

E&B: Mr.Tieman, thank you for accepting to give this interview. Let us start with the internal developments within the IMF. You are resident representative of the International Monetary Fund (IMF), running its office in our country. Few years ago the IMF opted to close a number of its offices in the region, but not the one in Skopje. How do you explain this?

Mr.Tieman: Thank you for asking me for this interview. The IMF office in Skopje, much like the offices in other countries, serves three main purposes. The first is to gain information and data about economic developments, and discuss economic policies in the country. The second goal is to provide information on how the IMF sees economic developments in the country, the region, and the world as a whole to domestic policy makers. Both of these goals involve frequent interaction with domestic policymakers, the business community, and civil society. The third goal is more general outreach to the public, through presentations at conferences and other events, but also by issuing press releases and presenting our views in the media. You can imagine that all of this is much easier done locally than from Washington. Thus, having a local office enables the IMF to have a much closer link to the country than otherwise would be possible.

The reasons that many offices were closed in 2007-08 were twofold. First, the economies of most countries in the region (including Macedonia) were doing well at the time, reducing the need for a local presence. Second, internally, the IMF went through a big reorganization, including large budget cuts, which meant having to make difficult choices, including firing staff at headquarters and closing local offices. This meant that for each office individually, the IMF management had to decide whether to keep it open or close it. The fact that the IMF has had a close relationship with Macedonia over the years, including many Fund programs, was a factor in deciding to keep the local office in Skopje open.

The global economic crisis that started in fall 2008 changed this picture. The economies of many countries in the region were hit severely, and many came to the Fund for assistance. As a consequence, new offices were actually (re)opened in the region.

E&B: Mr. Strauss-Kahn, the previous managing director of the IMF, was replaced several months ago. It is good that despite the huge media coverage of the case, the unpleasant developments have not dented the reputation of your institution.

Mr.Tieman: After the resignation of Mr. Strauss-Kahn as IMF managing director in May, the IMF Board moved swiftly to replace him. The application procedure was short and the selection of the new managing director, Ms. Christine Lagarde, was confirmed in late June. Ms. Lagarde has a long track record in both the business community, where she was chairman of a large global law firm from the United States, and public service, where she served in the government of France from 2005 onwards. First as minister of foreign trade and, from 2007 onwards, as minister of finance and economy.

The IMF Board and its member countries around the world have welcomed the new managing director to her post, citing her extensive experience. While the circumstances under which Mr. Strauss-Kahn resigned were obviously difficult, the work at the IMF, an organization with some 2,500 staff, continued as usual. And with the quick selection of the new managing director, and the appointment of three new deputy managing directors in the last year, the new management team is now complete.

E&B: While he was in charge, Mr. Strauss-Kahn started to somewhat change the IMF's philosophy and approach, making the institution more active in finding solutions for the global economic challenges, at the same time apparently "softening" the well-known toughness of the IMF. During the global financial turbulence in the last few years the IMF assisted substantially in overcoming the crisis, concluding promptly financial packages with a number of countries, introducing and promoting new instruments. What are the expectations from Mrs. Lagarde, the newly appointed managing director, is there going to be a change in the direction?

Mr. Tieman: During the economic crisis, the IMF became more responsive to countries with macroeconomic problems. This was evident in both the speed with which new IMF packages were negotiated, the size of those packages, and to some extent, the conditions attached to those packages. In many cases, the fund recognized that many countries had a track record of decent macroeconomic policies, which meant that there was both competence and ownership at the local level. This implies that there is less need for strict conditionality in IMF programs with such countries. Still, IMF programs will always aim to help countries come out of the crisis they are in, and when that requires tough medicine, in the form of difficult adjustment of policies, we will not hesitate to prescribe such strong medicine.

Perhaps the best example of the new ways in which the IMF looks at things lies in the creation of two new IMF facilities: The Flexible Credit Line (FCL) and the Precautionary Credit Line (PCL). Both facilities pre-approve countries for IMF credit. The facilities are available for countries that have a track record of good macroeconomic policies over a number of years. The FCL has supported Mexico, Poland and Columbia throughout the crisis, while Macedonia has had a PCL arrangement in place since January 2011.

I do not expect IMF policies in this regard to change substantially with the appointment of our new managing director. As finance minister of France, she was very much part of the group of (G-20) global policymakers that dealt with the global crisis. As such, she is intimately familiar with the role the IMF is playing in the crisis and its aftermath, and she has repeatedly praised the way the institution has acted in the crisis and continues to perform.

E&B: The global economy is entering a very uncertain period that has had an impact on the consumers' sentiment and investors' confidence. Which are the main generators of this global economic instability? Is there going to be a double-dip recession?

Mr. Tieman: The world economy has gone through the deepest economic crisis since the 1930s. This is particularly true for most of the developed economies of North America and Western Europe. While the height of the 2008 economic crisis seems to be behind us, these economies are recovering only slowly. One major factor in this slow growth is that households in many developed countries were over-indebted. This means that, going forward, these households will need to decrease their debt, which implies that they need to spend less and save more. Combined with higher unemployment, at the macroeconomic level, this leads to lower consumer and investor confidence, lower consumer spending, and lower growth. It also makes it more difficult for countries to increase their exports, as the final demand in many countries has not yet recovered to the level of before the crisis. The path to full recovery will hence be long and will exhibit bumps along the way.

Recently, the world economy seems to have hit such a bump. Uncertainties have increased, and growth numbers from the second quarter of 2011 have disappointed. Part of this picture were the high oil prices in the first half of the year, and the disruption to global supply chains as a result of the tsunami in Japan. In addition, off late, financial markets have displayed renewed uncertainty with respect to the Eurozone and the United States economies. While the risk of a double-dip recession has hence increased, it remains more likely that developed economies will continue to grow.

E&B: The world managed to get out of the last recession but obviously new measures are needed. FED applied quantitative easing, then gave an unusual announcement that the interest rate will remain very low and unchanged for two years. The ECB also reacted. Is the room for maneuver for the authorities to introduce new and effective measures reduced now, compared to three years ago, and what can be done? It seems that now the need for fiscal consolidation is more pronounced than before, but tight fiscal consolidation may stall the desired economic recovery. It is not simple to find the right path and the balanced solution.

Mr. Tieman: As I mentioned above, the current stage of the recovery remains fragile. In terms of policy instruments that can be used to stimulate growth, you are correct to state that much has been done already. Most countries have used considerable fiscal space since 2008 to soften the blow of the crisis, and monetary policy has been very accommodative ever since. Going forward, different policies would be appropriate for different countries. To a differing extent, almost all countries could undertake further structural reform, to free up labor and product markets. In addition, the countries that still have fiscal space should consider short-term fiscal stimulus, while spelling out how to normalize the fiscal situation in the medium-run. Monetary policy does not seem to have much further to go, with interest rate at rock-bottom and several rounds of quantitative easing (in essence, printing money to buy government bonds) behind us.

Going forward, it remains essential to build confidence, in financial markets, as well as with business and consumers. For the Eurozone, this means that it remains of crucial importance that financial markets can be convinced that a comprehensive political compromise to fully resolve the sovereign debt problems in the periphery countries is found. This will involve some difficult decisions to improve crisis management, but also decisive actions to strengthen banks' health and supervision, continued efforts at fiscal consolidation, and concerted efforts to re-launch Europe's growth engine through the implementation of structural reform. For the United States, political cooperation that would provide clarity on medium-term fiscal consolidation is important, and would open up the possibility for short-term stimulus. Working towards a solution on these important issues will provide more certainty to business and consumers, leading to more investment and growth, and serve to convince financial markets that problems are being dealt with.

Closer to home, most economies in Central, Eastern, and Southeastern Europe are recovering from the crisis. But renewed turbulence in Europe in particular, could once again hit these export-dependent economies. It hence remains essential to build up buffers, and remain cautious and vigilant in economic planning going forward.

Indeed, it is not simple to find a balanced solution at these difficult times. However, policies along the lines outlined above should rebuild confidence and lay the basis for long-term sustainable economic growth.

E&B: What are the IMF's views about the developments in the EU, our largest trading partner? What are the prospects for EU to return to the faster growth path within the next 24 months?

Mr. Tieman: The EU's recovery is well-underway, but uncertainties and risks remain, and developments over the summer have not been positive. First of all, the recovery in Europe has been uneven, with some countries continuing to suffer deep recessions, while other have rebounded relatively fast from the crisis. Overall, Eurozone growth is projected at 2 percent in 2011 and 1.7 percent in 2012. Such solid growth would be favorable for countries in Central, Eastern, and Southeastern Europe, for most of which (including Macedonia), the (other) Eurozone countries are by far their most important trading partners. However, given recent economic developments, and the increased uncertainty mentioned above, it is likely that these growth forecasts will be revised downwards. Because of the extensive trade links, slower growth in the Eurozone would have a considerable impact on the exports from, and hence growth of, economies of Central, Eastern, and Southeastern Europe, including Macedonia.

E&B: Now, let us turn from the global to our local economic developments. By providing the Precautionary Credit Line the IMF is the savior of the Government's budget. This credit line was not supposed to be used by the Government, but rather to serve as an insurance policy in case the Government could not finance the projected budget deficit by borrowing on the international financial markets. Anyway, so far the Government withdrew millions of euros from this credit line. At the beginning of this September, the Board of the IMF discussed the findings of the regular review made by the IMF mission team, led by Mr. Wes McGrew about the compliance with the requirements of the PCL. Could you share with our readers the main conclusions of the IMF's Board?

Mr. Tieman: The IMF Board completed the first review of Macedonia's Precautionary Credit Line arrangement on Friday, September 2. This was after an IMF mission visited the country in June. After the Board meeting, deputy managing director Ms. Shafik, who chaired the Board meeting, said that Macedonia continues to pursue sound economic policies that are consistent with the program supported by the PCL arrangement. Growth has picked up, underlying inflation remains low, international reserves have been broadly stable, and the 2011 fiscal deficit target under the program is within reach.

She also mentioned that, nonetheless, Macedonia's decision in March 2011 to make a purchase under the PCL arrangement highlighted remaining external vulnerabilities. The authorities are strengthening debt management policies and practices, focusing both on improving access to external funding and on developing the domestic public debt market. This will help to ensure that Macedonia is able to meet its financing needs from private market sources in the future. In this context, the authorities intend to publish an action plan on debt management reforms and will draw upon IMF technical assistance for this initiative.

In addition, Ms. Shafik cautioned that despite sound policies and fundamentals, Macedonia remains exposed to unusually high levels of risk related to global growth and financial conditions as well as regional developments. This calls for continued vigilance and further efforts to address remaining vulnerabilities and improve data adequacy. The PCL plays a valuable role in supporting market confidence by signaling Macedonia's commitment to prudent policies and strengthening its reserve buffers. While Macedonia is not expected to require further purchases under the PCL, the availability of these resources provides additional insurance against adverse external developments.

E&B: There are two major concerns related to the future economic sustainability of the country. One is the doubt about the actual size of the budget deficit. It is measured on cash basis, which does not capture the liabilities undertaken but still not paid by the Government. If there are arrears and if they are sizeable, the budget deficit might be much larger than perceived. What is the IMF's view on this?

Mr. Tieman: Most countries in the world compile their budgets on a cash basis. Nevertheless, it is important to incorporate unpaid future liabilities into the forward-looking calculations of the government finances. Such contingent liabilities include commitments on pensions, public sector wages, and health care expenditures. In the case of Macedonia, there is also the Skopje 2014 building project. The most important thing is to be transparent about current and future costs and commitments. That way, the public can be fully aware of contingent liabilities, and act accordingly.

In the case of Macedonia, there is clarity about some payment arrears in the health sector, which have repeatedly built up and been cleared over the last few years. To deal with the buildup of these deficits requires a more comprehensive reform of the health sector, which I understand the authorities are working on. As to pensions, the deficit in the state pension fund is made up from general tax revenues. Going forward it is important to ensure that this deficit does not increase, as it would then take a substantial part of tax revenue to make up for such an increased deficit. A similar story applies to public sector wages, which are also paid out of general tax revenue. I understand that, after several years of public sector wage freezes, the government plans to increase wages in three stages, toward the end of 2012, 2013 and 2014. Such wage increases should go hand-in-hand with comprehensive public administration reforms, to increase the efficiency of the administration, and make employment and promotion policies more merit-based.

As to the budget deficit, the authorities have committed to keep the deficit to 2.5 percent of GDP this year, and lowering it to no more than 2.2 percent in 2012. While this is indeed the deficit on a cash basis, we believe it presents a good picture of the country's fiscal situation.

E&B: The second concern is the overall debt of the country. Not the size of the debt, where there is room for further borrowing. The concern is related to the pace at which the debt increases. Is this a matter of concern for the IMF?

Mr. Tieman: No. The current government debt (per IMF methodology) stands at 27 percent of GDP, which is a moderate level of indebtedness. Most economists would agree that a fiscal policy in which the authorities run a higher deficit in time of low economic growth is appropriate. Such countercyclical policies work to cushion the effects of recessions on the wider economy, as the government stimulates the economy at a time when the private sector retracts. A countercyclical policy of course also implies the reverse: when the economy grows fast, the deficit should be lower, or there should even be a surplus.

At this moment, the Macedonian economy is still growing below its potential growth rate, which we estimate to lie in the 4-4.5 percent range. Hence a deficit of the magnitude that the government is currently running remains appropriate. Once the economy grows faster, we believe the deficit should be reduced further. Reducing the deficit to around 1.5 percent of GDP would stabilize the government debt as a percentage of GDP at its current moderate level. Further reductions of the deficit to below this number would reduce the debt, and hence increase the country's fiscal buffers. Such a reduction of the

deficit to below debt-stabilizing levels in good times is therefore prudent and appropriate, as it would create room for higher deficits in bad times.

Deficit reduction going forward will prove challenging. There are many demands on the government budget from all parts of society. And, going forward, increasingly the government will want to allocate more money to capital investment. Such investments include building roads, railways, and schools, just to name a few examples. These kinds of investments increase the long-term growth potential of the country. Higher growth, in turn, will help increase the wealth of the citizens of the country towards European levels.

E&B: In your view, what should be the main economic moves of the Government in the next two years?

Mr. Tieman: The Macedonian economy is recovering steadily from the global economic crisis, and the government should take full advantage of that. First of all, the recovery means that there will be more money available in the form of higher tax receipts. A substantial portion of this money should be invested in physical and human capital to increase the country's long-term growth potential. I understand that the authorities are planning an increased capital investment budget, as well as attention for education. This will necessarily mean containing expenditure in all kind of other areas, which requires thorough and realistic budget planning, as well as considerable budget discipline. Fortunately, the authorities have a track record and hence experience in maintaining budget discipline, even under the difficult circumstances at the time of the crisis.

Another area of importance going forward lies in debt management. First, it is important that the government develops the domestic debt market further and borrows a larger share of its deficit domestically. A liquid domestic debt market acts as an insurance policy in the sense that money can be borrowed even when circumstances in external markets are difficult. In addition, having a government risk-free yield curve available would make it easier for the banks to lend money long-term to the business sector, which would in turn facilitate investment. Building up the government yield curve would entail lengthening the maturity of outstanding government bonds, even if this requires higher interest rates initially. Measures to increase the liquidity of the secondary market would further help increase domestic investor attention. Tailoring debt instruments to the needs of the second-pillar pension funds is another avenue that should be pursued.

In the media and at economic debates, I often encounter the argument that the state should not borrow more on the domestic market, as this would crowd out financing for the private sector. I think this argument needs to be nuanced. The Macedonia economy currently actually seems to face a situation of excess liquidity, as evidenced by the MKD 27 billion in central bank bills purchased by the commercial banks. In such a situation, increasing domestic government borrowing (while keeping the deficit at moderate levels) would not starve the private sector of capital. In contrast, as I have argued above, the buildup of a liquid domestic yield curve could actually serve to facilitate financing of the private sector.

Taken together, these arguments lead me to conclude that Macedonia should start issuing more domestic debt. It is a practice of modern debt management that most emerging market and developed countries follow. And fears of crowding out are misplaced in an environment where deficits remain moderate and there is ample liquidity.

As to external borrowing, the authorities should seek to increase liquidity of their debt instruments, manage rollover risk, and take advantage of favorable market conditions early to pre-finance future needs. The issuance of additional Eurobonds is appropriate, as it would work towards these goals. Eurobond issuance should hence be pursued, even knowing that market interest rates will vary. In this respect, financing the part of the 2012 budget deficit that is not financed domestically and the rollover of the € 175 million Eurobond that comes due in January 2013 are the main challenges.

Of course all government financing should be in the context of a responsible overall budget envelope. The (net) amount one needs to borrow is determined by the size of the deficit. As long as the deficit is modest, the net amount the government needs to borrow on the domestic and external market will hence remain contained.

Finally, a word to the Macedonian business community, and its invaluable contribution to the economy. At business conferences, or in the press, representatives of the business sector often ask the government for support to solve this or that problem. Demands range from additional regulation to subsidies or tax exemptions for pet projects. To me, the image comes across as the business community that thinks that the government should play a prominent role in business. This is very different from many major developed countries, where the business community would instead ask the government to “please get out of the way” by reducing regulation, subsidies, and taxes, and let business people do what they do best: run their business. The private sector is the main engine of economic growth in most of the world, Macedonia included. I believe the Macedonian business people are no different from business people elsewhere, and exhibit lots of entrepreneurial skills. They do not need additional regulation or subsidies to be good businessmen. Fewer and better laws, rules, and regulations, leaving the business community to itself to take advantage of such an environment, could unlock significant additional economic growth.

E&B: At the end, you have been running the IMF’s office in our country and you live here for two years already. What are your impressions about your life here, what are the things you like the most and things you like the least?

Mr. Tieman: My family and I have been in Macedonia almost exactly two years now. We fell in love with the country and are very much enjoying life here. The people all over Macedonia are friendly, open, and very hospitable. The food is good, and we have learned since we arrived that the Macedonian wines are of excellent quality. Also, the country has some stunning natural beauty, from the mountain resorts and ski centers in Sar Planina and Pelister, to the Tikves wine growing region, the clear mountain air around Berovo and in Galicnik, and of course mount Vodno right behind the city. On top of that, there is the history and culture that is very interesting, and evidenced by churches and mosques everywhere, most of all in Ohrid. We found Treskavec monastery, near Prilep, to be a dramatic combination of long history and spectacular natural beauty.

There is little I can think of on the down side. I would perhaps mention the smog that hangs over Skopje in the winter time. People that are born and raised here often take it as something normal. But to outsiders like myself, it is clear that this is not normal, but rather a serious long-term health problem. It’s man-made, and therefore can be solved by man as well. This would entail further cleaning up industry around Skopje, but also changing the methods by which people heat their houses in winter. More efficient wood and coal stoves, widely available in Scandinavia for instance, could be big contributors to deal with this problem.

E&B: Thank you very much for the interview.

Mr. Tieman: Thank you! Let me just add that all information related to the IMF and Macedonia can be found at our local website: <http://www.imf.org/skopje> .