

**PROJECT INFORMATION DOCUMENT (PID)**  
**APPRAISAL STAGE**

Report No.: PIDA35409

<b>Project Name</b>	Local and Regional Competitiveness Project (P154263)
<b>Region</b>	EUROPE AND CENTRAL ASIA
<b>Country</b>	Macedonia, former Yugoslav Republic of
<b>Sector(s)</b>	General industry and trade sector (80%), Vocational training (10%), Public administration- Industry and trade (10%)
<b>Theme(s)</b>	Infrastructure services for private sector development (30%), Micro, Small and Medium Enterprise support (20%), Regional integration (20%), Cultural Heritage (20%), Education for the knowledge economy (10%)
<b>Lending Instrument</b>	Investment Project Financing
<b>Project ID</b>	P154263
<b>Borrower(s)</b>	Former Yugoslav Republic of Macedonia
<b>Implementing Agency</b>	Cabinet of the Deputy Prime Minister for Economic Affairs
<b>Environmental Category</b>	B-Partial Assessment
<b>Date PID Prepared/Updated</b>	19-Nov-2015
<b>Date PID Approved/Disclosed</b>	20-Nov-2015
<b>Estimated Date of Appraisal Completion</b>	06-Nov-2015
<b>Estimated Date of First Grant Approval</b>	24-Dec-2015
<b>Appraisal Review Decision (from Decision Note)</b>	

## I. Project Context

### Country Context

FYR Macedonia is an upper middle-income country that has made great strides in achieving macro-fiscal stability over the last decade; however, more efforts are needed to generate and sustain economic growth that creates jobs and improve living standards for all. Following strong economic growth during the period 2002–2008 averaging 4.3 percent, average GDP growth has declined to 2.1 percent per year since 2009. Real GDP growth would need to accelerate to around 4.5 percent for FYR Macedonia to converge to the living standards of the new EU member states within the next 20 years.

Accession to the EU remains the anchor of the government's reform agenda. FYR Macedonia became an EU Candidate country in 2005, and since 2009 the EC has been recommending opening accession negotiations. However, the decision continues to be postponed in part due to the name dispute with Greece. The EC has an active program of assistance to FYR Macedonia, including IPA

funding, the largest source of concessional funds in the country.

The main drivers of growth since 2009 have been industry (particularly manufacturing), trade, transport, and accommodation services. Growth in manufacturing has been driven by foreign direct investment (FDI), which averaged 4.2 percent of GDP per year in 2006-2014, most of which has been greenfield. FDI has contributed to the increased diversification of FYR Macedonia's export basket in terms of products and destinations and the increased technological intensity of its exports. The contributions of agriculture, information and communication, and the public sector to GDP growth declined in 2009-2014.

Unemployment remains high, although it has declined from a high of 38 percent in 2004 to 28 percent in 2014. In fact, FYR Macedonia is the only SEE6 country where unemployment declined in the post-crisis period. Still, at 28 percent in 2014, its unemployment rate is the second highest among SEE6 countries. Youth unemployment remains at 53.1 percent in 2014, the second highest in the SEE6 region and significantly above the EU average of 23.6 percent. In addition, gender inequalities remain and female labor force participation (for women aged 15-64) remains low at 51 percent, well below the regional average of 62 percent.

Economic growth seems not to have translated into significant poverty reduction in FYR Macedonia before 2008, but poverty seems to have declined somewhat in recent years. Under a new method for measuring poverty in FYR Macedonia, poverty declined slightly from 27.0 percent in 2010 to 24.2 percent in 2013. Still, around 40 percent of the Macedonian population is considered to be severely materially deprived. This is more than double the average of the new EU member states and more than four times higher than the EU-28 average.

As a small, open economy FYR Macedonia needs to rely on further growth in exports and increased competitiveness to answer its long-term growth challenge. In spite of progress attracting export-oriented FDI, local small and medium companies face a number of challenges. Their capacity to further integrate into international markets is limited by their relatively low managerial, financial, and technical capacity. Continued efforts to improve competitiveness are particularly important given the country's exchange rate peg to the Euro. Further efforts to boost exports by investing in infrastructure, facilitating business growth and linkages, strengthening the investment climate, and supporting innovation will help the country foster sustained private sector-led growth.

### **Sectoral and institutional Context**

FYR Macedonia has good tourism potential, but is starting from a relatively low base. Capital city Skopje and UNESCO-protected Ohrid remain the key tourist destinations in the country, complemented by traditional Balkan village scenes and diverse communities, and ski resorts such as Mavrovo and Popova Sapka. Opportunities for the development of tourism sub-segments that appeal to niche markets and customers have emerged in recent years. These include rural, wine, adventure, cultural and spa tourism. Yet, the total contribution of travel and tourism to the country's GDP, employment, and total capital investment in 2014 was relatively small (5.2 percent, 4.7 percent, and 2.2 percent, respectively) in comparison with other countries in the region. By contrast, in 2014, tourism's total contribution to GDP in Bulgaria was 13.1 percent, and in Albania it was 21 percent. Growth in FYR Macedonia is, however, steadily increasing with direct GDP contributions from tourism increasing by 30 percent from 2010.

The number of tourists in FYR Macedonia has been steadily increasing, but there has been limited market profiling carried out. The total number of registered tourists (foreign and domestic) in 2014 was 735,650 (25.5 percent increase from 2010). This growth has been driven through intensive advertising activities, subsidies in tour and hotel operations, and the increasing fare and carrier competitiveness brought about by recent airport takeovers.

There are three markets identified in national and regional strategic documents: (1) domestic tourism (around 40 percent of the total) is the most developed in terms of product, but has been declining in absolute terms over the last 30 years as competition in neighboring countries increases; (2) regional tourism is the most significant foreign market in terms of overall volume and number of overnights for FYR Macedonia, with 23 percent of the total tourist numbers coming from Turkey, Bulgaria, Serbia and Greece, as has been the case for decades; and (3) international tourism (Western Europe and American) is the most significant in terms of per capita spend. Most international tourists arrive as part of tour groups, with a small minority of typically higher-spending independent tourists. Most incoming tour agencies offer packages of up to eight countries as part of a “Balkan tour” of 5 to 18 days, which tend to focus on the countries’ cultural attractions and experiences, with limited nature-based activities.

The sector faces a series of challenges in order to fully realize its potential. The key challenges include the following:

- a. The enabling environment: business environment (standards, licensing, ease of access to finance and knowledge, etc.), air access
- b. The offer: positioning, visitor information, product development, site management, standards
- c. Development/shared value: data collection, linkages, private sector engagement.

These challenges have been well articulated in a number of diagnostics over the years, and various international organizations (including USAID, UNIDO, Swisscontact, and GIZ) are very active in the sector. LRCP will focus on addressing a series of macro-level issues that are as yet not fully addressed under existing programs, together with destination-level interventions. This approach will complement the work already being done by the Government and other donors to ensure a comprehensive approach is being applied to the sector

The importance of the tourism sector is emphasized in national and regional strategies. The sector’s policy framework comprises the National Tourism Strategy 2009-2015; the Law and Strategy for Regional Development 2009-2019; the Programs for Regional Development 2010-2015 for each of the eight planning regions; and the Program of the Government of FYR Macedonia for the period 2014-2018. The Government, through the Ministry of Economy, plans to develop a new National Tourism Strategy for 2016 onward.

The key public sector entities with a mandate to facilitate tourism development include: The Cabinet of the Deputy Prime Minister for Economic Affairs (CDPMEA), based in the General Secretariat of the Government, serves as the main coordination and delivery body responsible for the oversight of strategy and program implementation in key economic sectors, including tourism. The Ministry of Economy, through its Department of Tourism, is the principle institution responsible for tourism policy and strategic planning. The Agency for Promotion and Support of Tourism (APST) is in charge of promoting the country as a tourist destination.

LRCP is based on a holistic approach to tourism development and destination management. Multiple interventions that tackle the needs of a destination are most effective when delivered in an integrated way, addressing issues ranging from policy to planning, security, access, infrastructure, and marketing. Because tourism is both produced and consumed at a local or 'destination' level, the best results are usually obtained through targeted, integrated interventions at a local level that are oriented to particular market requirements, integrated into thematic (e.g. cultural or spatial frameworks (e.g. clusters, corridors or circuits) and supported by wider sector reforms. The present project takes this approach, drawing from experience in WBG's Tourism Global Solutions Group.

## II. Proposed Development Objectives

The Project Development Objective (PDO) is to enhance the contribution of tourism to local economic development and improve the capacity of the government and public entities to invest in tourism growth and facilitate destination management.

## III. Project Description

### Component Name

Component 1: Technical assistance for tourism development (Bank Executed)

### Comments (optional)

This component will improve the capacity of institutions and business environment in support of tourism development at the national level, through advisory services, analytical assistance, and policy advice. Areas of focus are derived directly from diagnostic work that highlights key challenges. This component includes technical assistance for the following activities: (i) improve institutional coordination; (ii) review and advise on the draft National Tourism Strategy; (iii) improve the availability and use of data to inform policy-making; (iv) improve the business environment; and (v) support and just-in time technical advice to the implementation of the activities under the Recipient Executed components.

### Component Name

Component 2: Strengthening destination management and enabling environment (Recipient Executed)

### Comments (optional)

This component will support implementation of activities to enhance tourism development at the central government level and at the destination level. It will include the following:

- (i) Sub-component 2.1: Central level capacity, coordination, and policy. LRCP will support Recipient-executed activities to implement recommendations from Component 1.
- (ii) Sub-component 2.2: Destination Management: LRCP will build destination management capacity in the destinations selected for participation in the project, in order to more effectively manage tourism development and provide greater impacts for local people.

### Component Name

Component 3: Investment in tourism-related infrastructure and linkages at destinations (Recipient Executed)

### Comments (optional)

This component will support key investments that will make an impact on increasing the attractiveness of the selected destinations through upgraded product offerings and linkages with local economies to capture a greater share of economic benefits.

- (i) Sub-component 3.1: Infrastructure investments: This sub-component will finance infrastructure sub-projects and technical assistance that are critical for unlocking the destination potential by upgrading the quality of attractions, sites, and visitor experience.

(ii) Sub-component 3.2: Enhanced tourism service-delivery and local economic impact. This sub-component will fund matching grants for qualified organizational entities to improve access to information and services, improve service quality, linkages and innovation at the destinations.

#### **Component Name**

Component 4: Strengthening project management (Recipient executed)

#### **Comments (optional)**

This component will support the capacity of the Project Implementation Unit (PIU) to ensure that all Recipient Executed activities under LRCP are effectively implemented. It will finance technical expertise (consultants), training, equipment, operating costs, and equipment associated with implementation, monitoring and evaluation of the Recipient Executed activities under LRCP.

#### **IV. Financing (in USD Million)**

Total Project Cost:	22.98	Total Bank Financing:	0.00
Financing Gap:	0.00		
<b>For Loans/Credits/Others</b>			<b>Amount</b>
Borrower			3.62
Free-standing TFs for ECA CU4 Country Unit			19.36
Total			22.98

#### **V. Implementation**

The implementing agency will be CDPMEA. A Project Implementation Unit (PIU) will be established within CDPMEA, as per Decision of the Council of Ministers from November 2014. The PIU will oversee and coordinate all of the implementation, results monitoring, reporting, fiduciary functions, and safeguards of the recipient executed components, in close collaboration with the line ministries and public agencies. Selection of sub-projects for financing will be managed by the PIU, according to evaluation criteria and methodology documented in the Project Operations Manual. Proposals for infrastructure investments and selected linkages and innovation sub-projects, will be subject to review and no-objection by the World Bank, considering factors such as amount, complexity of activities, and capacity of the recipient. Capacity will be strengthened in the CDPMEA and the PIU on the Bank procedures and requirements for investment projects and trust fund management, through periodic training delivered by World Bank staff. Capacity-building will also be provided to the relevant public agencies and all beneficiaries of grants for sub-projects, in terms of their understanding of Bank fiduciary and safeguards procedures.

Visibility and local awareness of the European Union's funding contribution to LRCP will be promoted in accordance with a Visibility Note to be incorporated into the Project Operations Manual.

A Project Steering Committee will be established with participation of representatives of the CDPMEA and public entities with a mandate related to project activities. The Steering Committee will have responsibility for monitoring project implementation by CDPMEA and recommending measures to enhance results and sustainability, if any. The composition of the Steering Committee will be similar to the Working Group during project preparation, with a representative the CDPMEA and the relevant ministries and other public entities. The Delegation of the EU will have an advisory role to the Steering Committee.

**VI. Safeguard Policies (including public consultation)**

<b>Safeguard Policies Triggered by the Project</b>	<b>Yes</b>	<b>No</b>
Environmental Assessment OP/BP 4.01	x	
Natural Habitats OP/BP 4.04	x	
Forests OP/BP 4.36		x
Pest Management OP 4.09		x
Physical Cultural Resources OP/BP 4.11	x	
Indigenous Peoples OP/BP 4.10		x
Involuntary Resettlement OP/BP 4.12	x	
Safety of Dams OP/BP 4.37		x
Projects on International Waterways OP/BP 7.50		x
Projects in Disputed Areas OP/BP 7.60		x

**Comments (optional)****VII. Contact point****World Bank**

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