

## **Maja Kadievaska-Vojnovik: Foreign investment's importance to the Republic of Macedonia's economy**

Speech by Ms Maja Kadievaska-Vojnovik, Vice-Governor of the National Bank of the Republic of Macedonia, at the presentation of the Business Climate Survey in Macedonia, Macedonian-German Economic Association, Skopje, 10 April 2014.

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Dear Mr. Martin Knapp,

Dear guests,

It is an honor and pleasure to have this opportunity today to attend the presentation of the Business Climate Survey in the Republic of Macedonia, which is part of a regional survey of the representative offices of German Chambers of Industry and Commerce in Central and Southeast European countries.

Namely, the Survey provides significant information on the companies' perceptions about the Macedonian economy, and I would like to keep to some of its important aspects.

It is more than clear that there are tight connections between Macedonian and German economy, which are being realized through several channels, such as:

- trade channels
- capital flows and
- through the remittance channel.

First, Germany is and it raises its importance as the largest trade partner of the Republic of Macedonia. The share of the trade of goods with the EU member states in the total trade of RM of 52% before the crisis, in 2008, reached 67% in 2013. This significant strengthening of the trade relations with the EU member states is mostly a result of the intensified trade with Germany, and moreover, such development is fully conditioned by the increase in the exports of RM to Germany. Thus the share of the export of goods to Germany in the total export of goods of RM in 2008 equaled 14%, while in 2013 it climbed to high 36%, or in absolute amounts, from Euro 383 million, for only five years, it reached Euro 1,154 million. It is a significant increase, a triple increase.

It means that, despite the crisis in the Euro area and its negative implications, the strong economy based on sound and solid economic fundamentals – such as the German, proved to be our certain partner for placement of more than a third of the exports. Besides the traditional export products, i.e. the export of the domestic textile and metal manufacturing industry, in the last two years, Germany is important destination for export of the new capacities in the technological industrial development zones (TIDZs), i.e. for the export of machinery and equipment and equipment of automotive industry.

Second, Germany is our significant investor, which in 2013 advanced on the list of the ten most important foreign direct investors (9th). According to preliminary statistics for 2013, the total inflow of direct investment from Germany equals Euro 27 million, with the amount of the direct investment from Germany reaching Euro 111 million, or about 3 % of the overall stock of FDI (about Euro 4,000 million). However, this share is lower when compared with foreign capital originating from Austria (12%, or Euro 478 million as of 2013).

Third, the significance of the German economy for us is perceived also through the prism of foreign exchange inflows based on the Macedonian emigrants in Germany or the Macedonian citizens who are temporarily working in Germany. Thus, the growth of the German economy is closely correlated with the growth of this, to us, important income flow.

Generally, the German economy, the companies with German and Austrian capital that operate in the Republic of Macedonia, are extremely important for the local economy.

The results of the survey, i.e. the responses of the companies on the assessment of current business conditions and perspectives, at the level of both sector and company, regarding: trade, exports, employees – give an impression that a large percentage of respondents (over 80 %) have stable or positive expectations, i.e. claim that the environment is good or that it will improve. This is in line with our projections for 2014, according to which we expect economic growth of 3.7%, mainly determined by the growth of exports and fiscal stimulus in the construction sector. Also, the IMF assumes solid growth of the Macedonian economy of 3.2% in 2014, which is higher than the growth projected for the regional countries and wider, and provides a clear vision that there is potential for achieving the economic growth.

As the central bank, for us, it is extremely important that the surveyed companies largely expect increase in the exports. Thus the larger export potential, the higher foreign exchange inflows, i.e. narrowed trade imbalance. After all, in 2013 we witnessed trade deficit narrowing in the trade of goods that equaled about Euro 190 million, annually, given the increase in the exports (of 3.2%/3.9% in services) and a decrease in imports (of 1.5%/0.9% in services). This improvement in the trade is closely linked to the increase in the production capacity of the economy, i.e. the increase in the export potential. The policies that were applied in the previous period, which were aimed at attracting foreign investors in the tradable goods sector, which meant export diversification, proved as a good pillar for reducing the foreign trade imbalance. The export growth capacity of TIDZs plans indicated that the foreign exchange rate is not a barrier to exports, i.e. that it is not overvalued. On the contrary, the stability of the Denar exchange rate, in the past against the Deutsche Mark, and today against the Euro, is an important pillar of all business decisions. The applied monetary strategy of targeting the foreign exchange rate proved successful in maintaining low and stable inflation, that is, at the level of inflation in Germany, i.e. the level of the Euro area.

So, the competitiveness of the economy is not created through the exchange rate, but it should lay on sound fundamentals that will generate long-term sustainable growth. Despite the direct effects of the entry of foreign investment from the aspect of foreign exchange inflows, they created the potential for the Macedonian economy both in terms of reducing unemployment and in terms of transfer of know-how towards integrating local companies in international trade networks. Thus according to the Survey, an encouraging fact is that the respondents indicate presence and quality of local suppliers. The involvement of local companies in the chain of suppliers of major export capacities means true valorization of the secondary effects of the FDI inflow.

Also our expectations are towards further valorization of the positive effects of the structural policies that boost the competitiveness of the domestic economy. The macroeconomic policymakers should seek to improve the worst-rated local conditions, according to the respondents' opinion. Although some of them noted some progress in 2013, there is still room for their improvement. They relate to the improvement in the payment discipline, increasing the legal certainty and improvement of the public administration capacity, enhancement of the labor force qualifications in line with market demand through measures in the education system.

The Republic of Macedonia is on the map of foreign investors due to several factors, which were emphasized also by the surveyed companies. Low labor costs, i.e. low wages, low taxes, good qualification structure of the labor force, as well as the macroeconomic stability, mirrored in low and stable inflation, exchange rate stability, low levels of budget deficit and public debt. These were the core pillars the business decisions were laid on. Therefore, we – the macroeconomic policymakers, have an obligation to keep the solid fundamentals of the Macedonian economy in the next period.