast Europe features prominently among the overall objectives of the Stabilisation and Association Process; achieving this major goal implies both the involvement of central governments and, most crucially, the population at large through the development of civil society. A buoyant and free civil society is a necessary element of truly representative democratic systems and plays a fundamental role in holding governments accountable and directly promoting human rights and protecting minority rights. Civil society is organised largely through non-governmental organisations of which there are over 600 registered in the former Yugoslav Republic of Macedonia. However, not all of them can be considered to be active and the relative marginal

impact of the activities of local NGOs in the country is primarily due to the fact that the sector is donor-driven, largely atomised and it operates on a strong ethnic basis.

Even before the security crisis of 2001 the picture of Macedonian society was that of a society divided along ethnic lines, with parallel networks for ethnic Macedonians and ethnic Albanians, and a generalised lack of contact and interaction between ordinary people from different ethnic backgrounds. Distrust between the two communities has grown out of proportion and Macedonian society is today as polarised as it has ever been.

The relevant historical legacy is not one of ‘ancient hatreds’ but rather of the socio-economic structure left over from the Federal Republic of Yugoslavia. During the Yugoslav period, despite many human rights abuses, an extensive system of collective rights for minorities was established, particularly in the field of education. In reality however, some degree of discrimination against certain groups existed. During this period, the socio-economic, cultural and educational gap between ethnic groups widened. Today more than 50% of the Albanian and Turkish population live in rural areas (69.8% of Albanians, 56.1% of Turks) against only 35.7% of ethnic Macedonians.

The ethnic division of society has manifested itself in the local NGO sector; NGOs in fact operate in a context in which various ethnic groups seek to promote their own identity and to claim their rights in a mono-ethnic framework of a multiethnic and multicultural society. As a consequence it is broadly possible to say that local NGOs tend to deal with similar issues but their efforts are targeted at a specific ethnic community.

Objectives:

- (1) To promote the development of a buoyant and free civil society and favour inter-ethnic dialogue and reconciliation, and the prevention of future conflicts.
- (2) To promote the development of the social economy and to establish a more democratic and tolerant public service.
- (3) To reduce the atomisation of civil society and foster co-operation on an inter-ethnic basis in the NGO sector;
- (4) To increase the active participation of civil society in the policy-setting and decision-making process.
- (5) To increase tolerance towards minorities;
- (6) To support local NGOs in developing projects aiming at preventing inter-ethnic conflict, promoting tolerance and the principle of democratic citizenship.

Expected results: The establishment of a foundation for civil society, a contribution to the creation of a more active and articulated civil society measurable through an increase in the number of active NGOs; increased co-operation amongst local NGOs on cross-ethnic issues and increased “productiveness” of the local NGO sector manifested through a boost to the social economy and increased influence of civil society in the legislative process. X administrative staff of municipalities and central government institutions trained on minority issues, conflict resolution and ethnic reconciliation. Public information campaign on tolerance towards minorities and inter-ethnic dialogue completed.

Programmes to be implemented:

Coherence and effectiveness in the civil society will be enhanced through the establishment of a new foundation for civil society. The foundation will act as a catalyst for civil society organisations in the country and as a forum for co-ordination of efforts. This will reduce the atomisation of civil society and foster co-operation in the NGO sector. Technical assistance will be provided for the purpose. It is crucial that local NGOs be encouraged to serve as an integrative force of various ethnic groups living in the country rather than merely reflecting ethnic differences and reinforcing the isolation of the various communities. The role of NGOs is to represent various interests which should then be translated into policy actions by governments but not to represent ethnicity as it is often the case in the former Yugoslav Republic of Macedonia. Through the foundation for civil society small projects will be selected that promote co-operation on a cross-ethnic basis.

Increased participation of civil society in the policy setting and decision-making process and the establishment of a more democratic and tolerant public service will be sought by training municipal authorities and local opinion-makers on minority issues, conflict resolution and ethnic reconciliation. Tolerance towards minorities and an environment prone to inter-ethnic reconciliation will be promoted through a public information campaign.

Technical assistance will also be provided to promote a series of dialogue-workshops on conflict prevention and ethnic reconciliation, ethnicity, nationalism and political change. The workshops should involve parliamentarians, ambassadors, academics, university students, and representative of local and international NGOs.

Indicators of achievement: Reduced atomisation of the NGO sector and increased co-operation among local NGOs evidenced by an increase in the number of joint projects. Expanded measure of NGO pressure group activity evidenced by a higher involvement of NGOs in the legislative process. Increased number of NGOs working on a cross-ethnic basis.

Cross cutting issues: The assistance provided with this programme reinforces and extends the assistance being provided to the Justice and Home Affairs sector. In particular, it promotes the creation of a stable and conflict-free political and civil environment and favours the respect of human and civil rights while strengthening the functioning of democracy.

Conditionality: Full respect of ethnic and minority rights in accordance with the dispositions of the Framework Agreement and adoption of the Constitutional amendments and legislative modifications set out in annexes A and B of the Framework Agreement.

Other EC instruments: Complementarity of programmes in this field with the targeted projects funded under the European Initiative for Democracy and Human Rights will be ensured. The Initiative funds small projects to support NGOs development. Due account will also be taken of the support provided through ECHO programmes in the field of community services.

6.2. Economic and social development

6.2.1. Private and financial sector

Fund for Human Resources Development in Enterprises

Background:

The Stabilisation and Association Agreement signed between the EC and the former Yugoslav Republic of Macedonia on 9 April 2001 will create a new climate for economic relations, trade and investment, which are crucial factors for the economic restructuring, modernisation and development of the former Yugoslav Republic of Macedonia.

Local firms will therefore have to cope with increased competitiveness both in the internal and external market and, to be competitive, they will need to invest consistently to promote greater efficiency. This efficiency will largely depend on their flexibility, capability for innovation, access to financial investment and on the quality of their human resources.

Objectives:

- (1) To assist local training providers in developing high quality training programmes for enterprises, both vocational and management, in order to contribute to the improvement of their performance and efficiency.
- (2) To provide guidelines to the Government for the adoption of a policy to support, on a permanent basis, the development of human resources in enterprises.
- (3) To improve the efficiency and effectiveness (and therefore competitiveness) of the companies through an upgrading of human resources both at managerial and technical level;
- (4) To strengthen the capacities of local training and consulting organisations both in terms of quality and quantity of the services they may provide also through a partnership agreement established with a relevant EU institution;
- (5) To establish a network among training institutions, which may lead to the creation of an “ad hoc” association;
- (6) To provide orientations to the Government for the adoption of a policy to continue to promote on a sustainable basis investment in human resources development by the enterprises;
- (7) To promote best practices which will become a model for the enterprises not involved in the programme;

Expected results: Companies are made aware of the importance of investing in training to improve their productivity and efficiency. Progress towards the establishment of a local market for management training is made; the social partners actively promote investment in training in enterprises. Fiscal incentives are established by the Government to stimulate companies’ investment in human resources.

Programmes to be implemented: The programme will be designed to support the provision of consulting and training services to companies willing to invest in human resources development.

The management fields, may cover, among others:

- Marketing (i.e. how to locate the enterprise into the local and external market, how to launch a new product, modern selling techniques, etc.);
- Total quality (i.e. the concept of quality management, the process of ISO certification, etc);
- Finance (i.e. EU standard accounting system);
- Technological innovation, both linked to production and management techniques.

As regards vocational training, a priority will be given to the needs for the up-grading of the workforce arising from investment in technological innovations, of which the enterprises will need to provide evidence..

The support of social partners will be an advantage in the selection process of the beneficiaries.

A public awareness campaign will be organised to launch the programme.

Indicators of achievement: High number of enterprises involved in the programme. A network of training providers established and the ground set for the creation of an “association”. Projects are selected and successfully implemented; partnership agreements are established between local and EU training providers. The competitiveness of the companies involved in the programme is increased and concrete progress towards the establishment of a local market for training is made. The legal framework providing the sustainability of the programme is developed.

Cross-cutting issues: The assistance provided under this programme reinforces and extends the support being provided to Social Cohesion development. Economic growth, increased employment opportunities and the stimulus of the competitiveness of local enterprises are seen as complements to the alleviation of poverty and the easing of social tensions.

Conditionality: Respect of the policy of non-discrimination and equitable representation for employment in public administration and public enterprises in accordance with the text of the Framework Agreement.

Approximation of legislation to the internal market “acquis”

Introduction: Since independence in 1991, the Government has undertaken an extensive programme of legal reform to replace former Federal Yugoslav legislation which was unsuitable for the needs of a market oriented economy and was not conducive to the promotion of private enterprise and foreign investment.

The country has already developed a plan for the approximation of legislation to the European Community’s “acquis” but the legal framework is largely incomplete and several laws need to be improved and co-ordinated with both the Constitution, existing laws and Community legislation. The signature of the SAA renders the process of legal approximation all the more important since upon entry into force of the Agreement or, as in most cases after a transitional period, the country’s legislative framework will have to be largely in conformity with Community’s legal provisions and standards.

In this context it is evident that the gradual approximation of the internal market legislation is paramount for the effective and correct implementation of the Agreement and a successful process of progressive European integration. Among the different sectors included in the National Plan for Approximation of Legislation this programme has identified the following priority sectors for support during the time-period covered by the MIP: competition law and state aids, public procurement, and intellectual property rights. They are specifically dealt with in the sections below.

Competition law and state aids

Background: Competition law and provisions regulating state aids are one of the central planks around which the whole construction of the internal market of the European Community is built. By signing the Stabilisation and Association Agreement the former Yugoslav Republic of Macedonia pledged to bring its legislation in the fields of competition and state aids gradually in line with those of the European Community. Specific deadlines are set in 3 and 4 years following the entry into force of the Agreement respectively before the principles set out in the Treaty establishing the European Community are upheld.

A new legal framework in the domain of monopolies regulation and competition policy was set up through the adoption of the Law against unfair competition and the Law against limiting competition in December 1999. As prescribed by the laws a Monopoly Authority charged with the implementation of competition policy was created and has been operative since April 2000. The Authority has been created as a body within the Ministry of Economy and is endowed with a staff of eight: a Director appointed by the Government, three members of the Decision Board also appointed by the Government, two economists and two lawyers forming the Department for Supervision and Monitoring of the Market. During its first year of activity it has dealt with six cases five of which have already come to a head whilst the remaining one is currently in the appeal phases. The Authority's mandate includes vetting mergers and acquisitions, sanctioning possible abuses of dominant position by undertakings, evaluating practices and agreements which may cause restrictions of competition. The state aids sector is still unregulated.

The programme will be implemented over a two-year period (2003-2004). Co-ordination with a Regional Flagship Initiative (RFI) developed under the Investment Compact by the OECD over the years 2001-2005 will be actively and effectively sought in order to maximise benefits and avoid duplication of efforts.

Objectives:

- (1) To develop a legal framework in the fields of competition law and state aids which is fully in line with the EU's and establish the necessary conditions for its effective implementation and enforcement.
- (2) To create an independent agency charged with the supervision and the enforcement of state aid rules.
- (3) Strengthening the capacity of the Monopoly Authority;
- (4) To train relevant personnel in involved institutions and legal professions.
- (5) To raise awareness of private business and enterprises on the legal implications of and the means to resort to competition policy.

Expected results: Establishment of an independent authority charged with the supervision, implementation, and the enforcement of state aids rules. X number of state administrators trained in competition-related matters and X number of trainers trained. Public awareness-raising campaign successfully organised and performed; the Monopoly authority enforces competition rules pro-actively and effectively.

Programmes to be implemented: The establishment of an independent authority charged with the supervision and enforcement of state-aid rules will ensure an impartial and rigid implementation. Appropriate technical assistance will be provided for the creation of an Authority which is separate from the existing Monopoly Authority and fully independent.

An effective implementation and enforcement of competition policy requires fully trained personnel in the administration. The focus will lie therefore on adequate, well targeted, extensive and comprehensive training addressing: the members of the Monopoly Authority, judges and lawyers, governmental institutions. Particular emphasis will be laid on training of trainers in order to foster the creation of a self-sustainable system for the development of a comprehensive competition policy.

It is also to be noted that the public seems still to a large extent unaware of the existence and implications of a set of regulations dealing with competition policy. EU assistance will be directed at reinforcing FYR Macedonia's efforts to design an effective raising-awareness campaign through the provision of adequate technical assistance.

Indicators of achievement:

Independent authority charged with the supervision, implementation and enforcement of state aids rules established; the number of competition cases brought before the Monopoly Authority has significantly raised. The public is properly informed about the existence and the implications of a set of competition laws and the role of the relevant institutions.

Public procurement

Background: Public sector works and supplies account for a substantial percentage of economic activity. Transparency and open competition in the sector of public procurement are therefore indispensable elements of a market economy; it also enables industries to make the most of the economies of scale offered by large markets.

In the former Yugoslav Republic of Macedonia the legal framework covering the sector was set through the enactment of the Public Procurement Law which came into force in June 1998 and replacing the previously existing legislation in place since 1996. The law, which underwent some minor amendments in June 2001, is modelled along the lines of the relevant EC Directives and the UNCITRAL Model Law. The scope of the law covers the state budget beneficiaries, municipalities and local government non-budget funds, state-founded institutions and public enterprises.

As early as in the year 2000 an Assessment of the Public Procurement sector in the former Yugoslav Republic of Macedonia was carried out by SIGMA/OECD along the standardised assessment procedure for the needs of the European Commission already carried out in all candidate countries. The general comment/finding of the assessment was that the public procurement field is on the right track and has achieved substantial results. However, it identified areas still to be covered, clarified or strengthened for the purpose of achieving full harmonisation with EU legislation.

The public procurement sector is administered in a decentralised manner and the Ministry of Finance is charged with the supervision of the implementation of the law and of its observance. There is no separate Public Procurement Office for the purpose of the implementation of the law but a department of the Ministry of Finance was entrusted with the responsibility for drafting public procurement legislation, initiating policy changes, advising the contracting sides, interpreting the law, co-ordinating and conducting training activities, monitoring procurement activities and collecting statistics. Plans of creating an independent

Public Procurement Body/Agency within the Ministry of Finance similar to those set up in some eastern European countries exist but the current situation is still one of institutional vacuum which represents a serious constraint on an effective implementation of the law. It also appears that the independence and objectiveness of the decision-making of the second instance appellate body –the Appellate Committee – should be strengthened.

Past assistance under the PHARE 2000 programme addressed several of the shortcomings indicated above; however, the relevance and complexity of the sector suggest that further assistance be devoted to the approximation to EU legislation.

Objectives:

- (1) To promote the establishment of an institutional and legal system for public procurement fully compatible with EU legislation and support the full implementation of the requirements of the SAA in the specific sector.
- (2) Support to the establishment of an autonomous Public Procurement Office charged with supervising the correct implementation and enforcement of the Law on Public Procurement.
- (3) To promote the actual enforcement of the legislation on public procurement.
- (4) To raise awareness of the relevant public (in particular national enterprises) on the content and legal implications of the public procurement system.

Expected results: An independent Public Procurement Office established and its staff adequately trained. An information campaign on public procurement legislation performed. Progressive alignment of the country's legislation with the Community "acquis" on public procurement.

Programmes to be implemented: Appropriate technical assistance will be provided to the Ministry of Finance in order to support the establishment of an autonomous Public Procurement Office. The provision of adequate training to the staff of the Public Procurement Office and to relevant officials charged with ensuring the enforcement of the legislation will promote the correct and effective functioning of the system. A fair and fully functioning set of legislation on public procurement needs to be bolstered by a transparent flow of relevant information and widespread publicity of its rules and implementation mechanisms. An awareness raising campaign informing the relevant public (notably national enterprises) on the content and implications of the legislation on public procurement will be developed and appropriate technical assistance will be provided for the purpose. The provision of trainers' training can be envisaged in order to ensure the self-sustainability of the system and spread the know-how acquired by the Public Procurement Office.

Indicators of achievement: The Independent Public Procurement Office is created and training courses for its staff have been completed; the Office is in the condition to effectively run its day to day business and to transfer its know-how to other bodies involved in public procurement. The effectiveness of the awareness raising campaign is evidenced by an increased number of applicants in call for tenders for the awarding of public works and supply contracts. Increased number of judicial cases on Public Procurement related-matters. Judiciary trained on enforcement aspects of Public Procurement legislation.

Intellectual property rights

Background: The relevance of the sector is recognised in the Stabilisation and Association Agreement according to which the former Yugoslav Republic of Macedonia shall take the necessary measures in order to guarantee no later than five years after the entry into force of the agreement a level of protection of intellectual, industrial and commercial property rights similar to that existing within the Community, including effective means for the enforcement of such rights (Art. 71). For this purpose it is foreseen that the country will accede, within the same time-period, to the relevant multilateral conventions regulating the sector.

Currently the sector is only partially regulated in the former Yugoslav Republic of Macedonia through three different laws: an Act on Industrial Property enacted in 1993, a Law on Protection of Layout Design on Integrated Circuits enacted in 1998 and a Law on Copyright and Related Rights dating back to 1998. According to the Plan for Legislative Activities of the Ministry of Economy three new bills are under preparation: a Law on Patents, a Law on Trademarks and a Law on Industrial Design, all designed to bring about a thorough updating and harmonisation of the country's legislation with international requirements. According to the Plan all acts should be enacted in December 2001, although the troubled political situation in the country may well cause significant delays in the process.

At an administrative level two are the competent institutions currently in place: the Industrial Property Protection Office, an agency within the Ministry of Economy composed of two units dealing with trademarks and patents respectively and the Inspection Service for the Protection of Copyrights belonging to the Ministry of Culture.

European Commission assistance for the development of the sector was provided under the PHARE 2000 programme with the aim of providing legal advice for the amendment of the Law on Protection of Industrial Property Rights, providing training to legal professions and supplying software tools to favour the protection of industrial property rights. In order to promote a full and effective implementation of the Stabilisation and Association Agreement further assistance can be directed to the sector in particular to improve the country's capability to enforce the relevant legislation and promote a higher degree of legal harmonisation with Community rules.

Objectives:

- (1) To promote the establishment of a legislative and institutional framework in the field of industrial and intellectual property rights which is fully compatible with the European Community's.
- (2) To eliminate possible hindrances to free movement of goods and services, favour competition and combat the production of counterfeit goods.
- (3) To promote the gradual harmonisation of national legislation with the Community "acquis";
- (4) To provide assistance for the creation of a specialised court for intellectual property matters;
- (5) To develop effective means for the implementation and enforcement of the relevant legislation;
- (6) To support the Industrial Property Protection Office in the development of efficient and speedy administrative procedures;
- (7) To provide training to and develop an awareness-raising campaign targeting the main users of protected works, on intellectual property requirements and obligations.

Expected results: The legislative and institutional framework in the field of intellectual and industrial property rights will be brought increasingly in line with EC legislation and a special court for intellectual property matters will be set up. Xpolice and customs officers adequately trained on relevant issues concerning intellectual and industrial property rights and on enforcement methods. Enforcement capabilities significantly improved.

Programmes to be implemented: The gradual harmonisation of the national legislation with the Community “acquis” will be promoted through the provision of technical assistance which will be designed to help the process of drafting of new relevant rules. The development of effective enforcement methods will be promoted through the provision of appropriate training to police and customs authorities. The avoidance of irregularities and unnecessary delays in dealing with applications will be dealt with through the provision of assistance to the Industrial Property Protection Office and the Inspection Service for the Protection of Copyrights. In particular, their ability in dealing with applications and the development of efficient administrative procedures will be addressed.

Indicators of achievement: Enactment of a number of legislative acts and specialised court created. Number of infringement cases prosecuted raises significantly as well as the number of fines and jail sentences linked to violations of intellectual and industrial property rights. Number of trademarks and patent applications and number of those in force increased; average time-span between application and registration of patents and trademarks substantially decreased.

6.2.2. Trade

Background: The signature of the SAA and the entry into force of the Interim Agreement on 1 June 2001 including all trade-related matters open significant opportunities for FYR Macedonia while at the same time posing some important challenges to it. In this context it is paramount that the country is able to respect fully the obligations imposed by the Agreement. The former Yugoslav Republic of Macedonia has also applied for WTO membership and is now in the process of negotiating its accession. The process requires important legislative amendments in order to adapt the national legislation to WTO's; while some amendments are underway, additional legislative modifications as well as significant changes in the practices of the institutions dealing with trade-related matters are needed. It is also to be noted that once membership is acquired the proper implementation of WTO rules will require additional efforts on the part of the country.

The removal of tariff barriers and quantitative restrictions to the country's exports to the European Community opens up a major window of opportunity for the former Yugoslav Republic of Macedonia. In order to fully enjoy the potential of benefits that such measures entail the country's products must be up to EC internal market standards. In this framework, it will be necessary to upgrade infrastructure and introduce the relevant legislation in the field of standardisation, technical requirements and conformity assessment, veterinary and phytosanitary controls and bringing legislation in line with international (WTO and EU) requirements thus lending credibility to the system. This is particularly relevant in view of the necessity to negotiate Free Trade Agreements with the other countries of the region as stipulated in the Stability Pact Memorandum of Understanding.

The programme is specifically designed to support the former Yugoslav Republic of Macedonia's efforts to move in this direction and includes three components which taken together constitute an integrated approach to the enhancement of trade:

- a) Reinforcing and developing relevant legislation and institutions involved in facilitating and liberalising trade;
- b) Improving standards for industrial products and agricultural products as well as developing adequate sanitary and phytosanitary controls;
- c) Integrating the country in the international trading system through the provision of the necessary assistance to facilitate its accession to the World Trade Organisation.

Preliminary work has been undertaken in the fields of food, veterinary and phytosanitary controls. Under CARDS 2001, the European Commission is funding a study of the institutional, organisation and equipment needs of food quality control in the country. This will bring together information on the current situation and, in partnership with the government, create a 'roadmap' of the changes necessary to create a food quality control body similar to those that exist in the EU Member States.

The European Commission and the Government have both begun the work on improving the veterinary and phytosanitary control capabilities of the country. The Government has expended significant effort in upgrading the physical structures on the border points for this equipment. In addition to this laboratory equipment, the COP99 includes both equipment and technical assistance to further develop the animal identification system initiated on a trial basis by the Government. The animal ID forms the basis for the concept of 'stable to table' control of food products and takes in both food and veterinary quality control. Further funds in support of this measure have been allocated under CARDS 2001. The assessed needs for equipment have only been 30% met by the support of the European Commission, other donors and the Government, thereby leaving significant opportunities for funding within the MIP. Associated training and information systems will also be required, in conjunction with programmes addressing the needs of Integrated Border Management.

Objectives:

- (1) To improve the ability of Macedonian producers to trade with the EU and regional partners and the progressive integration of the country in the international trading system.
- (2) To assist the country in meeting the challenges that WTO accession imposes on the Government in meeting and implementing the requirements of WTO agreements.
- (3) To assist the country in negotiating and preparing Free Trade Agreements with the countries of the region in accordance with the Stability Pact Memorandum of Understanding.
- (4) To support the development and strengthening of the role of the relevant institutions involved in facilitating and liberalising trade.
- (5) To design and implement the institutional and organisational requirements for a Food Quality Control and Information structure.
- (6) To improve the veterinary and phytosanitary control capabilities of the relevant government ministries and border posts to EU standards.

Expected results: Establishment of the conditions for a full respect of the trade-related provisions of the SAA and of the requirements imposed upon the country by the future WTO accession. Enhanced capacity to trade notably through enhanced operational capabilities of the institutions dealing with trade-related matters and the raising of the quality of national products. Creation of a Food Quality Information network and of a Food Quality Control

Network. Adequate institutional changes carried out. Central and regional food quality laboratories are adequately equipped and equipment for veterinary and phytosanitary control for inspection at border posts is provided. A suitable animal ID system is established.

Programmes to be implemented: WTO accession imposes serious challenges on the government in meeting and implementing the requirements of WTO agreements. Support will be provided through the provision of technical assistance which should be directed to:

- a) Revising and as appropriate introducing new legislation to ensure consistency with WTO agreements;
- b) Strengthening the capacity of the institutions dealing with technical and industrial standards, sanitary and phytosanitary controls;
- c) Strengthening human resources capabilities through the provision of adequate training on all the above-mentioned sectors as well as on the provision of guidance to ensure the compatibility between the design and implementation of the trade policy and WTO accession.

A coherent and comprehensive strategy for the development of the country's trade technical and institutional capabilities. Technical assistance will be needed in order to raise the profile of the reformed institutions and strengthen their role as catalysts for the implementation of the partner country's international commitments and for the promotion of national products.

The review of the Food Quality structures to be completed under the CARDS 2001 programme will be substantially completed by mid 2002, enabling further funds to be targeted in 2003 and 2004 programmes. These will primarily involve equipment, but also specific technical assistance and training.

Veterinary and phytosanitary control capabilities will be strengthened through the training of end users and specific institutional advice to the Ministry. The animal ID programme, significantly funded under COP 99 and CARDS 2001, may require further funding to complete the system nation-wide.

To support and enable the development of the strategy, limited technical assistance and training will be given to improve external trade statistics and statistical data of regional interest.

Indicators of achievement: Improved readiness to implement SAA and WTO rules through the enactment of appropriate legislation and the strengthening of the institutional structure for dealing with trade-related matters. Restructured Chambers of Economy acts more actively to promote national products and to promote the competitiveness of national businesses and especially of SMEs. Increased responsiveness of industrial production to quality and safety standards of the Internal Market. The food quality review is completed and accepted by the Government. The design and implementation of Food Quality Information Network and of Food Quality Control Network (ALERT system) is performed. Equipment for central and regional food quality laboratories is procured. Staff is trained and well capable of undertaking their tasks. Inspection posts on the borders are fully equipped and the staff trained to meet the needs of veterinary and phytosanitary controls. Testing facilities are established as necessary on a regional basis and samples can be quickly processed. Delays due to inspection border posts are minimised and within acceptable levels and control facilities meet the standards of EU inspection teams. The animal ID system covers the national herd and is successfully

implemented and sustainable. The animal ID system is fitted into the food quality control systems to form the basis of 'stable to table' food control policy in accordance with EU practice. The amount of exports from the former Yugoslav Republic of Macedonia to the EU and regional markets rejected for quality or sanitary reasons in evident decrease.

Cross-cutting issues: The assistance provided under this programme complements that being provided to the Justice and Home Affairs sector under the Integrated Border Management Programme. In particular, all interventions in the fields of food quality controls, phytosanitary and veterinary standards reinforce and extend the measures envisaged in the field of customs controls and the strengthening of border controls under the Integrated Border Management programme.

Conditionality: Implementation of the programme is subject to the strict adherence to the rules of the Interim Agreement between the European Community and the former Yugoslav Republic of Macedonia regulating all trade-related matters.

6.2.3. *Development of local infrastructure*

Background: The needs for local infrastructure development in the country are significant and pressing and the limited financial and staffing resources of the municipalities severely limit their capacity to undertake the necessary actions. The CARDS 2001 assistance programme included a programme (€2.5m.) designed to set up a fund for the provision of grant in support of small projects aiming at raising the standards of physical infrastructure facilities in local municipalities and finance a number of start-up projects.

The EC intends to continue supporting the decentralisation process and help local municipalities address their needs for small infrastructure development through the newly created fund over the years 2002-2003. The country has significant needs in terms of infrastructure development, all the more so after the political and military crisis. Projects will be selected for funding throughout the country prioritising areas where needs appear most urgent. Therefore, the funds made available will be channelled towards those municipalities which are more disadvantaged economically as well as those most affected by the 2001 crisis.

Continued support will also be provided to the development of a balanced and effective policy of local self-government in accordance with the requirements of the Framework Agreement.

Objectives:

- (1) To promote small infrastructure development in local municipalities as well as favour local development and the easing of ethnic tensions.
- (2) The programme although focusing on small infrastructure development is two-pronged in its broad objectives:
 - To support investment projects promoted by local municipalities to improve infrastructure facilities.
 - To promote an equitable and balanced development of the country with a particular focus on the most disadvantaged areas.
- (3) To provide technical assistance both to favour the development of infrastructure projects and to support the establishment of an effective decentralisation policy.

Expected results: X small-infrastructure development projects identified, selected and carried out.

Programmes to be implemented: The programme aims at favouring the decentralisation process already underway, contributing to local development and contributing to an equitable allocation of resources among disadvantaged communities. Following the establishment of the fund foreseen in the 2001 CARDS programme and the selection of a series of start-up projects, additional projects will be identified and funded. The most disadvantaged areas will be specifically targeted in order to raise the living conditions of underdeveloped rural areas and promoting the re-establishment of normal conditions in the areas worst hit by the 2001 political and military crisis. Limited technical assistance and training will also be provided to improve the production of reliable statistic regional data.

Indicators of achievement: Number of projects successfully completed; the process of administrative decentralisation has started and local municipalities have increased their ability to assess their needs. Local infrastructure development furthered significantly and living-conditions of the population improved.

Cross-cutting issues: The assistance provided under this programme effectively complements the other programmes in the broad sector of Economic and Social Development as well as those in the sectors of Democracy and the Rule of Law and Justice and Home Affairs. In particular, it will provide employment opportunities in all areas concerned while contributing significantly to the establishment of better living conditions. It has an important indirect effect in that it aims at easing inter-ethnic tensions by promoting the development of the areas of the country where the specific needs are most urgent regardless of the ethnic composition of the population.

Conditionality: Adoption of a Law on Local Self-Government in accordance with the Framework Agreement and creation of the appropriate legal framework for the decentralisation process. .

Other EC instruments: In the aftermath of the 1999 Kosovo crisis as well as of the recent security crisis in the country, ECHO has funded programmes in the field of rural infrastructure (water and sanitation, rehabilitation of primary schools and health facilities) worth a total of € 6.4 million. Complementarity with these programmes will be sought.

6.2.4. *Social cohesion*

Fund for innovation in vocational education and training (VET) through international mobility

Background: Since 1997, the EC has provided a substantial assistance to the former Yugoslav Republic of Macedonia in the reform of vocational education and training, leading to the development of a system based on the life-long learning principles. Assistance has been provided in the revision of curricula, establishment of a national qualification system, teachers training, supply of equipment, partnership, institution building, etc. Both initial and continuing training have been covered by the previous assistance.

Pilot schools and regional centres have been selected for the implementation of the reform process and dialogue between education and of world of work has been strengthened at local level. These schools have become the catalysts for the process of modernisation and change

within a regional and European network, not only limited to vocational training but also to the promotion of democratic citizenship.

Objectives:

- (1) To support the consolidation of VET reform through the implementation of innovative initiatives linked to regional and EU partnership for the promotion of knowledge, aptitude and skills for successful integration into working life.
- (2) To promote mobility of students, workers and unemployed, and innovative pilot projects.
- (3) The above measures, whose maximum ceiling will be defined, will be aimed at:

Improving Employability: tackling youth unemployment, preventing long-term unemployment, transition from passive measures to active employment measures;

Promoting Partnership: social partners agreement to increase the employability, improving the quality of the school system, increasing the skill levels of young people, promoting a labour market open to all;

Stimulating adaptability and entrepreneurship: making it easier to start up and run businesses, promote job creation at local level, making the taxation system more employment friendly, modernising work organisation, up-grading skill levels in enterprises, etc.;

Strengthening the policies for equal opportunities: tackling gender gaps, reconciling work and family, and facilitating reintegration into the labour market.

Promoting the use of new technologies: bringing new communication technologies closer to daily life, making new technologies user friendly, making workers eager to use new technologies.

Expected results: Reinforced international co-operation in the field of VET; VET becomes a catalyst of a broader human resources development policy. The concept and principles of economic and social cohesion accepted and diffused; VET provision in the country is in line with EU standards. The institutional capacity in the sector is reinforced and the provision of VET made more suitable to the needs of the labour market.

Programmes to be implemented: The pilot schools and regional centres established under the previous EC assistance have become resource centres for the local community and additional support needs therefore to be provided in order to build on previous experience and to disseminate the process of reform of VET system to other schools within a context of regional and European dimension. The programme will co-finance grants through open call for proposals submitted by national training institutions. Grants will be provided to students, job seekers or workers willing to improve their career path by attending training courses abroad or carrying out a research on a specific subject under the tutorship of a training institution. The applicant will have clearly to demonstrate that this training will provide the trainees with a better access to employment or that it will be an instrument for career development. Particular priority will be devoted to the training related to technological innovations. The maximum ceiling per each mobility proposal will be established.

The process of reform can be successful and sustainable only if adequate support is provided at institutional level with the full involvement of the officials in charge of the administration and delivery of the system. It is therefore important that key stakeholders of the VET system, social partners, and employers institutions take part in study visits and training in other countries of the region and in the EU Member States. Precise programmes will have to be submitted by the applicant institutions concerning the planned activities, specifying also the

expected objectives and outcomes. As regards teachers, the activities will have to be aimed to introducing innovation in related subjects like, didactics, production of learning packages, curricula revision, use of information technology, assessment and evaluation. School principals will be eligible under the programme for activities focusing on school management.

Finally, pilot actions will cover more complex initiatives aimed at tackling the issue of human resources development within a context of economic and social cohesion, through a transfer of know-how and experience among countries in the region and in the EU at large. Projects focusing on the problem of high rate of unemployment among secondary school leavers, school drop-outs from ethnic minority groups, unequal access to the labour market for people with special needs, re-qualification of the workforce for people laid off by companies, which have been privatised will be financed. Many successful projects have already been financed on those subjects in other countries of the region or in EU, such as the territorial pacts for employment; this fund will therefore allow to transfer the experience in the former Yugoslav Republic of Macedonia.

Indicators of achievement: Higher enrolment rates to VET in the country; more active participation of the social partners to the issue of human resources development. The policy for human resources development is recognised as a top priority by the institution and made part of the national policy for economic and social cohesion. Higher rate of insertion in the labour market of unemployed and better access to career development for workers. Improved access to labour market for people with special needs; access to labour market is provided to ethnic minorities on a more equal basis. Key decision-makers aware of the European dimension in VET.

Cross-cutting issues: The assistance provided under this programme reinforces and extends that being provided to the private and financial sector and to economic development at large. Aligning the vocational education system more closely with the needs of the labour market will support the transition process and will assist the economy to enter global markets. By increasing education levels the programme clearly aims to contribute to promoting human development and reducing levels of poverty.

TEMPUS III

Background: The TEMPUS programme was adopted by the Council of Ministers of the European Union on 7 May 1990. The programme was set up in order to support the process of reform in the countries of Central and Eastern Europe in the area of higher education within the framework of the European Community PHARE programme. On 29 April 1999 a new decision on the TEMPUS programme “TEMPUS III” was adopted by the Council; the programme covers the non-associated countries of Southeast Europe and the Newly Independent States of the former Soviet Union. This new phase of the programme will run from 2000 to 2006. The former Yugoslav Republic of Macedonia became eligible for TEMPUS funding in 1997 and it has so far been allocated funds for a total of € 11.7 million.

Objectives:

- (1) To promote the reform of higher education institutions in view of improving the quality of academic teaching and learning in line with changing political, social and economic needs.
- (2) To increase synergies between higher education institutions at an international level;
- (3) To strengthen management and administrative capacity of higher education institutions taking part in the programme;

- (4) To promote the development of curricula which are more and more in tune with the current needs of employment markets at a national and international level;

Expected results: Increased synergy between higher education legislation and policy and reforms at the institutional level; strengthened strategic management capacities of higher education institutions; modernisation of management and administration of the participating higher education institutions; teaching and learning according to revised curricula and study courses in line with changes social and economic needs; improved skills of non-academic staff relevant for public administration reform and civic society development; increased mobility of students and academic staff; closer co-operation and sharing of resources and experience between higher education institutions at a regional level.

Programmes to be implemented: The programme is implemented through the financing of “Joint European Projects” and “Individual Mobility Grants”. Joint European Projects consist of co-operative activities between the European Union and partner countries’ higher education institutions. They aim to contribute to the long-term development and renewal of the partner countries higher education system and can focus on the following areas: (i) University Management, (ii) Curriculum Development, (iii) Institution Building, (iv) Mobility, (v) Networking Projects, (vi) Regional Projects. JEPs have a maximum duration of either two or three years, and must involve at least one higher education institution from the partner country and at least two institutions from two different EU countries, including at least one higher education institution. Individual Mobility Grants provide an opportunity to individuals to visit other countries for a short period of time (1-8 weeks) with the objective of disseminating the results of TEMPUS projects or networking in a particular area of relevance for the programme.

Indicators of achievement: Number of JEPs successfully implemented and of Individual Mobility Grants granted. Number of applications received and increase on annual basis. Number of new and revised university curricula successfully implemented. Number of students having followed new curricula. Time needed by students having followed new curricula to find employment.

Institution building for employment policy reform

Background: Given the extremely high unemployment rate (32.4%) in the country employment growth and the reduction in the number of job seekers is one of the main goals of the Government in the definition of its policies. The main actors in this field are the Ministry of Labour, the Employment offices (30 all over the country) and the Statistical Offices as regards collection of information on the labour market. Due to limited budget resources but also to a lack of strategic policy, the Employment offices carry out mainly passive employment measures such the payment of the unemployment benefits. Employment Offices also have the task of organising and co-ordinating training courses on the request of employers but due to limited budgetary resources passive employment measures are still their key priority task. In 1999 Employment Offices organised 105 training courses, which involved 2,984 unemployed people, and, after the training, 1,924 people were employed on a permanent basis, out of which 80% were women and 61% were below the age of 30. The employment fund contribution, which covers unemployment benefits and re-training programmes, amounts to 1.5% of gross salary. As a matter of fact, the Ministry of Labour is mainly in charge of

social protection whilst the Employment Offices are responsible for the provision of services related to unemployment and there is no single public national authority in charge of employment policy.

Objectives:

- (1) To assist the Ministry of Labour in the elaboration and adoption of a national employment policy based on the overall mid to long-term development strategy of the country and on the EU's employment pillars. The policy will also include the assessment and restructuring of the employment services.
- (2) Analysis of the effectiveness of the present network of the 30 employment offices, including staff, resources, equipment, organisational structure, geographical distribution, etc. Assessment of the needs for restructuring including timing, resources and objectives of the task;
- (3) Preparation and adoption of a national plan for employment in line with the EU employment policy guidelines and restructuring of the employment services on the basis of the assessment performed.
- (4) Full assessment of the budgetary, institutional and human resources development implications of the national action plan for employment. Priority measures to be taken and a realistic time-scale for implementation will be established. Necessary legislation to support implementation of the NAPE will be identified and drafted.
- (5) Implementation of pilot actions based on the objectives and principles of the national plan for employment, including the implementation of active employment measures (training, entrepreneurial skills development, career counselling, outplacement etc.) introducing a bottom-up approach based on local initiatives.

Expected results: An employment policy in line with European employment strategy is defined and backed by full support of key institutions for its implementation. Institutional dialogue on employment policy established; active employment measures implemented. A legal framework for the implementation of the policy is established.

Programmes to be implemented: The focus of the assistance will be on the provision of technical assistance to the Ministry of Labour, the Employment Offices and other relevant public institutions and social partner networks which will lead to the preparation and adoption of the national action plan for employment and the restructuring of the employment services. Study visits and training will be organised for key stakeholders of the Ministry of Labour, Employment Offices and other public institutions and social partners institutions in the EU in order to promote the exchange of experience and best practice related to employment policy implementation.

Pilot actions based on the objectives and principles of the national plan for employment will be financed through open call for proposals for projects submitted by training institutions, NGOs, private service providers, local communities and others. Applicants will have to demonstrate that their project will promote the employment of the participants.

Indicators of achievement: National employment plan adopted by the Government. X number of unemployed find a job after participating in the active employment measures and X number of unemployed set up their own business after participating in the active employment measures. Employment offices restructured with people trained and new equipment in place.

6.3. Justice and home affairs

6.3.1. Reform of the judiciary

Background: An independent, effective, just and efficient judicial system is an indispensable element for the establishment of a truly democratic system in which the respect for the rule of law is ensured. The modernisation, streamlining and improved efficiency of the court systems are also paramount in order to ensure a high degree of protection of individual rights and therefore increase citizens' faith and confidence in the state. In the former Yugoslav Republic of Macedonia the functioning of the court system is characterised by slow procedures and an inefficient allocation of competencies leading to long delays in the processing of cases. The system is composed of 27 Basic Courts, 3 Appellate Courts, a Supreme Court and a Constitutional Court. No specialised courts currently exist. By July 1996, over 660 judges had been appointed to the bench under the Law on Courts.

The signing of the Stabilisation and Association Agreement will have a positive impact on the improvement of the level of harmonisation of current legislation with EU legislation. Articles 68 and 74 of the SAA attach particular importance to the reinforcement of the law-enforcement institutions and the machinery of justice, and single out the improvement of the effectiveness and training of the legal professions as an area for co-operation. Apart from the need to train judges and prosecutors in performing their functions, it will be necessary to develop the skills of both new and experienced judges and prosecutors as well as those of the associates with respect to new laws, constitutional principles and international agreements signed and ratified by the former Yugoslav Republic of Macedonia.

European Community assistance to the process of reform of the judicial administration started with the PHARE 2000 programme and continued with the CARDS 2001 programme. Being a complex and difficult endeavour whose success is of paramount importance for the overall process of European integration, continued assistance appears necessary over the whole period covered by the MIP. This is all the more evident when the link between an effective judicial system and the respect of human and minority rights is considered.

Objectives:

- (1) To promote an independent and efficient judiciary and support the restructuring of the court system.
- (2) To support the process of adaptation and reorganisation of the judicial system and the streamlining of court procedures;
- (3) To ensure high standards of fairness and due process in judicial decisions taking into account appropriate measures to fight corruption;
- (4) To increase the efficiency of the court administration and assist in the process of computerisation of the courts;

Expected results: X number of government officials working in the court system trained; court procedures are simplified and the performance of the relevant officials significantly improved. The computerisation of the court administration and the streamlined court procedures will accelerate the exchange of data and improve the co-operation between different courts through the automatising of routine reporting and a more efficient workflow. X number of judges and prosecutors trained; this will favour the effective implementation and

enforcement of newly enacted legislation and raise the standards of court decisions ensuring due process and a higher degree of judicial fairness.

Programmes to be implemented: The reorganisation and adaptation of the judicial system will be promoted through the provision of technical assistance designed to streamlining court procedures as well as administrative practices. Officials working in the court system will be adequately trained on the changes made in the national legislation as a consequence of the process of harmonisation of legislation with the Community “acquis”. Training will be provided to legal professions, in particular judges and prosecutors.

Indicators of achievement: A successful implementation of the programme will be mainly visible through the decrease in the backlog of court cases and a reduced number of cases overturned in appeal.

6.3.2. *Integrated Border Management*

Background: An overall integrated border management approach is required in the former Yugoslav Republic of Macedonia to strengthen controls at the border, to facilitate trade across the border and to meet the needs of the regions spanning the border.

This is a necessary but ambitious approach that has clear national policy implications. It is therefore imperative that the country has the time to discuss and develop a coherent national Integrated Border Management strategy in close co-operation with its international partners. To this end, the strategy and programme preparation will be focused on in 2002-2003 with substantive implementation measures taking place in 2003-2004. However, emergency programmes may be addressed earlier where clearly identified. Assistance will follow up on the actions already undertaken under the 2000 PHARE programme and the 2001 CARDS programme. CARDS regional funds will be used to ensure regional co-operation and networking between the national agencies involved in the area of integrated border management.

Co-ordination with the World Bank Transport and Trade Facilitation Programme for South East Europe will be particularly important in the area of trade facilitation and shall be conducted through regular review mechanisms and direct Cupertino. Clear demarcation of activities between the two programmes will be covered within the national integrated border management strategies. This demarcation will respect the lead taken through on-going programmes and will specifically avoid crowding out by CARDS grant funds of TTFSE projects in Croatia, the former Yugoslav Republic of Macedonia, BiH and Albania.

Further details on the CARDS integrated border management approach including an accurate description of its objectives and components are sketched out in the CARDS Regional Strategy Paper.

Objectives:

- (1) To agree on the overall goals and work plan for integrated border management in the former Yugoslav Republic of Macedonia and establish an effective IBM strategy.

- (2) To develop an integrated border management strategy continuing the work undertaken under the 2001 CARDS programme and support the technical preparation of the specific programmes it entails;
- (3) To facilitate the flow of trade with the former Yugoslav Republic's SEE neighbours and with the EU and candidate countries;
- (4) Assistance for the strengthening of customs institutions taking into account appropriate measures to fight corruption;
- (5) To improve infrastructure that may, if necessary and most efficient, be located away within the country far from actual borders (e.g. Centralised information technology systems);
- (6) To establish greater security at international borders that will diminish cross border crime and illegal immigration;
- (7) To promote regional reconciliation and to ease border region tensions, where necessary.

Expected results: An Integrated Border Management Strategy that has been nationally agreed, as well as agreed for issues of common interest with neighbouring countries (e.g. deciding which priority crossings or common customs approaches). Increased levels of regional trade; completion of border crossings as specified and scoped in the national strategy: fully integrated facilities by 2006 at the major border crossings on Pan-European Networks (PEN). Facilities on second priority crossings where agreed by the two neighbouring countries involved and included in the country's border management strategy, although these will be less extensive than those on PENs. Enhanced institutional capacities of key agencies involved, including co-operation with counterpart agencies in neighbouring countries. Effective border security systems integrated with national police systems and demarcation of agreed national borders. Greater levels of economic and social development within problem border regions and greater levels of cross-border co-operation between border regions.

Programmes to be implemented: Support in 2002/2003 to the government for the development of an integrated border management strategy and for the technical preparation of the specific programmes. In general, the strategy process will: (i) detail each country's strategic goals in this area, based on a clear analysis of problems and work already completed; (ii) involve detailed discussions and agreement within an inter-service working group of the involved agencies; (iii) identify strategic priorities, programmes and indicators of achievement; and, (iv) prepare a clear and feasible work plan (including specifying studies, technical specifications and terms of reference to be produced) that will be needed to ensure implementation of the strategy.

CARDS regional funding will be available to ensure regional networking of involved national agencies between the five countries.

Enhancing border controls will involve the provision of equipment and the upgrading and building of infrastructure but, as a conditionality, will be complemented by institution building and technical assistance to ensure coherence, sustainability and the overall effectiveness of the institutions involved.

Considerable work has been done on customs and border crossings in the country which has recently signed a World Bank TTFSE loan. The integrated border management strategy will incorporate this completed and on-going work. The CARDS funding will be used to help implement the strategy, alongside national and other donor and IFI activities, specifically

financing border crossing improvements, institutional strengthening programmes and necessary technical work, including studies and training.

In terms of specific crossings, the following may be addressed under CARDS:

- (1) CARDS support will ensure full facilities are in place by 2006 on the crossings of Pan-European Network VIII linking Skopje with Tirana via Tetovo to the west and to the east to Sofia in Bulgaria. In addition, full facilities must be assured at Tabanovce on Pan European Network X linking Skopje to Nis in FRY. However, these crossings are targeted by the World Bank's Transport and Trade Facilitation Programme (TTFSE) and so may not require additional major inputs from CARDS to meet traffic flow requirements.
- (2) Crossing into Kosovo at Dolno Blace on the E65 linking Skopje with Pristina.
- (3) Crossings into Greece at Medjiteljia and Bogodorica if further improvement is required, noting that these have been a focus of past cross border co-operation programmes.
- (4) Crossing at Novo Selo linking Stip and Strumica to Bulgaria.

In addition to the work on specific border crossings, the Cards Regional Programme will also finance interventions:

- (1) to strengthen the national institutions (primarily customs and veterinary and phytosanitary agencies) involved in processing and handling trade.
- (2) to measure crossing times and identify trade flow problems, and to implement improvements often procedural and technical rather than infrastructural (e.g. co-ordination of closure times at border posts or simultaneous processing by involved agencies).
- (3) to improve infrastructure that may, if necessary and most efficient, be located away within the country far from actual borders (e.g. centralised information technology system).

Indicators of achievement: An Integrated Border Management strategy is produced and agreement is found with neighbouring countries on key issues of common interest. Increased flow of trade with neighbouring countries and with the EU candidate countries. Higher rates of detection of smuggling activities and of seizures of smuggled goods both at border points and inland. Increased efficiency of customs marked by faster processing at border points. Reduced instability at border regions.

6.3.3. (Im)migration and asylum

Background: The Stabilisation and Association Agreement requires that co-operation is established between the EU and the former Yugoslav Republic of Macedonia in the fields of visa, border control, asylum and migration and in order to prevent and control illegal (im)migration. The country has pressing needs to be addressed in order to bring legislation, standards and operational procedures in the above-mentioned fields up to EU and international standards and Community assistance will be addressed to gradually fill the legislative, institutional and infrastructure gaps.

Objectives:

- (1) To strengthen the capacity of the former Yugoslav Republic of Macedonia to formulate and implement an asylum and migration policy which is in line with EU and international standards.

- (2) To draft an asylum and migration strategy which is in line with EU standards and with the major international conventions;
- (3) To align the country's legislative framework to international conventions;
- (4) To develop procedures for the treatment of asylum seekers which are in accordance with international rules and best international practices;
- (5) To promote the effective functioning of the reception capacities for foreigners starting with the Transit Centre for Foreigners;
- (6) To establish a visa regime fully consistent with that of the EU.

Expected results: An asylum and migration strategy which is in line with EU standards and with major international conventions is prepared and a visa regime consistent with that of the EU is introduced. Asylum seekers are dealt with in accordance with international standards and in conformity with best international practices. Staff of relevant institutions is adequately trained and the conditions for the full implementation and enforcement of the system are established.

Programmes to be implemented: The focus of the programme will lie on the provision of technical assistance, training and investment in essential equipment and infrastructure. Community assistance will aim at strengthening the relevant institutional capacity of the country and adequately developing human resources. Training of relevant personnel and appropriate training of legal professions will ensure adequate implementation and enforcement of the new system.

Indicators of achievement: The asylum and migration regime is in line with international standards and EU's policy. The effectiveness of the system can be assessed by comparing the data regarding the number of **foreigners** entering/exiting the territory of the country in a regular way and the number of asylum seekers granted asylum and assisted in accordance with the new legislation. Increased detection rate of illegal **(im)migrants** and of trafficking in human beings. Improvements in bureaucratic and administrative procedures shown by the time necessary to process asylum and visa applications.

6.3.4. *Fight against crime*

Money laundering

Background: In the former Yugoslav Republic of Macedonia a Law Against Money Laundering was adopted on 29 August 2001 and is due to enter in to force on 1 March 2002. Being this a sector regulated completely anew and given the extreme importance that the new law is given effective implementation and strict enforcement, EC assistance assumes particular relevance. It is also important that this assistance be targeted to foster the complex work of creating an articulated and complete anti-money-laundering system in the country at an early stage; postponing action is in fact dangerous since the more action is deferred the more entrenched organised crime can become.

Such a system should envisage measures which can effectively deal with the different phases of the laundering cycle: the 'placement' stage in which the launderer introduces his illegal profits into the financial system, the 'layering' stage when he engages in a series of conversions or movements of the funds to distance them from the source and the 'integration'

phase in which the funds re-enter the legitimate economy. An effective regime aims to increase awareness of the phenomenon and then provide the necessary legal or regulatory tools to authorities charged with combating the problem. It should also bring law enforcement and financial regulatory authorities together with the private sector to enable financial institutions to play a role in dealing with the problem. This means for instance to involve the relevant authorities in establishing financial transaction reporting systems, customer identification, record keeping standards and a means for verifying compliance.

Objectives:

- (1) *To establish* a comprehensive anti-money laundering regime which is largely compatible with European Community's standards and multilateral initiatives in the sector.
- (2) To draft secondary legislation in the field;
- (3) To contribute to the creation of the relevant institutional framework for the effective monitoring, implementation and enforcement of anti-money laundering legislation. In particular, as provided by the requirements set by the Financial Action Task Force on Money Laundering, the creation of a Financial Intelligence Unit (FIU) charged with receiving, analysing and disseminating information on possible laundering activities could be supported;
- (4) To improve the performances and competencies of government officials, managers and employees of financial institutions as well as of members of legal professions;
- (5) To promote international and regional co-operation in the field;
- (6) To increase awareness of the relevant public on the relevance and effects of money laundering in the country.

Expected results: The necessary secondary legislation is drafted, enacted and implemented. The relevant institutional framework is created and a Financial Intelligence Unit is up and running. Xpublic officials, managers of financial institutions, and members of legal professions are trained; some mechanisms to establish an effective co-operation with other countries to improve the exchange of information and the capability to detect illegal activities are developed. An awareness raising campaign is carried out.

Programmes to be implemented: Support will be provided to the drafting of secondary legislation through the provision of technical assistance to the Ministry of Finance. Technical assistance will be provided to support the creation of the appropriate institutional framework designed to monitoring, implementing and enforcing anti-money laundering legislation. Support for the creation of a Financial Intelligence Unit will also be provided in the form of technical assistance and necessary equipment. Adequate training will be delivered to government officials, managers and employees of financial institutions as well as to members of legal professions. Regional and international co-operation in the field will be ensured through the funding of exchanges of key personnel and the organisation of international seminars. Technical assistance will be provided for the development of an awareness raising campaign specifically targeted to the relevant audience and designed to inform the public on the consequences and the scope of the phenomenon in the country.

Indicators of achievement: The number of cases of money laundering detected raises significantly. More effective collaboration between financial institutions and governmental authorities. All personnel trained are capable to perform effectively their tasks. The co-operation with other countries on common work to detect illegal activities has improved.

Police and fight against crime

Background: The former Yugoslav Republic of Macedonia is the crucible of a number of illegal activities ranging from the smuggling of goods, arms and tobacco to the trafficking in human beings and women in particular, to economic crimes of different kind. Police services which act effectively and in the full respect of democratic principles and capable of operating in conformity with international standards are paramount if efforts to quell criminal activities are to produce significant results.

Objectives:

- (1) To contribute to the development of an effective strategy to combat and reduce criminal activities in the former Yugoslav Republic of Macedonia.
- (2) To assist in the development of increased democratic accountability and effectiveness of the police. To promote the development of a national drugs strategy aimed at reducing supply and demand and tackle drugs smuggling.
- (3) To contribute to the process of reform of the police services;
- (4) To improve the accountability and operational effectiveness of police services;
- (5) To promote the implementation and the respect of a code of police conduct;
- (6) To improve co-operation between institutions responsible for the fight against organised crime;
- (7) To draft a comprehensive national drugs strategy;

Expected results: Police firmly subject to civilian control and acting fully in accordance with democratically accountable standards. Police are acting in conformity with the code of conduct. Training facilities are available and operative; a comprehensive drugs strategy is drafted.

Programmes to be implemented: The reform of police services will be supported through the provision of training for all police services; particular emphasis will be laid on respect of human rights in the carrying out of police duties. This will include training on management issues and training tailored to tackling specific typologies of crimes. Technical assistance will be provided in order to support the streamlining of police services. Exchange of police officers will be also promoted as a way of favouring acquaintance with EU's and international standards. Assistance to the development of a comprehensive drugs strategy broadly in line with the European Community's will also be provided.

Indicators of achievement: Increased effectiveness of police services measured by higher rates crime-detection and lower rates of crimes; number of complaints on human rights violations perpetrated in the performance of police operations has decreased. The government has made all necessary preparations for the implementation of the newly drafted drugs strategy

Cross-cutting issues: The assistance provided to Justice and Home Affairs reinforces and extends the support being given to Democracy and Rule of Law and Economic and Social Development. The support provided to the judicial system fosters the rule of law and the respect of human and civil rights. The reform of police services will help easing inter-ethnic tensions. Improved border controls will not only facilitate trade and ensure revenue, but will also enable the State to meet its obligations under international security and policing conventions. Fight against crime will help create a physically and legally secure environment and provide more favourable conditions for foreign investment.

6.4. Environment and natural resources

Background: Support for the protection of environmental resources and the development of a strategy for economic growth which is sustainable and respectful of the environment is a necessary element of the EC assistance strategy. By signing the Stabilisation and Association Agreement the former Yugoslav Republic of Macedonia commits itself to gradually adapting the national environmental legislation to the Community “acquis”. Previous support provided under Phare included projects for the approximation of legislation, provision of equipment, technical assistance for the drafting of the second National Environmental Action Plan and specific feasibility studies and investment proposals. However, there remains a significant need for further development of environmental policy and the strengthening of the institutional capacity of the country for managing and enforcing legislation. The institutional and administrative capacity of national and local governments in the field of environmental policy is weak, environmental civil society does not yet function as in the European Union, air pollution, poor water quality and waste management problems still exist and need to be addressed. The benefits generated by an effective and comprehensive environmental policy have also relevant repercussions of a political nature; pollution knows no boundaries and environmental disputes are a frequent source of regional tension. Preventing environmental dangers by balancing short-term action on immediate problems with longer-term assistance to ensure sustainable environmental protection does therefore contribute significantly to increase regional stability.

European Community assistance is therefore framed within a strategy which couples infrastructure and technical assistance interventions with the necessary legal, institutional and civil society reforms to ensure the establishment of a sustainable policy compatible with the long-term goal of European integration.

The main environmental problems in the country concern surface water quality of rivers, ground water quality, air quality in particular in the city of Skopje, management of waste, environmental monitoring. In addition, the need persists of improving the institutional framework for developing and enforcing environmental policy and regulations.

Objectives:

The definition of the specific objectives of EC assistance is heavily dependent on the priorities and objectives which will be identified by the second National Environmental Action Plan and by the feasibility studies and investment proposals forming part of the 2001 assistance programme. Assistance will be therefore specifically targeted to the effective implementation of the second NEAP in its various components. This will entail:

- (1) To favour the gradual process of harmonisation of the country’s legislation with the European Community’s legal standards and to contribute to the implementation of the second National Action Environmental Plan.
- (2) To promote conditions for sustainable development and improve the country’s environmental management capability and institutional capacity.
- (3) To support the creation of an independent Environmental Agency and an Environmental Inspectorate;
- (4) To draft studies for the preparation of a national plan for soil-pollution monitoring;

- (5) To provide assistance to the Ministry of Environment in the process of gradual approximation of legislation with the European Community “acquis”:
- (6) Investment works - subject to a satisfactory outcome of the feasibility studies and investment proposals on solid waste management envisaged under the 2001 CARDS programme, some funding will be provided for their implementation.

Expected results: National plan for soil-pollution monitoring prepared and ready for implementation. Establishment of an independent Environment Agency and an Inspectorate and provision of adequate training to the staff of the newly created institutions. Process of approximation of national legislation with the Community “acquis” gradually advancing.

Programmes to be implemented: Support to the creation of an independent Environmental Agency will be provided through technical assistance with the aim of setting up an independent authority capable of effectively monitoring abidance with environmental legislation. The provision of training to the staff of the newly created agency and to the environmental inspectors will ensure that the institutions will function in accordance with high standards of performance. Technical assistance will be provided to the Ministry of Environment and Physical Planning to support the process of harmonisation of the national environmental legislation with the Community “acquis”. The assistance will be aimed to analyse existing legislation and drafting new legislative texts. Assistance will also be provided to support the drafting of studies for the preparation of a national plan for soil-pollution monitoring which will then be prepared by the end of the programme. The programme will also fund some investment works on the basis of the outcome of the feasibility studies and investment proposals on solid waste management envisaged under the 2001 CARDS programme.

Indicators of achievement: National plan for soil-pollution monitoring approved. The independent Environment Agency and the Environmental Inspectorate are in the condition to perform adequately their functions. Increased rate of detection of violations of infringements of environmental legislation and increased awareness of environmental issues on the part of businesses and the public at large. A number of legislative changes in line with European Community’s environmental rules are performed.

Conditionality: The provision of technical assistance for the creation of an independent Environmental Agency and Inspectorate is subject to the adoption of the legislation enabling the creation and functioning of those bodies.

ANNEXES TO THE CSP AND THE MIP

ANNEX 1: Map of the former Yugoslav Republic of Macedonia

ANNEX 2: MIP – Allocation of resources

ANNEX 3: Other donors' activities

ANNEX 4: EC past assistance and lessons learned

ANNEX 5: CARDS programme 2001

ANNEX 6: 2001 Emergency assistance to FYROM

ANNEX 7: List of abbreviations used

ANNEX 1



ANNEX 2

**NATIONAL INDICATIVE PROGRAMME
FORMER YUGOSLAV REPUBLIC OF
MACEDONIA 2002-2004**

	2002	2003	2004	Total
I. DEMOCRACY AND RULE OF LAW				9
1.1 Inter-ethnic relations and civil society	3	3	3	9

II. ECONOMIC AND SOCIAL DEVELOPMENT				70
2.1 Private and financial sector (including approximation to Intern. Market)	2	4	4.5	10.5
2.2 Trade	4	5	5	14
2.3 Development of local infrastructure	14	8	8.5	30.5
2.4 Social cohesion	2.5	1	2.5	6
2.5 TEMPUS	3	3	3	9

III. JUSTICE AND HOME AFFAIRS				33
3.1 Reform of the judiciary	0	2.5	1.5	4
3.2 Integrated Border Management (Regional funding)	4	6	10	20
3.3 Immigration and asylum	2	1	1	4
3.4 Fight against crime	1	3	1	5

IV. ENVIRONMENT AND NATURAL RESOURCES				4
4.1 Environment	0	2	2	4

V RUNNING COSTS EAR³	4	5	3.5	12.5
VI RESERVE⁴	2			2
TOTAL ALLOCATION	41.5	43.5	45.5	130.5

N.B. The indicative allocation available to the former Yugoslav Republic of Macedonia between 2002 and 2004 is € 110.5 million , plus € 20 million from the regional programme which is being implemented nationally

³ Amounts for the years 2002 and 2003 include the costs of taking over management of ongoing 1996-2001 projects and Programme, totalling more than 110 million €

⁴ First call on € 1 m. in the reserve will be any need for additional running costs of the EAR in 2002

ANNEX 3 – OTHER DONOR ACTIVITY

Sectors		a) EU Donors			b) Other Donors										Total a+b	Percentage of Total a+b					
		EC	EU ms (*)	EU+ EUMs	EIB	EBRD	USA	UND P	IFAD	WH O	World Bank	Taiwan	Swiss	Total		EC	EUMS	EC+ EUMS	Other Donors		
1	Financial Sector	6,79	5,73	12,52	-	-	n/a	-	-	-	-	-	-	-	-	-	12,52	54%	46%	100%	0%
2	Private Sector and SME Development	16,20	41,59	57,79	-	17,40	n/a	-	-	-	n/a	25,43	0,79	43,62			101,41	16%	41%	57%	43%
3	Legal Sector	4,32	1,94	6,26	-	-	0,23	-	-	-	-	-	-	0,23			6,49	67%	30%	96%	4%
4	Public Administration Reform	12,70	1,55	14,25	-	-	-	-	-	-	-	-	-	-			14,25	89%	11%	100%	0%
5	Justice and Home Affairs	4,35	0,79	5,14	-	-	n/a	-	-	-	-	-	-	-			5,14	85%	15%	100%	0%
6	Local Self-Government	2,00	n/a	2,00	-	-	n/a	0,91	-	-	-	-	n/a	0,91			2,91	69%	n/a	69%	31%
7	Democracy, HR and Civil Society	1,72	11,18	12,90	-	-	n/a	-	-	-	-	-	n/a	-			12,90	13%	87%	100%	0%
8	Education	15,60	6,28	21,88	-	-	-	-	-	-	5,78	-	n/a	5,78			27,66	56%	23%	79%	21%
9	Culture	1,64	n/a	1,64	-	-	n/a	-	-	-	5,78	-	-	5,78			7,42	22%	n/a	22%	78%
10	Social Sector	2,00	9,14	11,14	-	-	n/a	-	-	-	53,29	-	-	53,29			64,43	3%	14%	17%	83%
11	Health	0,00	4,33	4,33	-	-	-	-	-	n/a	19,54	-	-	19,54			23,87	0%	18%	18%	82%
12	Agriculture	3,90	22,38	26,28	-	-	0,77	-	-	-	38,03	-	-	38,80			65,08	6%	34%	40%	60%
13	Environment and Water Sector	7,60	52,43	60,03	-	-	1,56	1,77	11,57	-	2,77	-	2,45	20,12			80,15	9%	65%	75%	25%
14	Transport	13,60	1,53	15,13	117,00	-	-	-	-	-	94,22	-	-	211,22			226,35	6%	1%	7%	93%
15	Border Crossings & Other Infrastr.	35,20	-	35,20	-	-	1,16	-	-	-	3,47	-	-	4,62			39,82	88%	0%	88%	12%
16	Assistance to the State Budget	165,00	18,54	183,54	-	-	8,44	14,10	-	-	-	2,31	2,64	27,50			211,04	78%	9%	87%	13%
17	Humanitarian Aid (**)	110,70	6,07	116,77	-	-	-	-	-	-	-	-	-	-			116,77	95%	5%	100%	0%
	Total:	403,32	186,92	470,04	117,00	17,40	12,16	16,78	11,57	-	222,89	27,74	5,88	431,42			901,45	45%	21%	52%	48%

Source: Information from EU member state embassies and donors as of December 2000. The data should be considered as indicative only since it was not possible to harmonise the reference period and to obtain complete data from all sources.

(*) - British bilateral aid of total MEUR 9.5 is not specified per sector

(**) - The Column EC includes the Critical Aid Programmes 1992/93, 1994 and 1995.

USA - bilateral co-operation and USAID - funding data is often not available

ANNEX 4

LESSONS LEARNED FROM PAST EC SUPPORT

Introduction

An independent evaluation of all past EC support to the former Yugoslav Republic of Macedonia was undertaken in 2000-2001. Along with monitoring and assessment reports on on-going programmes, this evaluation has been a key input in developing and focusing the CARDS Country Strategy Paper for the former Yugoslav Republic of Macedonia 2002-2006.

The evaluation has identified valuable lessons from past programmes and presents clear recommendations on ways that EC support can be improved in the future. The majority of its recommendations are being acted upon through the programming strategy and also through reforms to the approach on implementation of programmes in the former Yugoslav Republic of Macedonia.

However, only continued effort down stream – in the annual programming exercise, the implementation and the monitoring and evaluation – will ensure that the recommendations are acted upon and that future CARDS support is made more efficient and impact.

Lessons learned

A lack of strategy documents in the 1990's undermined the focus and direction of the EC programme. The annual programmes include little in the way of strategic analysis. Programming largely took place in headquarters, with relatively little consultation with other stakeholders.

The programmes need to ensure greater government ownership and take into account limited implementation and absorption capacity of the government.

Programmes are complex and rely heavily on the provision of equipment and hardware, even in the absence of a well-defined institutional framework. This undermines impact.

Recent programmes contribute to support national reconciliation (e.g. support to the Census and to the Implementation of the Law of Higher Education and the SEE University of Tetovo).

The shift to projects directly related to formal aspects of EU integration priorities and to the SAA rather than more general and basic institutional building efforts may lead to gaps of necessary support in certain areas.

Support for overall public administration has been at times over ambitious and insufficient account was taken of government commitment or key crosscutting issues (e.g. pay reform, politicisation of the civil service, etc).

Support to Vocational Education Training has contributed in reforming secondary vocational education and establishing partnerships at regional and EU level.

The large Cross Border Crossing programme has been unsatisfactory due to poor design and substantial delays.

The limited support in the area of democracy (e.g. support of the Census, SEE university in Tetovo and funds to deliver rapid rebuilding of areas affected by recent fighting) support the process of national reconciliation and have contributed to the stability of the country and the region.

To date, except in periods of serious crises, donor co-ordination has been weak and needs to be strengthened.

There are notable inefficiencies in implementation, leading to delays.

Recommendations and EC response

As can be seen, the principle recommendations arising from these lessons learned have indeed been integrated into the Country Strategy Paper. Obviously however, the detailed recommendations will be very useful in the annual Action Plans when designing specific programmes.

Recommendation: The report recommends that a programming strategy is required. *Response:* The Commission has produced the Country Strategy Paper to 2006.

Recommendation: The strategy should focus on support to comprehensive civil service reform, to civil society organisations, sustainable development and ethnic reconciliation. Support to the SME sector and the PIP process should be discontinued. *Response:* These are indeed core priorities within the strategy. The strategy also takes on board that support to the implementation of the Stability and Association Agreement should be gradual, reflecting the capacities and position of the former Yugoslav Republic of Macedonia at present. The support to SME and PIP has been reduced.

Recommendation: Programmes should be focused and not only ambitious. *Response:* The strategy has produced focus on limited areas, but also recognised that absorption capacity means concentrating excessively is not possible (nor desirable). The need to ensure projects are feasible and not only ambitious will be ensured through the annual programming exercise.

Recommendation: there should be systematic and transparent consultation. *Response:* The Strategy Paper is being consulted on extensively and the annual action plans – i.e. detailed programming levels – will ensure coordination and involvement, so helping commitment and feasibility.

Recommendation: More support to civil society. *Response:* This plays a central role in the strategy - to strengthen civil society and to promote national and ethnic reconciliation.

Recommendation: greater investment of resources in co-ordination. *Response:* the Commission's emphasis on co-ordination, especially locally, are expanding, following Council conclusions on this matter.

Recommendation: improve implementation efficiency and timing. *Response:* the approach on implementation is being revisited for the former Yugoslav Republic of Macedonia for exactly

these reasons – and a proposal for managing former Yugoslav Republic of Macedonia programmes from the European Agency for Reconstruction is being considered.

Overall Figures for EC Assistance Programmes - to the former Yugoslav Republic of Macedonia 1992 2000⁵

	<u>Commitments</u>
Humanitarian Aid (ECHO)	96.320.000
1) Critical Aid*	84.010.395
2) General assistance	
a) Economic reform*	17.639.774
b) Agriculture and environment	10.500.000
c) Infrastructure and cross border co-operation	54.600.000
d) Social sector (including education and culture)*	18.441.185
e) Institution building (including statistics)*	28.619.041
3) EIB Interest Rate Subsidies	20.000.000
4) Budgetary assistance (impact of refugees)*	25.000.000
Sub-Total assistance programmes	355.130.195
Macro Financial Support***	120.000.000
Total	475.130.195

*1) Aid given to the former Yugoslav Republic of Macedonia before it received funds from Community funds from the Community PHARE programmes for Central and Eastern Europe.

2)

a) Reform of the banking sector and support to SMEs.

d) Reform of vocational education and training, participation in TEMPUS higher education programme, social sector and culture. This also includes assistance to the South Eastern Europe University in Tetovo.

e) Reform of justice and home affairs, local government, public administration and statistics.

4) Exceptional measure to help the former Yugoslav Republic of Macedonia in coping with refugees from Kosovo.

** These are approximate payment figures. Humanitarian aid payments generally are very close to contracting figures since aid is delivered immediately.

*** Macro financial Support has been provided in 1997 in the form of a loan facility (40 million) subject economic conditions and a second support package has been agreed in 1999 (80 million) of which 20 million in grants and 10 million have been paid out so far, further payments to the former Yugoslav Republic of Macedonia complying with the conditions of its agreement with IMF.

⁵ The table does not include the CARDS 2001 assistance programme for which an allocation of €42.5m. was made.

ANNEX 5

**Former Yugoslav Republic of Macedonia
CARDS Programme 2001**

Sectors and Priorities	Budget	Description
1. <u>Justice and Home Affairs</u>	11.5	
1.1 Training of the Judiciary	2.5.	1.1 - Vocational training of Judges and Prosecutors - Assessment of the enforcement system
1.2 Integrated Border Management	5 ⁶	1.2. - Border demarcation with FRY and FRY/Kosovo - Integrated communications network for BCPs - Integrated border management strategy - Strengthening of control at 'Green Border'
1.3. Customs Administration	4	1.3. - Development of secondary legislation - Strengthening of customs administration
2. <u>European Integration</u>	10	
2.1 Environment	3.25	2.1. - Preparation of NEAP - Solid waste feasibility studies - Air quality monitoring stations
2.2 Agriculture	3	2.2 -Veterinary and phytosanitary control - Extension of animal identification systems
2.3 Support to Economic Reforms	3.75	2.3. - Support in preparation of a National Economic Development Programme - Support to the Institute for Norms and Standardisation - Policy advise to Ministry of Economy
3. <u>Infrastructure development</u>	13.5	
3.1 Transport	11	3.1 - Finalising the upgrading of the E75 road (Corridor X), section Negotino – Demir Kapija (Phase III) 3.2 – Small scale infrastructure Fund
3.2. Small Infrastructure for Local Governments	2.5	
4. <u>Education</u>	7	
4.1 TEMPUS	3	4.1. - Higher education
4.2 SEE University	4	4.2. - Support for establishment of the SEE University
5. <u>Small Scale Operations Fund</u>	0.5	
5.1 Small Project Fund Managed by the EC Delegation		5.1 – Funding of small scale operations to finance small projects (less than €50 000)
TOTAL	42.5	

⁶ These € 5 Million are part of the Regional Programme for "Integrated Border Management".

ANNEX 6

2001 Emergency Assistance to the former Yugoslav Republic of Macedonia

Financial Instrument	Sectors and priorities	Budget (million €)
Rapid Reaction Mechanism (RRM, Commission Decision 4 May 2001)	- Housing Reconstruction	2.5
Rapid Reaction Mechanism (RRM, Commission Decision 3 October 2001)	- Repair and Reconstruction of Local Infrastructure - Confidence Building Measures: <u>Strengthening of Civil Society;</u> <u>De-mining;</u> <u>High Level Policy Support;</u> <u>Support to the Reform of the Police and other JHA-related aspects;</u>	10.3
CARDS Additional Assistance Package	- Repair and Reconstruction of Housing and Local Infrastructure - Support to Families Hosting Internally Displaced Persons - Support to the Reform of the Police and other JHA-related aspects.	13.7
Humanitarian Assistance (Commission Decisions of 29 January, 3 May, 11 September, 20 November 2001)	- Food assistance to IDPs, vulnerable local population, refugees (residual caseload from Kosovo crisis) - Non food items (hygiene parcels, animal feed for livestock) for IDPs and host families; - Water and sanitation/emergency rehabilitation; - Community services - Health and social	5.4

ANNEX 7

ACRONYMS

CARDS	Community Assistance for Reconstruction Development and Stabilisation
CBC	Cross Border Co-operation
COP	Country Operational Programme
CSP	Country Strategy Paper
DFID	Department for International Development
DM	Deutsche Mark
DPA	Democratic Party of Albanians
EBRD	European Bank for Reconstruction and Development
EC	European Community
EIB	European Investment Bank
EIO	European Integration Office
EU	European Union
FA	Framework Agreement
FTA	Free Trade Agreement
GDP	Gross Domestic Product
GNP	Gross National Product
IA	Interim Agreement
IFIs	International Financial Institutions
IMF	International Monetary Fund
IPRSP	Interim Poverty Reduction Strategy Paper
MIP	Multi-annual indicative Programme
NDP	National Democratic Party
NEAP	National Environmental Action Plan
NGOs	Non-Governmental Organisations
NLA	National Liberation Army
OBNOVA	EC Emergency Support Programme for the Western Balkans
PHARE	Assistance Programme for central Europe
PDP	Party for Democratic Prosperity
SAA	Stabilisation and Association Agreement
SAP	Stabilisation and Association Process
SDSM	Social Democratic Alliance for Macedonia
SME	Small and Medium Enterprise
TTFSE	World Bank Transport and Trade Facilitation Programme for South East Europe
UNDP	United Nations Development Programme
UNHCR	United Nations High Commission for Refugees
US	United States
USAID	United States Agency for International Development
VAT	Value Added Tax
VMRO-DPMNE	Internal Macedonian Revolutionary Organisation-Democratic Party for Macedonian National Unity
WTO	World Trade Organisation