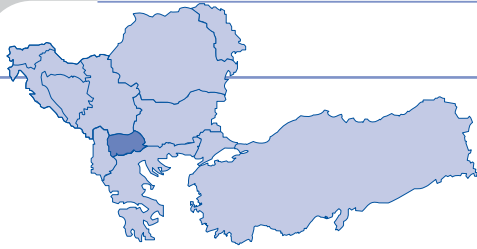


Macedonia



I. Economic overview

1.1. General economic indicators

| Indicators | 2000 | 2001 | 2002 | 2003 |
|---|-------|-------|-------|-------|
| 1. GDP, USD bln | 3.9 | 3.7 | 3.7 | 4.6 |
| 2. GDP per capita, USD | 1,924 | 1,830 | 1,835 | 2,316 |
| 3. Real GDP growth rate, % | 4.5 | -4.5 | 0.9 | 3.2 |
| 4. Industrial production growth rate, % | 3.5 | -3.1 | -5.3 | 3.8 |
| 5. Annual inflation average, % | 5.8 | 5.5 | 1.8 | 1.2 |
| 6. Annual unemployment rate, % | 32.1 | 30.5 | 31.9 | 36.7 |
| 7. Budget revenues, % of GDP | 24.5 | 22.2 | 23.5 | 22.5 |
| 8. Budget expenditures, % of GDP | 21.8 | 28.0 | 28.8 | 23.5 |
| 9. Current account, % of GDP | -2.1 | -6.8 | -8.6 | -6.2 |
| 10. Total foreign debt, % of GDP | 38.2 | 40.5 | 43.5 | 38.8 |
| 11. Interest rate on loans (annual average), % | 1.4 | 1.4 | 1.5 | 1.7 |
| 12. Gross external debt stock, USD mln | 714 | 775 | 734 | 903 |
| 13. Exchange rate of MKD for 1 EUR, end of year | 60.8 | 61.0 | 61.1 | 61.3 |

Source: National Bank of the Republic of Macedonia, Ministry of Finance, State Statistical office

1.2. Foreign trade

1.2.1. Foreign trade regime and major regulations

Following the WTO principle to eliminate quantitative restrictions on trade, an extensive liberalization of trade regimes has been implemented. Macedonia has joined the World Trade Organisation (WTO) on 4 April 2003. In the process of harmonization of the WTO sectoral agreements at the level of the highest tariff rate and following the bilateral and multilateral negotiations with the WTO members, the average tariff rate after the transitional period of WTO accession will be about 8%.

1.2.2. Customs regime, export and import quota and license system, tariffs

With the adoption of the Trade Law on 12 March 2004 (Official Gazette of RM No. 16/2004), the Republic of Macedonia made a complete harmonization of the trade regime with WTO rules. Pursuant to Articles XX and XXI of GATT 1994 the Law stipulates import and export licenses related to environmental protection, protection of human health, protection of animals and plants, protection of the historic heritage and trade in arms. The Law defines and regulates conditions under which measures can be taken for the protection of domestic production from increased and subsidized imports.

The Law on Customs Tariff (Official Gazette of RM No. 23/03) provides for complete compliance with the Harmonized system of the World Customs Organization and the Combined Nomenclature of the European Union.

1.2.3. Exports and imports

| Trade volume, USD bln | 2000 | 2001 | 2002 | 2003 | 2004 F |
|-----------------------|------|------|------|------|--------|
| Exports | 1.32 | 1.16 | 1.11 | 1.36 | 1.44 |
| Imports | 2.01 | 1.68 | 1.96 | 2.29 | 2.20 |

Source: State Statistical Office, Ministry of Finance

1.2.4. Major trade partners

Major export partners (2003)

| Country | % |
|-----------------------|------|
| Germany | 20.4 |
| Serbia and Montenegro | 20.1 |
| Greece | 13.2 |
| USA | 5.3 |
| Croatia | 4.8 |
| Netherlands | 3.4 |

Source: State Statistical Office

Major import partners (2003)

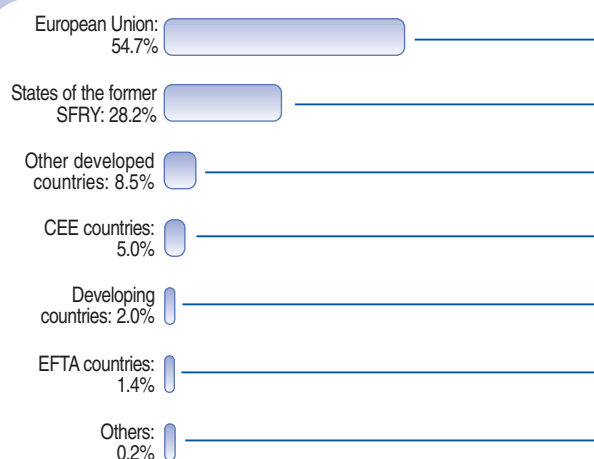
| Country | % |
|-----------------------|------|
| Germany | 13.2 |
| Greece | 13.1 |
| Serbia and Montenegro | 9.2 |
| Russian Federation | 7.7 |
| Bulgaria | 6.5 |
| Slovenia | 6.0 |
| Italy | 5.3 |

Source: State Statistical Office

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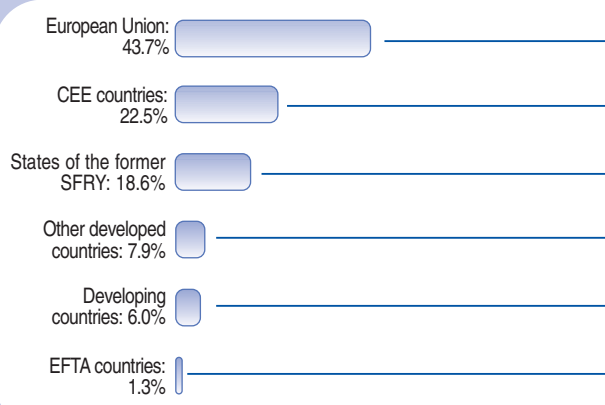
1.2.5. Structure of foreign trade by regions

Exports by country groups (2003)



Source: State Statistical Office

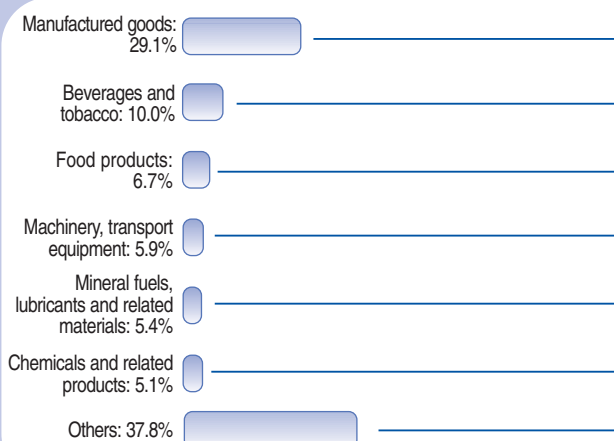
Imports by country groups (2003)



Source: State Statistical Office

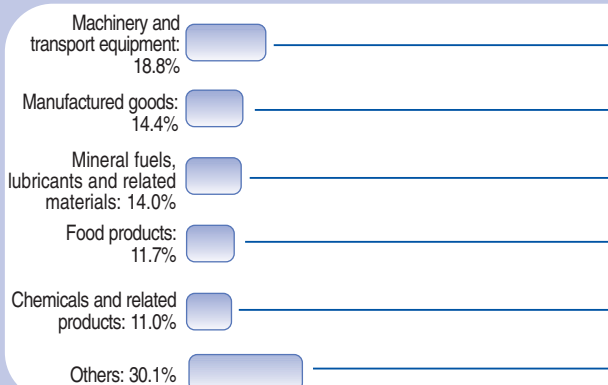
1.2.6. Structure of foreign trade by commodities

Exports by commodities (2003)



Source: State Statistical Office

Imports by commodities (2003)



Source: State Statistical Office

1.2.7. Major bilateral and multilateral Free trade Agreements

The Republic of Macedonia implements 11 Free Trade Agreements. Nine of these Agreements have been implemented on a bilateral basis with the following countries: Serbia and Montenegro, Croatia, Bulgaria, Romania, Bosnia and Herzegovina, Albania, Turkey, Ukraine and Moldova, and two of them are on a multilateral basis: the Free Trade Agreement with EFTA countries and the Stabilization and Association Agreement with the European Union.

Macedonia has submitted official application for CEFTA (Bulgaria, Romania and Croatia) membership as well. In Macedonia, more than 90% of trade liberalization in both industry and agriculture has been implemented with: Serbia and Montenegro, Croatia, Bosnia and Herzegovina, and Albania.

Macedonia has implemented more than 90% of trade liberalization only in the industrial sector with: Bulgaria, Romania and Moldova. The other 10% will be liberalized in 2005 with Bulgaria, in 2007 with Romania and in 2009 with Moldova. Now, only the most sensitive industrial products are subject to customs duties.

The implementation of the Free Trade Agreement between Macedonia and Slovenia provides for full liberalization of trade in industrial products on both sides. Since 1 May 2004, the trade between Macedonia and Slovenia adheres to the rules and provisions of the Stabilization and Association Agreement between Macedonia and the European Union.

The Free Trade Agreements with Turkey and EFTA states provide for the full liberalization of Macedonian exports of industrial products to their markets, which will take place in 2008 for Turkey and 2011 for EFTA.

The Free Trade Agreement between Macedonia and Ukraine provides for the full liberalization of exports of Macedonian industrial products in 2005, and for the full lib-

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eralization of exports of Ukraine's sensitive industrial products in 2007, while for the most sensitive industrial products - in 2010.

Trade in agricultural products is mostly in full customs duties, except for the products for which the countries on a mutual basis have determined tariff quotas under preferential conditions. This refers to all countries except four (Serbia and Montenegro, Croatia, Bosnia and Herzegovina, and Albania). Since 2001, trade between Macedonia and the European Union complies with the provisions of the Stabilization and Association Agreement. Macedonian industrial and agricultural products can be exported free of customs duties since June 2001, except for three agricultural products (veal, fish and wine), for which EU determines quotas on a yearly basis. EU's industrial products can be imported into Macedonia following a gradual reduction of customs duties over a transitional period of 10 years, till the end of 2010. On 1 January 2011, the customs duties for the export of industrial products will be abolished.

The Republic of Macedonia has submitted an official application for EU membership on 22 March 2004 in Dublin.

1.2.8. Free Economic Zones

The Law on Free Economic Zones enacted in 1999 (Official Gazette of RM No. 56/99, 41/00, 6/02) defines a Free Economic Zone (FEZ) as part of the customs territory of the Republic of Macedonia, in which economic activities are performed under special conditions.

The following activities could be performed in the FEZ: manufacture, services intended for export, foreign trade exchange activities, banking and other financial activities, property and individuals insurance and reinsurance, other commercial activities except for those related to textile industry.

In 2000, the FEZ Directorate has been established as a Governmental institution in order to carry out all activities regarding the development, establishment and monitoring of the activities in the FEZ. Furthermore, the Directorate is also engaged in attracting investors to the FEZ, as well as in the long-term relations of domestic and foreign investors.

Advantages and incentives in the Free Economic Zones

Monetary advantages:

- VAT and excise tax exemption
- Corporate income tax and property tax exemption for 10 years

| Tax | Tax duty | In the zone |
|----------------------|----------|-----------------|
| VAT | 18% | 0% |
| Excise tax | 5%-62% | 0% |
| Corporate income tax | 15% | 0% for 10 years |
| Property tax | 0.1% | 0% for 10 years |

- No customs duties for goods, equipment and machinery in the free zone

| Products | Customs duty | In the zone |
|--------------------------------|--------------|-------------|
| Raw materials | 0%-15% | 0% |
| Equipment | 5%-20% | 0% |
| Consumer goods | 15%-30% | 0% |
| Agricultural and food products | 20%-60% | 0% |

- No fees for construction, connection with water, sewerage, heating, gas and electricity

Commercial advantages:

- Foreign companies can start operations quickly
- Companies active in the FEZ can be 100% local companies, foreign-owned or joint-ventures
- There is no prohibition against selling from FEZ to the domestic market
- Companies can use the FEZ as a re-export center
- Bureaucracy in the FEZ is minimized

Employment advantages:

- The companies can easily recruit local workers
- Available high skilled employees
- Labour relations board

The user of a FEZ who reinvests its corporate income in capital assets in the FEZ is entitled to reduce the corporate income tax base for the amounts invested in capital assets, after the expiration of a period of 10 years and 1 day after the commencement of activities.

Pursuant to the Law, the free zone land may be leased to foreign investors for a period of 50 years, with a possibility of extension for another 25 years.

The contractor awarded the right to develop a FEZ by the FEZ Directorate is entitled to lease or sub-lease immovables within the FEZ and to transfer rights to the users of a FEZ.

The first Free Economic Zone in the Republic of Macedonia - "Bunardzik" covers an area of about 160 ha and is located 10 km east of Skopje, on the highway Skopje-Kumanovo (E75), and 3 km away from the "Petrovec" airport. The founder of the zone is Glyndwr Estates Limited from Wales, United Kingdom. Another FEZ in Macedonia, established in 2000, is FEZ "Nickel Valley" in Kavadarci. There are three more FEZ planned to be established: Prdejci - Gevgelija, Progres - Stip and Frinko - Bitola.

1.3. Privatisation

Privatisation in Macedonia is almost complete, with more than 95% of the state-owned companies sold. According to the Government Strategy, state-owned assets unsold after 31 December 2004 will be transferred to the Pension Fund, and the companies' assets (buildings, machines and other equipment) owned by the Macedonian Privatisation Agency (MPA) will be transferred to a public company for real estate management and MPA will be closed on 31 March 2005.

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Under the restructuring programme, within the FESAL II arrangement with the World Bank, 40 loss-making companies have been selected. They have to be sold to strategic investors or closed. The shares of both the operating and the assets of the liquidated loss-making companies are being sold by international tenders. This programme is co-ordinated by the Ministry of Economy and is near to its completion.

Privatisation of the banking system

The banks have been transformed as part of a wider financial sector reform. Their privatisation has been a passive one depending on the privatisation of their founding enterprises. However, looking for full capitalization, a number of Macedonian banks have attracted foreign investors as the banking sector is now fully reformed. Presently, the share of foreign capital in the total banking sector equals 47.2%, present in 15 banks, 8 of which are owned by foreign shareholders.

Privatisation plans

Restructuring and then privatisation of the following companies in the public sector is pending: Macedonian Power Utility - Electro Stopanstvo na Makedonija (ESM), Public Enterprise for Railway, companies from the healthcare sector. Privatisation of these companies is under the auspices of the respective ministries (i.e. Ministry of Transport and Communications, Ministry of Economy and Ministry of Health).

1.4. Foreign investment

1.4.1. Foreign investment by years and by type of investment

The total FDI stock in the Republic of Macedonia has reached USD 1 billion by the end of 2003. Year 2001 marked the biggest amount of FDI inflows as a result of the sale of the Macedonian Telecom to the Hungarian Matav for USD 310 mln. The majority of FDI inflows in the country have come through the privatisation process.

| Year | 2000 | 2001 | 2002 | 2003 | 2004 ^F |
|--------------|-------|-------|------|------|-------------------|
| FDI, USD mln | 178.5 | 445.1 | 77.3 | 97.5 | 200.0 |

Source: National Bank of the Republic of Macedonia

Note: ^F Forecast

USD 87.2 million of FDI inflows have been reported for the first half of 2004.

1.4.2. FDI stock by sectors (2000-2003)

Besides the largest investment generated through the privatisation of the Macedonian Telecom, the majority of FDI inflows has been attracted in the sectors of manufacturing, ferrous metallurgy, cement production, crude oil processing, food and beverages, textiles, as well as in banking and insurance.

FDI inflows by sectors, USD mln*

| Activity | 2000 | 2001 | 2002 | 2003 |
|-----------------------------------|--------|--------|-------|-------|
| Transport and communications | 2.36 | 337.39 | 10.28 | 32.32 |
| Financial intermediation | 104.70 | 11.20 | 24.78 | 28.80 |
| Manufacturing | 34.70 | 37.74 | 27.22 | 12.55 |
| Hotels and restaurants | 0.13 | 1.28 | 1.64 | 7.19 |
| Trade and repair | 3.50 | 5.15 | 6.97 | 4.73 |
| Business activities & real estate | 2.36 | 8.52 | 1.88 | 4.34 |
| Agriculture and fishing | 0 | 2.31 | 0.42 | 1.59 |
| Other services and not allocated | 2.56 | 27.03 | 2.79 | 1.43 |
| Construction | 18.90 | 12.32 | 4.01 | 0.27 |
| Mining and quarrying | 9.62 | 2.17 | 0.29 | 0.26 |
| Others | 0.01 | 0.02 | 0.02 | 0.60 |

Source: National Bank of RM

Note: * Preliminary data for 2003; sectors listed in descending order according to the cumulative FDI inflows

1.4.3. FDI stock by countries, USD mln (2003*)

| Country | % |
|------------------------|-------|
| Netherlands | 31.61 |
| Switzerland | 13.61 |
| Bulgaria | 9.26 |
| United Kingdom | 6.82 |
| Slovenia | 6.07 |
| British Virgin Islands | 5.85 |
| Germany | 4.87 |
| USA | 3.46 |
| Austria | 2.63 |
| Serbia and Montenegro | 1.09 |
| Others | 14.73 |

Source: National Bank of RM

Note: * Preliminary data

1.4.4. Government institutions in the field of foreign investment

The **Agency for Foreign Investments of the Republic of Macedonia**, which will be responsible for attracting and promoting foreign investments in the country, will be established by the end of 2004.

This institution will be highly professional, flexible, and will have great independence in the decision-making for the everyday activities; its task will not be only to attract foreign investors, but also to support foreign investors in the pre-investment, investment, and re-investment period. This will create conditions for the Agency to actively participate in the process of creating investment policy in the country by submitting proposals and changes, thus enhancing the legislation related to foreign direct investment.

Additionally, as an institutional support to FDI attraction, the Ministry of Economy has nominated investment representatives that will work in Italy and Germany for the promotion of Macedonian economy in these countries. This support will be further developed by increasing the number of investment promoters and targeting other countries.

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1.5. Investment opportunities by sectors

Macedonia is a small, but rather diverse economy, where a number of sectors have investment and export potential. The sectors considered with potential for FDI attraction include: finished textile and leather goods; shoes production; fruits and vegetables growing; lamb meat; processed food and packaging; wines; tobacco and cigarettes; tourism; steel and metal fabrication; chemical and pharmaceutical industry; vehicle and bus assembly; electrical equipment and electric motors production; construction; infrastructure; banking; telecommunications and other service activities.

1.5.1. Ferrous and non-ferrous metallurgy

A large number of facilities in the sectors of ferrous and non-ferrous metallurgy have been developed and are mainly export oriented. Ferrous metallurgy participates with 7% in the GDP of the country, and non-ferrous metallurgy with 3%. Main products include hot and cold rolled sheet steel, aluminium bars, rods and profiles, ferrous alloys, seamed tubing and ferrous-nickel products, lead, zinc, copper, gold, and silver.

1.5.2. Metal fabrication, vehicles and electrical equipment industry

Manufacture of various products, including buses, castings, steel pipes, batteries, cables, pumps, household appliances, etc. Machinery for metal, wood and plastics processing industries is available.

1.5.3. Chemical industry

The country has a large chemical industry, which accounts for 10% of industrial output. There is a well-developed capacity for the production of basic chemicals, synthetic fibers, polyvinyl chloride, as well as detergents, fertilizers, polyurethane foams and fibres, etc. Pharmaceutical and cosmetics companies are well established. The annual production is 3,500 tons of medicines and medical materials, and 12,500 of cosmetic products.

1.5.4. Textile and leather industry

This industry is a major employer (24.1%), participating with 8.8% in the total number of companies in the economy, and has a contribution of 20% to GDP. Cotton thread and fabrics, wool yarn, fabrics and knitted fabrics are the main products. The export potential due to increased demand for ready-made clothing in Europe and North America is based mainly on inward processing. In the past few years more than 400 new textile companies have been open.

The annual production capacities for hide and leather amount to 3,500,000 sq. m, of fur - to 1,300,000 sq. m, and of rubber products - to 5,000 tons. There are over 70 small

companies for shoes production. In 2003, 3,000,000 pairs of shoes and 360,000 sq. m of fur have been produced.

1.5.5. Construction industry

This construction industry relies on domestic raw materials: feldspar, calcium carbonate, bentonite, crumbled and micronized quartz, perlite, etc. Production includes china tiles, sanitary ware, asbestos, cement and cement products, gypsum and products thereof. The country has a well-developed construction industry dominated by six companies. The industry is recognized for its skilled personnel and use of modern technology, especially in the area of civil engineering and hydro-construction. Therefore, Macedonia has been a major supplier of construction labour for small and large-scale projects in Central and Eastern Europe, the Middle East and Russia. The annual turnover in civil construction amounts to over USD 400 million, about 20-25% of which have been generated in projects undertaken abroad. Locally established foreign construction companies can work without any restrictions on the Macedonian market. The main laws regulating the construction market are: Law on Urban Planning, Law on Construction of Business Premises and Law on Public Roads.

The state institution engaged in the regulation of construction and real estate is the Ministry of Transport and Communications. According to the Law on Public Procurement foreign construction companies can freely participate in the procurement procedures and in cases when the financier is a foreign financial institution according to its requirements.

1.5.6. Agriculture and agribusiness

The agribusiness sector (including agriculture and processing) is of great significance for the economy, and accounts for 15% of GDP. The primary agricultural sector remains a major employer, accounting for about 24% of the total working population. Agricultural land is 1.3 mln ha, out of which 43% are arable and 4% are vineyards and orchards; the rest is meadows and pastures. The private sector cultivates more than 80% of the agriculture land.

The climatic conditions are excellent for the growing of grapes, early market garden vegetables, fruits, and livestock breeding. A significant number of capacities exist in the food industry and the production of beverages. The overall exports of agricultural products range between USD 180 and 230 million, which accounts for about 20% of the total exports of Macedonia.

In 2003, the estimated value of agri-food export was about EUR 220 mln, including the following major export commodities: raw and manufactured tobacco, wine, lamb and horticultural products. Agri-food imports accounted for 13% of the total imports in 2003 (including frozen and processed meat, vegetables oil and animal fats, sugar and wheat as the main imported commodities). The major agri-food trade

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partners of Macedonia are the EU and Serbia and Montenegro. It is expected that the importance of agri-food trade with the EU will increase after 2004 with the expansion of the EU with 10 new member countries. Hence, Macedonia will be able to export most of its products duty free to an enlarged market and preferential import tariffs will be extended to significant trade partners.

1.5.7. Food and beverages industry

Food and beverages processing is a developed industry, with companies producing canned and bottled fruits and vegetables, wine and beer for export. Processing capacities for fruits and vegetables range between 70 to 100,000 tons of vegetables and 30 to 40,000 tons of fruits: 25,000 tons of processed fruits; 30,000 tons of processed vegetables; and 15,000 tons of confectionery products. The annual production of grapes varies from 200,000 to 240,000 tons, out of which approximately 32,000 tons are table grapes and 170,000 to 200,000 tons are wine grapes. The production of wine is carried out in 20 wineries with a total capacity of 220 million liters. Over 90% of the Macedonian wines are exported to the markets of Western Europe.

1.5.8. Tobacco and cigarettes

Tobacco growing and cigarettes production are traditionally important sectors in the Macedonian economy, because of the recognized quality of Macedonian tobacco. They have attracted foreign capital in the process of privatisation and post-privatisation. There are three large cigarette factories in Prilep, Skopje and Kumanovo and over 40 tobacco-processing stations. The annual production capacities for tobacco amount to 30,000 tons, and 20,000 tons for cigarettes. The area under tobacco production in 2002 was over 20,500 ha. Production in 2002 was 22,911 tons.

1.5.9. Tourism

The cultural heritage, combined with a temperate climate and beautiful landscape, makes Macedonia an attractive area with great tourist ambitions to become a top destination for foreign visitors.

Summer and winter tourism: As a continental country influenced by the Mediterranean, Macedonia has great potential for the development of both summer and winter tourism.

Eco-tourism: The unpolluted air, earth and water are a great precondition for the development of eco-tourism, which tops the offers of the main international tour operators.

Cultural tourism: with over 1,000 churches and monasteries, and more than 4,200 archaeological sites, Macedonia intends to be a leader in cultural tourism in Europe.

In terms of tourist opportunities and potential, Macedonia can be divided into five main regions. Winter tourism has

good potential, especially in the **Northwest part of Macedonia** where there are plenty of mountains and mountain peaks that are over 2,000 meters above sea level. The mountains are adequate for the development of winter tourism and sports. They can also be used as recreation centers in the summer. The most famous ski-centers are **Popova Sapka** (Sar Planina) and **Mavrovo National Park** (Bistra) with attractive ski slopes, and places for hiking, walking and ecological tours. These mountains are characterized by an abundance of flowers, forest and rich vegetation, as well as cold and unpolluted water. The mountain lakes, spacious pastures with lush green grass, wild fruits and flocks of sheep make these mountains a holiday destination throughout the year.

Northeast Macedonia is rich in cultural and historical sites and is distinguished by the high concentration of oxygen in the air (eco-tourism). This part is mostly mountainous, but only few of the mountain peaks are higher than 2,000 meters. The center of tourism in this region is the city of Berovo, which is part of a World Bank project on cultural tourism.

Southwest Macedonia is a region famous for its lake tourism. The greatest concentration of tourist facilities is found in this region of the country (the total bed capacity only of Ohrid is 30,732). **Lake Ohrid** (protected by UNESCO) is marked as one of the most beautiful tectonic lakes in the world. The second lake - **Prespa Lake** has endless sandy beaches, especially on its Northern side. This region is less densely populated.

Since 1948, a part of **Baba mountain** has been protected and the **national park "Pelister"** has been founded. Out of the natural tourism values, the most beautiful one is the mountain peak Pelister (2,061 m). The biggest attractions of the park are: the endemic five-needle pine named Molika, the Large and Small glacier lake of Pelister, the rare species of the European lynx, the bearded eagle, etc. More than 88 tree and plant species, as well as 62 animal species, out of a total of 135 that live on the whole territory of Macedonia can be found here.

Southeast Macedonia is a region with a great potential for spa tourism development. Several spa resorts are located in this region, such as Kezovica, Bansko and Negorci Spa. The natural lake of Dojran is also located here, whose waters heal due to the growing algae in it.

Central Macedonia has an excellent geographical position and offers huge opportunities for the development of transit and winter tourism. The main tourist center is the city of Krusevo which is of great historical value to the Macedonian nation.

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Comparative ranking of the tourist potential of Macedonian regions by tourist type

| | Investment opportunities | Places for investment | Infrastructure | Adequate tourism |
|------------------|--------------------------|---------------------------------------|--------------------------------------|------------------------------|
| Northwest | Excellent | Sar planina Mavrovo | Good | Winter, Summer |
| Northeast | Excellent | Berovo Pehcevo Stip | High-scale investment required | Culture, Eco |
| Southwest | Excellent | Struga Ohrid Prespa Baba Mt. | Good | Summer, Culture |
| Southeast | Good | Dojran Gevgelija Banjsko | High-scale investment required | Transit, Spa, All year |
| Central | Excellent | Krusevo | High-scale investment required | Summer, Winter |
| | | Skopje | Good | Convention, All year |

1.5.10. Telecommunications

The country has a well-developed communications network with teledensity of 26.7 lines per 100 inhabitants. The country has direct fiber optic links to the European backbones. The national telecommunications company - Macedonian Telecommunications was privatized in 2001. The new majority owner with 51% of the shares is Matav from Hungary (60% owned by Deutsche Telecom). The exclusivity period for fixed services has ended on 31 December 2004 and privatisation is expected to pave the way for full liberalization of telecommunications. The market for data communication, including Internet access is already fully liberalized.

Macedonian Telecommunications is in possession of the first GSM license in the country through its wholly owned subsidiary MobiMak. For the further liberalization of the GSM mobile phone network, a second license for providing GSM services has been awarded to OTE (Greece), which has started work in June 2003. At present, mobile phone users comprise about 35% of the population.

1.5.11. Energy**Electricity**

At present, Macedonia retains an installed power capacity of 1,444 MW, 30% of which comes from hydropower plants, and provides 6.5 TWh of own annual production. In addition, growing demand is met with more than 20% of imports. Roughly, 700,000 captive customers are connected to the distribution network, while 19% of electricity is consumed by large direct industry customers.

The vertically integrated, state owned power utility "Elektrostanstvo na Makedonija" AD (ESM) provides for the entire generation, transmission, distribution and supply of electricity, for imports and transits, as well as for maintaining the systems operation. It owns the mines for the two

lignite-fired plants, one of which ("Bitola") supplies around 70% of the overall production. The third thermal power plant is oil-fired and at present used mostly as a generation of last resort in the high season. The existing six main hydropower plants are estimated at 17% of the annual electricity production, leaving more than 40% of the hydro potentials available for current and future projects. The transmission system is interconnected on 400 kV to the systems in Greece and Serbia.

After the admission of the "Kozyak" hydropower plant earlier this year, several infrastructure projects are in advanced phases of preparation, such as the new 400 kV interconnections to Bulgaria ("Stip-Cervena Mogila") and Greece ("Bitola-Amindeo"), the "St. Petka" and "Boshkov Most" hydropower plants, and the 190 MW gas-fired cogeneration plant for electricity and heat ("Te-To") to be located in Skopje.

The Energy Regulatory Commission was founded by the Macedonian Parliament in 2003. The main duties of the five regulators are to implement and maintain the licensing system, structure and set prices of the regulated kinds of energy and services, define and monitor conditions, tariffs and mode of access to energy transportation infrastructure, engagement of capacities, etc.

Restructuring of the electricity market in the Republic of Macedonia has been coordinated to the Athens Memoranda 2002 and 2003, and the terms and principles set up in the EU Electricity Directive. The new market model is under consideration and scheduled for the end of 2004 along with the new Laws, Codes and Regulations required.

The process of restructuring and possible privatization of ESM started in early 2001. In 2004 this project resulted in a Law for transformation of ESM brought in April, and a design for the new corporate structure of the electricity industry, scheduled for court registration by the end of the year. The transmission infrastructure will be framed within a separate Transmission System and Market Operator ("MEPSO") company owned and controlled by the state, vis-a-vis the "new" production and distribution company ("ESM") which is foreseen as a subject of possible privatization soon.

Gas supply

The gas sector's current operation is related to the main supply pipeline from Skopje to the Bulgarian border. The industry supplying ring around the city is still under construction. Gas exploitation (currently around 10% of the available capacity) is expanding for the industry, while the wider commercial and household consumption is still in a preparatory stage. Pilot projects for construction of the required gas distribution infrastructure for commercial gas supply in some appropriate city areas, under concession schemes, are in preparation. Additional transportation branches and interconnection directions are considered as well.

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Among the representative projects in this area is the construction of a 190/150 MW gas fired cogeneration thermal power plant for electricity and heat ("Te-To") in Skopje. Along with related domestic industry co-financing and World Bank support, a dominant foreign investor is welcomed to build and operate the plant as an IPP (Independent Power Producer) project.

Another one is the "TAP" project for the construction of a gas transportation pipeline from Bulgaria to Italy. While in principle transiting the territory, this project will also serve to provide a second gas supply corridor for Macedonia. In addition to the Skopje-Thessaloniki crude oil pipeline, which follows Corridor 10 and serves mostly to supply the OKTA refinery, a study was done by a US consortium "AMBO" for construction of a pipeline that will follow the Corridor 8 route. The project would link the port of Bourgas, on the Black Sea coast of Bulgaria, with the port of Vlore, on the Adriatic coast of Albania, to transport oil from the Caspian region to Western Europe and United States refineries.

1.5.12. Information technology

The development and implementation of information technology strategy is a national priority. The IT market in Macedonia was estimated at approximately EUR 50 million in 2002. The software market in Macedonia in 2002 was EUR 15 million. The market for system software is approximately 14%, application software 66% and ERP 20%. There is a 20% growth rate compared to the previous year. The development of the IT industry indicates that the Macedonian market registers continuous growth and the use of the TRADO portal could open up the prospects for worldwide co-operation for Macedonian companies. In Macedonia there are two departments of "St. Cyril and Methodius" University that have programmes providing education and training for IT specialists. Each year, approximately 100 electrical engineers graduate with a major in computer engineering. Another sector operating within the Department of Electrical Engineering is for electronics and telecommunications. Approximately 70 electrical engineers graduate each year with a major in electronics and telecommunications. The Institute of Information Technology operates under the Department of Science and Mathematics. There are two sectors at the Institute: software engineering and theoretical foundation of information technology, generating 50 graduates each year. In addition to academic institutions, there is a number of high schools that offer educational programmes in computer science. There are several major associations of IT companies, such as the Macedonian Association for IT (MASIT). MASIT was established in 2000 as a result of the joint efforts of the managers of 15 leading companies on the Macedonian IT market. The number of members is constantly growing, and now there are 45 active members.

1.6. Foreign investment regime

1.6.1. Legal framework

Foreign investment in the Republic of Macedonia has a national treatment. This is guaranteed by the Constitution.

A foreign person may establish the same types of companies as a national of the Republic of Macedonia. There are no limitations on foreign investment in the Republic of Macedonia, except in the areas of the military industry, circulation and trade of arms, circulation and trade of narcotics, and protection of historical monuments and cultural wealth, regulated in Article 55 of the Constitution of the Republic of Macedonia.

According to the Law on Radio-broadcasting (Official Gazette of RM No. 20/97), foreign individuals or legal entities may participate in the capital of a broadcasting company up to 25%. The share of more than one foreign shareholder may not be higher than 49%.

The Law on Insurance Supervision (Official Gazette of RM No. 27/02, 84/02 and 98/02) stipulates that in an insurance company, the individual share of each shareholder (legal entity, individuals or linked entities / individuals) can go up to 25% of the equity with a right of management. If shareholders are banks or insurance companies there are no limitations in participation of the capital. For acquiring gradually or at a single time a stake of 20%, 33%, 50% or 75% of the shares with a right of management it is necessary to receive approval from the Minister of Finance. Foreign insurance company can open a branch in Macedonia after receiving permission from the Minister of Finance.

The Republic of Macedonia has concluded Agreements for the promotion and protection of investments with the following countries: Albania, Austria, Belarus, Belgium, Bosnia and Herzegovina, Bulgaria, China, Croatia, Czech Republic, Egypt, Finland, France, Germany, Hungary, Iran, Italy, Luxembourg, Malaysia, the Netherlands, Poland, Romania, Russia, Serbia and Montenegro, Slovenia, South Korea, Sweden, Switzerland, Turkey, and Ukraine.

1.6.2. Incentives for foreign investors

The incentives for foreign investors in Macedonia include exemption from customs duties as well as tax breaks, as follows:

- Foreign investors are entitled to a corporate income tax exemption for the period of the first 3 years, starting from the year in which corporate income is realized, on the condition that the taxpayer who has used this exemption is operating at least three subsequent years after the end of the ultimate year in which he has used the right of tax exemption. This is applicable in companies where foreign capital makes at least 20% of total invested capital;
- The tax base is reduced for the amount of the investments in movable and immovable assets, up to EUR

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100,000 in denar counter value, in the current year, excluding cars, furniture, carpets, works of art and other decorations for equipping of administrative offices.

In cases where the taxpayer does not use the tax exemption by the end of the current year, he has the right to transfer it to the next period till its complete use.

For the amount of the investments in movable and immovable assets exceeding EUR 100,000 in denar counter value, in the current year, excluding cars, furniture, carpets, works of art and other decorations for equipping administrative offices, the tax base is reduced up to 30%, but not more than the remaining unused part of the investment.

- The taxpayer who makes technological modernization, or purchases assets for protection of the environment and nature, has a right to accelerated depreciation of the fixed assets, but to the maximum value that exceeds by 25% the depreciation calculated by one of the methods of depreciation calculations.
- To the taxpayer that placed an investment in economically underdeveloped regions and in specific areas (hill-mountain regions, border regions and compact undeveloped regions), the tax base is reduced for the value of the invested funds, but maximum 50% of the base.
- The taxpayer who is a beneficiary of a free economic zone is exempt from corporate income tax for a period of 10 years starting from the date of initial operation in the free economic zone, under conditions and procedure stipulated by the Law for Free Economic Zones.
- To the taxpayer the tax base is reduced up to the value of the funds invested for protection of the environment and the nature (the amount invested for this purpose is acknowledged 100%).
- To the taxpayer who starts business activity for the first time, in the first year of earning corporate income the estimated tax is reduced by 50%, under condition of continued operation at least for three additional years from the day of implementing the reduction. Otherwise, he is due for the unpaid tax in amount revaluated by the retail price growth rate. A taxpayer who has made status changes (merger, acquisition, division, ownership transformation or similar) is not considered as a taxpayer who starts business activity for the first time.
- Corporate income tax is reduced for 50% for the taxpayer who is listed on the stock exchange in Macedonia, three years after the start of the listing. This tax reduction will be implemented until 31 December, 2005. Also, there is no capital gain tax for all securities transactions by the end of 2005; and there is no taxation on securities transactions.
- To the taxpayer who, pursuant to the Law on Registration of Cash Payments is obliged to introduce and use an

approved system of equipment for registration of cash payments, the estimated tax is reduced for the value of a maximum of 10 fiscal machines. If the taxpayer does not use the tax exemption by the end of the current year, they have a right to transfer it for the next period.

- Losses due to financial, business and non-business transactions may be compensated with the corporate income in the future reporting periods, but to a maximum of 3 years following the year in which they were registered. This right may not be used in the case of status changes of the taxpayer related to merger, acquisition, division, ownership transformation or similar.
- The capital gains from the sale of securities, equipment and immovables are included to the tax base in amount of 70%. The capital gains from securities will not be subject to taxation until 1 January, 2006, in order to contribute to the development of the securities market in the Republic of Macedonia.
- The dividends from participation in the capital of other companies are exempt from taxation under condition that they have been taxed by the taxpayer who makes a payment, according to the general rate of the Corporate Income Tax Law.
- For transfer of part of the corporate income earned by a foreign entity, corporate income tax is not paid for the amount which is transferred.

1.6.3. Property rights

Foreign persons may acquire ownership of buildings and other immovable assets for the purpose of business. They can become owners of apartments and apartment buildings, but may not acquire ownership right over construction land.

1.7. Small and medium-sized enterprises

The categories under the SME law in Macedonia differ from those applied in the EU due to the scale of the country's economy. In 2003 the number of active companies in Macedonia was 39,199, employing 262,728 people. Of this, 98.4% are small companies (10-49 employees), employing 42% of the work force, and 1.66% are medium and large sized companies employing 58% of the total.

SME national support policies

The strategic framework for support of the SME development is defined by the following documents: Small Business Development Strategy, Programme of measures and activities for the promotion of entrepreneurship and creation of competitiveness of the SMEs in Macedonia, European Charter for Small Enterprises, Law on Realization of Handicraft Activities, Law on the Agency for Promotion of Entrepreneurship of the Republic of Macedonia (APERM).

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For achieving a higher degree of coordination among the relevant bodies the National Council for Competitiveness and Entrepreneurship has been founded as an advisory body to the Government linking private and public sector for improvement of the climate for the development of entrepreneurship.

The Law on the Agency for Promotion of Entrepreneurship of the Republic of Macedonia was enacted by the Parliament in September 2003. According to it, SMEs are defined as:

1. Enterprises that have fewer than 50 employees, have an annual turnover not exceeding EUR 1.5 million or a total balance not exceeding EUR 1.1 million, are independent companies and are at least 51% privately owned;
2. Individual entrepreneurs;
3. Craftsmen;
4. Other service providers.

1.8. Public Investment Programme

The Public Investment Programme of Macedonia (PIP) for the period 2004-2006, includes investment projects which in accordance with the government priorities have a major contribution to the sector development. The PIP consists of 143 investment projects. The total cost of these projects is estimated at EUR 2,075.73 million. A part of the projects, valued at EUR 634.04 million was executed by the end of 2003. The fulfillment of certain activities, estimated at EUR 607.84 million, will be shifted beyond 2006.

PIP costs by sectors, 2004-2006, EUR mln

| Sector | 2004 | 2005 | 2006 | Total |
|-----------------------------|---------------|---------------|---------------|---------------|
| Energy | 63.43 | 45.22 | 36.22 | 144.87 |
| Transport | 94.64 | 98.68 | 92.71 | 286.03 |
| Water supply and irrigation | 18.33 | 26.17 | 22.85 | 67.35 |
| Communal Services & housing | 36.31 | 41.85 | 13.71 | 91.87 |
| Environment | 11.36 | 13.73 | 13.24 | 38.33 |
| Other sectors of economy | 5.03 | 5.06 | 5.09 | 15.18 |
| Education and science | 8.39 | 34.95 | 34.46 | 77.80 |
| Health | 7.93 | 1.93 | 1.93 | 11.79 |
| Non economic sectors | 26.85 | 35.71 | 37.73 | 100.29 |
| Total | 272.27 | 303.30 | 257.94 | 833.51 |

Source: Public Investment Programme of RM 2004-2006, Ministry of Finance, March 2004

Under PIP, an amount of EUR 643.63 million or 77.2% of the total costs planned will be allocated for economy infrastructure development, while EUR 189.88 million or 22.8% will be allocated for human resources development.

II. Establishing business in Macedonia

2.1. Forms of business and corporate governance

| | |
|----------------------------------|--|
| Company Regime | Legal Framework: Law on Trading Companies (Official Gazette of RM No.28/30 April 2004) |
| Types of companies | Sole proprietorship "Trgovac poedinec"; General partnership "Javno Trgovsko Društvo" (JTD); Limited partnership "Komanditno društvo" (KD); Limited liability company "Društvo so Ogranicena Odgovornost" (DOO); Joint-stock company "Akcionersko Društvo" (AD); Limited partnership by shares "Komanditno društvo so Akcii" (KDA) |
| Partnerships | Partners: 2 or more partners - domestic or foreign legal entities or individuals Characteristics: The general partnership is an association of two or more legal entities or individuals who bear joint and unlimited liability by their entire property towards the creditors. In a limited partnership where two or more persons are associated, at least one of them is liable for the limited partnership's obligations by his entire property (komplementar: general partner); at least one of them is liable for the limited partnership's obligations to the amount of the entered/registered investments in the limited partnership (komanditor: limited partner). There are no citizenship requirements to the shareholders. |
| Limited Liability Company | Members: From 1 to 50. If the whole capital belongs only to one member there is a single person limited liability company "Društvo so Ogranicena Odgovornost osnovano od Edno Lice" (DOOEL) Minimum capital: Denar equivalence of EUR 5000 Share and contribution requirements: The minimum contribution of each member shall not be less than the denar equivalence of EUR 100. At registration at least the denar equivalence of EUR 2,500 of the capital and 1/3 of each shareholder's cash contribution must be paid in. Contributions in kind must be fully contributed at registration. Company governance: The Meeting of the members is the decision making body of the company. It must be convened at least once a year. The members vote proportionally to their contribution unless otherwise agreed in the agreement of incorporation. One or more managers are appointed by the members for a period stipulated in the agreement of incorporation. If such a period is not determined the managers are considered elected for four years. There are no citizenship requirements for the managers. Supervisory bodies: Establishment of a Supervisory Board or appointing a controller is an option for the company. |
| Joint-Stock Company | Shareholders: 1 or more individuals or legal entities could found a JSC. Minimum capital: Denar equivalence of EUR 25,000 for companies incorporated simultaneously (without public call) and Denar equivalence of EUR 50,000 for companies incorporated successively (through public call) |

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| | |
|------------------------------|---|
| | <p>Share and contribution requirements: The nominal value of each share shall not be less than the Denar equivalence of EUR 1. The shares are freely transferable. At least 25% of the nominal amount of each share must be contributed at registration. The total amount of all payments in cash should not be less than EUR 12,500 or EUR 25,000. Multiple-vote shares are prohibited. Convertible bonds and other securities and financial derivatives can be issued.</p> <p>Company governance: The governance of the company may be organized as a one-tier system (Board of Directors) or two-tier system (Management Board or a manager & Supervisory Board). The General Meeting of shareholders takes decisions by a majority vote of the represented share capital, except in certain cases when super majority is needed. Pursuant to the one tier management system, the General Meeting appoints a Board of Directors with 3 to 15 members. The number of the non-executive members shall be higher than the number of the executive members. Legal entities may only be non-executive members. The board of directors elects a President among the non-executive members. According to the two-tier management system, the general meeting appoints Supervisory Board consisting of 3 to 11 members. The supervisory Board appoints the managing board with 3 to 11 members.</p> <p>Specific Feature: Bearer shares are not regulated by the Macedonian legislation.</p> |
| Branches | Foreign companies existing in their home country for at least 2 years can establish branches in the Republic of Macedonia. Branches have the right to carry out all forms of business and commercial operations and operate under the same conditions as domestic companies, which carry out the same of related forms of business. |
| Representative office | Can be opened by foreign companies, which are carrying out non-income generating activities, such as advertising or market research on behalf of their parent company. Representative offices cannot carry out commercial operations or act on behalf of any company other than their parent company. |
| Bankruptcy | Legal framework: Bankruptcy Law (Official Gazette of RM No. 55/97,53/00, 37/00) |
| Anti-Trust Rules | Legal framework: Law Against Limiting Competition (Official Gazette of RM No. 80/99) |

2.2. Labour force and employment regulations

2.2.1. Labour availability, employment and level of education

In 2003 the total labour force was 860,976 people, out of which 545,108 were employed, 315,868 unemployed, and 714,474 inactive persons. From the total number of employed people, 54.4% were employed in the private sector. The level of unemployment for 2003 was 36.7%.

Population in the Republic of Macedonia by economic activity

| Year | Total labour force | Employed persons | Unemployed persons | Inactive persons |
|------|--------------------|------------------|--------------------|------------------|
| 2000 | 811,557 | 549,846 | 261,711 | 722,699 |
| 2001 | 862,504 | 599,308 | 263,196 | 691,916 |
| 2002 | 824,824 | 561,341 | 263,483 | 742,129 |
| 2003 | 860,976 | 545,108 | 315,868 | 714,474 |

Source: State Statistical Office

Schools, pupils, students and teachers (2000-2003)

| School year | 2000/2001 | 2001/2002 | 2002/2003 |
|-----------------------------|-----------|-----------|-----------|
| Elementary education | | | |
| schools | 1,010 | 1,010 | 1,020 |
| pupils | 246,490 | 242,707 | 235,516 |
| Secondary education | | | |
| schools | 95 | 95 | 95 |
| pupils | 90,990 | 92,068 | 93,526 |
| Higher education | | | |
| schools | 2 | 1 | 1 |
| pupils | 840 | 1,123 | 893 |
| University education | | | |
| schools | 29 | 29 | 29 |
| pupils | 39,406 | 43,587 | 44,731 |
| teachers | 1,437 | 1,501 | 1,487 |

Source: State Statistical Office

Population by economic activity and level of education (2003)

| Level of education | Total population | Total labour force | Employed | Unemployed |
|----------------------------------|------------------|--------------------|--------------|--------------|
| Without education % | 3.8 | 1.2 | 1.2 | 1.2 |
| Incomplete primary education % | 10.8 | 5.8 | 6.1 | 5.3 |
| Primary education % | 34.8 | 27.3 | 22.4 | 35.6 |
| 3 years of secondary education % | 10.6 | 13.9 | 12.9 | 15.5 |
| 4 years of secondary education % | 29.4 | 36.7 | 38.1 | 34.3 |
| Higher education % | 3.2 | 4.4 | 5.6 | 2.4 |
| University level education % | 7.3 | 10.8 | 13.8 | 5.6 |
| Total in '000 | 1,579.5 | 861.0 | 545.1 | 315.9 |

Source: State Statistical Office

2.2.2. Labour legislation

The employment and labour relations are regulated by the Labour Law (Official Gazette of the RM No.80/93), the Collective Agreements and other legal acts. Collective agreements regulate employment rights, obligations and responsibilities of the employees and employers, in compliance with the law and other regulations. Collective agreements are concluded at country level. They can be concluded as branch agreements or as agreements with the employers on the level of the Republic. The leading trade union organization of the employees concludes a general collective agreement pertaining to employees and employers. This general collective agreement pertains to public services, public enterprises, government agencies, organs of the local self-government and other legal entities render-

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ing non-commercial activities.

Employment may commence for a period of time that has not been previously determined (full time employment). Also the employment may commence for a period of time that has been previously determined (part time employment), particularly in the following instances:

- seasonal work, for a maximum of 9 months in the course of one calendar year;
- increased scope of work, for a maximum of six months in the course of one calendar year;
- replacement of an absent worker, during the period of absence and
- work on a particular project, until the completion of the project.

Employees that have part time employment are entitled to the same rights and obligations as full time employees.

The salaries of employees rendering full working hours cannot be less than the lowest salary, which is determined for particular levels of work complexity, according to law or the respective collective agreement. Contributions and taxes on employees salaries are paid by employers together with the payment of salaries.

Employment can be terminated in the following instances:

- through agreement
- on expiry of the term of employment
- when enforced by law
- through notice and
- due to economic, technological, structural or similar transformations.

The public institution - Agency for employment, keeps record of unemployed persons, realizes preparatory training for employees, has active policy for employment, intermediates in employment and provides rights in the unemployment period.

2.2.3. Employment of foreign nationals

The law on Establishment of Employment Relations with Foreign Persons (National Gazette of SFRY No. 11/78 and 64/89) regulates the employment of foreign persons in Macedonia. According to the provisions of the Law, foreign persons, or persons without nationality, can be employed in Macedonia upon obtaining a work permit. The work permit is issued by the Employment Bureau of the Republic of Macedonia upon the employer's request.

2.3. Foreign exchange regulations

The foreign exchange regime is regulated by the Foreign Exchange Law (Official Gazette of RM No. 34/2001, last amendments 51/03) and accompanying regulations. According to this Law, payments to or from foreign countries are performed by banks authorized for foreign transaction by the National Bank of the Republic of Macedonia (Central Bank). Payments on behalf of and for the account of the Republic of Macedonia are carried out by the Central Bank.

All transactions that take place in Macedonia should be made in Macedonian Denars. Resident and non-resident companies and individuals may keep accounts in commercial banks in foreign exchange. There are no restrictions on the current account payments. Corporate incomes and dividends from inward investments can be freely transferred abroad, after meeting all tax obligations.

All nonresidents may open foreign exchange accounts with domestic banks authorised for foreign exchange transactions upon proof of identity. Nonresidents may operate accounts without restrictions, cash withdrawals are limited up to EUR 10,000 per month and for cash deposits above EUR 2,000 certificate from the Customs authorities is required.

Nonresident-diplomatic representatives of the foreign countries or international institutions may operate accounts without restrictions and no limitation is imposed.

Exports and imports of Denars are limited to MKD 20,000.

- Residents can freely export foreign currency banknotes and cheques up to EUR 2,000, and import up to EUR 10,000 without document. For export of foreign currency banknotes and cheques up to EUR 4,000, a document issued by an exchange bureau or a bank is needed. Export exceeding EUR 4,000 is not allowed. For import of foreign currency banknotes and cheques exceeding EUR 10,000, the rules for preventing money laundering apply.
- Nonresidents can freely export and import foreign currency banknotes and cheques. For export and import of up to EUR 2,000 there are no declaration requirements to the Custom authorities. Imports exceeding EUR 2,000 must be declared upon arrival in the country to the Custom authorities, and for export exceeding EUR 2,000 the document received upon arrival must be submitted to the Custom authorities .

Rules for preventing money laundering apply.

Non-residents are required to register the investment and all subsequent modifications thereof in the Ministry of Economy within 60 days. Registered foreign investments are protected from nationalization.

2.4. Legislative framework of concessions

Granting of concessions in general is regulated by the Law on concessions (Official Gazette of RM No. 25/02), and additional conditions are regulated with respective laws like: granting concessions for agricultural land is regulated in The Law on Agricultural Land, granting concessions for operating telephone networks is regulated in the Law on Telecommunications, granting concessions for broadcasting activity is regulated in the Broadcasting Act etc. According to the Law, concession may be given to domestic or foreign legal entities and individuals registered in Trade Register of the Republic of Macedonia.

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2.5. Legislative framework of public procurement

The new Public Procurement Law (Official Gazette of the Republic of Macedonia No.19/2004) is harmonized with the EU legislative. This law regulates the activities in the procedure for performing public procurements by: government bodies and bodies of local government units; legal entities established for specific purpose for meeting public interest needs, public enterprises, joint stock companies and limited liability companies in which the state or local government units have dominant ownership, civic associations and foundations to which the law grants public authorizations.

The provisions of the Law shall not apply to public procurement of items concerning state defense and security, and to public procurement for which funds have been provided by international organizations (donors and lenders).

The provisions of the law do not refer to procurement of:

- purchase or rental of land, buildings, or other real estate or rights deriving therefrom, except when provisioning of funds for their purchase or rental is needed (credits and loans)
- financial services related to issue, sale, purchase or transfer of securities or other financial instruments, brokerage services and services rendered by NBRM
- purchase, development, production or co-production of program materials by radio or TV broadcasters and for broadcasting period of TV and radio programs
- services for voice telephony, telex, radio telephony, paging and satellite services
- employment mediation services
- R&D services, except in cases when the research is used by the procurer for commercial purposes

A main principle of the law is providing fair competition, equal and non-discriminatory position of bidders and transparency during public procurement. The procurer must not discriminate in the sense of the nationality of bidders, or country of origin of goods.

A bidder can be any domestic or foreign legal entity or physical person - supplier or provider of goods, services or works that submits a bid. Public procurement is performed via the following procedures:

- Open invitation for bids
- Restricted invitation for bids
- Negotiated procedure
- Design contest and
- Restricted invitation for consultant services.

2.6. Dispute resolution mechanisms

Domestic sources of the Macedonian Arbitrary Law include the Constitution of the Republic of Macedonia, the Litigation Procedure Law (Official Paper of SFRY, No. 4/77), the Law on Disputes Settlement (Official Paper of SFRY, No. 43/82), concerning the laws and regulations of other countries in certain relations and the Macedonian Law on Trading

Companies. Within the Chamber of Commerce since 1993 there has existed Arbitration - Permanent Elected Court. From its establishment until today, there have been 24 requests submitted for conducting an arbitration procedure, from of which 3 cases relate to domestic legal entities, and the rest of the cases relate to disputes with foreign entities.

Macedonia has signed a number of bilateral and multilateral conventions, some of them inherited from former Yugoslavia on the basis of succession. Macedonia is a party to the New York Convention on Recognition and Enforcement of Foreign Arbitral Awards as well as the Geneva Convention on Execution of Foreign Arbitral Awards. Macedonia is also a party to the Washington Convention on the Settlement of Investment Disputes Between States and Nationals of Other States and the European Convention on International Commercial Arbitration. Ratified international agreements have preference over domestic legislation.

A new Law on International Commercial Arbitration is prepared undertaking UNCITRAL model and is in governmental procedure. This law regulates the Arbitrary establishments and the procedure in more precise manner.

2.7. Operational costs (2004)

| | |
|--|--|
| Nominal salary growth %, June 2004/June 2003 | 4.1 |
| Corporate income tax %, 2004 | 15 |
| VAT %, 2004 | 18 (5) |
| Office rent (2004), EUR per sq m/month | 5-35 |
| Office purchase price (2004), EUR per sq m | 500-4,000 |
| Price of land | |
| Agricultural land, (2004), EUR per sq m | 0.5-1 |
| Industrial land, (2004), EUR per sq m | 5-50 |
| Water charges for corporate clients incl. sewage, 2004, including 5%VAT, EUR per cubic m | 0.57 |
| Water charges for household use incl. sewage, (2004), including 5% VAT, EUR per cubic m | 0.25 |
| Telephone installation charge, VAT not included, (2004), EUR | PSTN: 20; ISDN: 60 |
| Monthly telephone subscription fee, VAT not included, (2004), EUR | PSTN: residential - 3.58-7.37; business - 11.38 ISDN: residential - 10.6; business - 15.4 |
| Telephone transfer charge, VAT not included, (2004), EUR | private and business - 20.45 |
| International phone call from Macedonia per 1 min, 18% VAT not included, (2004), EUR | 0.25-1 depending on the world zone |
| Electricity prices per kWh including VAT, (2004), EUR | |
| Industrial use | 0.07 |
| Household use, 2 tariff reading | |
| Expensive tariff | 0.04 |
| Cheap tariff | 0.02 |

Note: The Average monthly gross salary is EUR 200 as of June 2004.

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III. Taxation

3.1. Direct taxation

3.1.1. Corporate income tax (CIT)

| | |
|---|---|
| Legal framework | Corporate Income Tax Law |
| Taxpayer | The taxpayer of corporate income tax is a legal entity performing registered activity - resident of the Republic of Macedonia and earning a corporate income from an activity in the country or abroad. The resident is an established entity or has a head office on the territory of the Republic of Macedonia. The taxpayer is also a legal entity that is not a resident of the Republic of Macedonia, for corporate incomes earned through performing his activity on the territory of the Republic of Macedonia. |
| Tax base | The basis for computation of corporate income tax is the corporate income determined in the tax balance. The corporate income represents the difference between the total income and total expenditures of the taxpayer, in amount determined by accounting rules and standards. |
| Tax rate | 15% |
| Investment relief | The tax base of the taxpayer is decreased by the amount of his current investment in fixed assets undertaken so as to broaden the scope of his activities, but no such decrease occurs if funds are invested in cars, furniture, carpets, pieces of figurative and applied art and other decorative objects used to equip offices. The decrease must not exceed 25% of the tax base. The taxpayer is entitled to accelerated depreciation of fixed assets in cases of technological renovation or if he procures means for environmental protection, up to 25% over the depreciation. The tax base is reduced in the following cases as well: <ul style="list-style-type: none"> • The tax base of the taxpayer who has used his corporate income to invest in economically underdeveloped regions and in specific regions (mountainous areas, border belts and completely underdeveloped regions) is reduced by the amount of his investments. The decrease must not exceed 50% of the tax base. • The tax base of the taxpayer shall be reduced in amount of the funds invested in environment protection purposes. |
| Tax exemption | The taxpayer, resident of the Republic of Macedonia, who has paid tax in a foreign country on the corporate income earned through work abroad, is entitled to reduced taxation in the country, to the amount of the corporate income tax paid abroad, and not exceeding the anticipated tax by application of the tax rate of 15%. |
| Tax holiday for foreign investment | The tax base for companies with foreign shareholders (with holdings of at least 20%) is reduced by the proportion of the foreign investment, for the first three years following that investment. For example the tax rate for a company with a foreign shareholder of 60% is $15 \times (100\% - 60\%) = 6\%$. Therefore, 100%-owned subsidiaries of foreign companies pay no tax during the first three years of operation. There is no tax on the transferred corporate income. |
| Capital gains and tax losses | Capital gains realized from the sale of securities, equipment and real estate is included in the tax base in the amount up to 70%. Capital gains derived from securities will not be taxed by January 1, 2006 in order to contribute to the development of the securities market in the Republic of Macedonia. Tax losses can be carried forward up to 3 years. |

3.1.2. Personal income tax

Personal income tax is paid annually on the taxpayer's worldwide income from different sources. The following types of revenues earned in the country and abroad are included in the income according to which the tax base is determined: wages and salaries, income from agriculture, income from independent activity, income from property and property rights, income from copyrights and industrial property rights, capital revenues, capital gains, gains from games of chance and other prize games, and other revenues.

| | |
|------------------------------|---|
| Taxpayer | A taxpayer is any individual who is a resident of the Republic of Macedonia, for the income earned in the country and abroad. A resident is any individual who has permanent or usual place of residence on the territory of the Republic of Macedonia, or individual that resides continually on the territory of the Republic of Macedonia for at least six months. Taxpayer is also a non-resident individual for the income earned on the territory of the Republic of Macedonia. |
| Tax base | Tax base is the positive difference between the gross income of the taxpayer and deductions provided with the Personal Income Tax Law such as: contributions for pension and disability insurance, health insurance and employment, contributions for the voluntary pension and disability insurance, personal allowance which for 2003 amounts to 2,680 denars monthly or 32,160 denars annually, and other expenses. |
| Tax rate | The tax rates are progressive. 15% is applied to annual income up to 360,000 Denars, and 18% is applied for the income over 360,000 Denars. |
| Payroll contributions | Payroll contributions are payable by the employer, i.e. by the company, at the time of payment of the payroll. Employers are obliged to pay compulsory social contributions on the gross salary as follows: <ul style="list-style-type: none"> • 21.2% - pension and disability insurance • 9.2% - health insurance • 1.6% - employment |
| Withholding Taxes | Individuals pay personal income tax (withholding tax) on the following revenues: <ul style="list-style-type: none"> • Personal income from the employment, pensions, income of the members of the management and supervisory boards in the enterprises, and other types of revenues; • Income from royalties and royalties from industrial ownership; • Income from property and property rights if the payer of the income is a legal entity; • Gains from games of chances and other prize games; • Dividend distributions to individuals; • On the incomes from the interests of the savings deposits, current accounts and sights deposits the tax should not be paid, while the interests on the long-term savings deposits are tax free until 2006. |

3.1.3. Withholding tax rates under double tax treaties with Macedonia

| Country | Direct dividends % | Portfolio dividends % | Interest % | Royalties % |
|--------------|--------------------|-----------------------|------------|-------------|
| Albania | 10 | 10 | 10 | 10 |
| Bulgaria | 5 | 15 | 10 | 10 |
| China | 5 | 5 | 10 | 10 |
| China-Taiwan | 10 | 10 | 10 | 10 |
| Croatia | 5 | 15 | 10 | 10 |
| Czech Rep. | 5 | 15 | 0 | 10 |
| Denmark | 5 | 15 | 0 | 10 |
| Egypt | 10 | 10 | 10 | 10 |

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| | | | | |
|-----------------------|----|----|----|----|
| Finland | 0 | 15 | 10 | 0 |
| France | 0 | 15 | 0 | 0 |
| Hungary | 5 | 15 | 0 | 0 |
| Iran | 10 | 10 | 10 | 10 |
| Italy | 5 | 15 | 10 | 0 |
| Netherlands | 15 | 15 | 0 | 0 |
| Poland | 5 | 15 | 10 | 10 |
| Romania | 5 | 5 | 10 | 10 |
| Russia | 10 | 10 | 10 | 10 |
| Serbia and Montenegro | 5 | 15 | 10 | 10 |
| Slovenia | 5 | 15 | 10 | 10 |
| Sweden | 0 | 15 | 10 | 0 |
| Switzerland | 5 | 15 | 10 | 0 |
| Turkey | 5 | 10 | 10 | 10 |
| Ukraine | 5 | 15 | 10 | 10 |

Treaties with Germany, Belorussia and Spain have been concluded but not ratified yet.

3.1.4. Property tax

The main element of the Law on Property Tax relates to the ownership of property. It also deals with tax on inheritance and gifts and the sale of property and property rights. Liability to property tax arises from the ownership of non-agricultural land, buildings or flats, business premises, administrative buildings, garages, etc.; moveable property such as cars with more than 1.8 cc, buses, trucks, tractors, etc. if the assets are not used for business purposes. Land and buildings are taxed on their market value at an annual rate of 0.1%, which is applicable to movable property as well. The Law provides for exceptions depending on the type and the purpose of the property (e.g. agricultural land).

Tax rate on the sale of property and property rights is 3% and for the tax on inheritance and gifts by relatives of direct lineage up to the second degree is 3%, while by relatives of direct lineage up to the third degree or for a taxpayer not in a relative correlation is 5%.

3.2. Indirect taxation

3.2.1. Value added tax (VAT)

| | |
|----------------------------|--|
| Legal framework | Law on Value Added Tax |
| Subject of taxation | Turnover of goods and services, affected with compensation by the taxpayer in the scope of his business; import of goods. |
| Taxpayer | An individual, who, permanently or temporarily, self-performs a business activity, independent of the aims and results of this activity. |
| Tax base | The total amount of the compensation that is received, or that should be received for the turnover, in which the VAT is not included. The tax base for import of goods is the value of the imported goods, determined on the basis of customs provisions. |

| | |
|---|--|
| Tax exemption | The following is exempt from value added tax without the right for deduction of the previous tax: <ul style="list-style-type: none"> • turnover with residential buildings and apartments, in that part in which they are used for residential purposes, with the exception of the first turnover that will be effected within the period of five years after building or construction; • rental of residential objects and apartments, if they are used for residential purposes; • turnover of banking and financial services; • services for insurance and re-insurance, including the connected services of insurance brokers and agents that are connected with them; • lottery games and entertainment games; • services of radio and television broadcasting stations, except commercial activities; • international transport of passengers, etc. |
| | The following goods and services are VAT exempt with the right of deduction of the tax: <ul style="list-style-type: none"> • deliveries of goods that are transported or shipped abroad by the tax payer, recipient of goods or third person on their order, if the recipient of goods has a seat abroad; • turnover of goods that are transported or shipped from the country into free zones, customs zones or customs warehouses; • performing of services by brokers and other mediators that act on behalf and for the account of other person; • turnover of gold and other precious metals towards central banks; • international air transport of passengers. This tax release is valid for airway companies with a seat abroad, only in case of reciprocity, etc. <p>The following goods are exempt from value added tax, upon import:</p> <ul style="list-style-type: none"> • goods, the turnover of which is released from value added tax in the country in compliance with articles of this Law; • goods that are encompassed with the regime of goods in transit; • goods that fall under the regime for temporarily imported goods and goods for re-export; • goods that are imported from the side of a foreign diplomatic or consular representative office for business needs; • goods that are imported by international organizations and their members, under conditions and limits determined with international agreements; • goods intended for exhibits on fairs and trade exhibitions that will afterwards be exported, etc. |
| Tax rates | 18% general rate and a 5% preferential rate |
| Taxation period and calculation period | VAT is paid during the year as an advance payment, and after expiry of one-year taxation period, when the tax for payment is finally determined. If the taxpayer performed business activities in one part of the calendar year, only that period shall be estimated as taxation period. The calculation period for which advance payments are calculated and paid is one month. |

3.2.2. Excise duties

Excise duties are regulated by the Excise Duty Law of 1 July 2001, which aims to support the establishment of a new system of indirect taxation. Currently, excise duties are levied on the consumption of certain goods, such as oil derivatives, tobacco products and alcoholic drinks.

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Useful links - Governmental Bodies:

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|---|---|
| Government of the Republic of Macedonia | www.gov.mk |
| Ministry of Economy | www.economy.gov.mk |
| Ministry of Finance | www.finance.gov.mk |
| Ministry of Agriculture, Forestry and Water | www.mzsv.gov.mk |
| Ministry of Transport and Communications | www.dtk.gov.mk |
| Ministry for Foreign Affairs | www.mnr.gov.mk |
| Ministry of Environment and Physical Planning | www.moe.gov.mk |
| Ministry of Labour and Social Policy | www.mtsp.gov.mk |
| Ministry of Education and Science | www.mon.gov.mk |
| Macedonian National Bank | www.nbrm.gov.mk |
| Macedonian Stock Exchange | www.mse.com.mk |
| State Statistical Office | www.stat.gov.mk |
| Macedonian Privatization Agency | www.mpa.org.mk |
| Agency for Entrepreneurship | www.apprm.org.mk |
| Macedonian Economic Chamber | www.mchamber.org.mk |
| Macedonian Information Agency | www.mia.com.mk |
| General Information and Links | www.macedonia.org |
| Business Catalogue | www.unet.com.mk/mbc |
| The Macedonian directory | http://directory.macedonia.org |