

VI. External Sector

According to the Decision on foreign exchange policy and the Balance of payments projection for 1999, creation of conditions for more sustainable foreign trade, increased foreign exchange inflow on the basis of export of goods and services, regular payment of the external debt, maintenance of the Denar exchange rate on the targeted level, and increase of foreign exchange reserves was projected. However, due to the strong external shock caused by the war in FR Yugoslavia, a revision of the projection of the macroeconomic policy for 1999 was made, and herewith, of the Balance of Payments projection as well, which was later used as a basis for the Donor Conference in Paris. With the revised projection, deficit in the current account of the balance of payments in the amount of US Dollar 510 million was projected, as well as strong contraction of export and import of goods, and uncovered current account deficit in the amount of US Dollar 422 million. Still, despite the unfavorable external events in 1999, certain positive movements in the external sector of the Macedonian economy were registered, expressed through reduced current account deficit and increased foreign exchange reserves and preserved stability of the Denar exchange rate against the Deutsche mark. However, the high foreign trade deficit still remains a significant problem.

6.1. Balance of payments¹⁴

In 1999, the deficit in the current account of the balance of payments was significantly reduced. Namely, it equaled US Dollar 136 million, and was lower by US Dollar 172 million, or by 55.7% compared to 1998. Thus, the deficit in the current account of the balance of payments was reduced from 8.5% of GDP in 1998 to 3.9% of GDP in 1999. In addition, as a result of the reduced foreign trade and increased transfers, in the second and third quarters of the year a surplus in the current account of the balance of payments in the amount of US Dollar 9 million and US Dollar 18 million, respectively, was realized. However, in the last quarter of the year, the structure of the foreign trade of the Republic of Macedonia significantly deteriorated, due to the more dynamic economic activity and restructuring of the economy. In addition, high deficit in the current account of the balance of payments in the amount of US Dollar 109 million was realized.

However, the reduced deficit in the current account of the balance of payments was not a result of a significant decline in the trade account deficit. In 1999, the deficit in the trade account equaled US Dollar 409 million¹⁵, and compared to 1998 it is lower by only US Dollar 9 million, or by 2.2%. In addition, it should be taken into account that this deficit is registered despite the reduction in foreign trade by 7.0%, due to decline in the exports and imports of goods by 7.8%, and 6.4%, respectively.

¹⁴ Preliminary data.

¹⁵ The deficit in the trade account of the balance of payments differs from the deficit in the foreign trade presented by the Statistical office. The reason for this is that the imports in the balance of payments are presented on f.o.b. basis, while the official statistics presents imports on c.i.f. basis.

Table 16

Balance of payments of the Republic of Macedonia

(in USD million)

	1998 ¹				1998	1999 ²				1999
	Q1	Q2	Q3	Q4		Q1	Q2	Q3	Q4	
1. Current account	-86	-59	-17	-147	-308	-55	9	18	-109	-136
1.1. Goods, net	-73	-99	-70	-176	-418	-57	-66	-88	-198	-409
Exports, f.o.b.	292	336	339	325	1,292	254	250	346	343	1,192
Imports, f.o.b.	-365	-435	-410	-502	-1,711	-310	-316	-434	-541	-1,601
1.2. Services, net	-39	-45	-40	-50	-173	-34	-17	-12	-12	-75
1.3. Income, net	-14	-3	-19	-9	-44	-13	-2	-22	-6	-44
1.4. Current transfers, net	40	88	112	88	327	49	95	140	108	392
Official	8	4	4	12	28	15	36	5	9	65
Other	32	84	108	76	299	34	58	136	99	327
2. Capital and financial account	79	74	16	187	355	26	-25	-32	70	39
2.1. Capital account, net	0	0	0	-2	-2	0	0	0	0	0
Capital transfers, net	0	0	0	0	0	0	0	0	0	0
Official	0	0	0	0	0	0	0	0	0	0
Other	0	0	0	0	0	0	0	0	0	0
Acquisition/disposal of nonprod., nonfinan. assets	0	0	0	-2	-2	0	0	0	0	0
2.2. Financial account, net	79	74	16	189	357	26	-25	-32	70	39
Direct investments, net	1	21	40	56	118	10	7	3	3	24
Portfolio investments, net	1	2	1	4	8	0	0	0	3	3
Other investments, net	77	51	-25	128	232	15	-32	-35	64	13
Trade credits, net	27	18	-6	66	105	-23	-13	-21	55	-2
Loans, net	28	25	41	88	182	1	2	46	1	50
Foreign currency and f.c. deposits, net	22	8	-61	-26	-57	34	-25	-67	3	-55
o/w: Commercial banks, net	22	8	-35	-26	-31	34	-15	-62	3	-40
Other, nets	0	1	1	0	2	4	4	6	5	19
3. Errors and omissions	0	13	-1	-35	-23	29	44	65	74	212
4. Total balance	-7	28	-2	5	24	0	29	51	35	115
5. Financing	7	-28	2	-5	-24	0	-29	-51	-35	-115
5.1. Change in official reserves ³	7	-28	-2	-9	-32	0	-30	-73	-37	-140
Gross domestic assets	7	-40	0	-9	-42	4	-27	-86	-32	-141
IMF	0	12	-2	0	10	-4	-3	14	-5	2
5.2. Change in total arrears	0	0	0	0	0	0	0	0	1	1
New arrears	0	0	0	0	0	0	0	0	1	1
Repayment of arrears	0	0	0	0	0	0	0	0	0	0
5.3. Moratorium - Paris Club	0	0	0	0	0	0	1	18	1	21
5.4. Rescheduling	0	0	4	4	8	0	0	3	0	3

1/ Final data

2/ Preliminary data

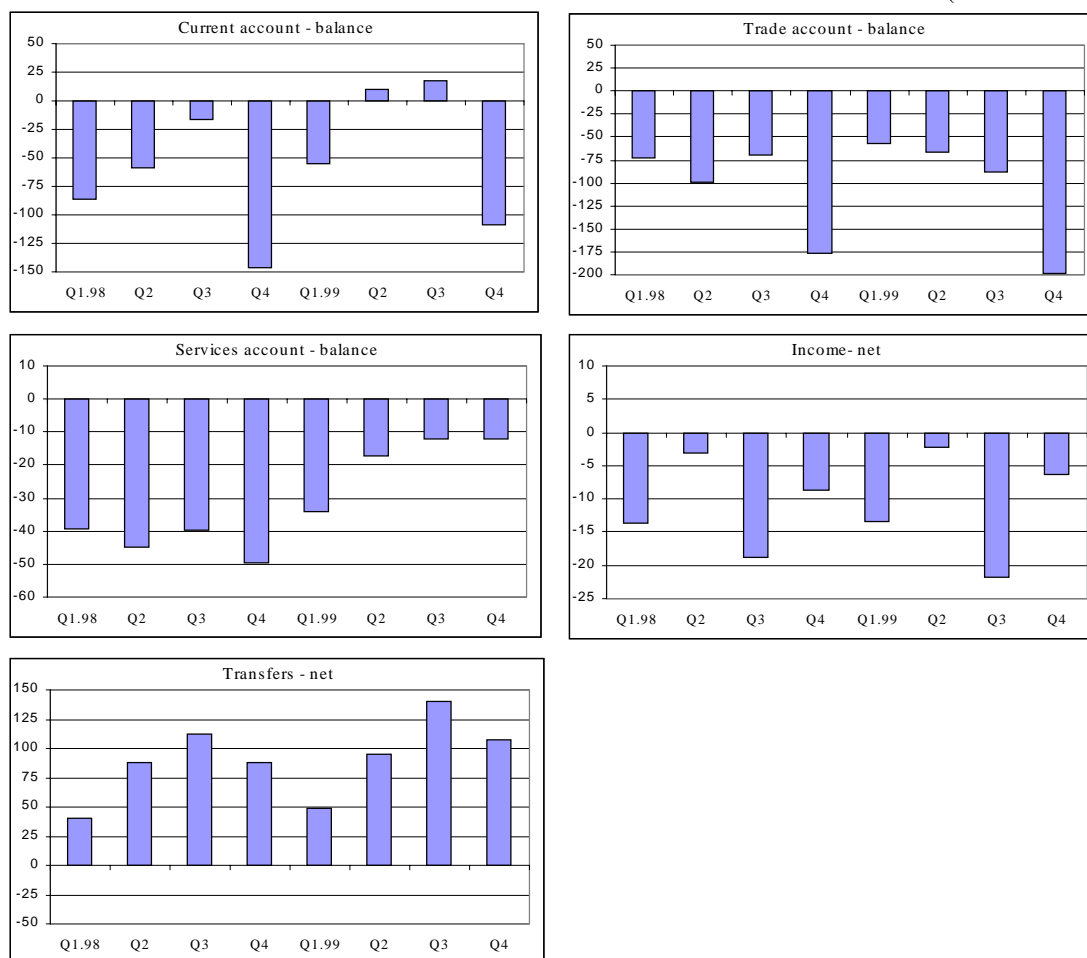
3/ Increase in assets is denoted by a negative sign

The reduced deficit in the current account of the balance of payments in 1999 is mainly due to the reduced deficit in the services and increased surplus in the current transfers. Namely, in 1999, the deficit in the services was US Dollar 75 million. Relative to the previous year, it is lower by US Dollar 98 million, or by 56.4%. The improvement in the balance of services is a result of increased logistic support, transport, telecommunications, business and other services provided to the nonresidents, especially in the period during and after the end of the crisis in the region (in the second and third quarter).

Chart 21

Components of the current account of the balance of payments

(in USD million)



On the other hand, a surplus in the current transfers in the amount of US Dollar 392 million was registered in 1999. Compared to the surplus registered in 1998, it is higher by US Dollar 64 million, or by 19.7%. In addition, the surplus in the official transfers increased by US Dollar 37 million, or by 130.6%, and reached US Dollar 65 million. This is due to the increased inflow of funds during the crisis in FR Yugoslavia (Kosovo). At the same time, the surplus realized in private transfers equaled US Dollar 327 million, which is by US Dollar 27 million, or by 9.2% more relative to the previous year.

The deficit in the "income, net" category of the balance of payments in 1999 was US Dollar 44 million, which mainly refers to net-interest. Namely, on the basis on net-interest, outflow of US Dollar 43 million was realized. In addition, compared to 1998, the deficit in the "income, net" category is almost unchanged.

In the previous years, the deficit in the current account of the balance of payments was mainly financed by financial transactions. In 1999, surplus in the amount of US Dollar 39 million was registered on the capital and financial account of the balance of payments.

The direct and portfolio investments in 1999 were US Dollar 27 million (out of which US Dollar 24 million are foreign direct investments). Compared to 1998, they are lower by US Dollar 99 million, or by 78.6%. In addition, despite the intentions to maintain the pace from 1998, when the highest amount of foreign direct investments in the Republic of Macedonia was achieved, the war in FR Yugoslavia in the second quarter of the year

increased the risk for investment in the region. However, in the second quarter of the year, several large projects for foreign capital inflow in Republic of Macedonia were agreed, expected to be finalized in the year 2000.

In 1999, in the "other investments, net" category from the balance of payments of Republic of Macedonia, surplus was registered in the amount of US Dollar 13 million, which is much lower than the surplus of US Dollar 232 million, registered in 1998. In addition, the lower surplus in this category is a consequence of the reduced amount of used foreign credits, resulting in an inflow of US Dollar 50 million and the larger amount of serviced than used trade credits (by US Dollar 2 million).

The total foreign assets¹⁶ increased by US Dollar 141 million in 1999, or by US Dollar 99 million more compared to 1998. In order to mitigate the negative repercussions from the Kosovo crisis on the balance of payments of Republic of Macedonia, on the March Conference in Paris a resolution was adopted for a one-year moratorium on the debt of the Republic of Macedonia towards the Paris Club of Creditors, or their reprogramming, resulting in a rescheduling of US Dollar 21 million of the Macedonian debt. At the same time, according to the 1997 agreement between the Republic of Macedonia and the London Club of Creditors, in 1999 a rescheduling of US Dollar 3 million of the Macedonian debt towards this club was made.

The current account deficit, which was only partly covered by the financial transactions and the increase of the foreign exchange reserves, was compensated in the balance of payments through statistical errors and omissions, which are positive and equal US Dollar 212 million. The large value of errors and omissions is due to the inadequate present statistics, i.e. inability to identify entirely the inflows from the humanitarian organizations, NATO forces and other non-residents.

6.2. Foreign trade

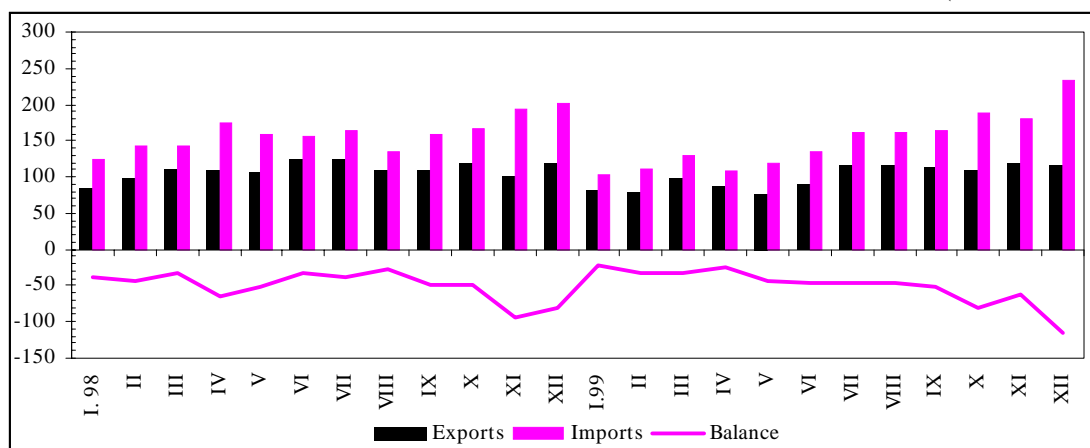
In the last few years, the foreign trade of the Republic of Macedonia has been continuously registering high deficits, which so far have been compensated through two items from the balance of payments: services and transfers. The unexpected strong external shock, caused by the war in FR Yugoslavia, had a negative impact on the foreign trade of Republic of Macedonia in 1999. Namely, in 1999, the foreign trade equaled US Dollar 2,988 million, which is by US Dollar 238 million, or by 7.4% lower compared to 1998. However, even with the foreign trade being reduced, in 1999, the deficit is almost equal to the one from the previous year.

¹⁶ The data for the total foreign assets shown in the balance of payments, differs from the data for the total foreign exchange reserves according to the official data, because balance of payments statistics does not include the exchange rate differentials.

Chart 22

Foreign Trade of the Republic of Macedonia

(in USD million)



In 1999, the foreign trade of the Republic of Macedonia was characterized by uneven dynamics. Namely, in the first half of the year, as a consequence of the external shock, a significant contraction in the foreign trade was registered. Hence, the foreign trade equaled US Dollar 1.214 million (20.6% less compared to the same period of 1998), or 40.6% from the total foreign trade in 1999. Following the end of the war in FR Yugoslavia and weakening of the restrictive effects of the external shock, in the second half of 1999 the foreign trade intensified. Thus, in the July-December 1999 period, the foreign trade equaled US Dollar 1,774 million, which is by 4.6% higher relative to the same period in 1998.

The value of the exported goods from the Republic of Macedonia in 1999, decreased by US Dollar 119 million, or by 9.1% compared to 1998 and was brought down to US Dollar 1,192 million in 1999. The decline is due to the significant contraction in the exports of goods in the first half of the year. Namely, the war in FR Yugoslavia resulted with the loss of the Yugoslav market, impossibility to use a very important transport corridor through this country, as well as the cancellation of many contracts for export of Macedonian goods to the US and EU markets. This was accompanied by the threat for the introduction of anti-dumping measures against the Macedonian producers from the iron and steel industry, a very important export oriented branch of the Macedonian economy. Therefore, in the January - June 1999 period, goods in the amount of US Dollar 504 million were exported, which is by US Dollar 128 million, or by 20.3%, less compared to same period in 1998. By the end of the war in FR Yugoslavia, the factors that negatively influenced the export of goods from the Republic of Macedonia were eliminated, which led to increased exports in the second half of 1999, although such an increase was not sufficient to compensate the fall registered in the first half.

In 1999, the imports of goods in Republic of Macedonia equaled US Dollar 1,796 million. In addition, the contraction in the economic activity caused by the war in the neighborhood, as well as reduced production in the iron and steel industry, due to the possibility of introduction of anti-dumping measures, negatively affected the imports of goods. Consequently, in 1999, the imports of goods in the Republic of Macedonia were lower by US Dollar 119 million, or by 6.2% compared to 1998. Also, on the imports side, the same uneven quarterly distribution is registered, with the imports of goods in the last quarter only reaching US Dollar 602 million, or 33.6% of the total imports of goods in 1999.

The deficit in the foreign trade of Republic of Macedonia in 1999 was US Dollar 604 million. It is almost unchanged relative to the deficit in 1998, which having in mind the reduced foreign trade by 7.4% indicates deterioration in the foreign trade structure in 1999.

Consequently, in 1999, compared to 1998, the import-export coverage ratio was reduced by 2.1 percentage points and was brought down to 66.4%.

The analysis of the exports and imports of Republic of Macedonia with regard to the economic use of goods also shows the deterioration in the foreign trade. On the exports side, in 1999, the exports of reproduction materials dominate with US Dollar 566 million, or 47.5% of the total exports. Relative to 1998, the share of these products in total exports is lower by 1.1 percentage points. At the same time, an increase in the exports of goods with a higher level of processing, or consumption goods, was not registered. Namely, in 1999, consumption goods in the amount of US Dollar 564 million were exported, or 47.3% of total exports. Means of production accounted for US Dollar 37 million or 3.1% of the total exported goods in 1999 (4% in 1998). In addition, there was a significant increase in the item "undistributed" (from 0.1% of total exports in 1998 to 2.1% in 1999), due to the foreign humanitarian aid received in 1999.

Table 17

Foreign Trade of Republic of Macedonia by Economic Use of Goods

Type of goods	Exports				Imports			
	1998 (in US Dollar million)	1999 (in US Dollar million)	index 1999/1998	structure 1999	1998 (in US Dollar million)	1999 (in US Dollar million)	index 1999/1998	structure 1999
Republic of Macedonia (total)	1,311	1,192	90.9	100.0	1,915	1,796	93.8	100.0
1. Reproduction materials	637	566	88.9	47.5	1,242	1,132	91.1	63.0
2. Means of production	53	37	70.2	3.1	248	253	101.9	14.1
3. Consumption goods	620	564	91.0	47.3	413	403	97.6	22.4
4. Undistributed	1	25	1,846.2	2.1	12	8	72.2	0.5

The unfavorable movements can be better observed on the imports side. In 1999, the largest portion of imports refers to import of reproduction materials, which accounted for US Dollar 1,132 million, or 63% of total imports. With respect to 1998, it represents a 1.9 percentage points decline, which is a consequence of the contraction in the industrial production in 1999. At the same time, consumption goods in the amount of USD 403 million were imported, or 22.4% of total imports. With this, the share of import of consumption goods in total imports increased by 0.9 percentage points in 1999. The import of means of production accounted for 14.1% of total imports in 1999 (13% in 1998), and 0.5% of total imports is undistributed.

Regarding the direction of the foreign trade of the Republic of Macedonia, in 1999, the group of developed countries continued to dominate. Bearing in mind the geographical location, out of this group of countries, the European Union plays the most significant role for the Republic of Macedonia. Its share in the foreign trade additionally increased by additional 2.5 percentage points and reached 42% of the total foreign trade of the Republic of Macedonia. The connection between the Macedonian economy and the economies of the countries emerging from the former SFRY can be seen through their share in the foreign trade of the Republic of Macedonia, which remained at the same level from the previous year (25.6% of total foreign trade) due to the developments in the region in the first half of 1999. The countries from Central and Eastern Europe, also represent an important trading partner to the Republic of Macedonia, especially on the imports side, because some of the more important industrial branches (iron and steel industry, production and processing of non-ferrous metal processing) of the Macedonian economy depend on imports of raw materials from these countries. Having in mind that the production in these branches was substantially reduced in 1999, the share of these countries in the foreign trade also declined by 0.6 percentage points and was brought down to 15.2% of total foreign trade. In 1999, in the foreign trade with these three groups of countries, the Republic of Macedonia registered deficits. The deficit registered in the foreign trade with the countries from the former SFRY was halved compared to the previous year, primarily because of the improved balance in the trade with FR Yugoslavia. At the same time, there was a considerable deepening of the deficit

in the exchange of goods with the developed countries, and it increased slightly in the exchange of goods with the countries from Central and Eastern Europe.

Table 18

Foreign Trade of the Republic of Macedonia by Economic Groups of Countries

(in USD million)

Economic groups of countries	Exports	Structure	Imports	Structure	Foreign trade	Structure
I - XII 1999						
Republic of Macedonia (total)	1,192	100.0	1,796	100.0	2,988	100.0
1. Developed countries	718	60.2	911	50.7	1,629	54.5
out of which:						
EU	533	44.7	721	40.1	1,254	42.0
EFTA	32	2.7	24	1.3	56	1.9
Other developed countries	153	12.8	166	9.2	319	10.7
2. Countries of Central and Eastern Europe and former USSR	75	6.3	378	21.0	453	15.2
3. Developing countries	33	2.8	96	5.3	129	4.3
4. Republics of the former SFRY	357	29.9	409	22.8	766	25.6
5. Other countries	9	0.8	2	0.1	11	0.4

The increased share of the group of developed countries in the foreign trade of Republic of Macedonia in 1999 is due to the increased import of goods from the EU countries. Namely, the value of the imported goods from EU in 1999, compared to 1998, increased by 3.8% and reached US Dollar 721 million, or 40.1% of the total imports of the Republic of Macedonia. With this, the share of EU in the total imports increased by 3.9 percentage points compared to 1998. On the exports side, EU accounts for 44.7% of total exports, or by 0.6 percentage points more than in 1998. In addition, the value of the goods exported on the EU markets was US Dollar 533 million in 1999, and is lower by 7.8% compared to 1998. The countries from the former SFRY represented a market for 29.9% (US Dollar 357 million) of the total exports of Republic of Macedonia in 1999. Relative to 1998, the value of goods exported in these countries increased by 1.0%, thus increasing the share of these countries in total exports by 2.8 percentage points. The imports of goods from this group of countries equaled US Dollar 409 million in 1999, or by 12.3% less than in 1998, and their share in the total imports fell by 1.6 percentage points.

With respect to individual countries, as well as in the previous year the same ten countries continued to dominate the foreign trade of Republic of Macedonia, with some slight changes in their order. Namely, in 1999 the most important trading partner is Germany, with exchanged goods in the amount of US Dollar 500 million, or 16.7% of the total foreign trade of Republic of Macedonia, which is almost an identical share as in the previous year. The exchange of goods with FR Yugoslavia in the first half of 1999 was to a large extent influenced by the administrative measures aimed to discourage imports implemented by the Yugoslav authorities, as well as by the war in this country. However, as a result of the revival of exports to Kosovo in the period after the war, in 1999, the value of foreign trade with FR Yugoslavia was significant. Namely, the foreign trade of the Republic of Macedonia with FR Yugoslavia equaled US Dollar 436 million, that is 14.6% of the total foreign trade of the Republic of Macedonia (0.3 percentage points fall compared to 1998). In the course of 1999, Greece was the third largest trading partner of the Republic of Macedonia (the fourth on this list in 1998), with the value of the goods traded equaling US Dollar 250 million, or 8.4% of the total foreign trade (2 percentage points more than in 1998). That is a result of the increased imports of goods from this country. The analysis of the foreign trade components indicates that in 1999, the biggest markets for the Macedonian goods were Germany and FR Yugoslavia, with a share in the total exports of the Republic of Macedonia of 21.4% and 21.3%, respectively, followed by the USA, where 11.4% of the Macedonian exported goods were sold. On the import side, Germany and FR Yugoslavia dominate with 13.7%, and 10.1%

of total imports of the Republic of Macedonia, followed by Greece with a 9.1% share in total imports in 1999.

Table 19

Ten Largest Trading Partners of Republic of Macedonia

	Foreign trade (in US Dollar million)	Share	Exports (in US Dollar million)	Share	Imports (in US Dollar million)	Share	Import-export coverage ratio
I-XII 1999							
REPUBLIC OF MACEDONIA (total)	2,988	100.0	1,192	100.0	1,796	100.0	66.4
out of which:							
Germany	500	16.7	255	21.4	245	13.7	103.8
FR Yugoslavia	436	14.6	254	21.3	182	10.1	139.8
Greece	250	8.4	86	7.2	164	9.1	52.5
USA	208	7.0	136	11.4	72	4.0	188.7
Slovenia	191	6.4	34	2.9	157	8.7	21.7
Italy	163	5.5	70	5.9	93	5.2	76.0
Ukraine	119	4.0	4	0.3	115	6.4	3.1
Bulgaria	117	3.9	26	2.2	91	5.1	28.6
Croatia	111	3.7	49	4.1	62	3.4	79.3
Russia	106	3.6	15	1.3	91	5.1	16.5
Total (10 largest trading partners)	2,201	73.7	929	77.9	1,272	70.8	73.1

In 1999, in the foreign trade with its ten most important trading partners, the Republic of Macedonia registered a deficit of US Dollar 343 million, or an import-export coverage ratio of 73.1%. In addition, surplus was registered only in the foreign trade with three countries, Germany, FR Yugoslavia and USA. The highest deficit in the foreign trade with the ten largest trading partners in 1999 was registered with Ukraine and Russia, due to the dependence of the Macedonian steel and iron industry on products for reprocessing, which are imported from these countries. The signing of the free trade agreement with Slovenia negatively influenced the trade balance of the Republic of Macedonia. Namely, the exchange of goods with Slovenia, a trend of rapid decline in the import-export coverage ratio is being registered (58.6% in 1996; 40.7% in 1997; 27.7% in 1998). This trend continued in 1999, with the import-export coverage ratio equaling 21.7%, and a foreign trade deficit in the amount of USD 123 million being registered.

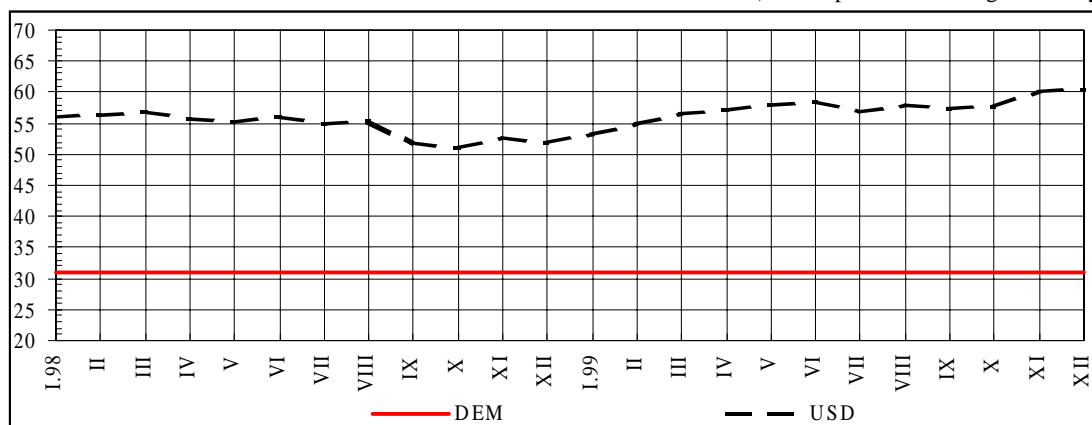
6.3. Denar exchange rate

During 1999, NBRM continued with successful implementation of the monetary strategy of targeting the nominal Denar exchange rate against the Deutsche mark. Consequently, in 1999 the Denar exchange rate against the Deutsche mark remained unchanged and thus on December 31, 1999, it equaled 31 Denars per Deutsche mark.

Chart 23

Nominal Exchange Rate of the Denar against the Deutsche Mark and the US Dollar

(Denars per unit of foreign currency)

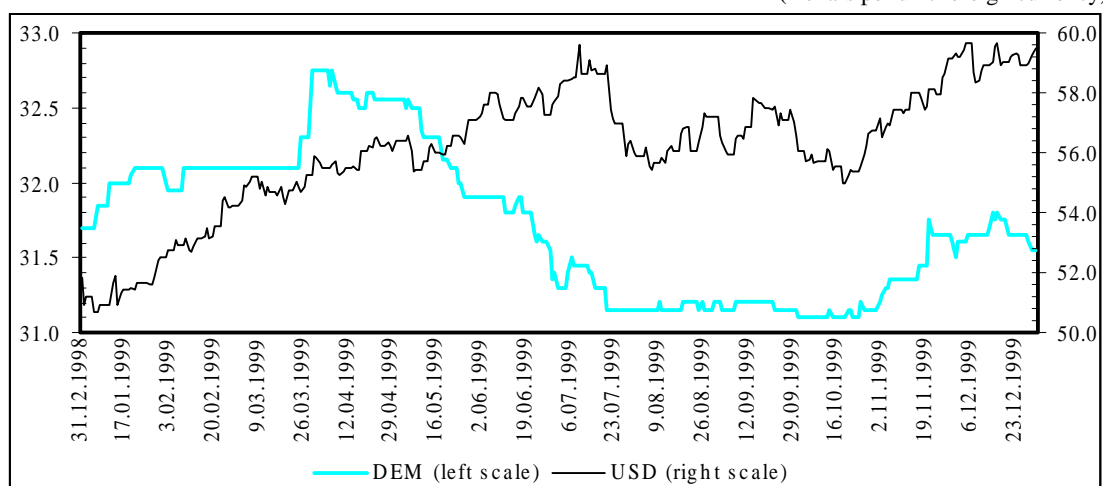


Contrary to the developments on the foreign exchange market, where deposit money banks and enterprises participate, and where no major fluctuations of the Denar exchange rate against the Deutsche mark were registered, and the targeted level of 31 Denars per Deutsche mark was preserved during the whole year, on the exchange offices market, in different periods the exchange rate fluctuated between 31.1 and 32.75 Denars per Deutsche mark. Namely, the beginning of the war in FR Yugoslavia resulted in foreign trade contraction and induced the economic agents' preferences for holding foreign currencies, whenever there are periods of crises. These tendencies were reflected on the exchange offices market through a simultaneous decrease of the supply and increase of the demand for foreign exchange. As a result of this, at the beginning of April, the average Denar exchange rate against the Deutsche mark on the exchange offices market equalled 32.75 Denars per Deutsche mark, which represents a 3.3% depreciation compared to the exchange rate at the beginning of the year (31.7 Denars per Deutsche mark).

Chart 24

Nominal Exchange Rate of the Denar against the Deutsche Mark and the US Dollar on the Exchange Offices Market

(Denars per unit foreign currency)



Contrary to this, in October 1999, compared to December 31, 1998, the exchange rate of Denar against the Deutsche mark appreciated by 1.9%, and was brought down to 31.1 Denars per Deutsche mark. Such a development was a result of the end of the war in FR Yugoslavia, as well as the increased number of non-residents (NATO, humanitarian

organizations, diplomatic core etc.) who acted as net sellers of foreign exchange. As of December 31, 1999, the middle Denar exchange rate against the Deutsche mark on the exchange offices market equaled 31.55 Denars per Deutsche mark, which compared to the level on December 31, 1998, represents a 0.5% appreciation.

As of January 1, 1999, the administrative implementation of the Euro, the new currency unit of European Monetary Union, started. As a result of the fixed rates of conversion between the Euro and the national currencies of the member countries of EMU, including Germany (1.96 Deutsche marks for one Euro), and the invariable exchange rate of the Denar against the Deutsche mark, the Denar exchange rate against the Euro during 1999 remained unchanged and equaled 60.62 Denars per Euro.

The implementation of the monetary strategy of targeting the nominal Denar exchange rate against the Deutsche mark, implies that the Denar exchange rate against other foreign currencies, including the US Dollar, is determined by the exchange rates of the Deutsche mark and these foreign currencies on the world financial markets. During 1999, the position of the US Dollar was continuously strengthening against the Deutsche mark, and as of December 31, 1999, 1.95 Deutsche mark per US Dollar were traded, compared to 1.67 Deutsche mark per US Dollar as of December 31, 1998. This resulted in a 16.4% depreciation of the Denar exchange rate against the US Dollar, with the exchange rate reaching 60.34 Denars per US Dollar. On the exchange offices market, in 1999, the middle exchange rate of the Denar against the US Dollar depreciated by 16.4% and on December 31, 1999 it equaled 59.51 Denars per US Dollar.

6.4. Foreign exchange reserves of the Republic of Macedonia

According to its definition, the total foreign exchange potential of the Republic of Macedonia consists of the foreign assets of NBRM¹⁷ and the foreign exchange reserves of the banks licensed to conduct international operations. At the end of 1999, it reached US Dollar 833 million, which is by US Dollar 142 million or 20.6% more compared to the foreign exchange potential at the end of 1998. This increase is due to the increase of the foreign assets of the Central Bank as well as the registered increase of the foreign assets of the banks licensed to conduct international operations.

At the end of 1999, the foreign assets of the NBRM equaled US Dollar 499 million, and compared to the end of 1998 they increased by US Dollar 132 million, or by 36%. The largest part of the foreign assets were deposited on NBRM bank accounts in foreign banks in the form of deposits (US Dollar 465 million) and monetary gold (US Dollar 28 million).

The gross foreign exchange reserves of the NBRM, which is a difference between the foreign assets and foreign liabilities of the NBRM, reached US Dollar 458 million at the end of 1999 and compared to the level from the end of 1998 they are higher by US Dollar 125 million, or by 37.5%. Hence, they reached a level equivalent to 3.1 months of imports of goods. The realized increase in the gross foreign exchange reserves of NBRM is primarily due to the net-purchase of foreign exchange at the foreign exchange market in the amount of US Dollar 118 million.

With respect to dynamics, two periods could be distinguished in the movement of the gross foreign exchange reserves of the NBRM - the period before and during the war in FR Yugoslavia, and the period after the war. Hence, until the end of the war, the gross foreign exchange reserves of the NBRM constantly declined, despite the reduced current account

¹⁷ The foreign assets of the NBRM represent a sum of the gross foreign reserves of the NBRM, temporary confiscated foreign exchange, deposits of the public sector institutions and other foreign assets.

deficit in the balance of payments. Although the Republic of Macedonia entered 1999 with the historically highest level of gross foreign exchange reserves of the NBRM of US Dollar 333 million, at the end of May 1999, they were reduced to US Dollar 306 million. The positive implications on the foreign trade coming from the re-opening of the market of FR Yugoslavia as well as the foreign exchange supply exceeding the demand on the foreign exchange market, contributed to a continuous increase of the gross foreign exchange reserves of NBRM in the period after the end of the war.

In 1999, the total inflow of foreign exchange assets in the gross foreign exchange reserves of the NBRM is US Dollar 512 million. Out of this amount, US Dollar 326 million, or 63.6% is foreign exchange purchased by the NBRM, which refers mostly to purchases of foreign exchange from the foreign exchange market and the exchange offices market. Foreign loans and donations account for US Dollar 58 million, where IDA loans dominate by a total amount of US Dollar 40 million. In August 1999, the CCFF (Compensatory and Contingency Financing Facility) arrangement with the International Monetary Fund was realized, on the resulting in an inflow of US Dollar 19 million. The remaining inflows are mainly related to interest received on the foreign exchange deposited abroad, which amounted to US Dollar 12 million at the end of 1999.

Table 20

Inflows and Outflows in the Gross Foreign Exchange Reserves of NBRM

(in USD million, end of period)

	31.12. 1998	Q1	Q2	Q3	Q4	01.01.99- 31.12.99
Foreign exchange reserves	333.5	318.8	347.9	441.5	458.4	
Change in foreign exchange reserves, net		-14.6	29.1	93.6	16.8	124.9
Inflows		31.6	88.2	54.8	44.3	512.4
Purchased foreign exchange		12.1	70.8	20.4	30.5	326.8
Interest received on foreign currency deposits		1.1	0.9	1.2	1.2	12.7
Foreign credits and donations		12.5	9.9	13.4	3.4	77.5
Other		0.0	0.0	0.0	0.0	0.0
Exchange rate differentials		5.9	6.6	19.8	9.2	95.4
Outflows		26.4	46.4	19.1	31.6	387.5
Sold foreign exchange		10.6	35.6	4.0	19.4	209.3
Debt payments		6.4	1.8	5.6	2.8	65.2
Exchange rate differentials		9.4	9.0	9.5	9.4	113.0

Outflows of foreign assets in the total amount of US Dollar 387 million acted towards a decline in the gross foreign assets of the NBRM. In addition, the largest part of the outflow refers to foreign exchange sold by the NBRM in the amount of US Dollar 209 million. This is primarily due to the NBRM interventions on the foreign exchange market, motivated by the fluctuations in the supply and demand. Also, there was a significant foreign exchange outflow for payment of the debt toward the IMF and other foreign creditors, in the total amount of US Dollar 65 million. As a consequence of the depreciation of the Deutsche mark against the US Dollar and the fall in the price of gold on the world stock exchanges, there was a net outflow based on the change in the cross currency rates (i.e. exchange rate differentials and changes in the price of gold) in the amount of US Dollar 18 million.

The net foreign exchange reserves of NBRM, as a difference between the gross foreign exchange reserves and the liabilities towards IMF were US Dollar 357 million as of December 31, 1999, thus increasing by US Dollar 126 million compared to the end of 1998. The increase is completely a result of the increased gross foreign exchange reserves of NBRM, bearing in mind that the liabilities towards IMF decreased by US Dollar 1 million on net basis. The minimal fall on net basis is due to the larger debt repayments than IMF borrowings (resulting entirely from the CCFF arrangement), as well as the change in the exchange rate between the Special Drawing Rights and the US Dollar. Thus, at the end of

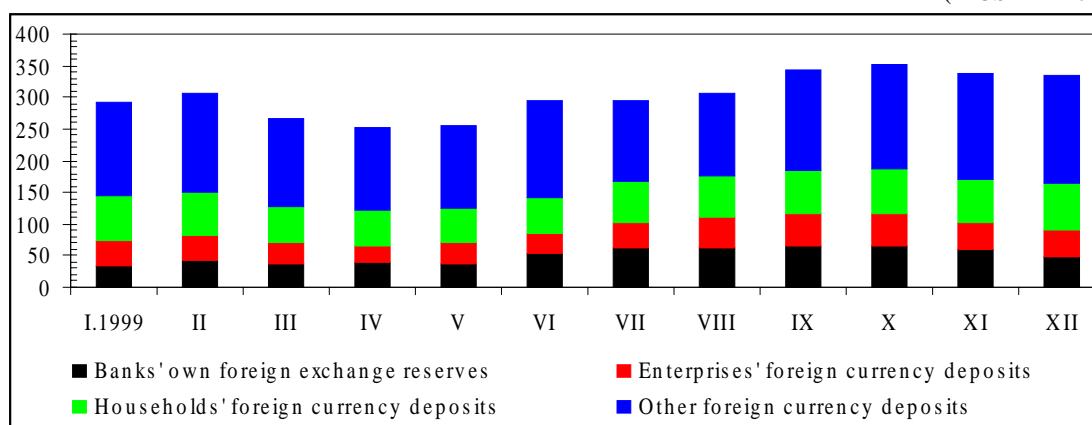
1999, the total liabilities towards the International Monetary Fund were US Dollar 101 million.

The total foreign assets of the banks licensed to conduct international operations, at the end of 1999 relative to the end of the previous year, increased by US Dollar 10 million, or by 3.1%, and reached the level of USD 334 million. In addition, the banks' own foreign exchange funds and the foreign currency deposits of the economic agents, which are the basic components of the total foreign assets of the banks licensed to conduct international operations, registered divergent movements.

Chart 25

Structure of the Foreign Exchange Funds of the Deposit Money Banks

(in USD million)



At the end of 1999, the banks own foreign exchange funds¹⁸ reached US Dollar 47 million, which compared to their level from the end of the previous year is an increase of US Dollar 13 million or by 40.6%. With respect to dynamics, a significant increase of the banks own foreign exchange funds was registered following the end of the military actions in the region. At the end of 1999, the foreign currency deposits of the economic agents (comprising of the foreign currency deposits, foreign currency credits and other short-term foreign currency liabilities of the residents and non-residents) with the banks reached US Dollar 287 million, which is by USD 3 million less relative to the end of 1998.

6.5. Foreign exchange market

With respect to the participants, the foreign exchange market in Republic of Macedonia is divided into two segments. On the first only licensed banks, domestic legal entities and NBRM can participate. The second segment, is the so-called exchange offices market, where individuals and exchange offices participate.

The total turnover registered on the foreign exchange market, where the banks, enterprises and NBRM are trading, during 1999 was US Dollar 1,411 million was realized. Compared to 1998, the realized turnover is higher by US Dollar 161 million, or by 12.9%. The largest part of it, 59.6%, or US Dollar 840 million, was realized through the transactions between banks and enterprises. The transactions between the enterprises follow, with a realized turnover of US Dollar 305 million, or 21.6% of the total turnover. In its operations on

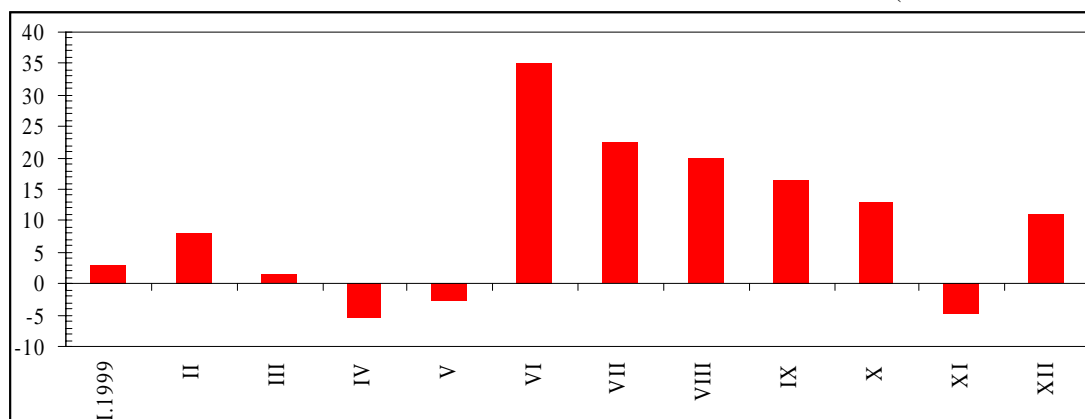
¹⁸ This is the difference between foreign assets and foreign liabilities of the deposit money banks, not including the long-term foreign credit liabilities and the short-term foreign currency liabilities based on credits taken on behalf of other legal entities. In the amount of the banks own foreign exchange funds, the foreign savings of the households (USD 30 million) are not incorporated, which according to the current legislation could be on bank's disposal.

the foreign exchange market, the Central Bank realized a turnover of US Dollar 199 million, or 14.1% of the total turnover in 1999. The remaining part of the total turnover (US Dollar 67 million, or 4.7%) refers to transactions among the banks.

Chart 26

Net-purchase of foreign exchange by NBRM on the foreign exchange market

(in US Dollar million)



In order to preserve the exchange rate of the Denar against the Deutsche mark at the targeted level, which is an intermediate target of the monetary policy, during 1999, NBRM intervened on the foreign exchange market by purchasing foreign exchange. In addition, with the supply of foreign exchange exceeding the demand, NBRM realized net-purchase of foreign exchange in the amount of US Dollar 118 million. Compared to the previous year, the realized purchase is more than tripled, or in absolute terms, the purchase is higher by US Dollar 82 million.

With respect to dynamics, net-purchase of foreign exchange was realized in all four quarters of the year. In the first quarter, US Dollar 12 millions were purchased on a net-basis, and in each of the three months a net-purchase of foreign exchange was realized. The crises in the region that escalated into a military conflict in FR Yugoslavia resulted in divergent movements on the foreign exchange market in the course of second quarter of the year. Namely, as a consequence of the pressures for depreciation of the exchange rate of the Denar, in April and May, NBRM intervened on the foreign exchange market, with a net-sale of US Dollar 8 million in these two months. After the end of the war, the inflow of foreign exchange from donations increased drastically, which led to a subsequent need for intervention of NBRM on the foreign exchange market, this time to prevent the appreciation of the Denar exchange rate. Thus, in June 1999, net-purchase of foreign exchange in the amount of US Dollar 35 million was realized, resulting in a net-purchase of US Dollar 27 million in the second quarter of 1999. The supply of foreign currency continued to exceed the demand in the third quarter of the year in which a net-purchase of US Dollar 59 million was realized. In the last three months of the year, on net-basis, US Dollar 19 million were purchased, even though in November due to speculations for an eventual change of the Denar exchange rate, there was a net-sale of US Dollar 5 million.

The activity on the exchange offices market in 1999 compared to the previous year declined, but the trend of the foreign exchange supply exceeding than demand continued. The total turnover at the exchange offices market in 1999 was US Dollar 498 million, which is by US Dollar 69 million less than in 1998. In the transactions with individuals, foreign exchange in the amount of US Dollar 387 million was purchased, and foreign exchange in the amount of US Dollar 111 million was sold. In this manner, a net-purchase of US Dollar 276 million was realized, which is by US Dollar 39 million, or by 16.3% more compared to the last year's realized net-purchase. This is due to the slower decline in the purchased foreign exchange (by

US Dollar 15 million) relative to the decline of the foreign exchange sold to individuals (by US Dollar 54 million). In addition, US Dollar 271 million, or 98.2% from the net-purchase was realized by exchange offices working on their behalf and their own account, while the rest was realized by exchange offices working on their behalf and for NBRM account.

6.6. External debt of the Republic of Macedonia¹⁹

6.6.1. External debt developments in 1999

At the end of 1999, the foreign debt of Republic of Macedonia on the basis of used short-term, medium-term and long-term credits equaled US Dollar 1,494 million with the principal being US Dollar 1,479 million. Compared to the end of 1998, the foreign debt of Republic of Macedonia increased by US Dollar 39 million, or by 2.7%. The increase of the foreign debt is due to the increase in the debt based on medium-term and long-term credits (which has a dominant share of 96.3% in the total debt), whereas the foreign short-term credits declined.

The external short-term debt of the Republic of Macedonia, was US Dollar 55 million at the end of 1999 and relative to the end of 1998 it decreased by US Dollar 14 million, or by 19.9%. During 1999, on the basis of short-term credits US Dollar 47 million were withdrawn, which is by US Dollar 20 million less compared to the previous year. At the same time, the Republic of Macedonia was making the payments on its short-term foreign liabilities regularly, resulting in an outflow of US Dollar 44 million (with the principal paid being US Dollar 42 million).

The external debt of the Republic of Macedonia on the basis of used medium-term and long-term credits reached US Dollar 1,438 million at the end of 1999, and relative to the level from the end of 1998 it is higher by USD 53 million, or by 3.8%. The principal equaled US Dollar 1,424 million. In addition, the increase in 1999 is slower compared to the corresponding one in 1998, which having in mind the regular servicing of the debt, is due to the reduced amount of withdrawn funds from approved credits. This corresponds to the increased risk following the escalation of the crisis in the region, that made foreign creditors cautious while extending new credits to the Republic of Macedonia.

Namely, in 1999, US Dollar 189 million were withdrawn from the approved medium-term and long-term credits, which is by US Dollar 106 million less compared to the withdrawal in 1998. From the viewpoint of the creditor, most of the new credits (57.8%), or US Dollar 109 million, were withdrawn from the multilateral creditors. In this category of creditors, the highest amount, or US Dollar 44 million, were withdrawn from the International Development Agency (IDA) for the Project for urgent imports (US Dollar 40 million).

Regarding the amount of the withdrawn funds, the European Investment Bank (EIB) follows. Namely, in 1999, US Dollar 24 million were withdrawn from this institution, which were used entirely for financing a road building project. Significant amount of funds were withdrawn from the International Monetary Fund (IMF), i.e. US Dollar 19 million on the basis of the approved CCFF arrangement.

In 1999, US Dollar 12 million were withdrawn from the International Bank for Reconstruction and Development (IBRD). Most of these funds are aimed for financial support for the project for development of transport (US Dollar 7 million). From the European Bank for Reconstruction and Development (EBRD) US Dollar 5 million were withdrawn, used

¹⁹ Preliminary data of the National Bank of Republic of Macedonia.

primarily for restarting and modernization of the production process in the Steel mill "Makstil"-Skopje. The amount of withdrawn funds from the International Finance Corporation (IFC) in 1999 was US Dollar 2 million.

In 1999, from the bilateral creditors, US Dollar 26 million were withdrawn, which represents 13.8% of the total withdrawn funds in the course of the year. The largest share of it is related to credits taken from the Republic of China- Taiwan.

In 1999, US Dollar 54 million were withdrawn from the private creditors, which is 28.3% of the total withdrawn funds. In addition, the largest amount of funds was withdrawn from "other private creditors" (US Dollar 47 million), out of which US Dollar 28 million as trade credits, US Dollar 11 million as financial credits and US Dollar 8 million as commercial credits. In accordance to the new financial agreement with the London Club of Creditors, the capitalized interest in 1999 reached US Dollar 7 million.

For regular debt payments, in 1999, the Republic of Macedonia paid US Dollar 155 million for the liabilities arising from the used medium and long-term credits. Out of it, US Dollar 103 million are payments on the basis of principal, while US Dollar 52 million were payments on the basis of interest. The largest share, or US Dollar 70 million from the debt payments in 1999 refer to paid liabilities towards multilateral creditors, out of which US Dollar 43 million are related to payment of principle. Among the multilateral creditors, the largest amount was paid to the International Monetary Fund (IMF - US Dollar 20 million) and the European Bank for Reconstruction and Development (EBRD - US Dollar 20 million).

In the course of 1999, US Dollar 22 million were paid on the basis of liabilities towards bilateral creditors (14.2% from the total amount paid), out of which US Dollar 13 million are related to payment of principal. The largest amount, or US Dollar 19 million was paid to the Paris Club of Creditors (US Dollar 11 million paid on the basis of principal). In addition, this amount was entirely paid in the first quarter of 1999. Starting from April 1, 1999, in accordance with the Resolution of the Paris Club of Creditors, a one-year moratorium was declared, i.e. postponement of all the payments of the Republic of Macedonia towards this Club. This Resolution was motivated by the deteriorated environment in the Macedonian economy, caused by the escalation of the crises in the region.

In the course of 1999, liabilities towards private creditors were paid in the total amount of US Dollar 64 million, or 41% of the total amount of liabilities paid this year. Most share of this amount (US Dollar 55 million) refers to paid liabilities towards private creditors distinct from the London Club of Creditors, out of which: US Dollar 40 million for used financial credits, US Dollar 13 million for commercial credits and US Dollar 2 million for trade credits. At the same time, liabilities in the amount of US Dollar 9 million were paid to the London Club of Creditors, referring to payment of interest.

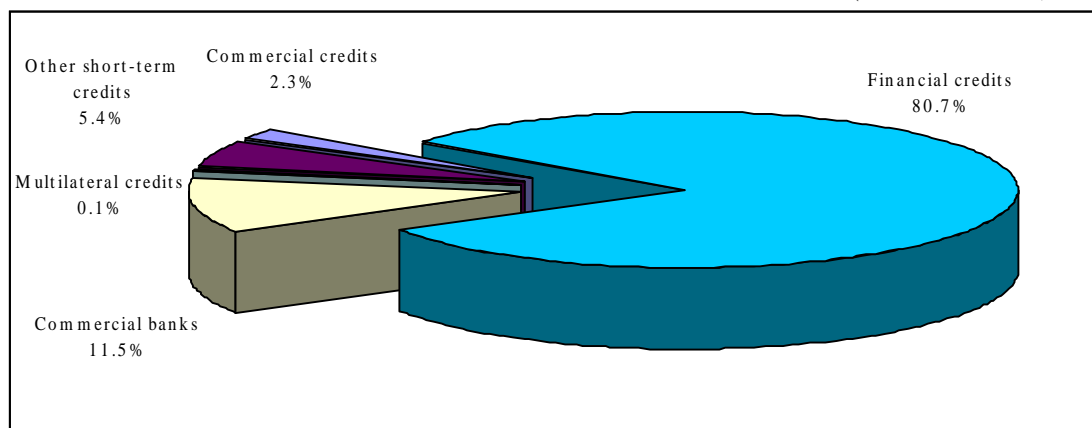
6.6.2. External debt structure

With regard to the type of used credits, financial credits have a dominant share (80.7%) in the structure of the short-term foreign debt of Republic of Macedonia in 1999. Short-term credit lines (11.5%), commercial credits (2.3%) and other short-term credits (5.4%) follow. The share of the multilateral creditors in the short-term foreign debt is insignificant or 0.1%.

Chart 27

Structure of the Debt by Types of Foreign Credits

(as of December 31, 1999)



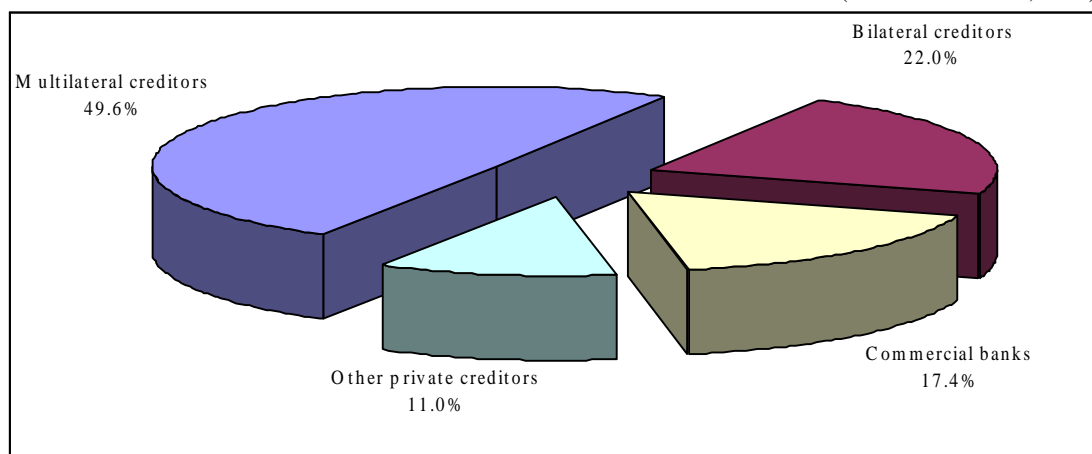
In the structure of the short-term foreign debt as of December 31, 1999, relative to the end of 1998, a significant increase is registered in the share of financial credits (by 21.6 percentage points) at the expense of the reduced shares of: commercial credits (by 13.9 percentage points), short-term credit lines (by 2.6 percentage points) and other credits (by 4.8 percentage points). At the same time, an important change in the structure of the short-term foreign debt in 1999 is the presence of multilateral credits, which were not registered in 1998.

In 1999, the structure of the medium and long-term foreign debt of the Republic of Macedonia by types of foreign creditors, did not register any significant changes. Namely, at the end of 1999, the official creditors still account for the largest share (71.7%) in the medium and long-term foreign debt by types of foreign creditors, whereas the share of private creditors equaled 28.3%.

Chart 28

Structure of the medium - term and long - term Debt by Types of Foreign Creditors

(as of December 31, 1999)



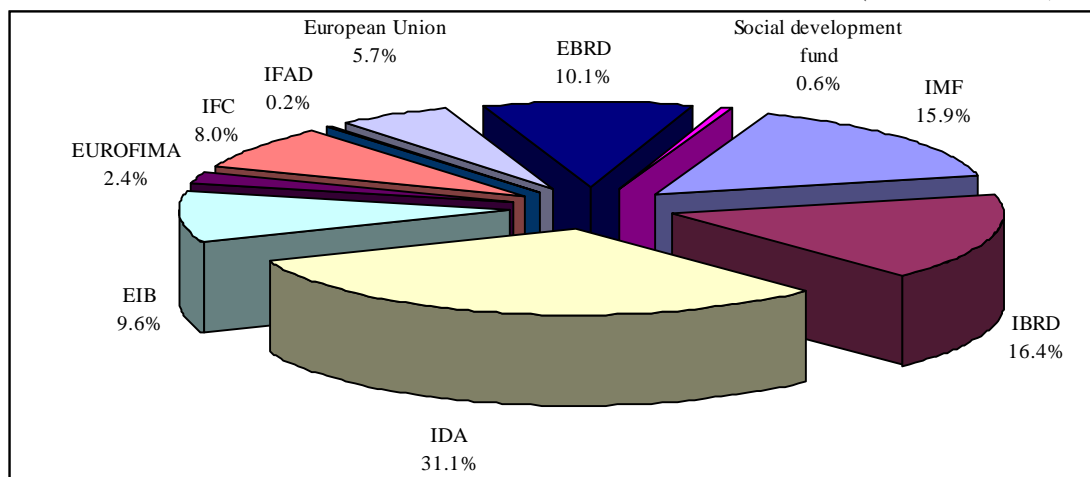
At the end of 1999, the foreign debt toward official creditors was US Dollar 1,031.0 million, out of which, US Dollar 714.0 million refer to foreign debt toward multilateral creditors. Herewith, the share of the foreign debt toward multilateral creditors in the total foreign debt based on used medium-term and long-term credits reached 49.6%. Among the multilateral creditors, the largest creditor of the Republic of Macedonia is the International Development Agency (IDA) with a share of 31.1%. That makes the structure of the foreign debt of the Republic of Macedonia relatively favorable, since these credits are taken at most

favorable conditions. According to their share in the debt toward multilateral creditors, the International Bank for Reconstruction and Development (IBRD) and International Monetary Fund follow with shares of 16.4% and 15.9%, respectively.

Chart 29

Structure of the Foreign Debt Towards Multilateral Creditors

(as of December 31, 1999)



At the end of 1999, the foreign debt towards bilateral creditors was US Dollar 317.0 million, or 22.0% of the total foreign debt based on medium-term and long-term credits. The largest share, or 83.7% of the bilateral credits refers to rescheduled debt towards the Paris Club of Creditors. The total share of newly signed credits and non-rescheduled debt is 11.8%, or 4.5% of the total bilateral debt.

At the end of 1999, the total foreign debt of the Republic of Macedonia towards private creditors was US Dollar 408.0 million, out of which, the largest share (60.2%) refer to the foreign debt towards the London Club of Creditors. At the same time, the medium-term and the long-term credits withdrawn from other private creditors reached US Dollar 157.0 million, out of which, the largest shares refer to financial credits (44.1%) and trade credits (39.4%).

6.7. Relations with the International Financial Institutions¹⁶

International Monetary Fund

In 1999, the Republic of Macedonia was supposed to finalize the successful realization of the ESAF arrangement with the IMF, contracted for the 1997 - 1999 period. However, due to the negative external shock caused by the escalation of the crisis in FR Yugoslavia in the first half of 1999, the necessary conditions for its entire completion were absent and the arrangement was terminated. However, since August 1999, the Republic of Macedonia has an arrangement with IMF for overcoming the losses from the unexpected decline of export income, as a consequence of the external shock. Actually, it is a credit for compensatory financing and financing of expenses against unexpected risks, the so-called CCFF¹⁷ arrangement.

¹⁶ NBRM data

¹⁷ CCFF - CCFF, Compensatory and Contingency Financing Facility

In the relations with the IMF so far, besides the financial support, the Republic of Macedonia received significant technical support in the fields of: monetary and balance of payments statistics, reform of the instruments of monetary regulation, foreign exchange system, foreign exchange market, banking supervision etc. In 1999, the good cooperation in this area continued.

World Bank Group

As of December 31, 1999, the Republic of Macedonia concluded numerous arrangements with the World Bank and its Affiliations. In the 1994 - 1999 period, the Republic of Macedonia concluded 8 arrangements with the International Bank for Reconstruction and Development (IBRD), totaling US Dollar 184.0 million. Out of that, in 1999, an arrangement was concluded for the project on transportation sector, in the amount of US Dollar 27.1 million.

In the 1994 - 1999 period, 12 arrangements were made with the International Development Agency in the total amount of US Dollar 280.7 million. In 1999 only, two arrangements were concluded: Loan for bridging the negative economic consequences from the external shock (US Dollar 50.6 million) and arrangement for structural reforms in the framework of the project for immediate social assistance (US Dollar 10.3 million).

In the 1997 - 1999 period, the International Finance Corporation financed private sector projects and engaged its own funds in the amount of US Dollar 78.7 million in the Republic of Macedonia. Out of that, one new project was financed in 1999, with the International Finance Corporation investing US Dollar 8.7 million.

European Bank for Reconstruction and Development (EBRD)

The EBRD Strategy for the Republic of Macedonia is focused on achieving three main objectives:

1/ Private sector development, by granting long-term loans to Macedonian banks, thus giving direct support to the development of small and medium size enterprises and to the acceleration of the privatization process. Also, EBRD grants credits and makes direct investments in the private industrial and agribusiness projects and gives active support to the foreign direct investments;

2/ financial sector strengthening, by systemic reconstruction of the banking sector. EBRD's strategy is focused on rehabilitation and privatization of the biggest Macedonian bank as well as on the consolidation and development of the small-size financial institutions through credit lines or participation in the equity capital;

3/ Key, essential investments in infrastructure, in which EBRD will also allocate its funds. At the same time, EBRD will participate in the realization of the specific infrastructure projects that facilitate the development of the private sector and regional integration of the country (transport, energy, telecommunications etc.).

In 1999, two additional projects were agreed with EBRD. In the financing of these projects this financial institution will engage its own funds in the total amount of US Dollar 27.5 million. At the same time, with regard to the previously contracted projects, US Dollar 4.6 million were withdrawn from EBRD. In 1999, a total of US Dollar 19.6 million was paid to the EBRD, out of which US Dollar 15.3 million were paid on the basis of principal. As of December 31, 1999, the debt towards EBRD equaled US Dollar 72.3 million.

Bilateral creditors

Until March 31, 1999, the Republic of Macedonia regularly settled its liabilities toward the Paris Club of Creditors. Due to the unfavorable external influences on the Macedonian economy as a result of the escalation of the crisis in FR Yugoslavia, starting from April 1, 1999, the Paris Club of Creditors agreed to a one-year moratorium on the debt of the Republic of Macedonia toward this group of creditors. The due payments in this period reached US Dollar 38.9 million and they will be additionally negotiated with the Paris Club of creditors.

In 1999, the Republic of Macedonia concluded new bilateral credit arrangements as follows:

- In May 1999, a commercial credit from the Government of the Republic of Italy in the amount of US Dollar 12.8 million;
- In June 1999, a credit from the Republic of China - Taiwan for development of the private sector in the amount of US Dollar 12.0 million, and
- In July 1999, a credit from the Republic of China - Taiwan for financing infrastructure objects in the amount of US Dollar 20.0 million.

Private creditors - London Club of Creditors

The total debt toward this group of creditors equals US Dollar 228.7 million. During 1999, liabilities in the amount of US Dollar 8.6 million based on the interest were paid to the London Club of Creditors and US Dollar 3.0 million were rescheduled. On December 31, 1999, the debt towards this group reached US Dollar 245.3 million, including the capitalized interest.