Republic of Macedonia

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Mood stays buoyant in spite of ethnic stress

Nation status: a young country, Macedonia is building monuments and statues to shape its heritage and create jobs Reuters

EU membership eludes Macedonia but it has raced up the World Bank's annual global survey on 'ease of doing business', reports *Kerin Hope*

At 9am on a hot summer Sunday a triple line of cars, trucks and gleaming tourist coaches stretches several kilometres back from the Gevgelija crossing point between the republic of Macedonia and its southern neighbour Greece.

It takes more than two hours for the daily Skopje-Thessaloniki bus, the only regular transport link between the two countries, to nudge its way past two sets of controls and enter Greece through its own prefecture of central Macedonia.

Dimitar, a 20-year-old engineering student from Skopje aboard the bus, is texting friends in Platamonas, an Aegean seaside resort popular with tourists from the Balkans and central Europe.

"They've found a job for me in a café, with luck I'll be making €50 a day with tips."

Macedonians and Greeks have little trouble keeping bilateral relations ticking over despite the diplomatic obstacles raised by a 22-year-old dispute over the former Yugoslav republic's name, which Greece sees as implying a claim on its own region of Macedonia. The neighbouring state is known officially in Athens as "Fyrom" (Former Yugoslav Republic of Macedonia). Most Greeks simply call it "Skopje".

Two-thirds of landlocked Macedonia's trade moves though Thessaloniki port, according to EU statistics. The country's main infrastructure priority is to complete a €220m upgrade of the highway to Gevgelija, with co-financing from the European Bank for Reconstruction and Development and the European Investment Bank. Greece is Macedonia's fourth-largest investor, accounting for about 10 per cent of total inflows of foreign direct investment since independence in 1991.

An estimated 400,000 Macedonians will take cheap sun-and-sea holidays in Greece this year. Another 800,000 will make weekend trips or visit Thessaloniki for a day's shopping, says an official at SETE, a Greek private sector tourism organisation.

Athens still blocks Macedonia's membership of Nato and the start of negotiations for EU accession because of the name dispute, even though its neighbour was deemed to have fulfilled all the criteria for joining Nato in 2008. It would have begun EU accession talks the following year were it not for the Greek veto.

> The dispute with Greece about the country's name still sours official relations

"In my opinion, Greece will not take steps to resolve the issue without pressure from the world's strongest countries," says Nikola Gruevski, Macedonia's prime minister.

"I understand they have problems because of their financial crisis, but I think they are using this as an excuse to avoid a dialogue with us and not find a solution."

A Greek government official shrugs off the criticism, pointing to the Skopje 2014 heritage project, which features a 30.5m-high equestrian statue – generally accepted as modelled on Alexander the Great, the ancient Greek warrior king – in the capital's main square, as an example of inflexibility on the Macedonian side. "It is hard not to see in this a deliberately provocative usurping of Greek identity, history and culture."

The Athens government recently brushed aside another effort by Mr Gruevski to intensify bilateral negotiations under UN auspices on an amended name, saying the arrangement of intermittent meetings should continue unchanged. Politicians on both sides tout "Upper Macedonia", which would satisfy Greece's insistence on a geographical qualifier, as a possible eventual compromise.

Ali Ahmeti, leader of the largest

Continued on Page 2

Inside »

Old rivals get to know each other in quest for stability

Politics The ruling coalition has proved itself unexpectedly durable, writes *Kerin Hope*

Even after seven uninterrupted years in power, premier Nikola Gruevski's Internal Macedonian Revolutionary Movement-Democratic Party for the Renewal of Macedonia holds a strong appeal for voters.

The right-of-centre VMRO-DPMNE and its coalition partner, the Democratic Union for Integration (DUI) – the largest ethnic Albanian political party – won an unprecedented 72 out of 84 mayoral races across the country at local elections in March.

Compared with previous elections, marked by violent incidents between the Macedonian majority and Albanian minority and accusations of ballot-rigging, the poll was fair and the best-managed since Macedonia declared independence from the collapsing Yugoslav federation in 1991, according to foreign observers.

Yet only two months earlier political tension had been running high. Lawmakers from the main opposition Social Democratic Union for Macedonia (SDMS) were ejected from parliament while a brawl over the 2013 budget raged outside the building.

It took an EU emergency mission to Skopje, led by Stefan Füle, the enlargement commissioner, to restore stability by persuading Branko Crvenkovski, the Social Democrat leader and a former prime minister, to return to parliament and drop a threat to boycott the local elections.

The crisis in the Social Democrat party played out at the polls, with voters deserting in droves. The party elected only four mayors, leaving Mr Crvenkovski with little option but to resign. Zoran Zaev, a 38-year-old businessman and mayor of Strumica in southern Macedonia, was chosen as leader at a party congress in June.

Observers monitoring the local government vote on behalf of the Organisation for Security and Co-operation in Europe (OSCE) found few irregularities on polling day, but noted "a blurring of state and party activities" during the campaign that gave a boost to candidates from the coalition parties.

"The public broadcaster and most private broadcasters displayed significant bias in favour of the governing parties," the report says, echoing concerns about freedom of expression repeatedly voiced by non-governmental organisations and international media watchdogs.

Macedonia fell 22 places this year to 116th out of 179 nations in an annual press freedom index published by Reporters Without Borders. Macedonian journalists complain of political pressure and intimidation which has resulted in increasing self-censorship.

Mr Zaev, elected in March to a third straight term in Strumica, says the opposition struggles to get across its political message.

"The government now controls all the media whether print or electronic. They are the biggest advertisers, so they can exert pressure," he says.

With a fresh-faced new leader in place, the Social Democrats are hopeful of making a comeback after a long period of infighting by senior party cadres whose political careers began under communism.

Yet it may be hard for the opposition to trump VMRO's mix of nationalist rhetoric and pragmatic policies ensuring subsidies for farmers, generous social handouts at election time and a trickle of new jobs provided mainly by foreign investors.

Macedonia is not due to hold a general election until 2015, but based on past form, Mr Gruevski may call a snap poll next year. Despite leading VMRO-DPMNE to victory at three successive elections, he has not served a full term in office.

While the VMRO is just short of an outright majority in the 123-seat parliament with 56 seats, it has governed effectively for the past five years in coalition with DUI, which holds 15 seats.

The coalition with DUI has proved unexpectedly durable, given that Mr Gruevski used to co-operate with its arch-rival, the Democratic Party of Albanians, a traditional VMRO ally.

It helps that DUI politicians have a substantial share of power with five out of 14 cabinet posts, including the defence and economy portfolios, and deputy ministers in the remaining ministries. Ali Ahmeti, the DUI leader and former rebel chieftain during a six-month insurgency in 2001, says: "Previously we (the two ethnic communities) did not have the possibility to know each other, now it is a very different situation."

Differences persist over the implementation of the Ohrid peace agreement brokered by Nato and the EU in 2001. The deal set a framework for Macedonian and Albanian coexistence in a multi-ethnic state in which minority rights would be guaranteed.

DUI lawmakers complain, for example, that a provision for Albanian to be used as an official language in areas where ethnic Albanians make up more than 20 per cent of the population has largely been ignored by Macedonian politicians. VMRO officials counter that Albanian politicians focus too much on their own community's concerns at the expense of broader national concerns.

Mr Ahmeti dismisses such criticism, insisting that DUI fully backs Macedonia's bid for Euro-Atlantic and European integration.

Demonstrable differences: Branko Crvenkovski, the Social Democrat leader (left), caught up in protests over the 2013 budget Reuters

Frustration rules during wait for seat at EU table

Opinion
Tony Barber

Enlargement of the European Union holds out the promise of peace, democracy and prosperity for countries once ravaged by war, dictatorship and poverty. The prospect of EU membership serves to tame rival nationalisms and calm border quarrels among neighbours.

Such is the theory – but Macedonia, the former Yugoslav republic, faces a stern test. In whichever direction the young state looks, it has problems with neighbours, especially Bulgaria, Greece and Serbia. Partly for this reason Macedonia is a somewhat immature and insecure democracy, not a confident and recognisably law-based state. It is economically underdeveloped, and sorely in need of jobs and foreign investment.

It would be naive to think that easy solutions to these problems are within reach. For their roots are to be found in the bitterly contested nature of modern Macedonian national and geographical identity. Nowhere in Europe – not in Northern Ireland, not in the Hungarian-populated lands of central Europe, not among ethnic Russians in Estonia, Latvia and Ukraine – is the question of identity as vexed.

The Macedonian question is both cause and effect of a profound tension among states, churches and peoples that has agitated the Balkans since the late 19th century.

For a long time neither Bulgarians nor Serbs accepted the existence of a distinct Slav Macedonian people, each preferring to view them as components of the Bulgarian and Serbian nations. Both Bulgaria and Serbia did, at least, grant Macedonia official recognition within its present borders after it declared independence from communist Yugoslavia in 1991. Yet disputes persist: the size, national consciousness and political status of a Macedonian minority in Bulgaria; a Bulgarian minority in Macedonia; and the refusal of Serbia's Orthodox Church to recognise the autocephaly of the Macedonian Orthodox Church, which seceded from its Serbian parent in 1967.

As for Greece, it chose to regard Macedonia's proclamation of independence as the first step to a territorial claim on a province of northern Greece that also is called Macedonia. By refusing to recognise the former Yugoslav republic under the name of Macedonia, Greece has blocked the new state's path to EU and Nato membership – even though the EU accepted Macedonia as an official candidate in 2005.

As if these troubles were not enough, Macedonia's politics are shaped by the fact that a quarter of its 2.1m people are ethnic Albanians, concentrated in north-western regions that border Albania and Albanian-majority Kosovo. Intense fighting in 2001 between Macedonian forces and ethnic Albanian insurgents almost led to a civil war. Political tensions, bursting at times into street violence, persist.

Since parliamentary elections in 2008, the country's leaders have given full vent to their frustrations. Blocked from joining the EU and Nato, and unable or unwilling to find a lasting political settlement with the ethnic Albanians, the nationalists who dominate the political stage decided five years ago to refashion their state, turning it into one that glorifies Slav Macedonian identity rather than find space for citizens of all ethnic origins.

This is above all the work of Nikola Gruevski, prime minister since 2006, and it runs counter to every liberal principle the EU purports to uphold. EU leaders responded at a June summit in Brussels by not bothering even to consider a date for opening formal membership talks with Macedonia. This is not to say that the wider Balkan region of which Macedonia forms part is incapable of making political, diplomatic and economic progress. Historically plagued by foreign oppression, economic backwardness, weak public institutions, ethnic hostilities and civil war, the region is edging closer to a European norm.

> Politics are shaped by the fact that 25% of the country's 2.1m people are ethnic Albanians

On July 1 Croatia became the EU's 28th member state, the second former Yugoslav republic after Slovenia to do so. Serbia will begin EU membership talks next year, and Kosovo, a former Serbian province that declared its independence in 2008, is to negotiate an association agreement that will be a milestone on the road to EU entry. The EU opened its arms to Serbia and Kosovo, wartime foes, as recently as 1998-99. They reached an accord in April this year on the status of the ethnic Serb majority of northern Kosovo.

The trouble is that these welcome trends will not, for the foreseeable future, include Macedonia. Its level of democracy and the rule of law do not meet EU standards, either in terms of the independence of the judiciary, government efforts to combat corruption or the official treatment of minorities. These shortcomings provide cover for Greece to maintain its diplomatic quarantine of Macedonia, and for other EU nations lukewarm on enlargement to keep Macedonia waiting at the entrance door. Macedonia finds itself in a European impasse. If there is a way out, it lies through reconciliation with neighbours and a less exclusively nationalist state at home.

Subsidies and friendly locals woo visitors

Tourism

Low-cost holidays hold out prospect of double-digit growth, writes *Kester Eddy*

Tim Bloom is quite candid as to why he and his girlfriend chose Macedonia for their holidays last year.

"First and foremost, it was down to cost. We chose the trip, since it was kind of cheap at €299 and another €99 for a four-day excursion package," says Mr Bloom, 28, a demolition project manager from The Hague, in the Netherlands.

The couple, who spent a week at Lake Ohrid, on Macedonia's southwestern border, say English language skills are sometimes lacking, and the hotel had been overfloridly described – but they found the country "offers a lot to suit different tastes".

Cheap and cheerful perhaps, but the couple did come back last month for a repeat stay, although at a different hotel.

News of returning visitors is music to the ears of Jordan Trajkov, director of the national tourism agency.

He says tourism is a priority sector, with much untapped potential. "Macedonia is a small country, but with so much to offer, from culture and history to nature and wine.

"We are targeting double-digit growth in tourism, and the figures so far this year show that this is feasible."

Last year, Macedonia hosted 350,000 foreign tourists, who spent 810,000 guest nights – a 7 per cent rise on 2011 – according to the state statistical office.

Such numbers may appear small compared with its neighbours. At the other end of the Balkans, Slovenia, for example, attracted 3.3m tourists and 9.5m guest nights last year.

Nonetheless, they represent a threefold jump on the figures from just a decade previously. Even at such modest levels, tourism creates about 3 per cent of GDP and employs some 16,500 people in an economy desperate for jobs.

Turks top the visitor charts, with 50,000 or 14 per cent of all tourists arriving last year.

Yet visitors from the Netherlands, who numbered only 27,000 (a little under 8 per cent of arrivals), made a greater impact. With the majority on package tours and staying a week or more, they made up 43 per cent of foreign guest nights in 2012.

The Dutch influx is the direct result of the government subsidising organised tours from 2009, says Doncho Tanevski, president of the Macedonian Hotels Association.

"Croatia subsidised tour operators to build up their tourist industry. I took that model to our prime minister, with a plan that showed the proposed subsidies would be paid back by the end of August through extra tourist spending. After that, everything would be a gain for the government," he says.

The subsidy – which for charter flights from Europe varies between €25 and €65 a passenger, depending on country of origin – combined with discounted rates of just €30 for a double room in a four-star hotel, makes package holidays at Ohrid outstanding value, Mr Tanevski says.

"I negotiated this deal with one Dutch tour operator, and we got three flights a week. Soon another signed a deal for two flights a week. The planes are not always full, but they brought an extra 20,000 tourists last year."

The Hotels Association also successfully lobbied to slash the VAT on accommodation to just 5 per cent, which has further boosted numbers, Mr Tanevski says.

He adds: "We calculate that the Dutch tourists who come spend between €50 and €70 more a day than the average; that's how the government makes up its revenues, through the VAT on that spend."

Macedonia is only really just beginning to exploit its tourism potential. It boasts great natural beauty, but is still largely unknown outside the Balkans and its transport and tourism infrastructure is in the main below par by west European standards

Mr Bloom says: "I've visited a lot of hotels in Germany, Benelux and France and a 4-star hotel in Macedonia is around the same quality as a 2- or 3-star hotel in those countries, here I'm talking mostly about the room".

Mr Trajkov insists that the government and agencies work hard to address such problems, but says 20 years of neglect cannot be quickly overcome.

He says: "The government has encouraged investment in new hotels, with several being built in Skopje. We support budget airlines, so Wizz Air, a Hungarian carrier, flies from an increasing number of European destinations. I think the figures show we are on the right track."

Tourists say one of Macedonia's greatest assets is its people.

As Mr Bloom notes: "The hotel we stayed in last year [on Lake Ohrid] took a lot of criticism and, God knows, the Dutch complain a lot. But staff tried to solve every complaint.

"Our lasting impressions are that people are willing to help in any way possible. We are sure to return some day, as we have this year."

Package deals: Lake Ohrid is a popular destination Dreamstime

Mood stays buoyant in spite of inter-ethnic divisions

Continued from Page 1

ethnic Albanian political party and a partner in Mr Gruevski's governing coalition, urges the premier to make the concessions necessary to secure Nato membership as soon as possible and put Macedonia on the road to EU membership. "I believe that as soon as we join the alliance we will see a big jump in foreign investment that will create many more jobs."

Zoran Zaev, the opposition leader, voices a sense of urgency: "We've been an official candidate for EU membership since 2005 but we have slipped down the ladder (of west Balkan applicants) when we could have been close behind Croatia," which joined the EU in July.

Macedonia's democracy remains fragile, though most analysts exclude the chance of a repeat of the 2001 ethnic Albanian insurgency. This left doubts about long-term regional stability, even after leaders of the ethnic Macedonian majority and the rebel Albanian minority renewed a commitment to coexistence under a peace deal brokered by Nato and the EU.

The appointment as defence minister in February of Talat Xhaferi, a former rebel fighter, triggered outrage among ethnic Macedonian armed forces veterans. Violent, if short-lived clashes ensued between rival ethnic gangs in Skopje, highlighting tensions underlying a five-year political partnership between Mr Gruevski and Mr Ahmeti.

Inter-ethnic divisions are evident, too, in the business community, with Macedonians controlling most larger companies. Ethnic Albanians run small businesses focused on boosting trade with neighbouring Kosovo and Albania.

"Things are better than they used to be but it's still a problem for Albanian companies to grow and flourish . . . Many bureaucratic obstacles are put in their path and it's harder for them to win state contracts," says Shefki Idrizi, an ethnic Albanian businessman who is founder and chief executive of Renova, a producer and exporter of specialised building materials.

Mr Gruevski's six-year campaign to put Macedonia on the global investment map as a cost-competitive centre for manufacturing and services is proving successful. This was despite initial scepticism that an impoverished southeast European country of 2.1m people would be able to attract high-quality international investors.

Macedonia has raced up the rankings since 2006 from 96th to 23rd place in the World Bank's annual global "ease of doing business" survey, ahead of most EU member states. It takes only a few hours to set up a company at Skopje's "one-stop-shop" for investors, while average monthly wages of €330 compare favourably with neighbouring Bulgaria and Serbia.

More than 30 companies, from Johnson Controls of the US, a maker of printed circuit boards which has built a second factory, to the Belgian bus manufacturer Van Hool, a recent arrival, are established in an industrial and technological zone outside Skopje. The unemployment rate has edged down to 30 per cent.

The stand-off over EU accession talks has seen Mr Gruevski seek investors from further afield. On a trip to Beijing in June, he renewed an earlier proposal to set up a special industrial and technological zone for Chinese companies seeking a European manufacturing hub. In July, Macedonia signed an agreement with Russia to build an offshoot of Gazprom's South Stream pipeline project to bring natural gas across the Black Sea to the Balkans and central Europe.

At home, the prime minister faces criticism over a media crackdown that has attracted the attention of Frank La Rue, the UN's special rapporteur for freedom of speech. On a visit to Skopje in June, he noted an "atmosphere of intimidation towards any kind of critical press". He called for a detailed investigation into the death in March of Nikola Mladenov, an investigative journalist killed in a traffic accident, to dispel "the cloud of suspicion and fear it provoked".

Mr Gruevski dismisses such accusations, saying the Macedonian media is "too deeply politicised". "I'm not saying there aren't weaknesses . . . after all we are a developing country. The problem is that the overwhelming majority of journalists are affiliated with political parties and only about 10 per cent are really independent."

Debt worries raise questions about state of public finances


Proactive policies: pursuing foreign investment has helped reduce unemployment and avert a deep recession Ivan Blazhev

Economy Fears of financial contagion from the Greek crisis are being played down by the government and central bank, says *Kerin Hope*

Macedonia can boast of having experienced the shallowest recession in southeast Europe, thanks in part to its policy of aggressively pursuing foreign direct investment.

After contracting by 0.9 per cent in 2009, the economy maintained positive growth until 2012 when it shrank by 0.3 per cent. An export-led recovery is projected to bring growth of about 2 per cent this year.

Even though inward investment slowed sharply last year, incentives that include a 10-year tax holiday for companies setting up in a special development zone, subsidies for greenfield plants and some of the lowest wage costs in Europe helped Macedonia attract a new high-profile investor from Germany.

The Dräxlmaier group has opened a €30m plant in the southern city of Kavadarci, producing wiring harnesses for the European automotive industry. The plant employs a 500-strong workforce which is expected to grow to 4,000 over the next three years. "Despite turbulent times in Europe in the past five years many foreign companies have reinvested here within a short period of time," says Viktor Mizo, chief executive of the directorate for technological industrial development zones, the agency responsible for operating them.

Macedonian economists worry that foreign manufacturers have few links with local suppliers.

Delays in carrying out infrastructure projects could undermine Macedonia's competitiveness as an investment destination once European economies start to recover.

"If we're going to bridge the gap with the EU, we need improvements in education and training and much more investment in roads and electricity production," says Mihail Petkovski, an economics professor at Skopje's Saints Cyril and Methodius university.

The coalition government led by Nikola Gruevski, the prime minister, is backing several large infrastructure projects, including upgrading the highway to Greece and building a railway link with Bulgaria, while at the same time seeking strategic investors to modernise the energy sector.

Zoran Jovanovski, chief economist at Komercijalna Banka, a leading Macedonian lender, says financing has become an issue given the country's rapidly rising public debt.

"It's not so much the level of the debt but the pace at which it's increasing. It raises questions about the sustainability of public finances," he says. "It's like seeing clouds massing on the horizon even though it's a sunny summer day."

At 34 per cent of economic output, Macedonia's debt has doubled over the past four years, though it is still among the lowest in the region.

The budget deficit, however, has remained stable at about 2.5-3.5 per cent of output.

"In the short term Macedonia has no urgent pressure for fiscal consolidation . . . The pace of consolidation will be in line with the pace of economic recovery," says Zoran Stavreski, the finance minister.

The International Monetary Fund is pressing for a tighter policy framework.

"We'd like to see the government adopt a medium-term fiscal strategy, which would make policy trade-offs explicit. In the absence of such a strategy, fiscal policy making becomes a bit ad hoc," says Alexander Tieman, until recently the Fund's resident representative in Skopje.

Dimitar Bogov, the central bank governor, says there is still room for further borrowing but only to finance infrastructure projects.

"We have to be very cautious," he says. "We have to think of fiscal consolidation in the medium term and the sustainability of public debt at a much lower level than 60 per cent of gross domestic product."

> 'It is like seeing clouds mass on the horizon even though it is a sunny day'

The domestic debt market is being restructured with IMF assistance, with the aim of lengthening maturities and gradually reducing dependence on international borrowing. More than 50 per cent of domestic issuance is now offered at maturities of 12-24 months, attracting pension funds, banks and companies with strong liquidity as well as individual investors.

Multilateral institutions have also provided support. In 2011, Macedonia drew €220m from a €463m IMF precautionary credit line after postponing plans for a eurobond issue because Mr Gruevski had called an early general election.

Critics say a sizeable chunk of IMF funding went on social spending aimed at benefiting candidates from Mr Gruevski's Internal Macedonian Revolutionary Organisation-Democratic Party for Macedonian National Unity (VMRO-DPMNE) at the polls.

This year, Macedonia borrowed €250m from Deutsche Bank to finance the budget deficit, winning favourable terms thanks to a World Bank guarantee for most of the loan.

Prospects for returning to international capital markets have receded following Macedonia's downgrade in May by Standard & Poor's by one notch to double B minus.

The rating agency cited, among other factors, "recent increases in public capital expenditure on non-productive assets", a reference to spending overruns of more than €100m on the government's controversial "Skopje 2014" heritage project.

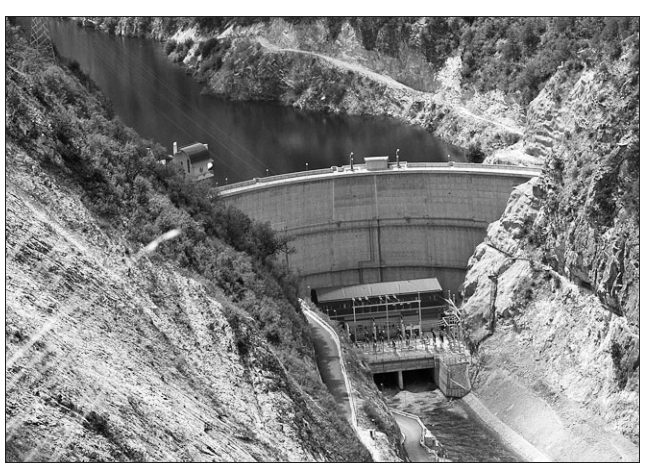
Mr Bogov plays down fears of financial contagion from the Greek crisis. Large Greek investors in manufacturing and retailing have stayed the course. Stopanska Banka, controlled by Greece's second-largest commercial lender, National Bank of Greece, is profitable on a standalone basis.

A second bank of systemic importance, NLB Tutunska Banka, also has a struggling parent, Nova Ljubljanska Banka of Slovenia. Yet the sector remains strongly capitalised with an average capital adequacy ratio of 17.1 per cent and lending at less than 90 per cent of deposits, says Mr Bogov.

Long-term returns prove difficult in uncertain environment

Energy

Foreign investors have often found it hard to do business, writes *Kester Eddy*


Overhaul: Sveta Petka, Elem's automated hydropower plant

With a click on his computer, Kocho Angjusev projects a map of Macedonia on to his flat screen monitor in his Skopje office. The map highlights each of his 14 mini-hydro plants located on rivers round the country, varying in capacity from 3.5MW to just 120kW.

With five more plants under construction, Mr Angjusev, an industrialist-cum-university professor, heads the largest private producer in renewable energy in Macedonia.

"Mepso, the [state-owned] market and grid operator, takes all the power we produce, but we are dependent on the hydrology. I take that risk. Last year was awful, there was not enough water and we only generated about 60 per cent of the expected electricity," he says. This year, however, he looks set to produce the 57GW hours set out in his business plan – the electricity needed to pay off his investment of close to €40m in the nine to 11-year target period.

Macedonia currently imports about 30 per cent of its gross annual consumption, which amounted to 9,550GWh in 2011, according to statistical office data.

Both the government and Elem, the state-owned generation company, are keen to reduce what they see as an over-reliance on electricity imports.

"The government, as never before, is considering new projects as part of a very serious, integrated approach to solving the country's electricity needs," says Dejan Boshkovski, general manager of Elem.

Both Mepso and Elem have implemented plans to modernise their respective assets. Mepso is building a second high-voltage connection with Serbia, representing an investment of €10m, along with upgrades in the domestic grid valued at €5.5m. Medium term, it plans a €40m link to the Albanian system at Ohrid.

But as Sinisa Spasov, general director of Mepso, says: "Most of the lines in the system were built in the 1950s and '60s. These are all now obsolete."

Elem, which generates an annual 6,000GW hours – "98 per cent of all domestic production", says Mr Boshkovski – faces a similar investment problem, with the need to overhaul ageing thermal and hydro power plants, plus install new and more diversified capacity.

It has drawn up a formidable list of projects for the period 2012-2020, including new mines, thermal and hydro plants which, if fully realised, will require more than €2bn in investment. These include the continuing €88m refit at the Bitola lignite-fuelled power plant, which single-handedly accounts for almost 80 per cent of Macedonia's domestic production, and a new 68MW pump-storage scheme at Boskov Most. Groundwork on this €107m project is expected to start in the near future, and take five years to complete.

Mr Boshkovski is adamant that funding for projects under way is assured, but accepts that foreign investment will be needed for the planned 300MW Mariovo coal-fired plant, expected to cost some €350m.

The government plan – as outlined to the FT by Nikola Gruevski, the prime minister – is to find an investor willing to inject capital into Elem in return for a 49 per cent stake in the generator, with the new funds used on expensive, but much-needed, investments like Mariovo.

Power projects involving long-term returns for foreign investors are fraught enough when the investor takes a majority stake. Any involving less than full executive control are yet more difficult to structure successfully.

The plan has not started well. A tender called to select the principal consultant was pulled this summer due to the lack of a "reputable candidate", says Mr Boshkovski.

Nor does the experience of EVN, the Austrian utility, bode well. The company took a 90 per cent stake in the Macedonian electricity distribution company in 2006. Renamed EVN Macedonia, it has invested almost €200m into modernising the network, and in June proudly revealed plans to invest a further €1bn into the network over the next two decades.

Barely a month later, EVN learned that the Macedonian regulator had cut the tariffs it is allowed to charge customers, while also raising the regulated prices charged by both the generator and the grid.

The distributor, stunned by the news, warned that the decision "directly endangered" the stability of the company and would "certainty influence the intensity of the planned investments and co-operation with 5,000 business partners in Macedonia."

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Constructing history for a new era

Urban renewal

Costly regeneration projects have divided the community. But the government insists that its programme will help unify the young nation, writes *Kester Eddy*

Building blocks: national projects, such as the Archaeology Museum, have helped create 10,000 jobs Getty

It is a hot, summer Sunday lunchtime, and Senad Hodzic is having his photo taken by his young, polyglot nephew in front of the fountains in Macedonia square, the focal point of Skopje city centre.

Towering above the pair on top of a 16-metre high column is a 14.5m bronze statue of a warrior on a rearing horse.

"It's very good. It beautifies the square and attracts tourists," says Mr Hodzic, a truck driver and ethnic Bosnian with Macedonian nationality living in Skopje.

But when questioned as to costs, and best use of public resources, his enthusiasm wavers.

"Yes. We don't need all of these," he says, pointing to other statues dotted around the square and along the banks of the nearby Vardar river. "We only need one statue, not so many. They should have spent some of the money on hospitals."

The statue – generally understood to represent Alexander the Great, although not named as such – is just one element of a giant project involving scores of new state institutions, civic buildings, statues and ornamented public facilities initiated by the government of prime minister Nikola Gruevski – who claims the concept as his own.

Dubbed Skopje 2014 (the title indicating the year of completion), the project is designed to give the Macedonian capital – previously a nondescript provincial town dominated by uninspiring Socialist-era architecture – an imposing image meant to raise national pride and attract tourists.

The new state buildings will save on rents and, it is hoped, enhance the efficiency of public administration.

"We are a very young country, only 23 years old. As part of Yugoslavia, national feelings were suppressed, and Yugoslav feeling had to be cultivated. [On independence, we had] one country, one nation with a history, [but] no monuments or statues to express our nationhood," Mr Gruevski explains.

Moreover, by creating up to 10,000 jobs at its peak, the project has "helped the construction industry to survive," the prime minister argues.

But Skopje 2014 has provoked fierce protest: apart from what opponents say is the opaque squandering of scarce public funds, the project is denounced on grounds ranging from racism and sexism to the falsification of national and cultural history.

Ivana Dragsic, a co-founder of Freedom Square, a civic association formed to oppose the project, points to the first manifestation of government plans for the city – a kind of proto-Skopje 2014 proposal to construct an orthodox church in Macedonia Square – as symbolic of all that is wrong with both the concept and its backers.

"They wanted to use public funds – so money from all citizens, including atheists and Muslim minorities – in a secular country to build a church on public land. And, of course, if they built a church, the Islamic community wanted a mosque. We thought this a very bad idea in a society such as ours; it creates potential conflict," Ms Dragsic says.

More fundamentally, the government appeared set on implementing its plan without consultation, spurring the first street protest from a motley collection of activists, centred on a group of architecture students.

"It was March 28 2009. There were about 150 of us, and, according to police reports, 4,500 counter protesters, who attacked us. It was a messy affair, the police did not react, we were spat upon, sworn at and pushed off the square," she recalls.

Although the government later relocated the planned church – it has yet to be built – when the full Skopje 2014 plans were revealed a year or so later, these went ahead based on a similar pattern, with no public discussion, no transparency – and widespread intimidation of opponents.

"They say they are against the communist Yugoslav era, but they are acting just the same," Ms Dragsic says.

Meanwhile, with the project now well on the way to completion, the cost has escalated from an initial target of €80m to – according to opponents' estimates – €400m and above.

Mr Gruevski sticks to the latest official figure of €207m. To put this in context, he says "in the same period, we have spent €100m on new hospital equipment, €100m on hospital modernisation, and €100m on farmers' subsidies and other expenses."

He admits that, for some citizens "it's too much in a too short time", but stresses opinion polls show "more than 60 per cent support the project".

But in Skopje's Centar district, home to many new developments, voters showed their disapproval by electing Andrej Zernovski, an opposition candidate, as mayor in March. "Voters decided it was too expensive and they were right . . . We face big cost overruns that we can't afford. We have no idea where the money went," he says.

"We had no baroque in our architectural history. But we can't pull them down and take them away."

The statues are a different matter, Mr Zernovski says. "People from other cities complain they're paying for statues which are only in Skopje. They are easy to remove. We could send them all around the country."

Automation has been a driving force

Foreign investment

Johnson Matthey produces 4m converters a year worth €500m, reports *Kester Eddy*

Eight metres above the main floor of Johnson Matthey's Macedonian plant, automated guided vehicles, orange lights flashing, shuttle between lines of gleaming tanks, tubes and vats containing an array of chemicals. In one, a gauge indicates the contents – 4.7 tonnes of "washcoat".

Sometimes a green, sometimes a yellow-brown liquid, depending on specification, washcoat is the medium by which the active elements of a modern catalytic converter – platinum, palladium and rhodium – are transferred to the "substrate" (the ceramic or metal core, honeycombed with fine passages, that provides the basic structure for these units) used by the auto industry to absorb toxic exhaust emissions.

On the two 90-metre-long production lines below, staffing is largely concentrated in small teams at either end of the process, preparing, inspecting, and packing the finished product. In between, the washcoat is induced by a vacuum to spread its precious metals on to the substrate's myriad internal surfaces, before heat treatment at 500C.

This plant, representing an investment of €60m, is "one of the most automated in the group," says Jatin Thakrar, managing director of Johnson Matthey Catalysts.

Established in 2009 in a spacious industrial zone 10 miles east of Skopje, it produces 4m units a year worth €500m and is touted as a flagship investment both by its owner, Johnson Matthey, the British chemicals and precious metals company, and by government officials.

"Since starting in 2009, we've had more than 40 audits by customers – big auto companies that are very demanding – and they have all been impressed," says Mr Thakrar.

Encouraged by initial results, and against a background of the European Union ratcheting up demand for catalytic converters by imposing ever tighter exhaust emission limits, the parent company decided in May 2012 to double plant capacity, installing two lines that are starting production this month.

This expansion makes Johnson Matthey the single largest foreign investor in Macedonia, with close to €120m tied up in the country, says Viktor Mizo, chief executive of the Directorate for Technological Industrial Development Zones (DTIDZ), the agency responsible for operating the business parks.

"Our zones have proved very good locations for investment, even during these last five turbulent years in Europe," says Mr Mizo.

He adds: "The fact that Johnson Matthey – and others, – have reinvested after such a short period is, I think, proof of the very positive business environment here, the one-stop-shop system and other support provided by government institutions."

Not that the project has been without challenges, and ironically the high level of automation has caused recruitment headaches.

"It's not as if we've been able readily to recruit people on the job market," says Mr Thakrar.

"There's not a great deal of industry here, so there is a lack of experience, but what we've done is target training. For example, we've taken electrical engineers with a software interest, and made them into automation technicians, and they've been able to support the plant."

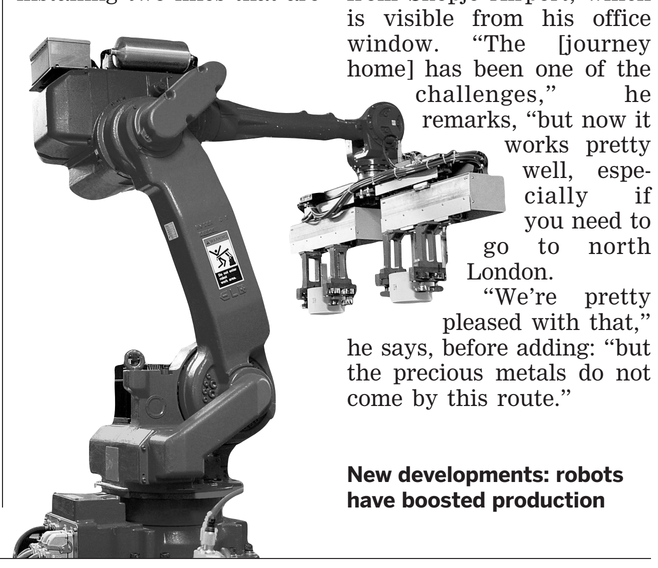
With the factory now expanding staff numbers from the 350 needed in the first phase to an expected 550-600, Johnson Matthey has also cultivated relationships with Skopje university in order both to train and recruit engineers and chemists with practical skillsets. It typically offers about 20 internships to graduates each year, with half of those taking up permanent positions on completion. Recruits have proved "adaptable, and eager. They generally like working for a multinational," Mr Thakrar says.

As for logistics, he is understandably unforthcoming about how precious platinum and other metals arrive at the plant, only saying that "they don't come by road".

The finished product, however, is trucked to a central distribution point in Bavaria, Germany, before onward shipment to exhaust manufacturers.

And, as a UK citizen, he appreciates the arrival of Wizz Air, the central European no-frills carrier, that now has regular flights to London's Luton airport from Skopje Airport, which is visible from his office window. "The [journey home] has been one of the challenges," he remarks, "but now it works pretty well, especially if you need to go to north London.

"We're pretty pleased with that," he says, before adding: "but the precious metals do not come by this route."



New developments: robots have boosted production

Medals mount for wines on an international mission

Viticulture

Developing taste for more varieties has boosted the industry at home and abroad, says *Kester Eddy*

Perhaps it is the giant 4,500 litre Slavonian oak barrels, deep in the cellars and dating from the Yugoslav era, that prompt Aleksandar Ristovski, hospitality manager at Tikves Winery, to tell the story of the "super harvest" of 1982.

By then, the winery, with an annual capacity of 50,000 tonnes of grapes, was already the largest in south-east Europe. But that year, spurred by the communist authority's obsession with production figures, local vineyards yielded 75,000 tonnes. Tikves was ordered to process the lot.

"It was an enormous amount. They filled the public swimming pool in town for open fermentation, they cleaned oil storage facilities, and fermented there too. It was an awful thing, nobody asked for quality in those days," he says.

Fast forward three decades, and the philosophy of Tikves, located in the town of Kavadarci, southern Macedonia, could not be more different.

"We're not part of that game any more," says Mr Ristovski. "Producing bulk wine, you just survive with a very small profit margin; you will never become a famous winery.

When it was privatised in 2003, with M6, a local investment fund, taking majority ownership, new management reviewed every aspect of the business, from vine care to labelling. Foreign consultants, including Philippe Cambie, the renowned French winemaker, were called in when necessary.

Underpinned by a €25m investment programme into new vineyards and state-of-the-art equipment, Tikves has transformed itself, raising standards across the board and targeting the very best *terroirs* to produce premium wines. As a result, the value of wine has more than tripled, from €0.50 to €1.85 per litre.

And, after several years of struggle, the wine world began to notice. In 2011, Robert Parker, the influential American wine critic, awarded 94 points for Tivkes' flagship Bela Voda red cuvee.

"People used to ask: where is Macedonia? But this really opened doors for us," says Mr Ristovski.

Tikves is not alone: in 2010 it and a dozen Macedonian wineries, all striving to raise quality levels, formed an association – Wines of Macedonia – to further their cause. Members include Stobi, like Tikves, a well-funded former state winemaker, and family concerns, including Bovin – generally recognised as the Macedonian vintner that blazed the trail for premium wines.

The association, representing about 80 per cent of domestic production, is dedicated to promoting wine culture at home, and marketing Macedonian wine abroad. Exports are vital, given that domestic consumption made up just 10 per cent of the 120m litres of wine produced last year. Gorgi Petrusev, director of Wines of Macedonia, says: "With the support of the Dutch government, we identified key markets in Europe, the US and China, and we then started on an operational level promoting our wines."

Quality has greatly improved

The results are clear, he says: "Medals are mounting like inflation: at almost every international competition Macedonian wines win awards. Exports of bottled wines last year were 66 per cent up on 2011."

This, however, is from a low base: bulk wines still make up about 85 per cent of exports, with Germany taking roughly 40 per cent of Macedonia's total wine production.

But one step at a time.

Doing their bit for the industry, Vladislav Popov and his wife Zoya are to be found most weekends at their winery in the village of Sopot, a few miles north of Kavadarci, where they bought a small vineyard comprising just 0.5 hectare of vines in 2001.

While his head may be in information technology – he runs his own systems integration company in Skopje – his heart veers towards the vine. In the past 12 years Mr Popov has pumped most of his company profits – a sum which he says "can be expressed with seven digits in euro" – into expanding that initial investment into 45ha under vine, plus a modern winery with a capacity to process 400,000kg of grapes.

Popov Winery exports nearly a third of annual production of 130,000 litres, including shipments to Japan, Canada, Germany and Switzerland. While Tikves likes to experiment, with 250 workers awaiting salaries every month, it must maintain a certain throughput: the Popovs, with just 10 employees, are freer to follow their winemaking whims.

Their flagship, oak-aged reserve, for example, is made not from four wines that have been fermented individually, but from a mixture of the grapes – Merlot, Cabernet Sauvignon, Cabernet Franc, and Vranec – fermented together.

As Orde Ivanovski, from the Tikves marketing team, said after a recent tasting: "It's really, really tough to ferment all these varieties together. To keep account when every variety comes into the winery, and they need different temperatures and times. It's a good experiment, and the end-product is really nice."

Challenges remain in untouched sovereign territory

Capital Markets

Frontier market is in favour but remains too small for most investors, says *Robin Wigglesworth*

In recent years, one of the hottest investment themes has been frontier markets, recondite countries that represent relatively untouched territory for international finance – much like Macedonia.

The drive has been spurred partly by disillusionment with the big emerging economies – particularly Brazil, Russia, India and China – but also by the cheap valuations, favourable demographics and relatively robust economic growth rates of these more exotic markets.

The very fact that they are off the beaten investment track means that frontier markets are less correlated to the ebb and flow of global investor sentiment, an attractive characteristic when hard-to-predict political events in the eurozone or Washington DC can rattle mainstream markets.

But even among frontier markets, Macedonia is on the periphery. The Macedonian Stock Exchange only has 14 listings with a total market capitalisation of MKD107bn, or €1.7bn – not trifling relative to the size of the Macedonian economy, but far too small to interest international fund managers – even those who specialise in exotic markets.

Stocks trade infrequently, making share price movements volatile, and the main gauge has shed 10 per cent over the past 12 months. This year, Macedonian stocks soared in January, before giving up most of their gains by mid-September. However, Macedonia has benefited from the global hunger for higher-yielding bonds.

As the returns offered by western government bonds have slumped to record lows, many investors have been forced into increasingly remote corners of the world for securities that still offer a decent return. This pushed the yield offered by Macedonia's €150m bond maturing in 2015 to a record low of 3.85 per cent early this year, down from a peak of 13.4 per cent at the depth of the financial crisis of 2007-08.

More recently, the US Federal Reserve's plans to end its quantitative easing bond-buying programme has triggered turbulence in the stocks, bonds and currencies of the developing world, one of the prime beneficiaries of super-easy monetary policy in the US.

Although a small and sparely traded sovereign bond, Macedonia has not escaped the subsequent turmoil unscathed. The 2015 bond yield climbed to almost 4.6 per cent in mid-July, up almost a percentage point from its lows.

While this is a better performance than many other emerging market bonds – partly because investors have focused on selling bigger positions in more liquid markets before mulling the merits of smaller holdings – Macedonia's actions have failed to calm analysts.

Even before the recent emerging market sell-off, Gabriel Sterne, an economist at Exotix, a boutique brokerage, recommended that investors sell the Macedonian bond after the government unexpectedly tapped a precautionary credit line (PCL) from the IMF in March 2011. The Macedonian government said the €220m drawdown of the recently negotiated €476m IMF facility was caused by delays in issuing another international bond and accelerated elections at the time.

But the explanation did not impress Mr Sterne, who says PCL arrangements are primarily put in place in the event of unexpected and rapid financial deterioration. In contrast, Macedonia's economy is doing fairly well, and its bond yield was near a record low.

> So far, investors appear to have given Macedonia the benefit of the doubt

"We think such use of the PCL increases risks to bondholders, because IMF lending is senior to the eurobond, whose worth is correspondingly devalued in the – still unlikely – event of a restructuring," Mr Sterne wrote in a note.

Macedonia may find use for that PCL soon. Some analysts and investors fear the shift in US monetary policy could prove painful to countries that depend on foreign capital flows to finance budget and current account deficits.

In a recent study of which emerging markets are exposed to a slowing or even reversal of international capital flows, Standard & Poor's, the rating agency, put Macedonia near the top in each of its vulnerability metrics.

Macedonia's current account deficit stood at 3.9 per cent of GDP last year, even as the economy contracted 0.3 per cent in real terms, according to IMF estimates. The country's external indebtedness rose 4 percentage points to 68.6 per cent of GDP and the budget deficit widened to 3.8 per cent of output.

So far, investors appear to have given Macedonia the benefit of the doubt, but a more severe questioning of emerging markets more widely could well prove more problematic.