Impact of global economic crisis on the economies of Western Balkan (Macedonian economy)

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Abstract

The paper intends to analyze the impact of global economic crisis on the economies of Western Balkan (Macedonian economy). The purpose of the paper is not to analyze the global crisis impact on specific sectors of the economies of the Western Balkan Countries, indeed, it focuses mainly on the macroeconomic level, identifying and analyzing fluctuations of major macroeconomic indicators of the economies of this Region. In this regard the paper analyzes the trends of macroeconomics indicators that reflect the development and macroeconomic balances of those economies, such as GDP, the level of employment, inflation, budget deficit, trade relation, etc, in two periods of time: before the crisis, and during the years of crisis. Highlighting the deterioration of these indicators, the paper tries to identify factors that have contributed to these results, for example the level of opening of the economies of these countries, foreign direct investment, remittances, etc.

This paper basically discuss the financial crisis and impact of financial crisis in Balkan. There is a fear that his economic crisis will take hold of Europe if it is not controlled. Europe is one of the biggest economies of the world so almost all the countries over the globe are also having a threat of facing the financial crisis. The world financial crisis emerged from a property bubble and a credit boom. Bad debts soared and banking sector in the developed economies became insolvent. The implication of the crisis to the western Balkans has been not of a sort of financial crisis, but an economic turbulence which has occurred as a result of lack of demand in the world markets to the Western Balkan products and falling sources of finance.

Investments, remittances, industrial production, foreign exchange reserves and employment rates have fallen

Abstrakt

Nëpërmjet këtij punimi synohet një analizë e ndikimit të krizës ekonomike globale mbi ekonomitë e Ballkanit Perëndimor me theks të veçantë në ekonominë e Maqedonisë. Qëllimi i punimit nuk është të analizojë ndikimin e krizës botërore në sektorë të veçantë në ekonomitë të vendeve të Ballkanit Perëndimor, por fokusohet kryesisht në nivel makroekonomik, në identifikimin dhe analizën e luhatjeve të treguesve kryesorë makroekonomikë të ekonomive të këtij rajoni. Në këtë punim analizohen trendet e treguesve makroekonomikë që reflektojnë në ekuilibrat makroekonomikë dhe të zhvillimeve ekonomike, siç janë: PBB-së, niveli i punësimit, inflacioni, deficiti buxhetor, marrëdhëniet tregtare, etj. në dy periudha kohore: para krizës dhe gjatë viteve të krizës.

Duke theksuar përkeqësimin e këtyre indikatorëve nëpërmjet punimit bëhet përpjekje të identifikohen disa faktorë që kanë kontribuar në këto rezultate, për shembull niveli i hapjes së ekonomive të këtyre vendeve, investimet e huaja të drejtpërdrejta, dërgesat etj.

Ky punim gjithashtu flet edhe për krizën financiare dhe ndikimin e saj në Ballkan. Ekziston frika se kriza ekonomike do të marrë kahe të ndikimit në shumë vende të Evropës, nëse nuk kontrollohet me kujdes. Si në të gjitha vendet e globit, edhe ekonomia evropiane nuk mundë të anashkalohet nga kriza financiare. Kjo krizë që u shfaq nga një flluskë e pasurisë dhe një bum krediti, pati si rrjedhojë borxhet e këqija , të cilat u rritën dhe ndikuan keq në sektorin bankar të ekonomive

të zhvilluara. Kështu u humb aftësia për t'i paguar ato. Implikimi i krizës në Ballkanin Perëndimor nuk ka qenë i një lloji të krizës financiare, por çrregullimi ekonomik që ka ndodhur është si pasojë e mungesës së kërkesës në tregjet botërore të produkteve të Ballkanit perëndimor dhe e rënies së burimeve financiare, investimeve, dërgesave të prodhimit industrial, rezervave valutore e, gjithashtu, edhe e normave të punësimit të cilat kanë pësuar një rënie të dukshme.

Апстракт

Во овој труд се анализира влијанието на глобалната економска криза врз економиите на земјите од Западен Балкан со посебен акцент врз македонската економија. Целта на трудот не е анализата на влијанието на кризата во посебните сектори туку се фокусира во главно врз влијанието на кризата на макроекономско ниво, во економите на земјите од регионот. Се анализираат макроекономските индикатори кои се рефлектираат врз развојот и макроекономскиот баланс на тие економии, како што се БДП, стапката на вработување, инфлацијата, буџетскиот дефицит, трговските односи, во два периоди: пред и за време на кризата.

Нагласувајќи го влошувањето на овие индикатори преку трудот се обидувам да ги идентификувам факторите кои придонесоа за овие резултати, на пример нивото на отвореност на економиите на овие земји, странските директни инвестиции, дознаките од странство итн.

Во овој труд, исто така, се дискутира за финансиската криза и влијанието на финансиската криза на Балканот. Постојат стравувања дека доколку не се контролира кризата ќе има влијание во многу земји на Европа. Европа е една од најголемите економии во светот и исто како и на сите земји на светот постои закана да се соочи со финансиската криза. Глобалната финансиска криза се појави од шпекулации со недвижнини и кредитен бум. Лошите долгови се зголемуваа и банките не беа способни за да ги наплатат долговите. Импликациите на кризата во земјите од Западен Балкан не е вид на финансиска криза, но економско безредие кое се случи поради недостаток на побарувачката на светските пазари за производите од Западен Балкан и пад на инвестициите, индустриското производство, стапката на вработеност и девизните резерви кои исто така претрпеа значителен пад.

Introduction

Towards the middle of 2008th, when the global financial crisis was hanging with all its strength, the Macedonian Government thought that Macedonia will not feel the effects of the global financial crisis. It even stated in certain occasions that the Macedonian economy will make profit out of the crises. This statement has been supported with the fact that The Macedonian Financial and Banking Sector wasn't integrated enough in the global one, and its liquidity was based on stable sources (deposits of the citizens and cooperative sector), so significant disrupt in the Macedonian economy couldn't occur. One year after this "Don't worry" policy, Macedonia has already strongly felt the effects of the global financial and economic crisis, and the country has entered the recession. According to the official preliminary data from the State Statistical Office, Macedonia's GDP in the first two quarters notes decreases of 0,9 % and 1,4 %. Macedonia is small country and its economy is based on liberal external trade; on the annual level it reaches about 100% and more of the annual GDP of the country. The economy depends on the import of goods, which is nearly twice bigger than the export of the country. As a result of that, Macedonian trade deficit reached the level of over 25% of the GDP in 2009 with absolute value of over 2, 5 million dollars. Traditionally, in significant part, the high trade deficit has been financed from the money transfers of Macedonian workers abroad. The global crisis has affected these transfers despite the fact that the growth of the trade deficit has remained on the same level. These disadvantages have created huge deficit on the current account, of 14% of the GDP in 2009. Thus, Macedonia has entered the state of economic recession, followed by a strong decline of the situation in the external sector.

Financial crisis in the world, economic crisis in the Balkans

What started as a global financial crisis has become an economic crisis. The world financial crisis emerged from a property bubble and a credit boom. Bad debts soared and banking sector in the developed economies became insolvent. The implication of the crisis to the western Balkans has been not of a sort of financial crisis, but an economic turbulence which has occurred as a result of lack of demand in the world markets to the western Balkan products and falling sources of finance. Investments, remittances, industrial production, foreign exchange reserves and employment rates have fallen. As a result, growth has slowed down. Expansionary

fiscal policies on top of external trade deficits growing at record levels, calls into question the ability of the western Balkan economies to finance the needs, that in turn increases their vulnerability and that may lead to a possible financial crisis in future if the global financial crisis continues to sustain until 2010. The governments of the region of the western Balkans, when the crisis hit in September 2009, argued that they were immune to the crisis. However, as their export-oriented economies began to slump in the autumn of 2009 due to the slid in the world commodity prices, which resulted in tens of thousands of citizens of western Balkan countries loosing their jobs, the governments of the region became more open about the difficulties of their economic situation, although continuing to argue that the effects of the financial crisis are least to be felt in western Balkans in comparison with other regional economies of Europe such as that felt in Iceland, Baltic states or Ukraine. The culprit many of the governments have now settled on is the world out of Balkans. Even wider publics took comfort of this argument due to relatively low exposure of the local economies to the world financial markets. Although the governments continue to predict that the economies would show growth and small contraction in 2009, the economic indicators show that the economies are in some degree of trouble at the moment with industrial output, foreign investment and remittances fall and unemployment rising. * Growth forecasts are down across the region from 5 to 3%, investors are slowing projects and governments are drawing up rescue plans.† Independent economists think that 3% growth of GDP for 2009 is wildly optimistic. Depending on the world manufacturing and commodity prices, they could show growth by 2 or even 1% of GDP. For the small economies of a scale of western Balkans that have boomed for the past seven-eight years, following the end of conflicts in the region in 2001 - that last one being the conflict of Macedonia in 2001 - with annual average GDP growth reaching 5%, economic slowdown and contraction in GDP that has started to be seen starting from the autumn of 2009 is a particularly harsh blow to western Balkans. The whole region, except Serbia and Croatia, has escaped the global financial crisis however it has run into economic crisis due to the recession in its export markets, including EU. As small open economies the western Balkan countries are uncomfortably exposed to the world crisis and particularly to EU as their trade with the EU member states comprises their largest trade volume. Since the global financial crisis hit in September 2009 growth has turned to contraction and unemployment is mounting in the region. Also, any lingering hopes that the western Balkans might escape relatively unscathed from the global financial storms

* The Economist, "The Balkans: A year in the life of Kosovo", 14 February 2009, p. 14.
† The Economist, "The western Balkans: A stuck region", 14 February 2009, p. 36.

were dashed when managers of the foreign banks in the region, mainly those of Austria and Greece, sought support from the international finance institutions. This shows that, although the economies are small and relatively well protected, they are exposed to the global financial crisis that has been replicated in the region in the form of economic crisis.

The falling manufacturing and commodity prices in the world markets are causing problems. Depended on steel and metal exports, the region has been hit hard by the global slump in commodity prices and by the expensive imported electricity, sending metal prices into a tailspin. The price of the metals has fallen by almost two-thirds since mid-2009 leading to slowdown in the region's economies. More than a fifth of economic output and employment are based on exports, making them particularly vulnerable to a fall in global growth and trade. Manufacturing and exporting economies are grinding to a halt, as demand across the world melts away. The western Balkan economies contracted further in last quarter of 2009, as a dispute between Russia and Ukraine over gas prices reduced energy supply to the region and forced the countries' heavy industries to go slow, cutting production or even halting assembly lines. For example, Silmak, a significant producer of ferro-nickel in Jegunovce, in the western part of Macedonia, has cut production and has laid 700 workers due to the drastic fall of the ferro-nickel's price in the world markets.‡ The nearby brick factory Kiro Kucuk in Veles, in the central part of Macedonia, also exemplifies the gravity of the setback. On 1 March 2009 the employees turned up for their final day's work. The factory will not reopen until the economy recovers.§ A similar story could be told in many countries of the region. Macedonia is not alone depended on exporting metallurgical industries. Serbia has suffered far more as global demand for the goods in which its industry specialises has evaporated. For example, US Steel, one of Serbia's leading exporters, closed one plant.** These examples are reflection of the data released for January 2009 that industrial production, which accounts for a fifth of total value added in Macedonia and Serbia has plummeted by 17%, its steepest fall in years.†† The Macedonian State Statistics Office reported that the local companies have been operating by using 50% of their capacities in the course of January 2009 and their situation has deteriorated on a monthly basis, which has

‡ Dnevnik, "Silmak prekina so rabota", 2 Mart 2009, p. 7.
§ Utrinski, "Rabotnicite od Kucuk izvisija", 3 Mart 2009.
** European Commission, DG ECFIN, EU Candidate and Pre-Accession Countries Economic Quarterly, 9 January 2009, p. 30.
†† Utrinski, "Pad na proizvodstvoto za 16.7%", 27 February 2009.

led to a drop in employment rate as well as a large fall in production due to the reduced foreign demand for Macedonian products, insufficient domestic demand, uncertain economic situation and the financial problems. These are hotbeds that might be transferred to other economic sectors, such as the textile and leather industry and to the construction sector, which comprise large share in the country's GDP. The gloom reflects growing worries about underlying weaknesses that make the countries specially vulnerable to recession happening in the EU and other economies to which Balkan economies are depended. So companies have announced big lay-offs as demand has fallen and factories have closed.‡‡ The official unemployment figure of Macedonia already stands at 33% (unofficially it is probably 35% or more) and is set to rise as the new basic salary estimates will only count employed those who pay social security benefits. Unemployment rate in Bosnia and Herzegovina and in Kosovo are more than 40%. The unofficial unemployment rate is, however, much higher and many who say that they have jobs are in fact on indefinite unpaid leave. The economists forecast that unemployment

region-wide will rise. Most of that rise will be the result of fall in trade (many exporting companies have laid off workers), and due to declining investments. Coffee streets from Knjez Mihajlova in Belgrade to Kej Vardar in Skopje to Bash Charshija in Sarajevo are busy during sunlight as young people, forming more than 50% of the unemployed force in the region, sip their coffees. Unemployment rates are soaring and offices of the Employment Agencies in whole region are full with people looking for work.

The stock markets have plunged as well. The Zagreb stock exchange index lost 42% during the last quarter of 2009 and others such as Sarajevo Stock Exchange, dropped by 19% during the same quarter, leading to an annual decrease of 67% in 2009. The Belgrade Stock Exchange tumbled and its index lost 75% during 2009.§§ An important sector that waits to be affected is the real estate market as the credits have gone down and the borrowers are unable to pay back their monthly loans. The scale of the bubble in the region is as big as in troubling EU cities. House prices rose further in Belgrade than they did in Tirana. So did commercial-property prices. As a result, demand for new homes has dried up

‡‡ International Monetary Fund, "Former Yugoslav Republic of Macedonia: Staff Report for the 2009 Article IV
Consultation", Prepared by Staff Representatives for the 2009 Consultation with Former Yugoslav Republic of
Macedonia, 11 November 2009, p. 11.

§§ European Commission, DG ECFIN, p. 23.

although prices have remained stable and over inflated, with Belgrade topping the prices where average residential square meter is sold at 2000 euros. The housing boom in the region is among the extreme, measured by real price increases and resulting overvaluations. This is a bubble which is waiting to burst. Another bubble which is waiting to burst is commercial property where office blocks and shops are overvalued. Both these booms have been fuelled by debt, another reason why the region looks particularly vulnerable now. There is much to suggest that the pain is felt most by small enterprises, labelled as small and medium sized enterprises (SMEs) that are the backbone of the western Balkan economies. SMEs seem especially vulnerable to the downturn. Many specialise in textile and these are also the products whose orders are the first to be cancelled when economies slow and companies trim investment. These firms are finding themselves chronically short of orders and capital.

The governments in the region have launched actions to stimulate their economies. Montenegrin government launched a plan with significant capital expenditures and other stimulus to businesses at some 10% of the projected GDP for 2009.*** In November 2009, the Macedonian government unveiled measures worth 5-6% of GDP.††† Other governments as well have unveiled packages that include extra billions to finance investment, infrastructure projects, extra benefits for poorer and tax cuts. The central banks as well have joined in tightening monetary policies and increasing controls of the credit markets. These measures mean the economy may suffer only a mild downturn. Tightening of control by the central banks has encouraged banks to drastically decrease the amount of lending. When there are no loans for companies and consumers, the consumption of domestic and foreign products decreases, leading towards economic stagnation. So officials are also trying to inject cash and confidence into the banking system, avoiding confidence crisis that in October 2009 hit Albania, Bosnia and Herzegovina, Montenegro and Serbia where the lack of confidence led to a withdrawal of deposits by population.

They have done this in various ways. Croatian central bank has abolished reserve requirements. The Bank of Albania has limited Banks' exposure towards their foreign parent companies. The National Bank of Serbia has eliminated the tax on savings income to help boost foreign exchange liquidity. The Bosnian central bank has increased the level of guaranteed savings deposits from 3500 to 10.000

*** Ibid, p. 31.

††† Ibid, p. 31.

euros and the Montenegrin government has given full guarantee to deposits. The Montenegrin government has also given capital boost to ailing Prva Banka to allow it to expand landing, especially for small businesses.

Recovery is possible only through strong demand in the rest of the world (which is to lack for some time), that would lead exports to soar, allowing quick recovery. However, today demand is falling rapidly across the globe and most big developed economies buying Balkans products face simultaneous banking crises. With demand weak everywhere, the familiar route to recovery is blocked. For the largest trading partners of western Balkan economies, the EU countries, figures that came out in February 2009, showed that Euro-area GDP shrank at an annualised rate of around 5% in the fourth quarter of 2009. The IMF has forecasted that Euro-area GDP will decline by 2% in 2009 and barely recover in 2010. Countries with huge current-account deficits are most exposed in a credit drought. So the hope had been that weaker economies of Balkans would be offset by faster economic recovery in EU economies and support by the local banks mother banks' in EU. Unfortunately, the EU economies are facing recession and mother banks and mother countries have asked them to lend first to domestic businesses and households and not to transfer money to their subsidiaries in Balkans. The Greeks publicly advised banks to be more prudent about transferring bail-out funds to Balkan subsidiaries.

The western Balkan countries face a current account deficit this year in average of around 14%. Nevertheless, the crisis for example has not stopped the Macedonian and Kosovar governments from doling out billions of euros' worth of cultural projects. Financial crisis is also having effect on remittances, a large share in GDP of the economies of Balkans. Foreign workers have been first to be laid off in the western economies. Remittances make up more than a tenth of the GDP of Balkan economies. Although they are likely to fall as a result of the slumping world economy, as it has been the case with Albania, where remittances' inflows have declined from 13% of GDP in 2007 to 11% of GDP in the last quarter of 2009, they may be less affected by the world economy. It is expected that people keep the cross border payments going even when their incomes fall. Migration from western Balkans to EU countries is expected to rise as the borders are getting opened through visa facilitation and liberalisation programmes. However, this rise will be balanced with the recession in the EU economies where it means fewer jobs for migrants.

In surveys, the economy has leapt to the top of voters' concerns. Overall the public is scared and uncertain. So far, the Balkans has escaped the civic unrest seen

in the Baltic States, Iceland, or elsewhere. There are not yet signs of discontent, except concerns expressed by politicians and economists. Thousands taking to the streets to protest against crises in Baltic States and Ukraine have not resembled in Balkans. However, pundits predict unrest in towns that rely entirely on one ailing factory or industry. But so far the signs are limited.

The middle class in the whole region is under a great threat. The middle class flourished during communist times. As economy goes into reverse they may well be hit harder than the rich or poor. They work in export industries so their jobs are unsafe. The other part of the middle class, who are employed in the state administration, and whose jobs are relatively safe, they have started to borrow, so are hurt by the credit crunch.

The impact of the world crisis on the Macedonian economy

Towards the middle of 2008th, when the global financial crisis was hanging with all its strength, the Macedonian Government thought that Macedonia will not feel the effects of the global financial crisis. It even stated in certain occasions that the Macedonian economy will make profit out of the crises. This statement has been supported with the fact that The Macedonian Financial and Banking Sector wasn't integrated enough in the global one, and its liquidity was based on stable sources (deposits of the citizens and cooperative sector), so significant disrupt in the Macedonian economy couldn't occur. One year after this "Don't worry" policy, Macedonia has already strongly felt the effects of the global financial and economic crisis, and the country has entered the recession. According to the official preliminary data from the State Statistical Office, Macedonia's GDP in the first two quarters notes decreases of 0,9 % and 1,4 %. Macedonia is small country and its economy is based on liberal external trade; on the annual level it reaches about 100% and more of the annual GDP of the country. The economy depends on the import of goods, which is nearly twice bigger than the export of the country. As a result of that, Macedonian trade deficit reached the level of over 25% of the GDP in 2009 with absolute value of over 2, 5 million dollars. Traditionally, in significant part, the high trade deficit has been financed from the money transfers of Macedonian workers abroad. The global crisis has affected these transfers despite the fact that the growth of the trade deficit has remained on the same level. These disadvantages have created huge deficit on the current account, of 14% of the GDP

in 2009. Thus, Macedonia has entered the state of economic recession, followed by a strong decline of the situation in the external sector.

Tabel: Foreign direct investments (FDI) in Macedonia 2007-2011

	2007	**2008**	**2009**	**2010**	**2011 (jan-june)**
trade deficit	-1,063	-1,284	-1,630	-2,552	-1,030
Private transfers	987	1,163	1,352	1,376	492
current account	-158	-56	-597	-1,210	-569

Source: NBM, data for FDI 2007-2011

This tendency has continued in the first half of 2009 with the same intensity. Mostly affected by the crisis were the general export sectors of the Macedonian economy: metallurgy, textile industry and the export of agricultural products. These sectors, that take two-thirds of the total export, have decreased their export due to the decreased demand for their production and due to the successive fall of their prices on the global market. At the same time, big part of the employees in these industries, have remained without job; have used forced vacation or minimum paid absence. The Government didn't undertake any measures to help them, but only used to give populist statements as "we expect from the owners and managers of the endangered companies not to fire the employees but instead to spend their "high profits in this period of crisis earned in times when the metal prices on the world stockexchange were high and when the level of accomplished export was acceptable".

Conclusion

The global financial crisis has serious impact on the worsened economic situation in Macedonia. The worsened situation is being felt generally and over two-thirds of the citizens are seriously concerned about the consequences of the financial crisis on the Macedonian economy. The concerns of the further worsening of the economic situation in Macedonia come at a time when almost 4 / 5 of the population, the general situation in the Macedonian economy is assessed as poor or very poor. This situation is not only a result of the crisis but also of the Macedonia's economic situation for a long time. In this sense, for example, every second citizen of Macedonia, the Macedonia's economic situation, compared with the last 12 months (or before the beginning of the global financial crisis) has evaluated as the same (39%) or at least somewhat improved (12%). Big part of the citizens (every fourth) considers that the worsened economic situation in Macedonia is only a result of the global financial crisis and the Government does not have any responsibility. More than every third considers that the worsening in terms of the global financial crisis is a result of the weakness of the domestic policy (38%) and even 36% considers that the worsened situation in the Macedonian economy this year is a result only of the weakness of the domestic policy. Regarding of the expectations for getting out of the crisis, citizens do not share the optimism of the Government, which suggests that at the end of this year can be expected getting out from recession and GDP growth. Almost two in three citizens (61%) consider that it could be expected that the Macedonian economy will start to grow even after 2010 or later. The expectations regarding the Macedonian economy in a year from now, 44% considers that it would be the same as the current and 16% considers that it would be at least somewhat worse than the present. These findings indicate that the impact of the global financial crisis on Macedonia is perceived as serious and damaging, and the optimism for a soon recovery from the crisis is not big, because of the general awareness in the public for the weaknesses of the domestic political and economical factors for dealing with the crisis and the long existing weakness of the Macedonian economy. Regarding to general evaluation there is no statistically significant differences between the different ethnicities in Macedonia, and for the distribution of the population by regions. More negative assessments of the situation, gives the respondents with higher education and members of the economically better situated families, but optimism for getting out of crisis is lower among the less educated respondents, unemployed and economically weaker situated families. Although

most of the people in Macedonia, don't see opportunities for getting out quickly from the economic crisis, 38% of population expects that the financial situation of their household would be at least somewhat improved already after 12 months. This attitude of the Macedonian people is probably a result of the promises of the Government that Macedonia will get out of a recession at the end of this year and the information that most countries have already come out of recession. More optimistic are households of a young people from 18-29 years (44%), employees of the private sector (41%) and households with monthly income of 25 – 40 000 den. i.e. 400-650 Euros) (47%).

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