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Croatian and Macedonian Economy in the 2007 economic and financial crisis and after

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1. Introduction

The states of Balkan – to different degrees – were affected by the global crisis. The crisis, which began in 2007, reached the region in the second half of 2008. The performance of economies in the area fell back, because of reduced demand for their exports and less foreign direct investment. Fiscal positions deteriorated in all economies. Unemployment, already high in several countries, started to rise further. The macroeconomic situation remains fragile. The aim of the study is to analyze the European Union's two official candidate countries (Croatia and the Former Yugoslav Republic of Macedonia – see later as Macedonia) in the economic and financial crisis and to present their economic forecast. In the end of the article we can conclude that Croatia was strongly affected by the economic crisis but its impact has been mitigated by a resilient banking sector and strong foreign reserves. Macedonia was also affected by the economic crisis but the slowdown of growth was mild and mitigated by a stable banking sector and sustained private consumption. According to economic forecasts, prospects of Croatia for a short term economic recovery are highly uncertain, while in Macedonia the mild recession followed by a mild recovery.

2. Summary of the impacts of global crisis in the Western Balkans

The global financial crises affected all countries in the region in the second half of 2008. Most of countries has felt in to recession till 2009 (see Table 1). Probably the most strongly affected countries are Bosnia and Herzegovina and Serbia, this countries' common feature that both of two turned for support to the International Monetary Fund (IMF). The crisis strongly affected these countries, their economic activity hardly decreased. The crisis had a serious effect on Croatia's economy where the previous dynamic economic increase had taken back significantly. The crisis moderately affected Macedonia and Kosovo, more less Albania. Montenegro successfully decreased its impacts with different steps.

Table 1: Real GDP growth in the Western Balkans between 2004 and 2009 (%)

	2009	2008	2007	2006	2005	2004
Croatia	-5,8	2,4	5,5	4,7	4,21	4,25
Former Yugoslav Republic of Macedonia, the	4	5,9	5,9	4	4,1	4,1
Albania	n/a.	7,85	6	5,43	5,72	5,71
Bosnia and Herzegovina	-2,9*	5,7	6,2	6,1	3,92	6,27
Montenegro	n/a.	6,9	10,7	8,6	4,2	4,4
Serbia	-2,9*	5,5	6,9	5,2	5,6	8,3
Kosovo (under United Nations Security Council Resolution 1244/99)	n/a.	n/a.	n/a.	n/a.	n/a.	n/a.

Source: Eurostat[1], IRBRS[2] (*)

[1] Eurostat (2010): Candidate countries and potential candidates- real GDP growth rates
http://appsso.eurostat.ec.europa.eu/nui/show.do?dataset=cpc_ecnagdp&lang=en (downloaded: 2010-08-29)

The Western Balkan countries (which include Croatia, the Former Yugoslav Republic of Macedonia, Albania, Bosnia and Herzegovina, Montenegro, Serbia and Kosovo) have limited scope for a strong domestic macroeconomic policy response to the current crisis. There are significant constraints on monetary and fiscal policy measures because of previous pro-cyclical fiscal stances, foreign currency denominated credits and mortgages and large external imbalances. In these circumstances, the response to crisis has been appropriate in most countries of the region and in some cases they have an initial lack of acknowledgement of the severity of the challenge. The perspective of EU accession has helped to retain confidence in the economies in the Western Balkan region and provided an anchor for economic policies in the recent period.

Over recent years these economies introduced structural reforms, which helped to moderate effects of the crisis. For example Croatia improved financial regulation, which contributed to banking sector stability and resilience. In Serbia and Bosnia and Herzegovina, due to previous expansionary policies, external imbalances widened and public finances were particularly affected, which was financed from external sources.[3] This increased the debt of countries, and because of the crisis, the discharge was in danger. Thus, the two countries obtained to IMF for support.

The crisis, particularly its impact on the real economy, including on the employment and social situation, is continuing in these countries. The unemployment rate has grown all of the countries, which is much higher than in the European Union. In the EU27, the total unemployment rate is about 9-10%, while in the Western Balkans – expect Croatia - this rate is the EU's average double. (See Table 2)

Table 2: Candidate countries and potential candidates – total unemployment rate between 2004 and 2009

	2009	2008	2007	2006	2005	2004
Croatia	9,1	8,4	9,6	11,1	12,6	13,6
Former Yugoslav Republic of Macedonia, the	n/a.	33,8	35	36	37,3	37,2
Albania	n/a.	13	13,5	13,8	14,1	14,4
Bosnia and Herzegovina	24,1	23,4	29	31,1	43,94	41,76
Montenegro	19,1	16,8	19,3	29,6	30,3	27,7
Serbia	16,1	13,6	18,3	21	21,1	18,7
Kosovo (under United Nations Security Council Resolution 1244/99)	n/a.	47,5	43,6	44,9	41,4	39,7

Source: Eurostat[4]

Recovery will take time, as economic activity in the main trading partners is projected to pick up slowly. The economic performance of these countries highly depends on main trading partners. Capital inflows to stimulate domestic demand are likely to remain subdued in the near future. Short-term measures have been taken to mitigate the social impact of the crisis for the most vulnerable parts of society. (According to latest data, 25 per cent of population of Croatia, 23,4 per cent of population of Serbia and 28 per cent of population of Bosnia would sink into poverty if financial supports would not be received)[5]. In medium term, ensuring a sound fiscal policy is of great importance, with emphasis on more efficient and effective public spending and on investment. Employment policies and social protection measures are needed to address structural unemployment (to decrease it) and protect vulnerable groups. According to European Commission the response to the crisis needs to take into account the need for sustainable development and the challenge posed by climate change and give priority to measures leading to a safe and sustainable low-carbon economy.

[2] Database of Economic Indicators of the Republic Srpska
http://www.irbrs.net/Statistika.aspx?tab=2&lang=eng (downloaded: 2010-08-30)
[3] European Commision [2009]: Enlargement Strategy and Main Challenges 2009-2010, Brussels
[4] Candidate countries and potential candidates – total unemployment rate:
http://appsso.eurostat.ec.europa.eu/nui/show.do?dataset=cpc_pslm&lang=en (2010-08-29)
[5] Eurostat [2010]: Living condition of candidate countries and potential candidates -
http://appsso.eurostat.ec.europa.eu/nui/show.do?dataset=cpc_psilc&lang=en (2010-08-30)

EU supports the Western Balkan countries in different ways. For example, pre-accession assistance has been programmed to support the competitiveness of countries, which include banking sector, infrastructure projects, SMEs and job creation, including in rural areas. €200 million in grants from the Instrument for Pre-accession Assistance (IPA) have been allocated for this purpose, which will leverage investments for at least €1 billion, co-financed by IFI loans. The Commission has proposed that the co-financing requirement for beneficiary countries in IPA assistance be reduced. The Commission provided direct budget support through IPA to Serbia to mitigate the effects of the financial and economic crisis. In addition, the Commission proposed to the Council to approve a macro-financial assistance in the form of a €200 million loan to Serbia. If needed, these possibilities are open to the other countries. In both cases the financial assistance is conditional, including upon an agreement with the IMF on sound macroeconomic policies. The Commission works closely with the IFIs, which have committed themselves to increase their lending to the Western Balkans and Turkey to more than €5 billion in 2009.[6]

3. Impacts of global crisis in Croatia

Croatia excels in the implementation of the accession conditions. Achieving the membership, Croatia has to launch further reforms on the field of jurisdiction, struggle against corruption, organized crime and war crimes trials, struggle for minority rights protection, and the case of the reception of the political refugees is not solved yet. The process of accession can be slowed by the fact, that Croatia was strongly affected by the economic crisis. But its impact has been mitigated by a resilient banking sector and strong foreign reserves. Enhanced structural reforms and the adoption of a credible medium-term fiscal strategy would be essential to improve its competitiveness.

The economy of Croatia has been increasingly hit by the global crisis. Over the last few years and before the crisis, Croatia had a relatively strong economic growth, averaging 4.3% between 2004 and 2008. The growth performance was primarily domestic-demand driven, fuelled by large capital inflows and strong credit growth. This was accompanied by a marked expansion of non-tradable industries, such as retail, construction and the financial sector. The global crisis severely affected the Croatian economy which went into a deep recession. Real GDP declined by 5.8% in 2009, driven by a strong fall in domestic demand. Private consumption declined by around 8.5% and total investment by 11.8%.[7] (See Table 3)

Table 3: Main features of Croatia between 2006 and 2009 (%)

	2006	2007	2008	2009
GDP-growth	4,7	5,5	2,4	-5,8
Private consumption	2,7	6,2	0,8	-8,5
Unemployment rate	11,2	9,6	8,4	10,4
Current account balance	-7,0	-7,6	-9,3	-5,1
General government balance (GDP %)	-3,0	-2,5	-1,4	-4,1
General government gross dept (GDP %)	35,7	33,0	33,5	38,5

Source: European Commission [2010][8]

The country turned into recession in the first half of 2009 and unemployment increased (but less than in the European Union). In March 2010 total employment fell by 2.4 percent. In January 2010 the number of registered unemployed is about one third higher than before the crisis and over 20 percent higher than a year earlier. Currently, the unemployment rate in Croatia is slightly higher than the EU average. The employment/working age population ratio dropped, which is 57.8 (one of the lowest in Europe). An important factor that limited the employment impact of the crisis has been wage moderation. Real wages remained stagnant when economy slowed down and since September 2009 started to fall. At the end of 2010,

6 European Commission [2009]: Enlargement Strategy and Main Challenges 2009-2010, Brussels
7 European Commission [2010]: European Economic Forecast, Spring 2010, p. 152
8 Ibid p. 154

the average real wage is nearly 3 percent lower than it was a year earlier. The reduction of wage pressure helped to cut labour costs and thus to limit the layoffs. Wage flexibility is a notable new phenomenon because until recently wage pressures pervaded the Croatian economy and were contributing to high unemployment. Before the crisis, absolute poverty[9] was low, and relative poverty was at the level of region thanks to strong economic growth coupled with job creation, and high spending on social safety nets. The crisis has had a substantial impact on both the poverty rate and the profile of poverty. The fall in employment coupled with the fall in real wages caused the reduction in incomes, and consequently pushed many of the unemployed workers into poverty. The "new poor" tend to be different from the "old poor": they are better educated, younger and economically active. Faced with a severe economic downturn social policy faces challenges. It needs to provide income support to individuals who lost their jobs and families who fell into poverty and to prevent short-term unemployment turn into long-term unemployment. Social protection policy in Croatia was adjusted only marginally to these challenges. Income support was provided in the form of unemployment benefit; however many of the newly unemployed were not covered by the system. Active labour market programs, which are meant to help workers escape unemployment, are run on a very limited scale and were not expanded during the crisis. There is substantial room to improve the efficiency of the system and to build resilience of the social protection system against potential future adverse demand shocks. In April 2010, the Government of Croatia adopted the Economic Recovery Program along with the detailed action plan for its implementation. The priorities for example: focus employment programs on the provision of technical/vocational training to the unemployed, limit the duration of unemployment benefit (including for persons with over 30 years of service who are currently eligible for benefit of unlimited duration) and strengthen relationship between schools and labour market..[10]

Macro-economic stability has been preserved by a prudent monetary policy. The macroeconomic policy response has by and large been appropriate to address spillovers from the crisis. Some efforts to rebalance the budget were made, but the fiscal deficit increased significantly. The banking sector remained sound and resilient to the crisis. A high level of external indebtedness and large short-term repayment obligations are key vulnerabilities of the economy. The process of economic restructuring and privatisation has remained slow and limited improvements in the business environment have been made. [11] In the end of August 2010, World Bank criticised Croatia's budget rebalance and expected greater a expenditure reduction. Furthermore, the growth of deficit is moving in the opposite direction from other European states that are also working on improving their public finances. The World Bank also expects the reform of the social sector, subsidies and public administration.[12] It is necessary to solve these problems in order to decrease vulnerable of the Croatian economy. It is also necessary to make easier the foundation of companies, improve investment climate.

In sum, monetary policy contributed successfully to preserving financial stability mainly by alleviating foreign exchange liquidity constraints through regulatory changes. In reaction to mounting fiscal pressures, some adjustments in spending as well as measures to compensate for falling revenues were adopted in the context of successive budget revisions. External imbalances have narrowed, exchange rate stability has been preserved, and the banking sector remained resilient to shocks and credit growth has declined. Although, risks of higher spending and further declines in revenues have materialised. The fiscal deficit increased significantly. The late policy response revealed weaknesses in the budget planning process. Little progress has been achieved in increasing the efficiency of public spending. Social transfers remained high and not well-targeted and a large number of public and state-owned enterprises continued to receive state support through subsidies and guarantees.

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[9] According to World Bank, absolute poverty means that people live in less 5 dollar per day (in purchasing power)

[10] The World Bank Group [2010]: Croatia Social Impact of the Crisis and Building Resilience, World Bank Report No. 55111-HR

[11] European Commission [2009]: Enlargement Strategy and Main Challenges 2009-2010, Brussels

[12] Croationtimes.com [2010]: World Bank criticizes Croatia's budget rebalance - http://croatiantimes.com/news/Business/2010-08-30/13409/World_Bank_criticizes_Croatia%B4s_budget_rebalance (2010-09-03)

4. Impacts of global crisis in The Former Yugoslav Republic of Macedonia

The Former Yugoslav Republic of Macedonia received the status of candidate country in December 2005, but the negotiations has not started yet (the European Commission initiated it in October 2009). The country has made good progress in improving its ability to assume the obligations of membership, in particular as concerns transport, customs and taxation and justice, freedom and security. However, sustained efforts are needed to strengthen administrative capacity for the implementation and enforcement of legislation. Institutional weaknesses and the rule of law need to be improved to allow for smooth functioning of the market economy. Further efforts are needed to strengthen public administration and the judiciary, in order to improve legal certainty and improve business environment. Despite efforts to reduce the unregistered economy, the issue remains an important challenge. It is important that the country manage its name debate with Greece.

Macedonia built a strong record of macroeconomic stability in the past years. GDP growth picked up to 5.9 and 4.8 per cent in 2007 and 2008 led by stronger domestic demand and increasing investments. In the last quarter of 2008 and in the first half of 2009, however, the economy began to feel the impact of the global financial crisis. Exports, capital inflows and investments as well as industrial production dropped significantly. [13] At the same time, the number of non-performing loans increased to 8.4 per cent at June from 6.8 per cent at the end of 2008[14], and is expected to increase further as a result of the economic downturn. However, so far the banks remain well capitalised and the central bank remains committed to the current fixed exchange rate system and the bank can intervene to protect this aim. Despite of crisis, the exchange rate of the Denar has remained largely unchanged against the euro at a level of 61.4 MKD/EUR. The Central Bank intends to maintain its current informal peg to the euro. The banking sector has been less affected thus far than other countries in the region due to Macedonia's lower level of financial integration, limited financial intermediation and an improvement in regulation and supervision. However, there has been a material reduction in bank lending, which is having a serious impact on the real economy, while the annual growth of deposits came to a virtual standstill. The crisis has had only a limited impact on commercial banks' liquidity and deposit withdrawals have been limited, too. Bank lending to the private sector slowed significantly, more than 22 per cent between the end of 2008 and July 2009. [15]

We can see that the country was affected by the economic crisis but the impact of the global financial crisis has remained rather moderate, with output declining by only about 0.7% in 2009. The slow-down of growth was mitigated by a stable banking sector and sustained private consumption. Private consumption remained rather resilient, benefiting probably from a reduction in the savings rate and slightly increasing private transfers, rising to 17% of GDP. [16] The financial intermediation slightly dropped, but it was not significantly hit by the crisis. To increase the competitiveness of the country, it is important to concentrate to fiscal policy, structural unemployment and to improve quality of human capital.

Table 4: Main features of Macedonia between 2006 and 2009 (%)

	2006	**2007**	**2008**	**2009**
GDP-growth	4,0	5,9	4,9	-0,7
Private consumption	6,0	9,8	6,9	0,2
Unemployment rate	36	34,9	33,8	32,2
Current account balance	-0,9	-7,2	-13,1	-4,2
General government balance (GDP %)	-0,5	0,6	-1,0	-2,7
General government gross dept (GDP %)	31,4	23,4	21,4	23,7

Source: European Commission [2010][17]

[13] European Commission[2009]: Enlargement Strategy and Main Challenges 2009-2010, Brussels
[14] IMF [2010]: Global Financial Stability Report, Meeting New Challenges to Stability and Building a Safer System, April 2010, p.213
[15] EBRD [2010]: Strategy for the Former Yugoslav Republic of Macedonia 2010-2013
[16] European Commission [2010]: European Economic Forecast, Spring 2010, p. 155
[17] Ibid. p. 156

However, in the context of the election period and the global economic crisis, the economic policy has deteriorated. The quality and effectiveness of public finances has declined, with a strong increase in public spending, notably in income transfers and subsidies and pensions, which rose well above inflation. This contributed to a sharp increase in external imbalances, while the public sector financing needs crowded out funds for private investment. Public sector debt has increased, but is still relatively low. FDI inflows – like tendencies of the world - decreased markedly, largely due to the deteriorated international environment.

As a result of the crisis, Macedonia had a negative GDP growth in 2009, and the unemployment remained high (32,2% - see Table 4), which is already one of the highest rates in the region. In the medium-term, it is expected that economic recovery and the country's growth potential depend on export markets as well as continued progress in the EU accession process. [18]

Building on this strong record of reform in recent years, the main challenges for the close future: 1) acceleration of improvement in the business environment, 2) further strengthening of the financial sector to improve private companies' access to finance and 3) modernisation of infrastructure. Significant improvements in the business environment were achieved before the crisis, among other things by reducing the taxes for corporate and personal income, simplifying business registration, strengthening competition law. In the financial sector, the implementation of a new banking law has strengthened the stability of the banking system and the central bank's supervisory authority. In infrastructure for example, the country has increased competition in the telecommunication sector and has improved tariff setting methodology for water and waste water. Despite reforms, corruption and judicial shortcomings and the lack of effective rule of law and the uncertainty of property rights undermine investor's confidence. Banks still face problems with enforcement of financial collateral and the court procedures. Lending has become more restricted as a result of the crisis and the major problem is that companies see poor access to credit in those times, where they have to have it. Ensuring reliable power supplies is still a concern. The policy of gradually increasing electricity prices to market-based cost recovery levels must continue. In the field of transport, the main challenges are the further upgrade of the regional and local road networks and the improvement of railway operations. In this area with different devices (for example through IFI) the European Union helps Macedonia.[19]

5. Economic forecast in Croatia

Prospects for a short-term economic recovery remain highly uncertain. At the current stage, there is no clear evidence that economic recovery has started to unfold. Economic activity continued to fall, but the worst of the current recession seems to be over. However, a clear turnaround has not yet been reached and marked stimulation of economic activity over the short term is currently not to be expected. Domestic confidence levels may not recover quickly and market expectations are expected to remain subdued. This does not support a strengthening of domestic demand. The effects of the recession the labour market, declining employment and rising unemployment will continue to be felt in 2010. Bleak job prospects and lower wage growth will limit the scope for an increase in incomes. Therefore, private consumption will decrease. Domestic credit growth has decelerated significantly during the crisis, due to both demand and supply factors. Lower demand for loans as well as tighter financing constraints and higher risk awareness by banks have led to a slowdown in bank lending, particularly to private households. Although the banking sector is well-capitalised, sound and profitable, risk perception by banks remain elevated. As a result of liquidity problems of the corporate sector, the ratio of non-performing loans has been rising (from 2008 to 2009 from 4,9% to 6,4[20]) and the quality of the loan portfolio of banks may further deteriorate. In spite of the recent government measures to stimulate lending, banks are expected to remain reluctant to accelerate lending activity quickly. The relatively low growth of private sector borrowing, in combination with higher interest rates, is expected decrease economic activity.

[18] European Commission [2009]: Enlargement Strategy and Main Challenges 2009-2010, Brussels
[19] Ibid.
[20] IMF [2010]: Global Financial Stability Report, Meeting New Challenges to Stability and Building a Safer System, April 2010, p.213

In short term, public consumption and investment are unlikely to accelerate in view of the fiscal constraints and huge refinancing needs of the public sector. In medium or long term, it appears that Croatian economy may come from net exports. However, it is still to be seen to what extent improvements in the external environment, notably a recovery of global and EU demand, will translate into a strengthening of export growth. [21]

Overall, the Croatian economy is projected to record a negative growth rate in this year. Upside risks are mainly related to the economic recovery in the EU, to the clear prospect of Croatia's accession in the near future, which may be an additional impetus to the economy through, with stronger net FDI flows. But there are also significant downside risks, which are mostly related to the process of real sector restructuring, high subsidies of the state and inter-company payments problems. For 2011, the forecast projects positive growth of around 2%, mainly based on a slight acceleration of private consumption and investment growth.

Table 5: Main features of Croatia between 2009 and 2011 (%)

	2009	**2010***	**2011***
GDP-growth	-5,8	-0,5	2,0
Private consumption	-8,5	-0,5	2,0
Unemployment rate	10,4	11,5	11,0
Current account balance	-5,1	-5,5	-5,9
General government balance (GDP %)	-4,1	-4,0	-3,9
General government gross dept (GDP %)	38,5	42,5	44,5

Source: European Commission [2010][22] (* provision)

As a result of financial crisis, the high external deficits of the past years have decreased. From 2008 to 2009, the latter fell from 9,3% to 5.1% of GDP – see earlier Table 3. Reduced capital inflows and domestic demand have led to a sharp reduction in the trade and the high current-account deficits because of decreased foreign direct investments and imports. In the near future, current-account deficit will arise again, because total exports are expected to recover slowly, in line with an expected strengthening of foreign demand in key trading partners. Also total imports will pick up only slowly thereafter. However, the current-account deficit is projected to remain below 6% of GDP in 2010 (see Table 5).

As a result of rapidly contracting domestic demand and lower commodity prices, average inflation came down significantly (in 2009, to 2.4% compared to 6.1% a year before). Inflationary pressures are expected to remain low over. Domestic demand is set to only slowly recover. The higher prices for imported raw materials are likely to have an effect on the domestic price level, which can increase inflation. Moreover, some mild inflationary pressures will result from further adjustments in administrative prices which will be necessary in the context of EU accession. At the same time, it is reasonable to assume that a stability-oriented monetary policy framework will help to prevent a significant re-acceleration of inflation over the medium term.

In 2010, the unemployment rate will continue to increase (while in 2009 it was 10,4%, in the end of 2010 it will reach the level of 11,5%). The slight recovery of economic activity forecast for 2011 is expected to increase a significant growth of employment. (see Table 5) Fiscal deficit widened significantly despite several re-balancing measures. The global crisis brought Croatia's public finances under severe pressures, necessitating subsequent budgetary adjustments (the government accepted reforms also in April and July of 2009). A number of fiscal adjustment measures were taken to compensate for rapidly falling revenues, such as a VAT increase, a special tax on income and decreased current spending (for example public-sector wages were decrease). These were not effective, because total spending in the third revised budget remained at the level of the original budget, while budgeted revenues were reduced by around 10%. The deficit was 4.1% of GDP in 2009, which is 0.7% above the target, and there are little prospects for rapid fiscal consolidation due

[21] European Commission [2010]: European Economic Forecast, Spring 2010, p. 152-153
[22] Ibid. p. 154

to the lack of public expenditure reforms. Finally, the general government debt-to-GDP ratio is set to increase markedly. Overall, public finances in Croatia will remain under pressure on both the revenue and spending sides of the budget. Therefore, a key challenge will be to implement a medium-term fiscal strategy, aimed at reducing budget rigidities and enhancing the efficiency and quality of public spending. [23]

6. Economic forecast in The Former Yugoslav Republic of Macedonia

The impact of the global financial crisis has remained rather moderate, with output declining by only 0.7% in 2009. Private consumption remained rather resilient, benefiting probably from a reduction in the savings rate and slightly increasing private transfers, which reached 17% of GDP. Furthermore, increased public transfers have helped to stabilise domestic income and demand. Similar to Croatia, during 2009 investment significantly decreased in response to sharply declining export demand and continued uncertainty. In response to the financial crisis, the government between December 2008 and March 2010 adopted four anti-crisis packages, which has envisaged an increase in public investment. However, the actual impact of all packages on public revenue and expenditure so far has been very limited: total government spending actually dropped by nearly 1% of GDP, while revenues declined by 2,5%, bringing the fiscal deficit from 1% of GDP in 2008 to 2.7% in 2009. According to survey of European Union, in 2010 and 2011 the fiscal deficit will decrease slightly, which means that European Union thinks that the country will respect its fiscal targets.

Table 6: Main features of Macedonia between 2009 and 2011 (%)

	2009	**2010***	**2011***
GDP-growth	-0,7	1,3	2,0
Private consumption	0,2	1	2,0
Unemployment rate	32,2	31,7	31,0
Current account balance	-4,2	-6,2	-7,9
General government balance (GDP %)	-2,7	-2,5	-2,5
General government gross dept (GDP %)	23,7	25,4	26,7

Source: European Commission [2010][24] (* provision)

Consumer-price inflation was slightly negative during most of 2009, leading to an average decline of consumer prices by 0.8%. In the beginning of 2010, inflation remained low, as the continued decline in food prices helped to compensate rising costs for housing and transport. Official labour-market data point to a continued increase in overall employment, despite significant job losses in those industries primarily affected by the global crisis (steel and textile industries). However, employment at municipalities and in the trade sector appears to have increased markedly. The former is probably due to increased public spending, the latter to strengthened registration procedures. Unemployment continued to decrease slightly, but still remained at high level. Youth unemployment stayed at some 55%, which gives rise to concern.

According to forecasts we can observe a moderate recovery, but structural challenges remain. Moreover, in 2010 the main shock of the global crisis is expected to subside, which should allow the economy to expand by around 1,25%. The main sources for recovery will be private and public consumption, while exports are likely to remain in same level. In 2011, economic activity is expected to increase by some 2%, benefiting from the recovery in the country's export markets. Because of the uncertainties related to the global economy, domestic demand and real disposable income will be key factors for the country's growth dynamics, which probably will stagnate in the next two years. The wages depend on inflation which depends on international prices of energy and raw materials. The inflation will be stay in low level till prices of energy and raw materials do not grow significantly. [25]

[23] European Commission [2010]: European Economic Forecast, Spring 2010, p. 153-154.
[24] Ibid. p. 156
[25] Ibid. p. 155

In 2010 and 2011 the current-account deficit is likely to deteriorate, due in particular to increasing investment. In the end, general government gross dept will increase (see Table 6), which will be caused by the fact that the budget for 2010 and programmes for 2011 envisage a significant increase in public spending. The forecast expects that in case of spending constraints, the authorities will reduce capital spending, as has happened in the past at similar situations. Accelerating domestic activity and improved efficiency in tax collection should help to reconcile targets. [26]

7. Conclusions

As wee see above, the crisis reached Croatia and the Former Yugoslav Republic of Macedonia. The two candidate countries of the European Union were affected by the crisis in different measures in spite of the fact that they belong to the same region. Before the crisis both country reached a significant economic growth, but the effect of crisis Croatian economy felt down more considerably (see Table 7). In both countries – similar to global trends – the amount of foreign direct investments decreased significantly and inflation dropped. In Croatia, the impact of crisis has been mitigated by a resilient banking sector and strong foreign reserves, while in Macedonia by a stable banking sector and sustained private consumption (in which the government helped). Considering forecasts, in Croatia the short term economic recovery is uncertain, and depends on growth of export, while in Macedonia the moderate decline will be followed by moderate recovery, which depends on private consumption. In accordance with the above, we can conclude that the answers to moderate the effects of crisis were not really successful, which partly can be explained by the countries' little world economy weight. Macedonia less integrated into the world economy system than Croatia, thus Macedonia was less affected by the crisis. In spite of these, both countries depend on the current situation of world economy and global demand, and mostly on the economy of European Union.

Table 7: Real GDP growth in Croatia and Macedonia between 2006 and 2011

	2006	2007	2008	2009	2010*	2011*
Croatia	4,7	5,5	2,4	-5,8	-0,5	2
Macedonia	4	5,9	4,9	-0,7	1,3	2

* Provisional values
Source: Eurostat [2010][27]

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www.southeast-europe.org

[26] European Commission [2010]: European Economic Forecast, Spring 2010, p. 154
[27] Website of Eurostat [2010]: http://epp.eurostat.ec.europa.eu/tgm/table.do?tab=table&init=1&plugin=1&language=en&pcode=tsieb020 (2010-10-16)