

National Bank of the Republic of Macedonia



Annual Report 2009

Skopje, March 2010

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Dear Sirs and Mesdames,

We find ourselves in a period in which we are trying to get clearer picture for the roots of the world crisis, to summarize consequences it leaves on the global economy, to systemize the main challenges and "lessons", with which we, the policymakers, faced with and learned during the last two years. The challenges the financial crisis posted, actually meant a need of fast, innovative and decisive reaction through the macroeconomic policies. The drastic and continuous downward revision of the macroeconomic forecasts as of the beginning of 2009 (from 3.8% to 0.5% of the global growth for 2009¹) confirmed the doubts that the financial crisis in USA will not be isolated case and that it will lapse into world recession. The intensity of the crisis transmission on other economies was fast and huge, which is not surprising regarding the high degree of trade and financial integration. However, the fast response of the macroeconomic policies to the global recession through drastic conventional and non-conventional measures enabled stabilization of the financial systems, recuperation of the impaired confidence and faster than expected exit from the crisis of large number of economies. Hence, 2009 will be remembered in the modern economic history as a year in which many businesses and households have suffered, but also a year in which the decisive and coordinated action of the policymakers prevented further escalation of the crisis and contributed to economic stabilization and beginning of a process of gradual recovery of the economies.

The domestic economy failed to stay immune to the synchronized global developments. The decrease in the export demand, the worsening of the expectations of the economic agents and the decrease in the capital inflows were the first transmission channels of the crisis. These trends created pressures on the stability of the domestic currency. High degree of trade integration (over 80%), given the collapse of the world trade, meant losing the role of the export sector as a significant growth generator. Historically the deepest decrease in the effective external demand of 3.7% and the decrease in the metal prices on the international stock exchanges of about 30%, annually, hit especially the metal processing sector, which is one of our key export sectors. The exports registered significant drop since the end of 2008, while the imports reacted more slowly. In the first three months of the year, the trade deficit significantly widened, while it contracted in the remaining part of the year, parallel to the downward adjustment of the domestic demand and contraction of the negative energy balance. Until the end of 2009, the external misbalances reduced parallel to the stabilization in the expectations and reduced pressures on the imports. The current account deficit of 13.1% of the GDP in 2008 reduced to 7.3% of GDP in 2009.

The global crisis influenced on significant rise in the negative expectations of the domestic economic agents, especially at the beginning of the year when the crisis staggered the confidence, thus resulting in the increased demand for foreign exchange on the currency exchange market. These tendencies, together with the widened negative gap in the foreign trade and low capital inflows, conditioned significant deepening of the gap between the supply of and the demand for foreign exchange in the first months of the year. In conditions of fixed foreign exchange rate, this gap was supplemented through foreign reserves, with the interventions on the foreign exchange market until May reaching 5.1% of GDP on cumulative basis. Parallel to the interventions on the foreign exchange market, the NBRM responded to the pressures on the foreign exchange rate also with monetary policy contraction. Thus in March the core interest rate went up from 7% to 9%, while in May Decision on increasing the banks' reserve requirement rate in foreign currency (from 10% to 13%), and banks' liabilities with FX clause (from 10% to 20%) was adopted.

The undertaken monetary measures and improved perceptions for the global economy stabilized the expectations significantly and contributed to trade deficit contraction. This was evident through the upward trend of the private transfers, which together with the continuing narrowing of the negative gap in the trade in the second quarter and the increase in the capital inflows (in one part as a result of the Government's debiting on the international capital market), enabled

¹ According to World Economic Outlook (April 2008, January 2009).

continuing net purchase of foreign exchange. Until the end of the year, the level of foreign reserves went up thus exceeding the expectations in the NBRM projections. This together with the more favorable forecasts for the global economy created better environment for the monetary policy. In such conditions, already from the end of November, the NBRM commenced with gradual relaxation of the monetary policy.

The lower pressures on the foreign exchange market in the second half of the year were conditioned, to large extent, by the downward adjustment of the domestic demand and thus lower import pressures. Namely, in 2009, the new investments of the corporate sector declined. The lower profit, the worsened perceptions for the movement of the domestic and foreign demand and the lower availability of additional domestic and external financing were the main factors for the negative changes in the corporate sector's investment policy. The lower investment activity meant also lower import pressures, with the import of investment goods registering an annual drop of roughly 6%. In 2009, the uncertainty for the future movement of the income, as well as the employment and for the recovery dynamics of both the domestic and the world economy was especially evident. Together with the hindered access to financing, it resulted in larger restrain from consumption and investments. The banks' activity on the credit market significantly slowed down, reducing the credit growth from over 30% in 2008 to 3.5% in 2009. Such adjustments of the credit market segment were triggered by the deteriorated expectations of the banks, reduced sources of financing, as well as the lower demand for credits. Thus despite the relatively stable labor market, the reduced credit support by the banks, together with the worsened expectations, resulted in stagnation of the households' consumption, especially of durable goods.

The decrease in the domestic demand was partially neutralized with the positive contribution of the net export, with the decrease in the domestic economy in 2009 being minor and it equaled 0.7%. Thus the real economy in 2009 showed as relatively more resistant compared to the other economies, where the decrease was significantly larger. There are several reasons for that. *First*, the lower exposure level of the domestic banks to external sources of financing prevented an emergence of larger distortions. The banking sector remained stable, while the confidence in it remained high. The measures undertaken by the NBRM also contributed to this situation. Thus with the first tide of the crisis at the end of 2008, Decision on bank's liquidity risk management was enforced, which introduced the banks' obligation for the banks to maintain certain minimal level of liquid assets. Also the Decision on foreign currency deposit with the NBRM was adopted, which enabled the banks to reduce the credit risk through investments in foreign currency deposits with the NBRM. *Second*, the low integration level of the domestic economy on the international financial markets meant smaller possibility for sudden capital outflows. Namely, before the crisis emerged, the Macedonian economy was not in an "overheating" stage, supported by the high capital inflows. On the other hand, it was not the case with part of other economies, where the high growth before the crisis was significantly supported by the capital inflows, which "dried up" during the crisis. Thus what was an obstacle for more intensive increase in the domestic economy before the crisis, emerged in different circumstances as relaxation of the external shocks. *Third*, the credibility of the NBRM in the maintenance of the foreign exchange rate stability despite the pressures at the end of 2008 and at the beginning of 2009, significantly stabilized the expectations of the economic agents in the second half of the year. *Fourth*, the movements on the labor market became favorable during the year, thus lowering the uncertainty related to the increase in the employment and significant decrease in the income. However, the possibility for delay in the adjustment of this market segment should also be taken into consideration, which is significant risk factor for the economy growth in the future period. *Fifth*, the depreciated domestic demand and poor utilization of the capacities condition noticeable downwards correction of the imports, thus alleviating the decrease in the Macedonian economy.

To summarize, the Macedonian economy coped with the global economy relatively good. The fall in the economic production was moderate, the inflationary pressures significantly reduced, the external misbalance registered positive correction and the stability of the banking system was preserved. However, the macroeconomic risks are not depleted. From the aspect of the monetary policy, in conditions of estimates for low inflation, they refer to the external position of the economy

to large extent. The gradual closing of the negative production gap, given the estimates for recovery of the domestic and external demand, means new potential pressures on the import demand. Thus together with the high degree of energy dependence and the anticipated rise and stabilization in the oil price on higher balance level would mean widening of the trade negative balance. Having in mind that the larger part of the negative gap in the trade balance is financed through the private transfers, the uncertainty about its financing remains. Moreover, this becomes even more important in conditions of still present uncertainty for the recovery of the global financial flows, more specifically for the future path of the stable sources of financing - foreign direct investments and possibility for debiting on the international financial markets. In this context, the viability of the economy's recovery will be of key significance for the forthcoming period. The experience showed that the exit from the global crisis is slow and unsynchronized. Although the recovery signs of the global economy are present, the uncertainty related to the recovery pace remains.

Dear Sirs and Mesdames,

The latest crisis, with dimensions that have not been seen for a long time, emphasizes the need of continuous implementation of the prudent policies, focused on the middle-term viability. The fiscal problems, which emerged on the surface during the crisis in large number of developed economies, clearly illustrate this. This crisis was a kind of test for us, as well, which should have shown whether in case of such strong external shock we have enough capacity to conduct disciplined and prudent macroeconomic policy. The fast and timely monetary reaction during the crisis and the successful maintenance of the monetary objectives, as well as the illustrated fiscal prudence, show that we passed this test successfully. The awareness for the consequences for creating non-viable misbalances before the crisis and the conduct of disciplined macroeconomic policy, contributed the Macedonian economy to have relatively better macroeconomic indicators relative to large number of other economies. In any case, having in mind the already mentioned challenges for the monetary policy, we as monetary authority, keep monitoring the risks and maintain the capacity for timely and adequate reaction to the potential pressures on the nominal anchor, the foreign exchange rate of the Denar. This, together with the current activities for timely anticipation and response to the challenges in the financial sector, are the two load-bearing pillars through which the NBRM actively contributes to more stable and more efficient economic and financial system.

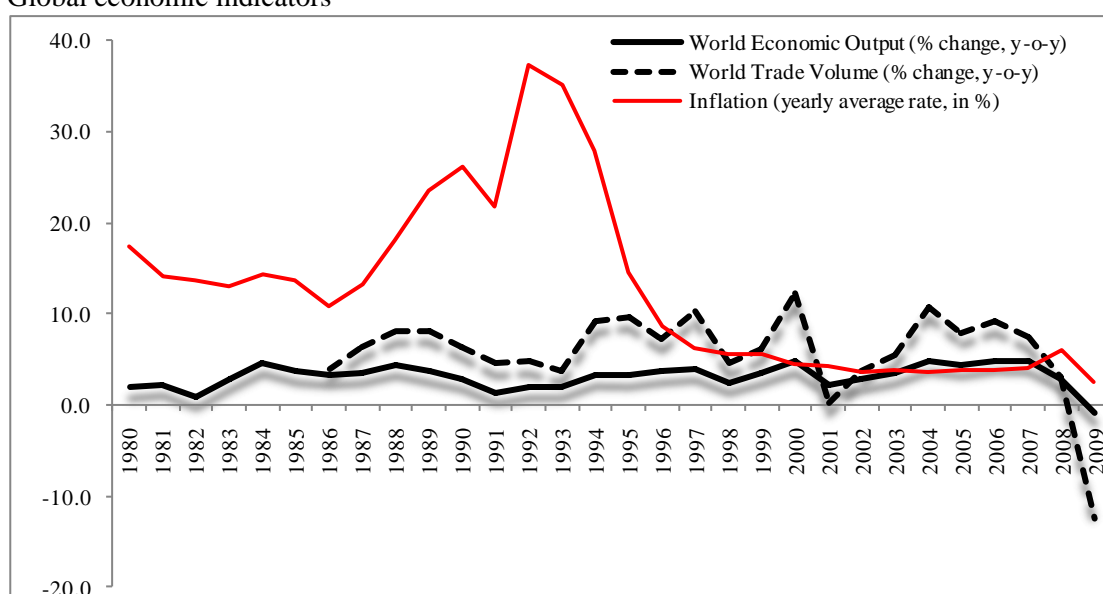
Skopje, April 2010

Petar Goshev, M.Sc.
Governor and President
of the NBRM Council

I. Economic developments in the world

After the slowdown registered in 2008, in 2009 the global economic growth entered the zone of negative changes and equaled -0.8%. Lower global demand had negative implications on the global flows in the trade, which registered a substantial fall of 12.3%, relative to the preceding year. At the same time, the inflationary pressures from the preceding two years were exhausted (caused by the growth in the price of oil and primary products in that period), with the average inflation rate on a global level being reduced to 2.5%. Throughout the year, the trends in the global economy were changing. In the first half of the year, economic activity fell sharply, as a result of the emphasized financial restrictions and the extremely low level of confidence. In the second half of the year, the effects from the proactive monetary and fiscal policies were more pronounced, when the first signs of recovery of the global economy appeared.

Figure 1
Global economic indicators



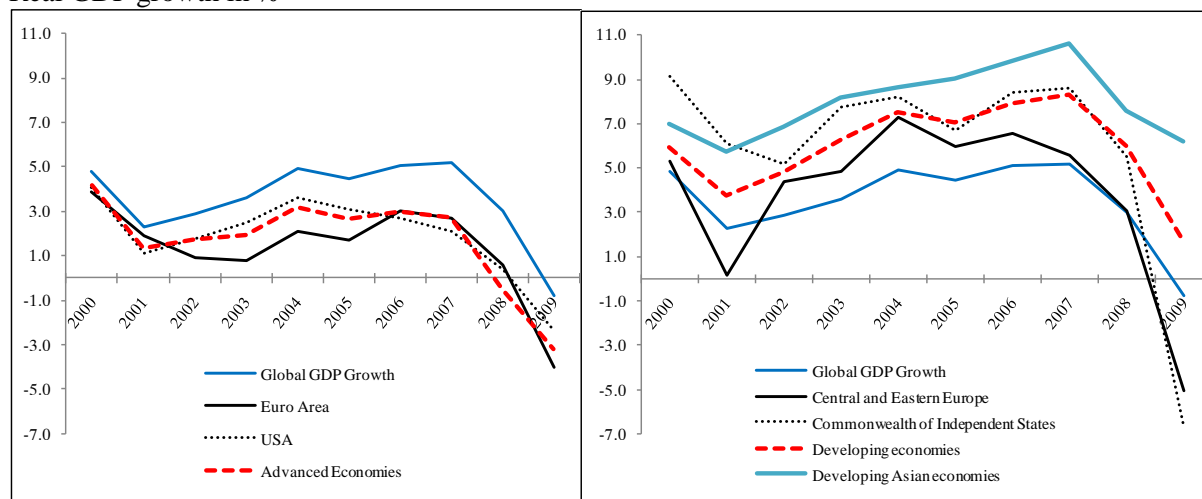
Source: World Economic Outlook -WEO

The financial crisis in the USA, which began in the middle of 2008, grew into a synchronized world economic recession in 2009. In the first half of 2009, most of the countries worldwide registered a rapid deceleration of the economic activity and a significant slowdown of the international trade. Amid high level of globalization, liquidity problems of the banking and the insurance sectors in the USA quickly spilled over globally. Along with the tightened lending terms and lower supply of credits by the credit institutions, there was a high level of uncertainty with the business sector and consumers. This has led to a significant decline in the investment and private consumption, rapid fall in the prices of shares on the world markets and a decline in the value of companies and banks, and it has caused an additional decline in the prices on the real estate market. Developed economies (USA, Eurozone, Japan and the United Kingdom) entered a recession, while in the emerging economies (China, India, ASEAN²), the economic growth has slowed down. In conditions of high level of uncertainty regarding the intensity and duration of the recession, households' consumption and investments of companies reduced significantly. Thus, in this period a decline in the demand and piling up of stocks were registered. Developed countries (USA and the EU Member States) responded to the increased uncertainty and greater liquidity problems of the financial systems with nationalization of a large portion of the problematic banks. At the same time, a number of countries adopted packages of fiscal measures in order to stimulate the economies, while the monetary authorities reduced the key interest rates to historically low levels, and also, through their

² Indonesia, Malaysia, Philippines, Thailand and Vietnam.

operations they supplied a large amount of additional liquidity in the systems. Coordinated public interventions were aimed at reducing the systemic risk on the financial markets and simultaneously at incurring the demand, by reducing the uncertainty and increasing the liquidity.

Figure 2
Real GDP growth in %



Source: Source: (IMF World Economic Outlook Database, Eurostat).

The initial signs of recovery of the global economy appeared in the second half of 2009. The stabilization of the expectations of the economic entities, along with the undertaken macroeconomic measures, had a positive effect on the economic activity in most of the world. The global recovery was evident from the growth in the industrial output and change in the cycle of stocks, stabilization of the retail trade, regaining of the consumers' confidence and strengthening of the real property market. However, the pace of recovery was slow, and the economic activity was much lower, compared with its level before the crisis. Thus, the dilemma regarding the sustainability of the positive growth rates and the possibility for "double decline" of the economic activity, remained. The main risk factors that are emphasized in this regard are the high budget deficits and their sustainability, the increased public debt and high probability that credit flows and high unemployment will still restrict the private consumption.

Table 1
Indicators for the world economy

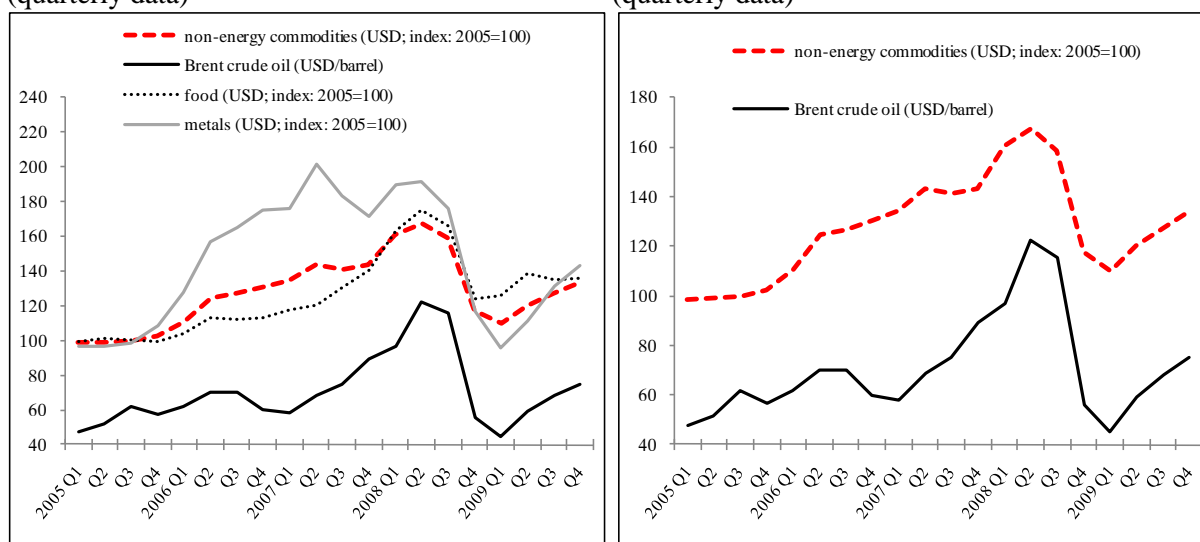
	2005	2006	2007	2008	2009*
<i>Gross Domestic Product, Global real growth rate</i>	4.5	5.1	5.2	3.0	-0.8
Developed Countries	2.6	3.0	2.7	0.5	-3.2
USA	3.1	2.7	2.1	0.4	-2.4
Euro-Area	1.8	3.1	2.7	0.5	-4.0
China	10.4	11.6	13.0	9.9	8.7
India	9.2	9.8	9.4	7.3	5.6
Central and Eastern Europe	6.0	6.6	5.5	3.1	-4.3
CIS	6.7	8.4	8.6	5.5	-7.5
<i>World Trade Volumes (growth rate)</i>	7.8	9.1	7.3	2.8	-12.3
<i>Inflation rate</i>					
Developed Countries	2.3	2.4	2.2	3.4	0.1
USA	3.7	3.2	2.6	4.4	-0.8
Euro-Area	2.2	2.2	2.1	3.3	0.3
China	1.8	1.5	4.8	5.9	-0.1
India	4.2	6.2	6.4	8.3	8.7
Central and Eastern Europe	5.1	5.4	5.6	7.9	3.9
CIS	12.1	9.4	9.7	15.6	11.8
Russia	12.7	9.7	9.0	14.1	12.3
<i>Commodity Prices</i>					
Oil	41.3	20.5	10.7	36.4	-36.1
Nonfuel	6.1	23.2	14.1	7.5	-18.9
					(in percent of GDP)
<i>Savings Rate</i>	22.9	24.1	24.5	24.2	21.7
<i>Investments</i>	22.6	23.3	23.9	24.0	21.9
<i>Nominal Exchange Rate (U.S. Dollar/EUR)</i>	1.2441	1.2556	1.3705	1.4708	1.3948

*Estimation

Source: IMF (IMF World Economic Outlook Database 2009, IMF World Economic Outlook January 2010) and Eurostat

The deceleration in the global economic activity caused a decline in the global demand for oil and primary products. In 2009, the average price of crude oil equaled US Dollar 61.9 per barrel, registering an annual rise of 36.7%. The price of crude oil Brent reached the lowest level of US Dollar 43.2 per barrel in February (annual decline of 53.5%). After the rapid decline in the oil price, OPEC adopted a decision on adjusting the production to the demand for oil, which contributed to stabilization of the price. With the rise in the global demand and the economic growth, the price of crude oil - Brent, started to follow an upward trajectory. Thus, the average price of crude oil in the second, third, and last quarter equaled US Dollar 59.1; 68.4 and 75 respectively, per barrel.

Figure 3
Movement of the index of world prices of primary products and crude oil
(quarterly data)



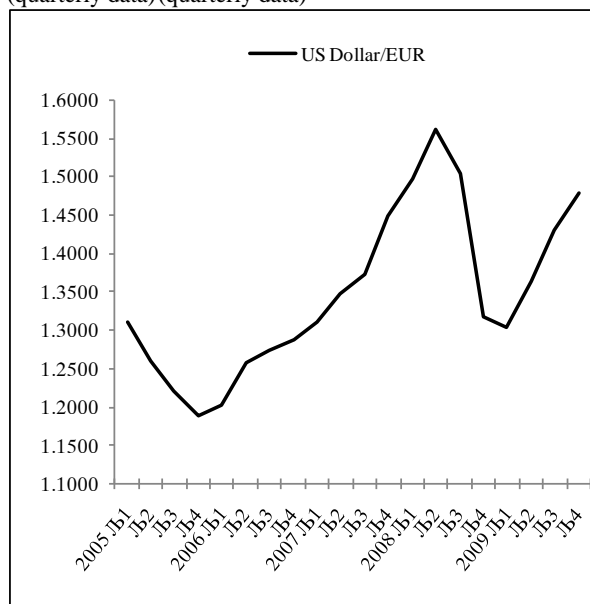
Source: IMF, monthly database

Source: IMF, monthly database

Movements in the oil price were followed by the prices of the primary products and metals, which have the oil price as an input element in production and transport. Amid lower global investment activity and lower production costs, prices of metals dropped significantly in the last quarter of 2008 and in the beginning of 2009. However, given the stabilization of the economic developments, starting from the second quarter until the end of the year, the prices of metals increased on a quarterly basis, a rise of 16.3% in the second quarter, 18.1% in the third quarter and 9% in the last quarter. Due to the higher comparison basis, the index of the metal prices registered an annual fall in the first three quarters (49.7%, 42.0%, 25.0%, respectively) and a positive growth (22.4%) in the last quarter, so that the average price index for 2009 was by 23.6% lower than the index for 2008. Similarly as with the price of metals, price indices of primary products started with a quarterly growth in the second quarter of the year, amid higher price of oil, with the annual change in 2009 registering a decline of 18.7%, compared with 2008. Thus, after the decline in the price index of primary products of 6.5% in the first quarter, in the remaining part of the year this index registered a quarterly growth of 9.4%, 5.9% and 5.3%, respectively.

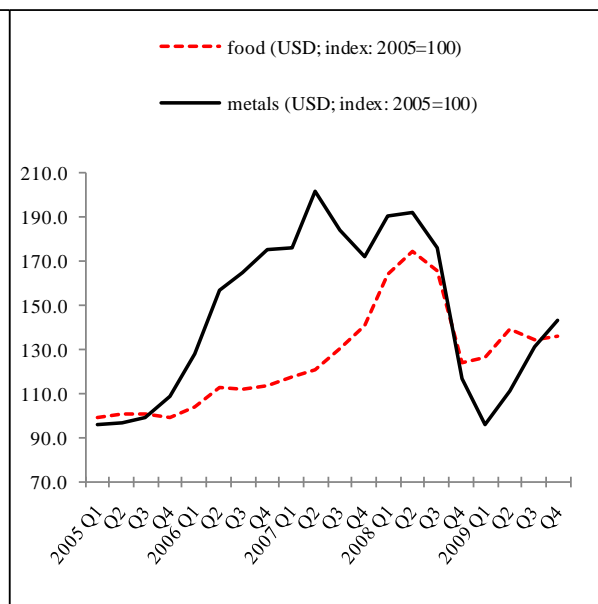
Figure 4

Exchange rate movements
(quarterly data)(quarterly data)



Source: ECB

Food and metal prices index



Source: IMF, monthly database

Global developments, and especially the outlook for the US and Eurozone economies, and the measures undertaken in these economies, had a significant influence on the US Dollar-Euro exchange rate. The spillover of the financial crisis from the USA to the economies in the Eurozone at the end of 2008 and in the beginning of 2009, reflected in the weakening of the Euro, i.e. in the strengthening of the US Dollar. However, such a tendency ceased with the gradual stabilization of the economies in the Eurozone, so that in the remaining part of the year the US Dollar depreciated by 16.7% (from February to November), i.e. from 1.28 US Dollars per Euro to 1.49 US Dollars per Euro. This trend of depreciation of the US Dollar is explained with the more positive assessments of the economic entities of the stability of the Euro and the stability of the economies of the Eurozone, but also with the interest rate spreads between the key interest rates of FED (0.25%) and ECB (1.0%). However, in conditions of unfavorable expectations, due to the huge budget deficit of Greece (of 12.7% of GDP), the Euro depreciated relative to the US Dollar in November and in December by 4.3%, i.e. the price of the Euro reduced from 1.49 US Dollars to 1.43 US Dollars.

1.1 Developed countries³

At the beginning of 2009, the outlook for the economies of the more developed countries was relatively unfavorable and accompanied by high uncertainty. Throughout the year, however, the economic condition in the developed countries stabilized, when the initial rates of positive quarterly growth were registered, i.e. the economies came out of recession. Such turning points could be largely explained with the coordinated macroeconomic policies, which have prevented the collapse of the financial system and which were aimed at stimulating the industrial sector and consumers, i.e. at strengthening the confidence of the economic agents. However, developed economies have also been facing certain restrictive factors for the economic growth. Actually, one of the main issues is the issue of the sustainability of such trends. The increased unemployment rate, increased public debt and the early termination of the macroeconomic stimulating measures, could slow down the growth or lead to another deceleration of the economic activity. At the same time, the higher demand may reflect in an increase in the prices of primary products, which also could bear negative consequences for the growth. Hence, despite the generally improved trends, the central scenarios primarily indicate moderate growth in this group of countries in the forthcoming period.

³ The analysis is mainly based on data undertaken from: Eurostat and ECB (ECB Monthly Report, April 2009, July 2009, January 2010)

In 2009, the USA economy registered a decline of 2.4% and moderate deflation of 0.4%.

In the beginning of the year, the reduced liquidity in the financial sector, the fall in the aggregate demand, production and trade were the reason for adopting a package of measures by the US Government. In February 2009, the American Recovery and Reinvestment Act was adopted, in the amount exceeding US Dollar 787 billion. Fiscal measures were aimed at creating conditions for maintaining and creating new jobs, promoting the economic recovery through investments aimed at creating economic efficiency and technological progress; providing funds for investments in infrastructural programs which will bring long-term economic benefit; and stabilizing financially the state and local government budgets in order to ensure quality services and avoid the raise of taxes. In other words, the package consisted of fiscal measures for support of the companies and budgets of the Federal States. Beside the American Recovery and Reinvestment Act, the US Government adopted the Troubled Asset Relief Program -TARP. In the fiscal year 2009 (as of September 30), USD 363.8 billion were allocated⁴ for recovery of liquidity problems (recapitalization of banks) in order to restore the stability of the financial system. The funds were also used for taking over the insurance company American International Group-AIG and for financial assistance for the automobile industry. Along with the fiscal stimulus, the Federal Reserves System-FED continued to conduct a relaxed monetary policy throughout the entire 2009 (as in the preceding year), maintaining the key interest rate at a low level of 0.25% and intervening with respect to providing additional liquidity in the domestic financial system. Facing with the risk of breaching the so-called "zero bound on interest rate", FED has attempted, through a more significant change in the structure and the number of its balance sheet items to act toward stabilization of the financial markets and stimulation of the economy. Such an approach implied massive liquidity support by using the standard, already existing monetary instruments, their adjustment, or introduction of new instruments, as well as by a direct purchase of securities.

The positive effects from the undertaken fiscal measures and the relaxed monetary policy became evident in the third quarter, when the US economy emerged from the recession (in the third and fourth quarters, positive quarterly growth⁵ of 0.6% and 1.4%, respectively, was registered). The recovery reflected in the growth of private consumption (especially on the automobile market) and households' investments in real property. Positive signs were registered also with the investments of business entities, public consumption and exports. As for the labor market, during 2009, the condition worsened continually, while the unemployment rate of 7.7% in January increased to 10.1% in October. Positive signals were registered in the second half of 2009, when the unemployment rate stabilized and even declined moderately (a decline of 0.1 p.p. in December 2009).

The shortfall in the economic activity in the Eurozone was higher than the one in the USA, i.e. the real GDP growth in 2009 was -4%, amid moderate inflation of 0.3%. The financial and trade integration of the Eurozone, and of the European Union in general, with the US economy, implied rapid spillover of the crisis. As a response to the deteriorated economic condition and in order to maintain the liquidity of the financial system, as early as in October 2008, the European Council adopted a Decision on increasing the minimum deposit insurance to Euro 100,000. In cooperation with the International Monetary Fund and the World Bank, the European Commission gave away Euro 14.6 billion as a support for the balance of payments of the Member States from Central and Eastern Europe (Euro 6.5 billion for Hungary, Euro 5 billion for Romania and Euro 3.1 billion for Latvia). In December 2008, the European Council adopted the European Economic Recovery Plan⁶ which was agreed by all Member States. According to the Plan, the total fiscal stimulus in 2009 was supposed to equal minimum 1.5% of the GDP of EU (over Euro 200 billion), with full compliance with the provisions of the Stability and Growth Pact). According to the assessments of the European Council March meeting, the total number of fiscal measures undertaken by the Member States in 2009, exceeded the expectations and are in the amount of over Euro 400 billion (3.3% of GDP of EU). They

⁴ Annual Financial Report on TARP - 2009, of the Federal Treasury Department.

⁵ Quarterly data pertain to changes in the seasonally adjusted data.

⁶ The European Economic Recovery Plan implies synchronized fiscal measures of the EU Member States aimed at: increasing the cash flows and increasing the financial system liquidity; increasing the national budget stimulus in order to boost demand, through relaxed tax policy, direct financial support for the companies; and support of the four priorities of the Lisbon Treaty: (1) employment and entrepreneurship, (2) financial support for small and medium enterprises, (3) support of the measures from infrastructure and energy, and (4) support of research and innovations.

are aimed at mitigating the effects from the crisis and boosting the economic growth. Out of this amount, Euro 79 billion were direct assistance from the European Investment Bank - EIB, and Euro 5 billion were from the EU budget.

Table 2
Economic indicators for the developed countries

	GDP (real growth rate in %)			Average Inflation rate (in %)			Unemployment rate (in %)			Consolidated Budget balance (% of GDP)			Current Account Balance of the BOP (in % of GDP)		
	2007	2008	2009*	2007	2008	2009*	2007	2008	2009*	2007	2008	2009*	2007	2008	2009*
Developed countries	2.7	0.5	-3.2	2.2	3.4	0.1	5.4	5.8	8.2	-1.2	-3.5	-8.9	-0.9	-1.3	-0.7
USA	2.1	0.4	-2.4	2.6	4.4	-0.8	4.6	5.8	9.3	-2.8	-5.9	-12.5	-5.2	-4.9	-2.6
Japan	2.4	-1.2	-5.0	0.1	1.4	-1.3	3.9	4.0	5.1	-2.5	-5.8	-10.5	4.8	3.2	1.9
EU	2.9	0.8	-4.1	2.3	3.7	1.0	7.1	7.0	8.9	-0.9	-2.3	-6.9	-0.5	-1.1	-0.8
UK	2.6	0.5	-5.0	2.3	3.6	2.2	5.3	5.6	7.6	-2.6	-5.5	-13.0	-2.7	-1.7	-2.0
Euro Area	2.7	0.6	-4.0	2.1	3.3	0.3	7.4	7.5	9.4	-0.6	-1.2	-6.2	0.3	-0.7	-0.7
Germany	2.5	1.3	-5.0	2.3	2.8	0.2	8.4	7.3	7.5	0.2	0.0	-3.4	7.5	6.4	2.9
France	2.3	0.4	-2.2	1.6	3.2	0.1	8.4	7.8	9.4	-2.7	-3.4	-8.3	-1.0	-2.3	-1.2
Italy	1.6	-1.0	-4.7	2.0	3.5	0.8	6.1	6.7	9.1	-1.5	-2.7	-5.3	-2.4	-3.4	-2.509
Greece	4.5	2.0	-1.1	3.0	4.2	1.3	8.3	7.7	9.2*	-3.7	-7.7	-12.7	-14.2	-14.4	-10.0

Estimation Source: IMF World Economic Outlook Database 2009, European Central Bank, European Commission, National Central Banks

At the same time, the European Central Bank (ECB) was continuously lowering its key interest rate from 4.25% in September 2008, to 1% in May 2009. Only in 2009, ECB lowered its key interest rate on four occasions by 150 basis points, from 2.50% in January 2009, to 1% in May 2009. Similarly to FED, except the relaxation of the key interest rate, ECB has used additional measures, aimed at increasing the liquidity and intensifying the activity on the financial markets.

As a result of the coordinated fiscal and monetary measures, as early as in the second quarter of the year the decline in the Eurozone GDP slowed down, while in the third quarter, a positive quarterly growth was registered (of 0.4%, after the continuous fall in the preceding five quarters). The growth was generated by the net-exports and investment consumption, while personal consumption remained unchanged. One of the restrictive factors for growth of the private consumption was the unemployment rate, which increased in the Eurozone from 8.5% in January to 10% in December 2009. The growth in the Eurozone, which slowed down in the last quarter of 2009 (to 0.1%), was uneven in the largest economies of the Eurozone. In the last quarter, while the growth rate of the economy of France reached 0.6%, Germany did not register quarterly growth, and the growth rate in Italy was negative (0.2%).

The fall in the economy of the United Kingdom in 2009, equaled 4.8%, amid registered deflation of 0.4%. The beginning of the year, as with the other developed countries, was marked by the decline in the industrial output, lower private consumption due to the decline in the disposable income, but also the strong depreciation of the British Pound Sterling, which reflected adversely on the inflation rate (3% average annual rate in the first quarter). As a response to the slower economic activity, the Bank of England and the Government continued to conduct a relaxed monetary policy and expansive fiscal policy⁷. In the first quarter, the Central Bank of England reduced its key interest rate to 0.5% and continuously increased the money supply, through purchasing securities⁸ by the newly-established Asset Purchase Facility - APF. Starting from December 2008, the Government reduced the VAT rate from 17.5% to 15% in order to stimulate the consumption. Along with this change in the tax policy, the undertaken fiscal stimuli were aimed at stimulating the industrial output, boost private investments and saving and increase the supply and selling of real property. Such measures had positive implications for the industrial output and the services sector and caused an increase in the private consumption, which reflected in the continuous growth in the prices of real property in the

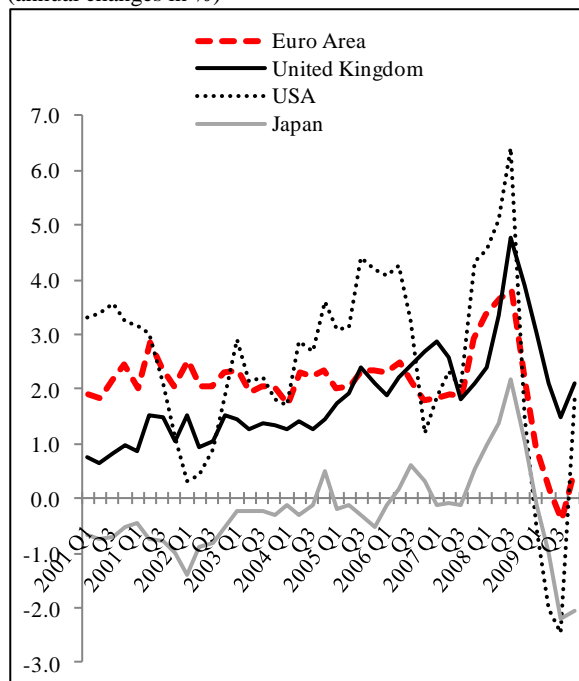
⁷ Information on government measures taken from the Report on the 2009 Budget of the Ministry of Finance of the United Kingdom.

⁸ In January 2009, the Bank of England established the Asset Purchase Facility (APF), which during the year purchased securities in the amount of GBP 190,053 million, of which GBP 188,076 million were government bonds, GBP 1,549 million were long-term commercial papers and GBP 429 million were short-term commercial papers.

second half of 2009. In the last quarter of 2009, there was an insignificant quarterly economic growth of 0.1% in conditions of still high unemployment rate (of 7.8% in November 2009).

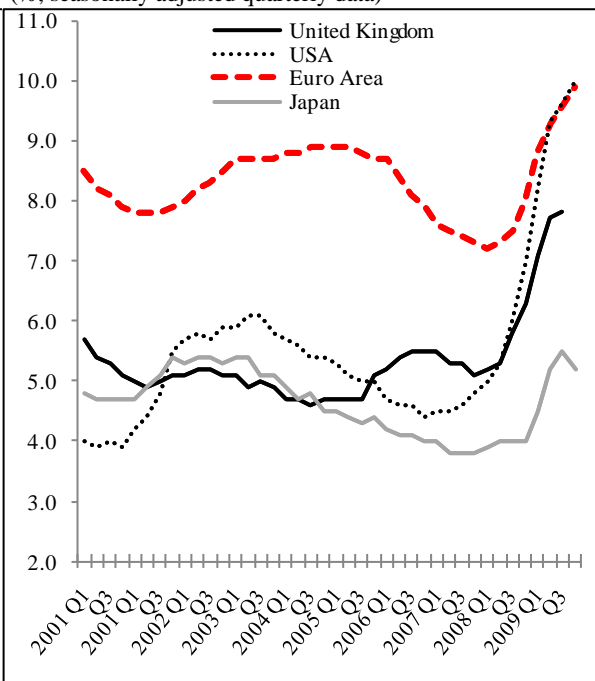
Figure 5

Inflation rates
(annual changes in %)



Source: Eurostat and national data

Unemployment rate
(%, seasonally adjusted quarterly data)



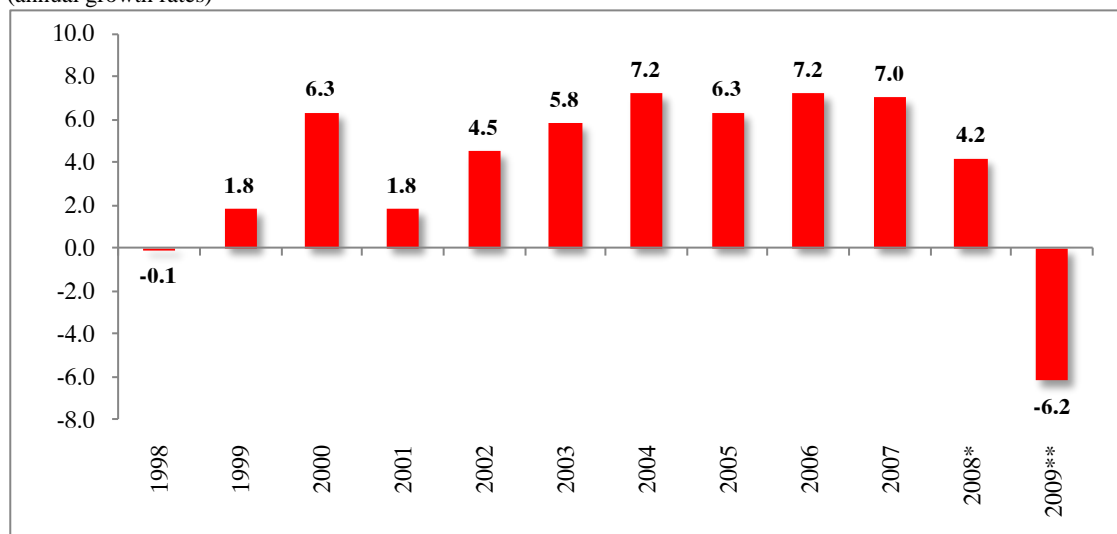
Source: Eurostat

1.2. Countries in transition in 2009⁹

The recession in the developed economies spilled over into the group of countries in transition, and in 2009 these economies faced with the deepest crisis after the crisis during the fall of the centrally-planned system in the early nineties. In conditions of lower domestic absorption and exports, the decline in the economic activity in this group of countries equaled 6.2% in 2009. Such a change is a significant downward adjustment after the average GDP growth of 6% in the preceding seven years. However, it should be emphasized that the slowdown of the economic activity in some of the countries of this group started before the beginning of the global crisis. This primarily refers to the Baltic countries, where after the phase of a credit "boom", overheating of the economy and inflationary pressures, in 2007 an adjustment in the opposite direction started (partially driven by the slower credit growth, due to the tighter regulatory policy). With the initial signs of the crisis in the developed countries, there was a significant slowdown in the capital inflows in certain economies (Baltic countries and Croatia), which has additionally restricted the financial flows, causing further slowdown of the growth. The transformation of the financial crisis into an economic recession has resulted into a larger dispersion of the negative transmission effects in the group of transition countries.

⁹ It refers to the Central-Eastern European and Baltic countries (CEB) - Croatia, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Slovakia, Slovenia, South-Eastern Europe (SEE) - Bulgaria, Romania, Albania, Bosnia and Herzegovina, Macedonia, Montenegro, Serbia, Eastern Europe and Caucasus - Armenia, Azerbaijan, Belarus, Georgia, Moldova, Ukraine, Central Asia - Kazakhstan, Kyrgyzstan, Mongolia, Tajikistan, Turkmenistan, Uzbekistan, and Turkey and Russia.

Figure 6
Real GDP in transition economies
(annual growth rates)



*estimated data, **projected data

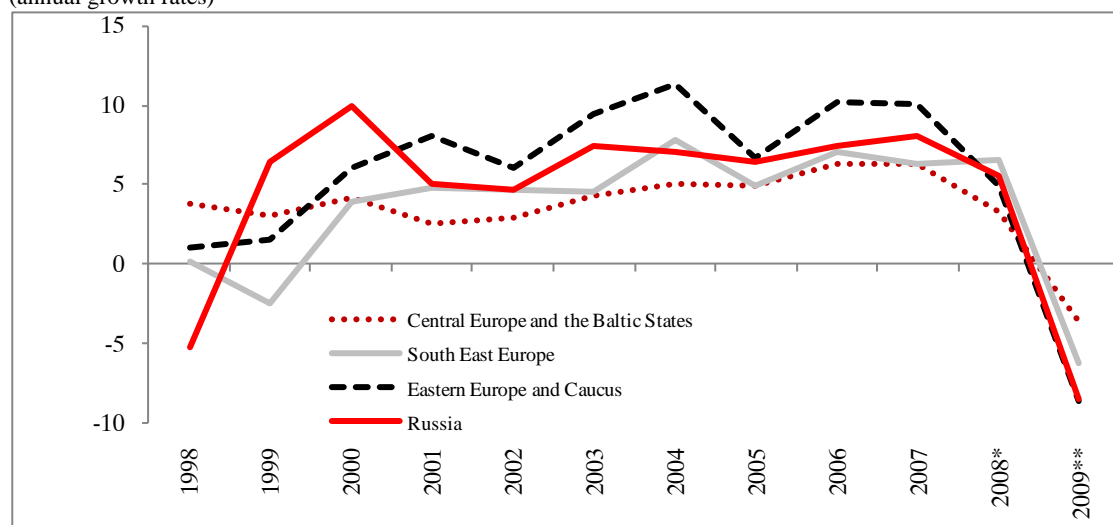
Source: EBRD, Transition Report 2009

The collapse of the export prices and of the export demand, further slowdown of the capital flows, but also the substantial decline in the remittances from abroad in some countries¹⁰ are the main factors of decline of the economic activity. The effects transmission channel through the capital flows was especially emphasized in the countries with more integrated financial systems. These economies absorbed large amounts of capital inflows in the pre-crisis period. Amid evident uncertainty and risks, as well as slowdown of the global financial flows, capital inflows and outflows of short-term capital diminished, which led to a significant decline in the credit support and tightening of the terms of lending. This affected the domestic demand. However, on average, common for the entire group of countries was the fact that during this crisis, the phenomenon of "sudden stop" in the capital inflows¹¹ did not happen. The high share of foreign capital in the banking systems of a larger number of the countries is considered to be one of the important factors for such a condition, having in mind that the capital flows between the parent companies and their subsidiaries are significantly more stable compared with the other financial flows.

¹⁰ It refers mainly to Moldova, Kyrgyzstan and Tajikistan, where large amounts of remittances from abroad are common source of financing of the domestic demand. With the decline in the activity in the EU and in Russia, as main countries where remittances come from, a significant decline in these flows was registered.

¹¹ EBRD, Transition Report 2009, Transition in crisis?

Figure 7
Real GDP by groups of countries
(annual growth rates)



*estimated data, **projected data

Source: EBRD, Transition Report 2009

Slowdown of the economic activity was common for almost all transition economies, but with varying intensity. Analyzed from a viewpoint of groups of countries, from among the transition economies, the largest GDP fall was registered in the countries of Eastern Europe and Caucasus region (real GDP decline of 8.7%). From among the individual economies, the most significant slowdown of the economic activity is expected in the three Baltic economies - Estonia, Latvia and Lithuania, where double-digit rates of GDP decline are registered. These countries were among the first transition economies which felt the effects of the global financial and economic crisis, amid high level of integration in the international capital market and emphasized macroeconomic imbalances in the period before the crisis. The termination of the large capital inflows which were common for the pre-crisis period, high current account deficits, and sharp fall in the real property prices, resulted in a significant adjustment of the economy and decline in GDP. On the other hand, two European countries, Poland and Albania, avoided recession in 2009. The former due to the relatively small macroeconomic imbalances before the crisis and the relatively small significance of the exports, i.e. small dependence on the foreign demand. The latter, due to the high government investments in the infrastructure and good results in the telecommunications and services sectors.

In the countries of South-Eastern Europe (SEE), the group which includes Macedonia, real GDP is expected to fall by 6.2% on annual basis¹². The analysis by individual country shows that such a sharp fall in the activity was generated by two countries (Bulgaria -6% and Romania -8%), given the lowest decline in Macedonia and real GDP growth in Albania. Crisis transmission channels are generally the same in all countries of the group, i.e. lower exports, decline in the capital inflows, slowdown or decline in the credit growth and downward adjustment of the domestic demand. However, the intensity of the effects is different, which is of course caused by the different starting points before the crisis, county specifics, labor market adjustment degree, as well as the reactions of the macroeconomic policies.

¹² The data on GDP in the countries of South-Eastern Europe exclude Croatia, which according to the latest EBRD Transition Report is classified in the group of Central Europe and Baltic countries.

Table 3
Economic indicators for the countries of South-Eastern Europe

	GDP (real growth rate, %)			Average inflation (growth in %)			Current Account of the Balance of Payments (% of GDP)			Consolidated State Budget Balance (% of GDP)		
	2007	2008*	2009**	2007	2008*	2009**	2007	2008*	2009**	2007	2008*	2009**
Albania	6.0	6.8	3.0	2.9	3.4	1.7	-10.6	-15.1	-14.5	-3.5	-5.7	-6.3
Bosnia and Herzegovina	6.8	5.4	-3.1	4.9	6.5	3.0	-12.2	-14.7	-9.6	-0.1	-3.0	-4.0
Bulgaria	6.2	6.0	-6.0	8.4	12.3	2.6	-25.4	-25.2	-12.6	3.5	3.0	-0.1
Macedonia***	5.9	4.8	-0.7	2.3	8.3	-0.8	-7.3	-13.1	-7.5	0.6	-1.0	-2.7
Romania	6.0	7.1	-8.0	4.8	7.9	5.3	-14.4	-12.3	-6.0	-3.1	-4.9	-7.3
Serbia	6.9	5.4	-4.0	6.7	11.7	8.3	-15.7	-17.2	-12.9	-1.9	-2.4	-4.5
Croatia	5.5	2.4	-5.4	2.9	6.1	2.5	-7.5	-9.4	-8.5	-2.5	-1.4	-3.3
Montenegro	10.7	7.5	-4.1	4.2	7.4	1.8	-29.4	-33.6	-22.8	6.4	1.5	-3.0

* Estimation, except for the data on the Republic of Macedonia

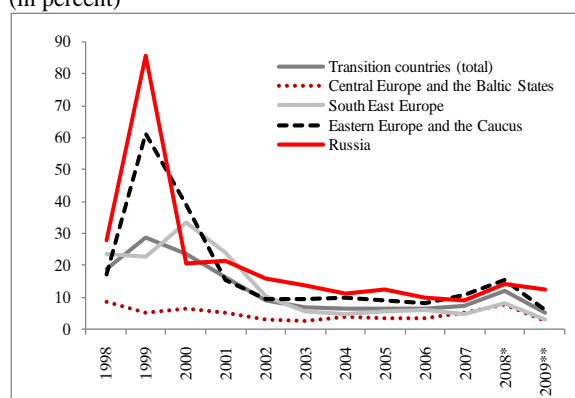
** Projection

*** Source of data for the Republic of Macedonia are the respective official institutions.

Source: EBRD, Transition Report 2009

The slowdown in the activity in the real sector contributed to a significant decline of the inflationary pressures, but also to a correction of the current account deficits. Thus, along with the significantly lower pressures from import prices (after the extremely high growth in the prices of food and energy in the previous year), the decline in the economic activity contributed to the decline in the average inflation in the group of transition countries of 11.9% in 2008 to 5.1% in 2009. The inflation rate registered in 2009 is the lowest average growth in the average price level since 1997. The decline in the pressures from domestic and export demand implied smaller needs for imports, which also enabled narrowing in the current account deficit. On average, in the group of countries in transition, the current account deficit in 2009 was estimated at 4.9% of GDP, as opposed to 7.6% of GDP in the preceding year. The largest adjustment was registered in the countries of Central Europe and Baltic countries, given a lower deficit of 6.6 percentage points (double-digit declines in GDP in the Baltic countries indicated a shift into a zone of current account surplus), as well as in the countries of South-Eastern Europe, with smaller deficit of 5.8 p.p.

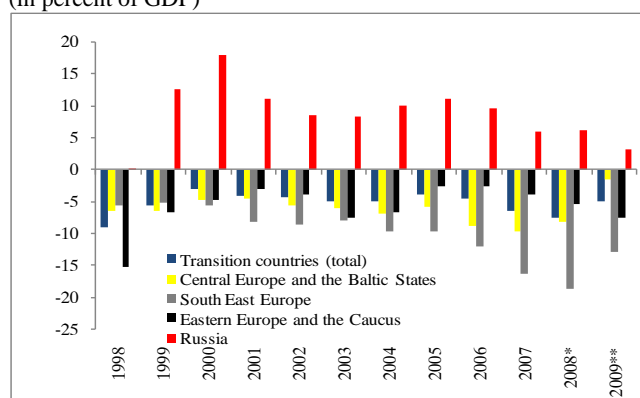
Figure 8
Inflation rate
(in percent)



*estimated data, **projected data

Source: EBRD, Transition Report 2009

Figure 9
Current account balance
(in percent of GDP)



The response of the macroeconomic policies to the effects of the crisis, was basically determined by the specific features of the individual economies. However, in general, one may argue that the changes in the monetary policy were directed toward relaxation, while major deterioration in the fiscal positions, on average, was not registered. Thus, in most of the countries, the monetary policy reacted with a decline in the key interest rate¹³. However, in the countries with

¹³ Thus, a decline in the interest rates was registered in Albania (from 6.25% in December 2008, to 5.25% in March 2010), Romania (from 10.25% in August 2008, to 7% in February 2010) and in Serbia (from 17.75% in November 2008, to 9% in March 2010).

fixed exchange rate regime, or countries which faced a significant depreciation of the domestic currency, in the periods of stronger pressures the monetary policy reacted with an increase in the interest rate (for example Russia, Hungary, Macedonia). As for the fiscal policy, the potentially more difficult access to financing, was probably the restrictive factor for more intensive budget spending. Thus, budget deficit increased by 4 p.p. of GDP relative to 2008, given a minimal growth of the budget expenditures of 1.3 p.p. of GDP. However, observed by individual economies, fiscal positions differ depending on the realized budget revenues, adjustment of the budget expenditures, possibilities for financing, influence of the automatic stabilizers (which is, for example, strong in Poland), adoption of packages of fiscal stimuli (for example, such packages of larger volume were adopted in Kazakhstan, in the amount of 9.5% of GDP and in Russia in the amount of 5% of GDP), as well as the differences in the meaning attributed to the crowding out effect of the private sector.

Table 4

Indicators of progress in the transition for the countries of South-Eastern Europe

	Enterprises			Markets and trade			Financial institutions		Infrastructure
	Large-scale privatisation	Small-scale privatisation	Governance and enterprise restructuring	Price liberalisation	Trade and foreign exchange system	Competition policy	Banking reform and interest rate liberalisation	Securities markets and non-bank financial institutions	Overall infrastructure reform
Albania	4-↑	4	2+	4+	4+	2	3	2-	2+
Bosnia and Herzegovina	3	3	2	4	4	2	3	2-	2+
Bulgaria	4	4	3-	4+	4+	3	4-	3	3
Macedonia	3+	4	3-	4+	4+	2+	3	3-↑	3-↑
Serbia	3-	4-	2+	4	4↑	2	3	2	2+
Croatia	3+	4+	3	4	4+	3↑	4	3	3
Romania	4-	4-	3-	4+	4+	3-	3+	3	3+
Montenegro	3↓	4-	2	4	4	2↑	3	2-	2+↑

Source: EBRD, Transition Report 2009

The global recession in 2009, also slowed down the pace of institutional reforms in the transition countries, amid absence of a more significant progress in most of the countries. The indicators of progress in transition of the EBRD for 2009, show that in 2009 the progress was most significant in the countries of the Western Balkans, which registered 7 improvements (of the total number of 14 in all 29 transition countries) and only one deterioration (of the total number of 4 in all transition countries). Largest progress was made in the field of infrastructural reforms, where two improvements have been registered. Analyzed by country, the most significant progress registered in 2009 is that of Macedonia, which has implemented two reforms, one of which is the introduction of the third pension pillar, and the second one is in the area of telecommunications. Second best in progress is Montenegro, which has also registered two improvements, in the area of competition and infrastructure. Montenegro has, however, registered deterioration in the area of privatization of large enterprises. In 2009, institutional reforms were registered also in Serbia, in the area of the trade system, and in Albania, due to the privatizations in the energy sector, telecommunications and banking system, and in Croatia, due to the continuous improvement in the field of legislation governing competition policy.

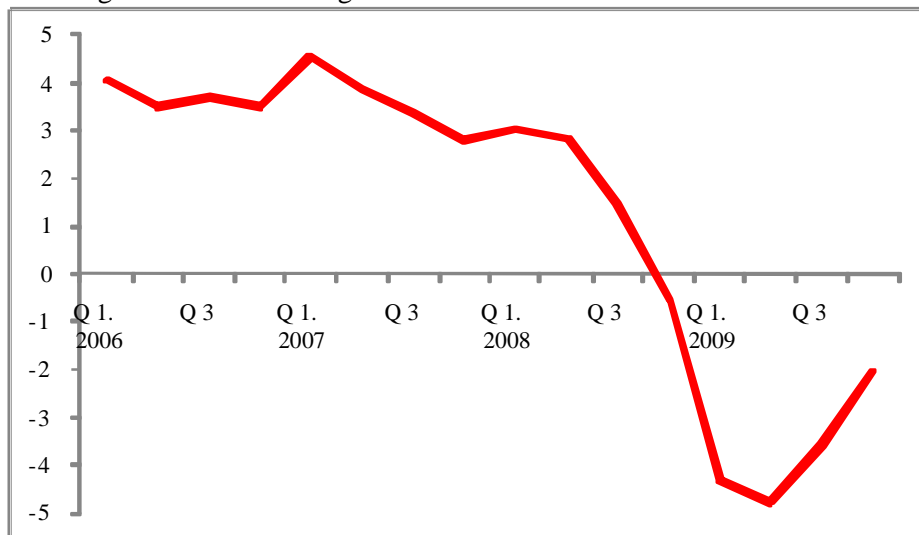
a. Foreign effective demand

The slowdown in the economic activity of the most important trading partners of the Republic of Macedonia had an adverse impact on the foreign effective demand¹⁴, which registered the historically fastest decline of 3.7% in 2009. The decline in the foreign demand was most significant in the first half of the year (4.5%), when the strongest effects from the global crisis and the largest uncertainty regarding the recovery of the global economy, were registered. The decline continued in the remaining part of the year, but with relatively more moderate rates (2.8%), as a reflection of the first signs of emerging from recession of some of the trading partners. Analyzed by

¹⁴ Foreign effective demand is a sum of weighted indices of GDP of the most important trading partners of the Republic of Macedonia. Weights have been calculated on the basis of the share of these countries in the exports in 2006. GDP data for the countries - trading partners of Macedonia are taken from the Eurostat database (New Cronos database), and from the Serbian Statistical Office. The calculation of this index includes Germany, Greece, Italy, the Netherlands, Belgium, Spain and Serbia.

country, the largest contribution to the fall in the foreign effective demand in 2009 was that of the decline in the economic activity in Germany and in Italy, followed by the decline in Greece and in Serbia.

Figure 10
Annual growth rates of foreign effective demand



Source: Eurostat and the State Statistical Office of Serbia and calculations of the NBRM.

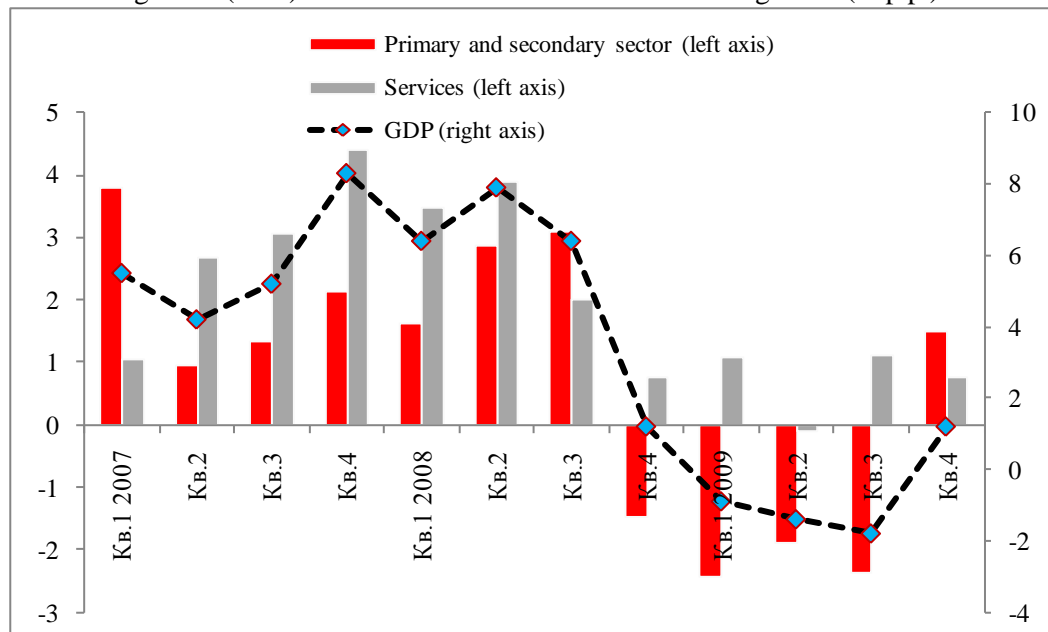
II. Economic developments in the Republic of Macedonia

2.1. Economic activity

The adverse effects from the global financial and economic crisis on the domestic economy led to a decline in the domestic economic activity in 2009. The initial effects were evident in the last quarter of 2008, with the deceleration of the annual growth, while during 2009, GDP registered an annual decline of 0.7% in real terms¹⁵. Thus, for the first time after 2002, domestic economy registered a slowdown in the economic activity. Negative results were common since the beginning of the year, and the most intensive deceleration of the economy was registered during the third quarter, while the initial positive annual changes were registered in the last quarter (real growth of the economy of 1.2%). After the significant decline in the exports at the beginning of the year, driven by the fall in the foreign demand, in the remaining part of the year there was a significant downward adjustment of the domestic demand. The refrain of the households and the corporate sector due to the high uncertainty, as well as the significantly lower credit support, are part of the factors which explain such trends. On the other hand, the stagnation of the private consumption and decline in investments, combined with the fall in the foreign demand, caused a significant downward correction of the imports. Thus the contribution of the net-exports to the economic activity was positive. From a viewpoint of the main sectors of the economy, worse performances compared with the preceding year were registered in the primary and in the secondary sector, entirely driven by the large negative contribution of the industry, partially offset by the increased construction and agricultural activity. The significant negative contribution of the primary and the secondary sector was partially mitigated with the positive contribution of the services sector, driven primarily by the increased value added in the financial intermediation.

Figure 11

Real GDP growth (in %) and contributions of the sectors to the growth (in p.p.)



Source: State Statistical Office and calculations of the NBRM. * Data on 2008 are preliminary, while data on 2009 are estimated.

Compared with the countries of the region, the Macedonian economy has experienced a relatively small contraction of the economic activity. For one part, this could be explained with the weak international financial integration, due to which there was no sudden termination of

¹⁵ Data on GDP for 2009 are estimation of the SSO.

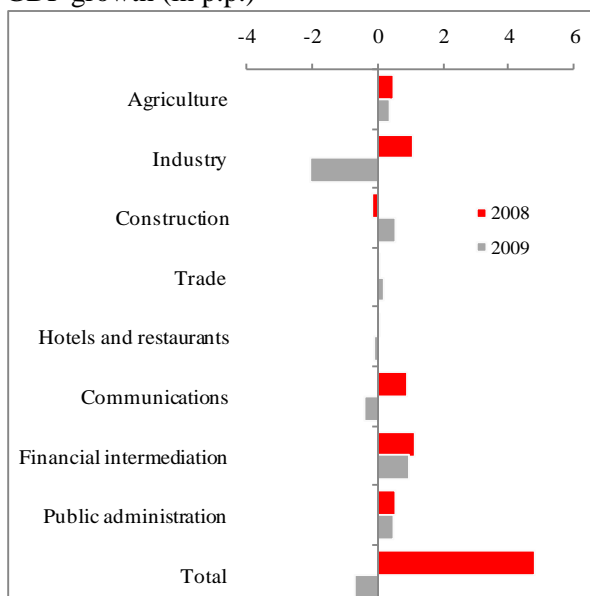
the external financial support for the economy. This was not the case with part of the other economies, in which the fast growth before the crisis was supported with high capital inflows. Their decline during the crisis caused a significant economic contraction. At the same time, the movements on the labor market, as well as the significant downward correction of the import demand, also explain the slower decline of the Macedonian economy. Also, despite the significant fall in the foreign demand and exports, the inertia in the concluded contracts in the period before the crisis mitigated the deceleration of the activity of some of the exporters. From a viewpoint of individual country, most severely hit was the Turkish economy with real GDP fall of 8.6% in the first three quarters of 2009, followed by Romania (-7.0%), Croatia (-6.2%), Bulgaria (-4.6%), Montenegro (-4.0%) and Serbia (-3.6%). Positive results in the countries in the region were registered only in Albania (GDP growth of 4.9%), which is to a large extent explained by the large government investments in infrastructural projects.

2.1.1. Domestic supply

The effects from the global recession were gradually transmitted on the domestic economy in 2009. Thus, in the third quarter the sharpest fall in the domestic economic activity was registered since the beginning of the global financial and economic crisis, of 1.8% (in the preceding two quarters, the real GDP fall was 0.9% and 1.4%). However, in the last quarter of 2009, the first signs of recovery of the domestic economy were registered, when the real GDP growth was 1.2%, whereby the average annual decline of the economy for the entire 2009 was 0.7%. The deceleration of the economic activity in 2009 was a result of the lower domestic and export demand. Depreciated demand had transmission effects on the activity in several branches, reducing the new supply in the economy. The analysis by branches indicates that the industry registered the fastest decline (9.4%) and has dominant contribution to the total deceleration of the economy. Permanent negative results were registered also in "hotels and restaurants" (a decline of 4.8%) and in "transport and communications" (a decline of 4.6%). On the other hand, the other activities registered positive results, with more significant growth being registered in the construction activity (9.6%) and in financial intermediation of 7.1% (however, this growth is lower compared with the growth of 8.7% in 2008).

Figure 12

Contribution of individual components to the GDP growth (in p.p.)

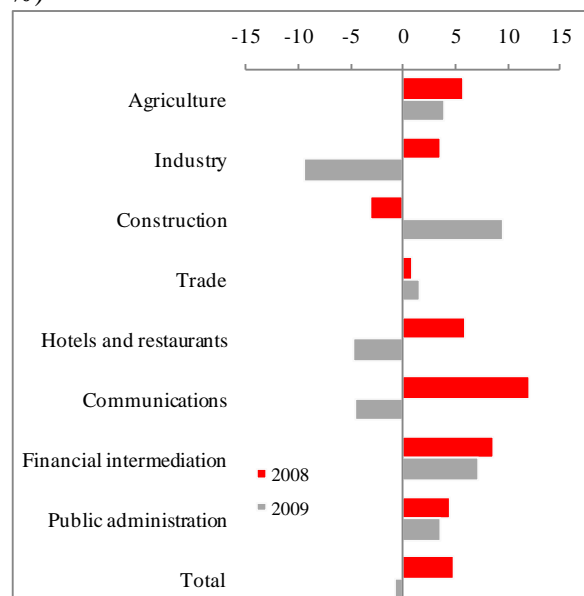


Source: State Statistical Office and calculations of the NBRM.

* Data on 2008 are preliminary, while data on 2009 are estimated.

Figure 13

Annual growth rates of GDP and components (in %)

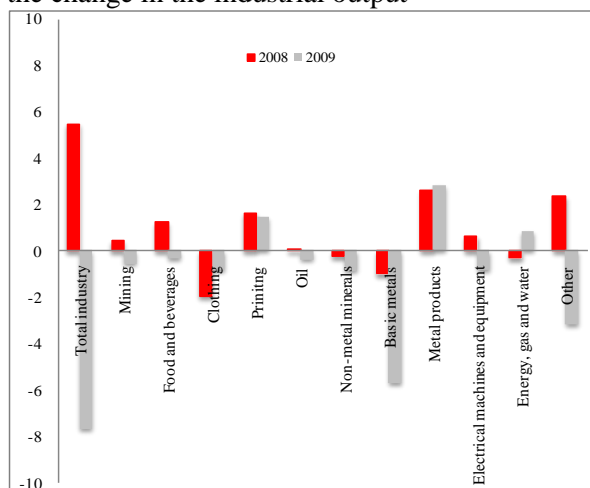


Source: State Statistical Office.

The insufficient utilization of the capacities in the export-oriented branches, supplemented by the fall in the activity due to the lower domestic demand, caused a decline in

the value added in industry of 9.4%¹⁶ in 2009. The low comparison basis in the last quarter of 2008, when the first more serious effects of the global crisis emerged in this segment, resulted in an annual rise of the value added in industry of 3.5%¹⁷ in the fourth quarter of 2009. Such a growth in the last quarter of 2009 mitigated the cumulative annual decline in the industrial output, which equaled 7.7% for the entire 2009. The results accomplished in 2009 are any way better than the results of the countries in the region. Croatia, Turkey, Serbia and Montenegro registered annual rates of decline of 9.2%, 9.6%, 12.1% and 32.2%, while only Albania had a lower decline in the industrial output (in the first three quarters the decline in industry equaled 6.3%). In 2009, decline in industry was registered in 21 out of 24 branches, accounting for 81.4% of the index. The decline in the *production of basic metals* had the largest continuous influence on the decline in the industrial output in 2009, with contribution of 5.7 p.p. The decline in the total index was supported also by the reduced production of the *textile industry*, products of *other non-metal minerals*, *electrical machinery and apparatus*, as well as manufacture of *chemicals and chemical products*. From among the branches which registered positive results, more significant were the positive results in the *manufacture of fabricated metal products*, as well as in *printing* (partially due to the local and presidential elections). Also, positive contribution was that of the production of *electricity*, due to the improved hydro conditions in the country, as a result of the favorable weather conditions.

Figure 14
Contributions (in p.p.) of individual branches to the change in the industrial output



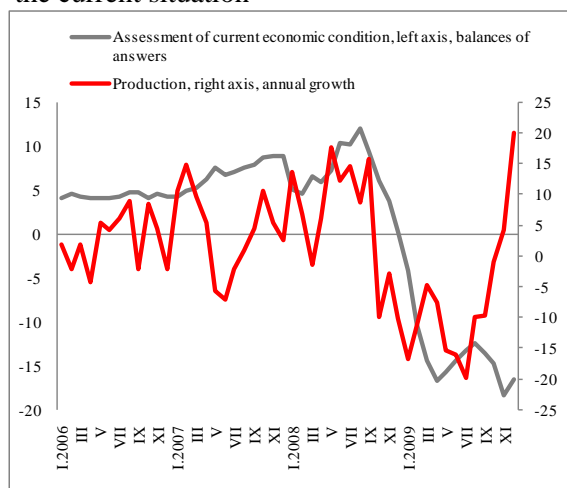
Source: State Statistical Office and calculations of the NBRM.

Net responses, presented on the left scale, show the movement of the indicators rather than the real volume, i.e. they indicate improvement or deterioration of the situation. Net responses are obtained by weighting the individual responses. The responses of the managers are qualitative (good, bad, increase, decline, etc.) rather than quantitative.

The deterioration in industry is indicated by the results of the Survey on Business Tendencies in Manufacturing of the State Statistical Office¹⁸. The observations of the managers from the manufacturing industry confirm the condition in industry during 2009, and according to them the business condition of the companies has been continuously deteriorating since the beginning of 2009. Most emphasized restrictive factors for the manufacturing are the lower foreign and domestic demand, uncertain economic environment and lack of finances.

The annual fall in the production of *basic metals* in 2009 was 42.1%, given the lower prices of metals and lower foreign demand. Analyzed from a viewpoint of the dynamics, it is evident that the decline which started in August 2008 continued without interruption until the third quarter of 2009. The positive production in the last quarter of 2009 with annual growth of 13.4%, is a

Figure 15
Industrial output and managers' assessments of the current situation



Source: State Statistical Office.

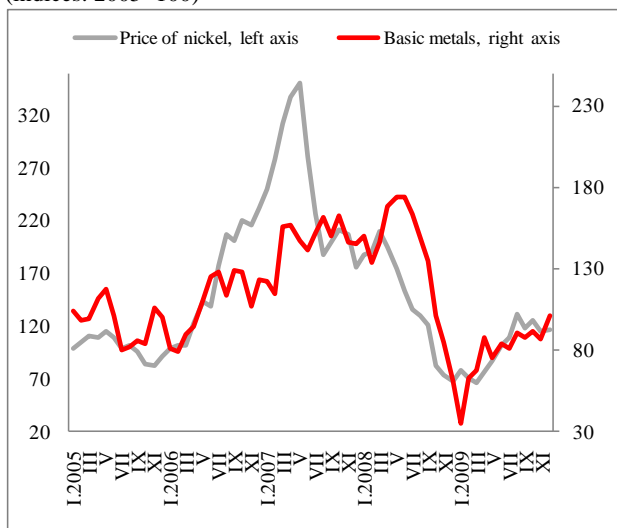
¹⁶ At the same time, the decline in the volume of the industrial output equaled 7.7%.

¹⁷ The growth in the volume of the industrial output in the last quarter equaled 7.5%.

¹⁸ From December 2009.

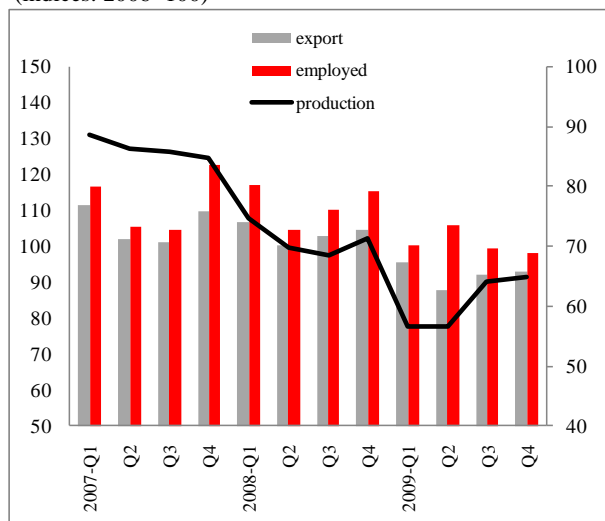
result of the comparison basis effects from the low production in the same period of the preceding year, but also of the recovery of the world metals market since August, 2009. Significant deterioration was registered also in the *textile industry* (branch employing the largest number of workers), where the volume of production in 2009 registered an annual decline of 14.8%, the exports fell by 11.0%, and the number of employees dropped by 9.7%. However, the annual rates of decline of the textile production registered in the second half of 2009 are much lower compared with those registered since the beginning of the year.

Figure 16
Basic metals production
and price of nickel
(indices: 2005=100)



Source: State Statistical Office and IMF

Figure 17
Production and exports of textiles and employees in
the textile industry
(indices: 2006=100)

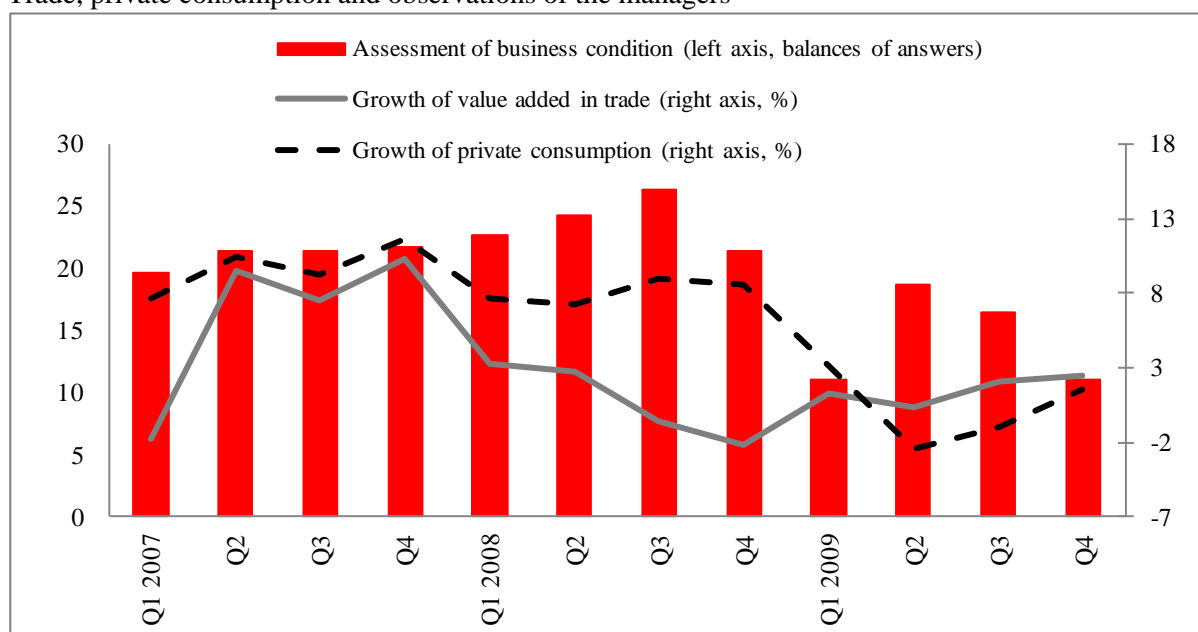


Source: State Statistical Office.

Value added in trade (second most important activity in the economy, according to the share in GDP creation) during 2009, went up by 1.5% in real terms, given a minimum increase in private consumption of 0.2%. At the same time, the number of employees in this sector increased by 11.8%, compared with the preceding year. However, the assessment of the growth of the trade activity is consistent neither with the real decline in the VAT revenues (by 8.6%), nor with the real decline in the total trade turnover (by 9.1%). Such trends do not correspond either with the assessments of the managers of the trading entities¹⁹, which describe the business situation in 2009 as worse compared with 2008, emphasizing lower demand, higher financial costs and difficult access to credits as the most important restrictive factors.

¹⁹ Survey on the Business Tendencies in Trade of the State Statistical Office, fourth quarter of 2009.

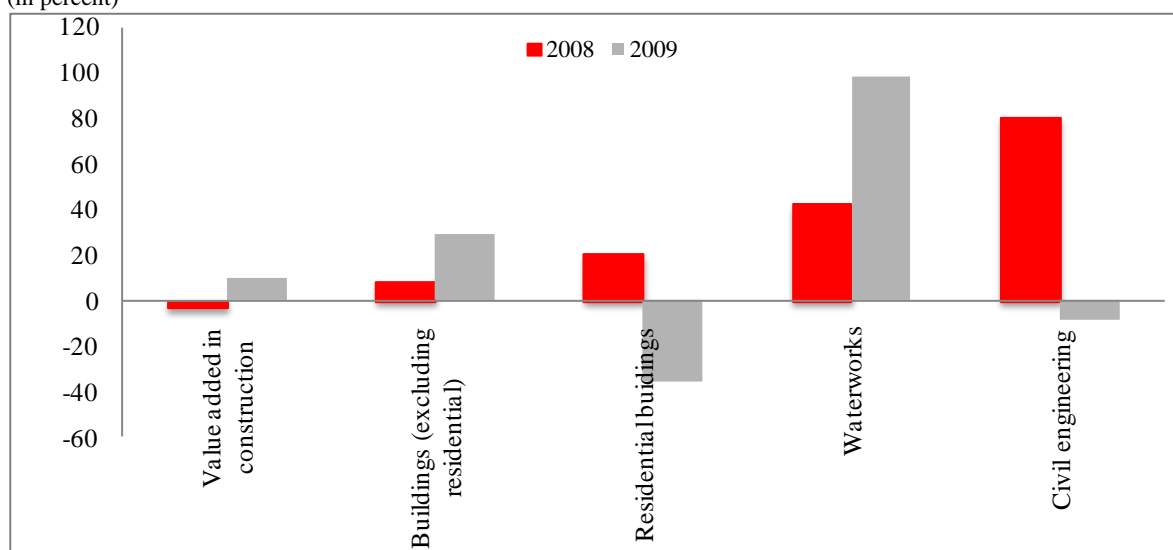
Figure 18
Trade, private consumption and observations of the managers



Source: State Statistical Office.

The accelerated activity in the construction during 2009 largely contributed to the mitigation of the GDP decline. Thus, in this period, construction activity increased by 9.6%, with remarkable acceleration in the second quarter of 2009, which corresponds with the growth in the capital investments in this quarter (by 7.1%). Observed by construction buildings, fast growth was registered in hydro construction and in building of 98.6% and 29.6%, respectively, while the number of completed residential buildings and civil engineering works is lower compared with 2008. However, managers of construction companies assess the business condition in 2009 to be worse than in the previous year²⁰, and they emphasize the insufficient demand as the most serious restrictive factor.

Figure 19
Real annual growth rates in construction and nominal growth by individual type of construction (in percent)



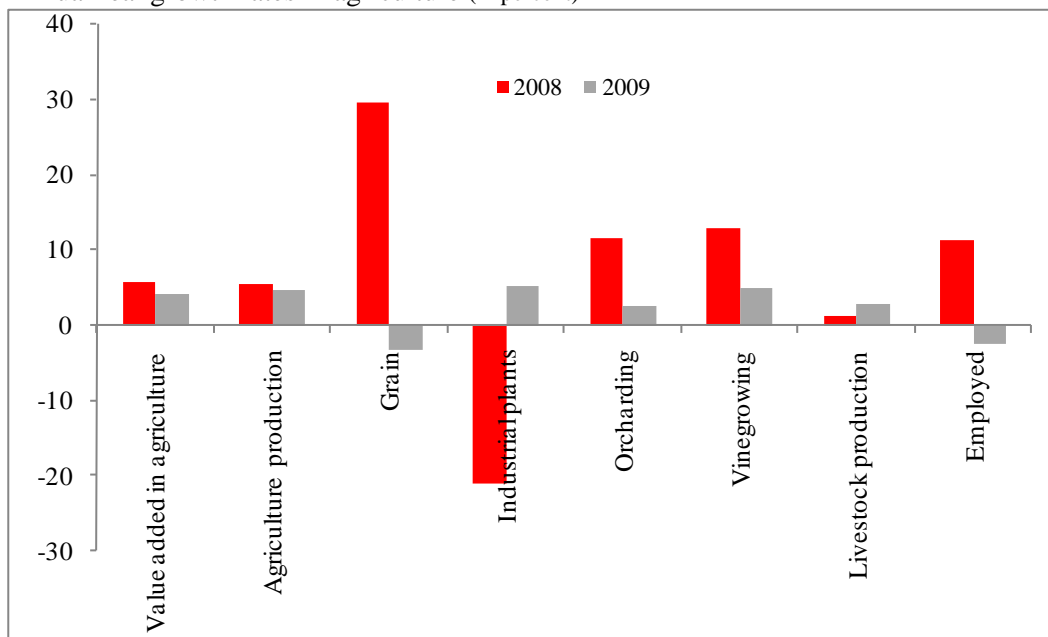
Source: State Statistical Office and Ministry of Finance.

²⁰ From the Survey on the Business Tendencies in Construction of the State Statistical Office, fourth quarter of 2009.

Beside construction, the agricultural sector has also given a positive contribution. Its increased production in 2009 acted toward mitigation of the decline in GDP. The annual growth of the value added in agriculture of 5.7% in 2008, continued in 2009 at a growth rate of 4.0%. The production of industrial plants, viticulture and livestock breeding had the largest contribution to the growth of the agricultural output. Along with the favorable weather conditions, important factor for the growing activity in the agriculture were the continuous government subsidies, which contributed to the stimulation of the production.

Figure 20

Annual real growth rates in agriculture (in percent)

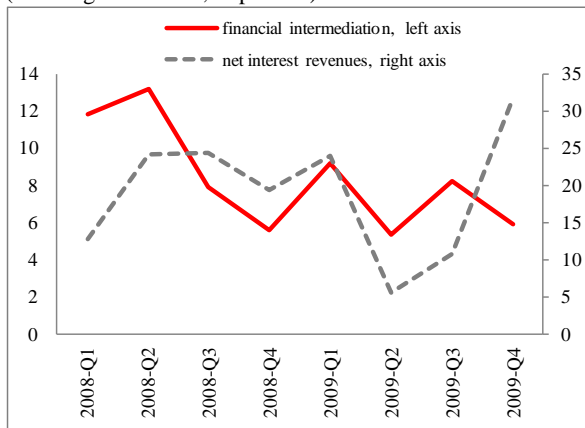


Source: State Statistical Office.

Value added in the sector comprising financial intermediation, real estate and other business activities, as well as other services, registered a real growth rate of 7.1%, which is a moderate deceleration of the growth intensity compared with the growth registered in 2008 (8.7%). The increased value added in this sector had the most important positive contribution to the creation of GDP during 2009. The movement in financial intermediation, covering around one third²¹ of this sector, is partially evident from the movement of the banks' net-interest income, which went up by 17.5% in nominal terms in 2009, and which is also slower compared with the growth registered in the preceding year (20.3%). On the other hand, the activity in the sector **transport, storage and communication** was mainly heading in the same direction as industry, and in 2009, it registered an annual decline of 4.6%. Such a decline is mostly a result of the significantly lower transport of goods, while the activity in the telecommunications sector continued to grow also in 2009.

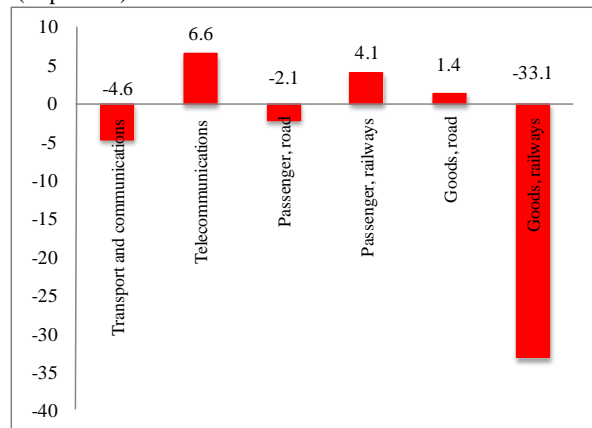
²¹ Data pertain to the share calculated on the basis of the preceding data of SSO about the GDP for 2008.

Figure 21
Value added in financial intermediation and net-interest income
(annual growth rates, in percent)



Source: State Statistical Office and NBRM

Figure 22
Real growth rates of the activities in the sector transport and communication
(in percent)

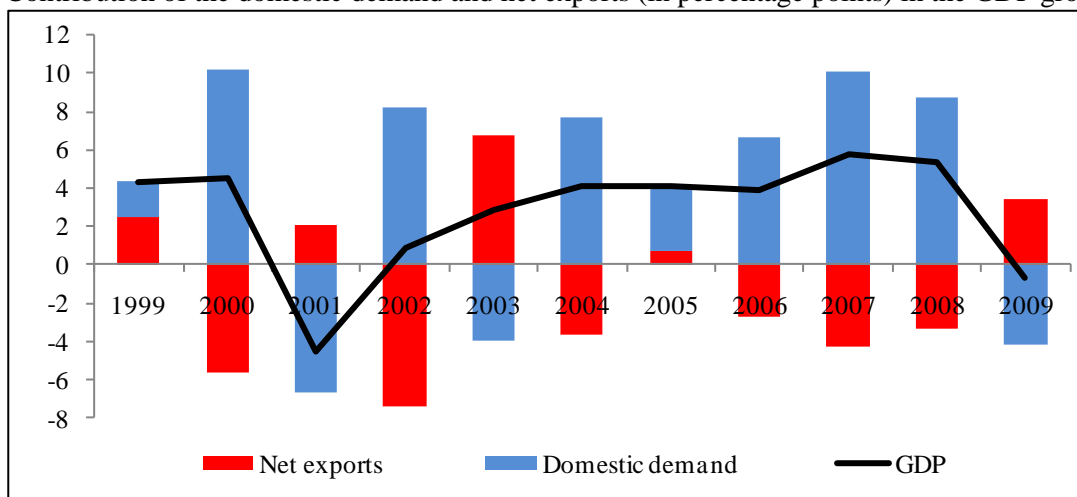


Source: State Statistical Office.

2.1.2. Domestic demand

Deteriorated expectations of domestic entities for decelerated activity and lower possibilities for financing, amid a decline in the global economic activity, caused a decline in the domestic aggregate demand. The structural analysis of the GDP decline of 0.7% in 2009, indicates negative contribution of the domestic demand given the simultaneously positive contribution of the net exports. Such changes indicate a modification in the structure of growth in 2009, compared with the preceding five years, when the domestic demand continuously moved within the zone of positive contribution.

Figure 23
Contribution of the domestic demand and net exports (in percentage points) in the GDP growth



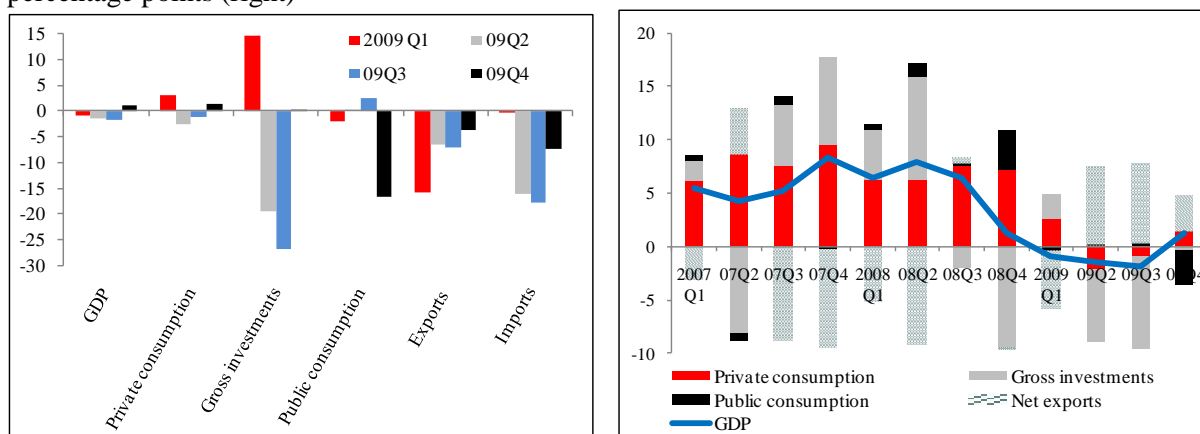
Source: State Statistical Office and calculations of the NBRM.

The analysis of the dynamics indicates the existence of two subperiods. The first one refers to the first quarter of the year, when the main factor of the decline in the economy was the fall in the export demand, led by the depreciated foreign demand, while the domestic demand still had positive contribution. In conditions of high degree of trade integration, the initial effects of the crisis were felt through the exports channel, which in the first quarter of 2009 registered a relatively high rate of decline. The second subperiod pertains to the remaining part of the year, when a significant downward adjustment of the domestic component of the demand was registered (although in the last quarter also the private and investment consumption grew minimally). Households refrained from consumption in

conditions of negative expectations about the future movements of the income and employment, and simultaneously, deteriorated conditions for additional financing had a significant effect. The new investments of the corporate sector also registered a decline, reflecting the continuous fall of the domestic and foreign demand, deteriorated terms of financing, as well as the uncertainty about the pace of recovery of the global economy. In such circumstances, a significant decline in the imports was registered, whereby the contribution of the net-exports to the change in GDP in this period was positive.

Figure 24

GDP according to expenditure components: annual growth rates (left) and contribution to growth, in percentage points (right)



Source: State Statistical Office and calculations of the NBRM.

After the high growth rates in the past two years, **in 2009 private consumption was relatively stable, despite the unfavorable economic environment and high uncertainty (minimal real annual growth of 0.2%).** Having in mind the growth in disposable income in 2009, the unfavorable future expectations of the households and the lower possibility for new borrowing, are factors which mainly drove the deceleration in the growth of private consumption. Thus the data on individual components of the disposable income point to its significant annual growth in 2009. The wage bill registered a high real growth rate of 14.6%, given a real annual growth of the net-wage of 10.8% and growth in employment of 3.4%. Also, during 2009, pensions registered a relatively high real growth rate of 9.6%, and positive annual dynamics was registered also in private transfers (real growth of 20.7%). **Despite the growth in disposable funds, propensity to consume was relatively low, especially in the second quarter of the year, reflecting the unfavorable perceptions of households. The negative expectations were heavily influenced by the uncertainty regarding the duration of the global economic crisis and its effects on the domestic economy, i.e. job security and sources of financing in the future.** However, the negative movements were interrupted in the last quarter of the year, when real annual growth rate of private consumption of 1.5% was registered, as a combined effect of the continuous growth of the disposable income and more stable perceptions of the households (due to the commenced recovery of the global economy and unrealized previous expectations regarding employment and income).

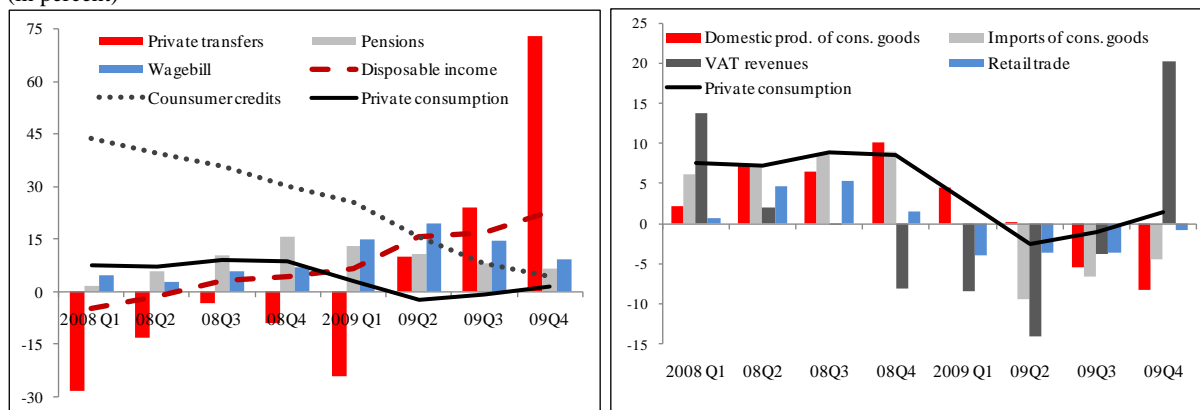
The narrowing of the new credit supply acted toward deceleration of the growth of private consumption. The real average annual growth rate of household credits²² dropped down to 13.5%, as opposed to the average growth of 46% in the 2004-2008 period. Also, in 2009, the share of household credits in GDP at the end of the period (in nominal amounts) equaled 17.4% and it is almost the same as in 2008, when it equaled 17.3%. This indicates an interruption in the trend of growth of financial intermediation of this segment, having in mind that in the 2007-2008 period the average increase of this indicator was 3.4 percentage points p.a. Such movements in 2009 were caused by banks' perceptions about the growing risks and slower growth of the sources of financing, which

²² Total household credits, excluding accrued interest.

resulted in an increase in the interest rates and tightening of the lending terms. At the same time, households' demand for credits declines, amid the uncertainty about the future and possibly higher costs of financing.

Figure 25

Annual real growth rates of the sources of financing of private consumption (left) and similar categories of private consumption (right) (in percent)

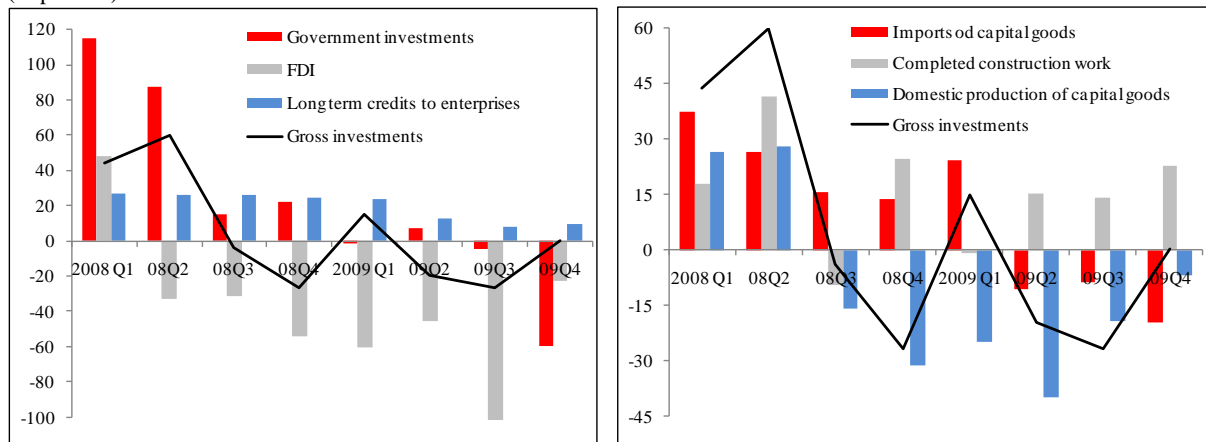


Source: State Statistical Office, Ministry of Finance and NBRM

After the growth in the previous year, investments registered a significant annual decline of 9.2% in real terms, thus giving the largest individual contribution to the GDP decline. The slower investment activity corresponds with the generally unfavorable environment for taking serious decisions on new investments throughout most of the year. Main feature of the investment activity environment was the extremely high uncertainty and the impossibility to assess the duration of the effects from the adverse shock in the second and in the third quarters of the year. Especially emphasized were the risks regarding the perspectives of the already significantly lower demand and the possibilities for maintaining or expanding the markets, access to financing, as well as regarding the future capital cost. Also, the fall in investments is partially explained by the relatively high comparison basis in 2008. From a viewpoint of the dynamics, after the relatively fast growth in the first quarter, investments registered high rates of decline in the second and in the third quarters of the year. The largest part of the fall in the investments could be explained by the significantly lower inflows through foreign direct investments (annual decline in real terms of 59.2%), as a result of the lower global liquidity and growing risk aversion of investors. The more difficult access to financing through bank credits, is also a factor which contributed to the decline in the investment activity. Thus, the growth rate of long-term corporate credits was twice lower than the one registered in 2008 (13.4%, as opposed to 25.9%), creating additional adverse effect on investments. Also, a decline was registered in government capital investments with annual growth in real terms of 14.6%. However, after the first positive signs of lower global uncertainty, in the fourth quarter investments registered a moderate annual increment of 0.3%, which is partially explained also with the low comparison basis from the preceding year.

Figure 26

Annual real growth rates of the sources of financing of investments (left) and similar categories of investments (right) (in percent)

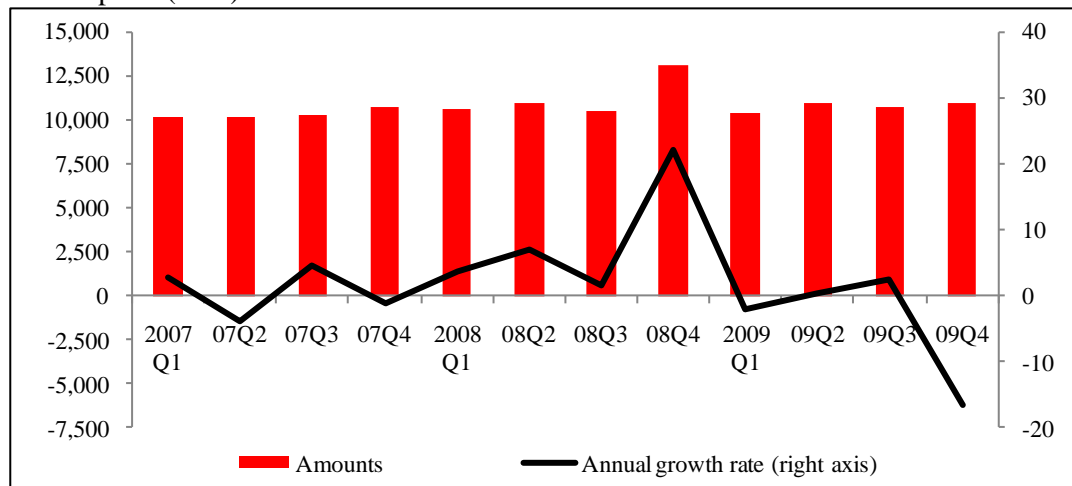


Source: State Statistical Office, Ministry of Finance and NBRM

Unlike the previous two years, government spending in 2009 was more moderate. In conditions of a nominal growth of 6.7%, in 2009, public consumption registered an annual decline in real terms of 4.7%. Lower public consumption in 2009, could be partially explained with the lower realization of revenues, which resulted in a downward revision of the total expenditures twice during the year, in order to remain within the framework of the projected deficit of 2.8% of GDP. The dynamics of public consumption was uneven during the year. Thus, after the neutral effect for the growth in the first three quarters (real growth of 0.2%), in the last quarter of the year the public consumption had a significant negative contribution, with an annual decline in real terms of 16.6% (given the high comparison basis from the previous year).

Figure 27

Real amount of public consumption (in millions of denars) and annual growth rates of public consumption (in %)



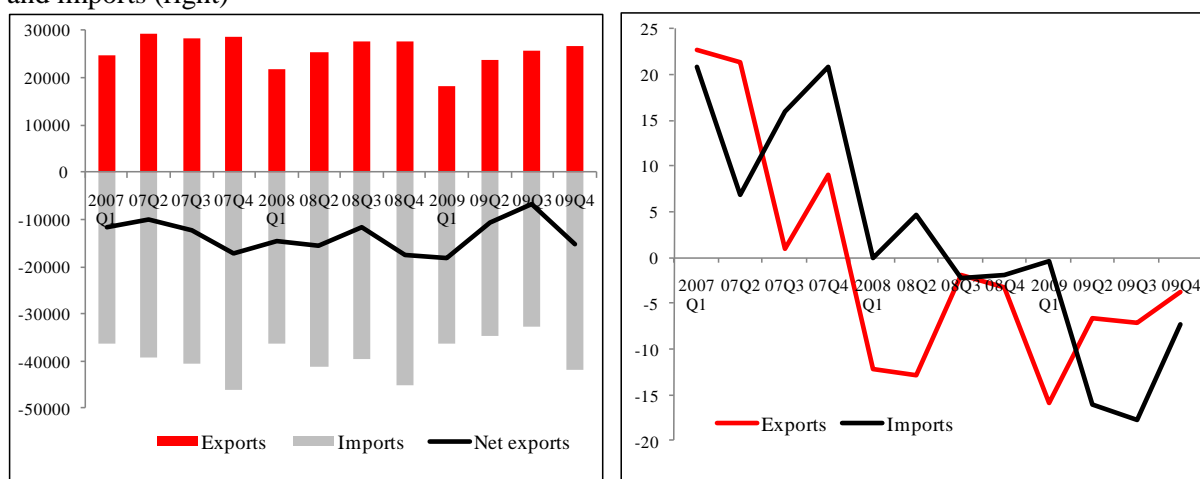
Source: State Statistical Office and calculations of the NBRM.

Despite the decline in the exports, the more significant downward correction of the import demand enabled the net exports in 2009 to have positive contribution to the total change in GDP. The largest decline in the exports was registered in the first quarter of the year, as a result of the lower foreign demand, as well as the decline in the prices of our main export products. The continuity of such trends and the uncertainty regarding the intensity and the duration of recovery of the global economy, were the main factors for continuation of the decline in the exports also in the other part of the year, although with relatively smaller intensity, especially in the last quarter. As a

result of such movements, the real decline in the exports in 2009 equaled 8.2%. On the other hand, the downward adjustment of the imports occurred with certain time lag, primarily due to the effect of a relatively more resilient private and investment demand at the beginning of the year. However, the downward adjustment of all components of the domestic demand, combined with the decline in the imports due to the reduced export demand, caused a significant decline also in the imports starting from the second quarter, so that for the entire year the decline in the imports in real terms was 10.7%. Similarly as in the exports, the rate of decline in the imports in the last quarter was relatively lower, as a reflection of the positive movements in both the private and investment demand and lower decline in the exports.

Figure 28

Real amounts of exports and imports, in millions of denars (left) and annual growth rates of exports and imports (right)



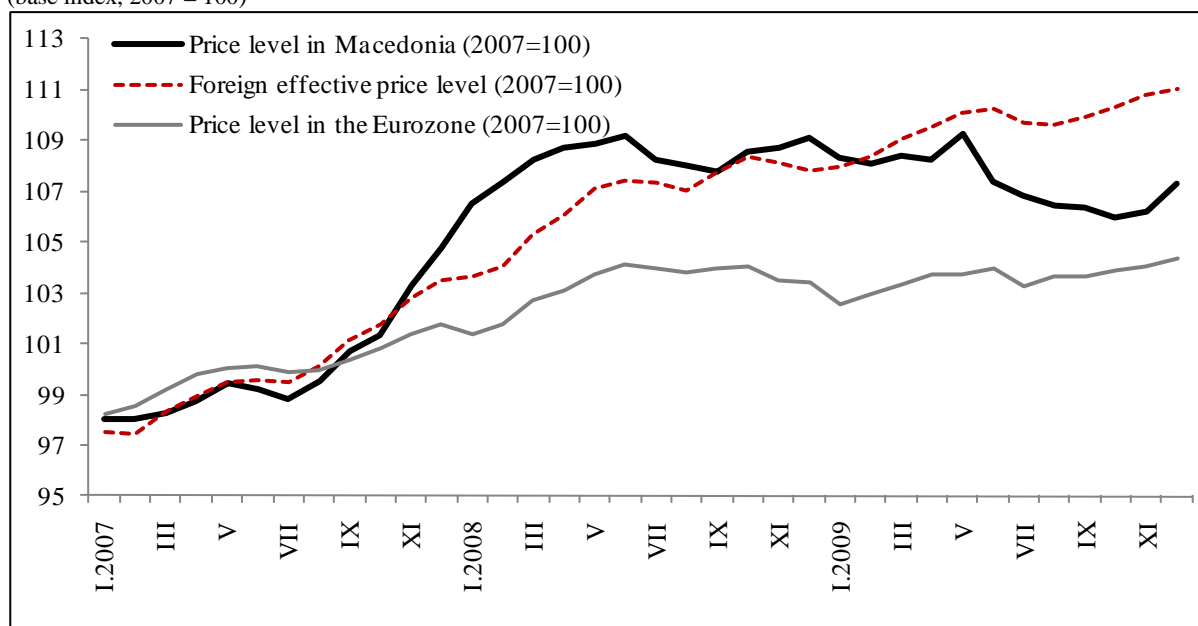
Source: State Statistical Office and calculations of the NBRM.

2.2. Inflation

The global recession interrupted the "price boom"²³ phenomenon relating primarily to the food and energy prices, stirring up significant downward correction of the global inflation in 2009. The fall in import prices triggered the disinflation process in the Macedonian economy as well, typical for both the overall and the core inflation. Thus, after the high average inflation of 8.3% registered in the preceding year, in 2009, the consumer prices went down by 0.8%. The average growth in core inflation slowed down significantly, reflecting the secondary effects of the fall in the food and energy component. The negative output gap made additional contribution to the downward trajectory of domestic prices. However, the downward correction of prices is not complete. The general price level is still higher (by 7.8%) compared to the period when the inflation started accelerating (August 2007), indicating certain downward price rigidity. The price cut tendencies were particularly noticeable in the second half of the year, when the annual inflation was constantly dwelling in the negative zone.

²³ Typical for a part of 2007 and 2008.

Figure 29
Price level in Macedonia, abroad* and in the Euro area
(base index, 2007 = 100)



*The price level abroad is a weighted sum of the price level in the countries considered the most important trading partners of the Republic of Macedonia.

Source: State Statistical Office and Eurostat.

The decomposition of changes in the inflation in 2009 shows that the major contributors to the decrease in the general price level include categories that reported the fastest growth in the preceding year, i.e. the food and transport equipment and services (i.e. oil derivatives). On the other hand, the most dramatic growth was registered in the housing, due to the transmission effect of the rise in electricity prices in November 2008²⁴.

Table 5
CPI structure

	annual changes in %		contributions in p. p.		contributions in %	
	XII.2009 XII.2008	2009 2008	XII.2009 XII.2008	2009 2008	XII.2009 XII.2008	2009 2008
Total	-1.6	-0.8	-1.6	-0.8	100.0	100.0
Food	-3.5	-1.6	-1.4	-0.7	85.49	80.53
Tobacco and beverages	3.3	3.9	0.2	0.2	-10.21	-24.58
Clothing and footwear	-2.5	0.0	-0.2	0.0	10.99	0.11
Housing	-0.5	4.5	-0.1	0.7	4.47	-82.19
Hygiene and health	1.2	2.1	0.1	0.2	-5.67	-19.77
Culture and entertainment	-6.5	-3.8	-0.3	-0.2	21.00	24.93
Transport and communication services	1.1	-8.0	0.2	-1.1	-9.35	133.02
Restaurants and hotels	-0.6	2.2	0.0	0.1	2.06	-14.26
Other services n.e.c.	-1.0	-5.8	0.0	0.0	0.18	2.13

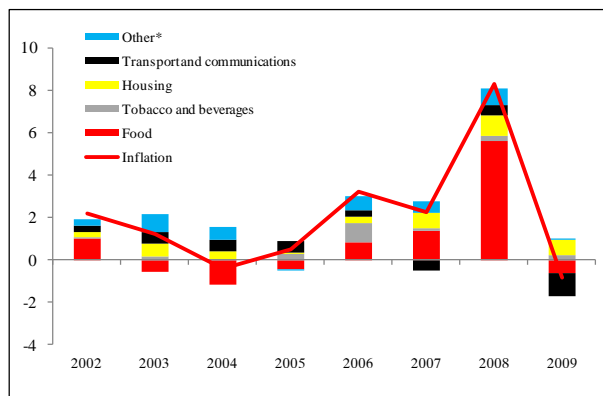
Source: State Statistical Office.

The greatest contributor to the negative change in the general price level in 2009 was the category of transport equipment and services (1.1 percentage points), mostly due to the cut in the prices of oil derivatives (contribution of 0.9 percentage points), and the decrease in the costs for car maintenance and the prices of the transport equipment. The change in the price of oil derivatives reflects the changes in the oil price on the international stock markets. Thus, given the fall in the global price of the "brent" oil of 36.7% in 2009, the domestic price of oil derivatives went down by

²⁴ Electricity price went up by 13.61% in November 2008.

21.2%. Reversal was registered in the last month of the year, when due to the base effect, the prices of oil derivatives registered an annual growth of 10.9%.

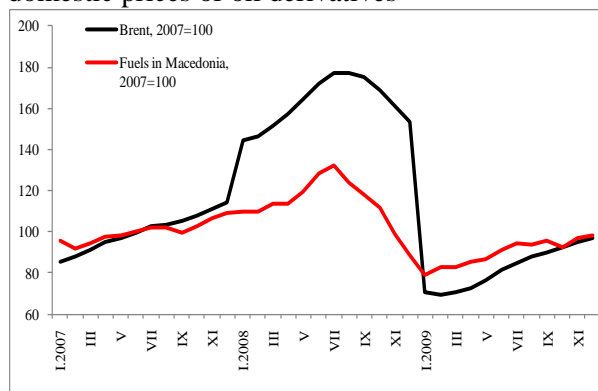
Figure 30
Inflation and major categories



*The remaining includes the categories of wearing apparel and footwear, hygiene and health, education, culture and recreation, restaurants and hotels and other services.

Source: State Statistical Office and NBRM calculations.

Figure 31
Price of "brent" oil on the global stock markets and domestic prices of oil derivatives



Source: State Statistical Office and IMF.

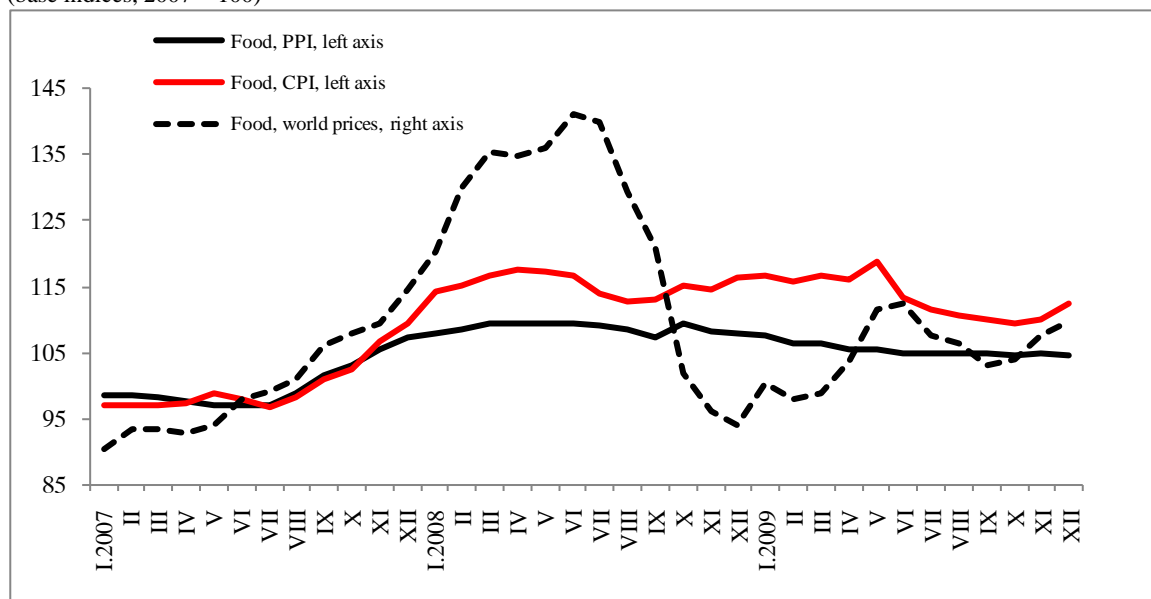
After the significant growth of 15.3% in the preceding year, the food prices in 2009 went down by 1.6%, which is the second major contributor to the fall in the general price level (0.7 percentage points). The fall in domestic food prices reflects the global fall of food prices and favorable conditions in the domestic agricultural production²⁵. However, compared to the 14.7%²⁶ fall in global food prices, the cut in the domestic prices of 1.6% is marginal. Additionally, the decrease in prices of domestic producers of food products was as twice as deeper (3.1%), indicating, most probably, the increase in sales margin in the trade. Compared to the level prior to the inflation period (August 2007), the retail food prices in December 2009 increased by 14.2%, compared to the production food prices and global food prices, which went up by 5.9% and 8.4%, respectively. Such perceptions not only confirm the ascertainment for higher sale margin, but also show that there is a room for potential further decrease in the food price food. Analyzing by group of food products, fastest fall was registered in the prices of fats (23.7%), milk and diaries (7.3%) and fruits (10.8%); the meat prices went up (7.2%), whereas the prices of grain products, as a group with the highest share, stagnated.

²⁵ The SSO initial estimations show an increase in the agricultural production of 4.6% in 2009.

²⁶ IMF food price index.

Figure 32

Retail food price (CPI), producer food price (PPI) and global food price
(base indices, 2007 = 100)



Source: State Statistical Office and IMF.

Unlike the prices of food and oil derivatives, the electricity price in 2009 went up by 10.7%, in line with the decision on increasing the price of electricity in November 2008 by 13.61%, whereas the prices of heating and services went down by 0.9%. In spite of the increase in these prices, however, the sharp decrease in the oil derivative price contributed to the 2% decrease in the energy price in 2009, compared to 2008.

Table 6

Price categories
(annual growth in %)

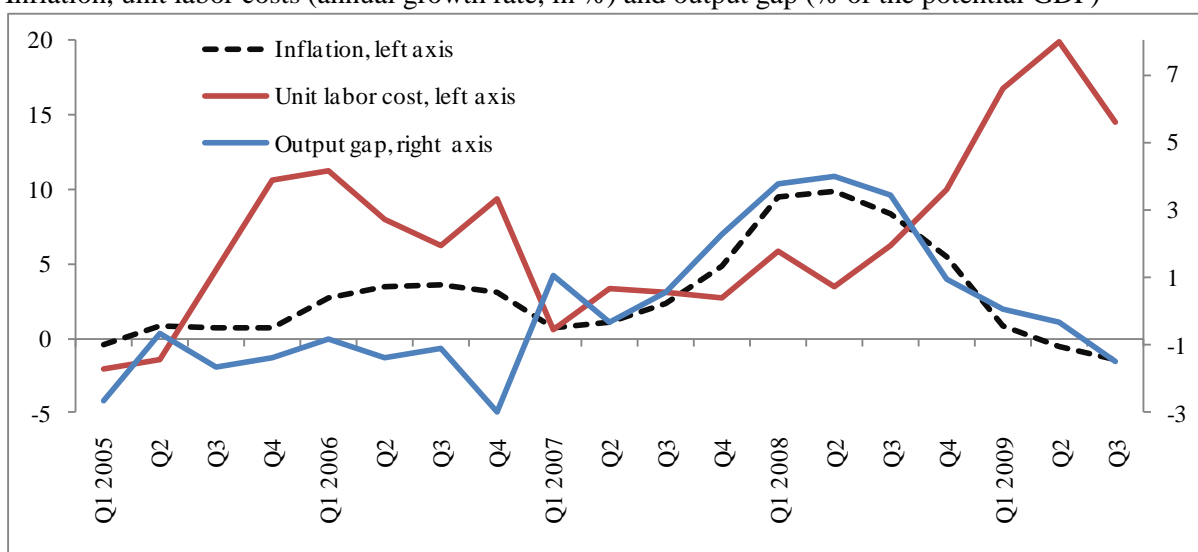
	Q1 2008	Q2 2008	Q3 2008	Q4 2008	2008	Q1 2009	Q2 2009	Q3 2009	Q4 2009	2009
Inflation (CPI)	9.5	9.9	8.4	5.4	8.3	0.8	-0.6	-1.4	-2.1	-0.8
Food	19.0	19.5	14.7	8.5	15.3	0.9	-1.0	-2.2	-4.2	-1.6
Fresh food	26.4	25.2	16.0	11.0	19.7	1.0	1.9	-0.2	-5.3	-0.6
Processed food	13.3	15.2	13.2	6.3	12.0	1.4	-3.0	-3.4	-3.6	-2.2
Energy	7.4	9.2	12.5	8.3	9.3	-1.6	-1.9	-3.4	-1.1	-2.0
Fuels and lubricants	18.6	22.6	23.6	-6.2	14.6	-27.1	-27.7	-24.6	-4.0	-21.2
Electrical power	1.6	0.0	0.0	8.7	2.6	13.1	13.1	13.1	4.0	10.7
Heating and services	4.6	10.9	23.2	25.3	16.0	4.2	3.6	-4.9	-6.2	-0.9
Food and energy (volatile prices)	16.1	16.9	14.1	8.5	13.9	0.3	-1.2	-2.5	-3.4	-1.7
Goods	11.0	11.4	9.0	5.4	9.2	0.8	-0.7	-1.3	-2.0	-0.8
Services	3.9	4.5	6.1	5.8	5.1	1.2	0.0	-1.8	-2.4	-0.7
Core inflation (inflation excl. food and energy)	2.9	2.8	2.5	2.2	2.6	1.5	0.3	0.1	-0.6	0.3
Producer prices	10.5	13.6	15.1	2.2	10.3	-6.2	-8.8	-10.1	-0.5	-6.5

Source: State Statistical Office and NBRM calculations.

In 2009, the fall in the economy output, amidst growth in wages, resulted in higher unit labor costs. In 2009, the unit labor costs registered a significant growth of 14.9%, with this trend being typical for almost all economy sectors. The increase in unit labor costs is probably one of the factors that explain the relative resilience of domestic prices, i.e. they are still relatively high (compared to the level prior to the inflation period). It is obvious, however, that the effect of this factor on the inflation was largely offset by the fall in import prices and the negative output gap.

Figure 33

Inflation, unit labor costs (annual growth rate, in %) and output gap (% of the potential GDP)



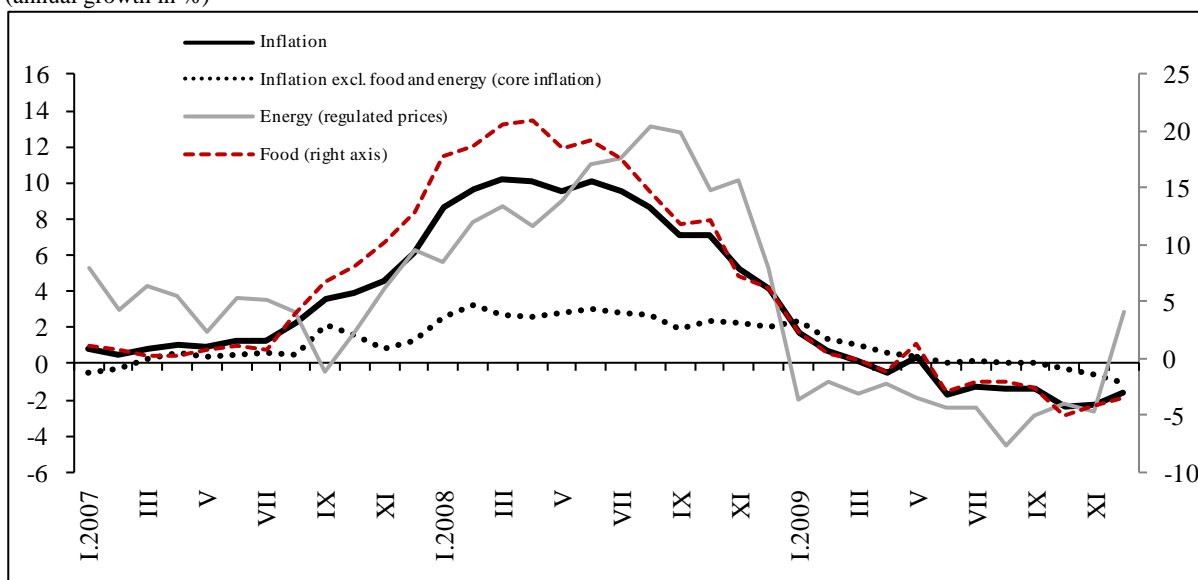
Source: State Statistical Office and NBRM calculations.

Core inflation in 2009 registered a moderate average growth of 0.3%, and after the faster growth of 2.6% in the preceding year, it returned to the zone of moderate positive changes. During the year, the growth of core inflation was slowing down steadily, and in the last quarter of the year it was negative. Such dynamics of core inflation is a mixed effect of the secondary effects of the food and energy prices, and the substantially eased pressures on the demand side. Nevertheless, the fast normalization of the long-term inflation component clearly indicates stable price environment and predominantly adaptive inflationary expectations.

Figure 34

Inflation

(annual growth in %)



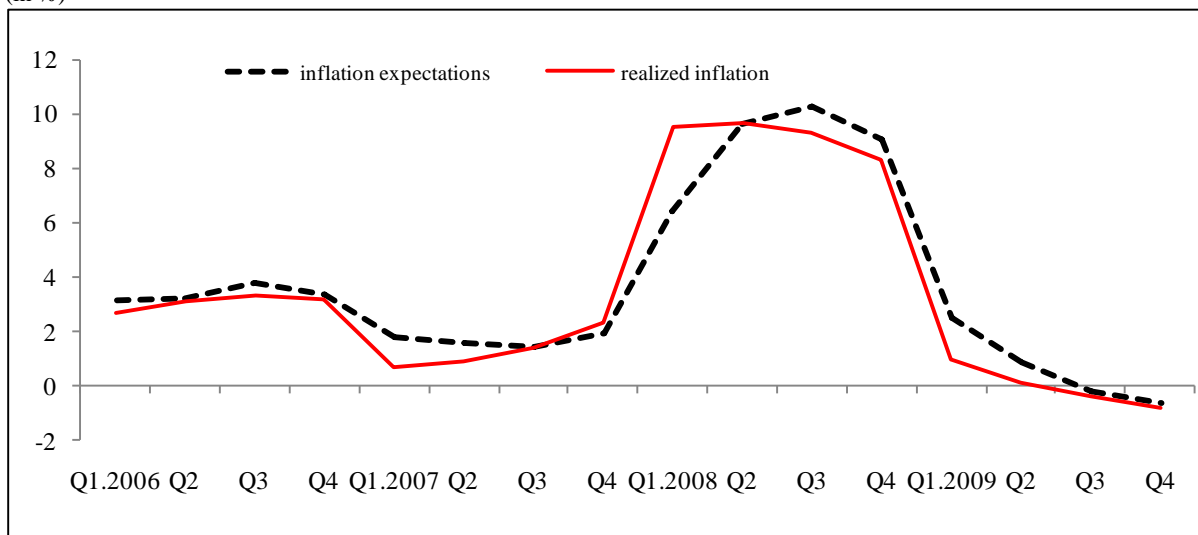
Source: State Statistical Office and NBRM.

The Survey of inflationary expectations of economic agents in 2009, same as before, showed high synchronization of the expectations and inflationary performances. Hence, the expectations of the domestic economic agents for the future inflation are predominantly adaptive, i.e. based primarily on the current inflation performances. Since the beginning of the year, the economic agents expected the inflation to increase, mostly due to the announcements for potential rise in

electricity price, and the inertia in the expectations, that is, the 2008 inflation. In the second half of the year, most economic agents expected the inflation rate to decrease additionally, primarily due to the lower economic activity, the uncertainty regarding the recovery from the crisis, and the expectations for lower public consumption and stricter lending terms.

Figure 35

Average annual inflation as of the current quarter and expectations for the average annual inflation to the yearend
(in %)

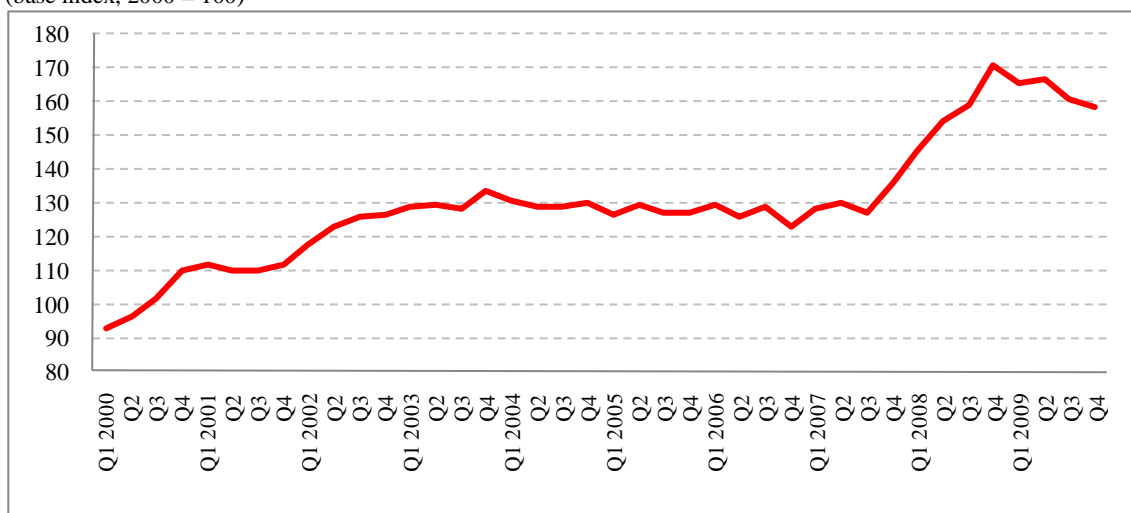


Source: State Statistical Office and NBRM Inflationary Expectations Survey.

After the growth in the last two years, the real estate prices in 2009 decreased. After peaking in the fourth quarter of 2008, the apartment prices in 2009 registered a downtrend, and at the end of 2009 they were by 7.5% lower compared to the end of 2008²⁷. Notwithstanding the permanent fall over the year, the price correction was minor, illustrated by the fact that the average price in 2009 exceeds the average price in 2008 by 3.5%.

Figure 36

Apartment price index
(base index, 2000 = 100)



Source: NBRM.

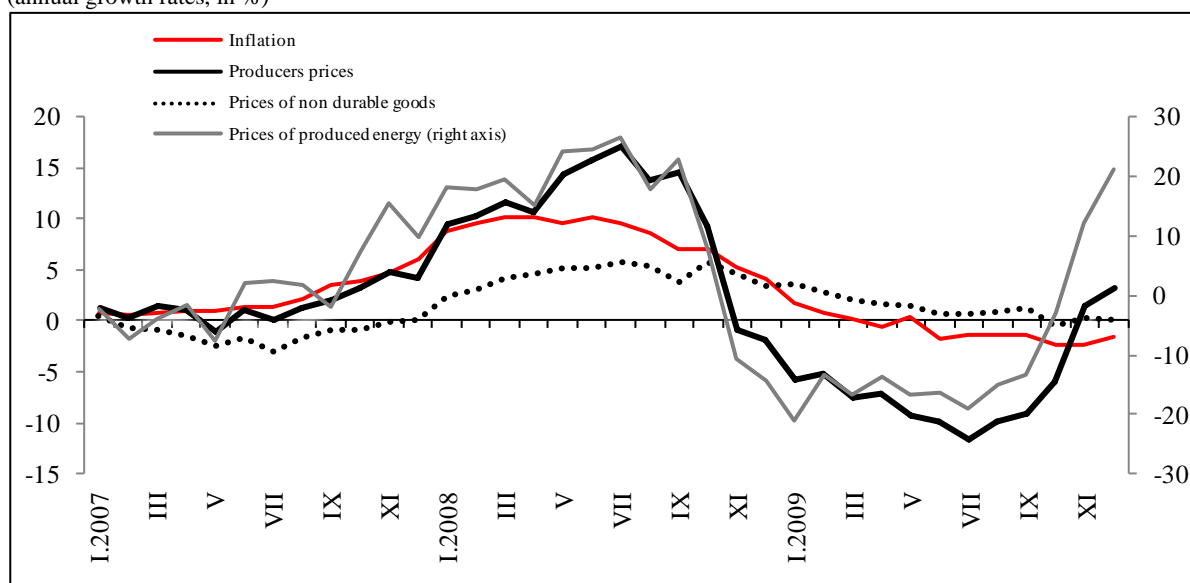
²⁷ According to the hedonic house price index compiled by NBRM. Apartment prices are not included in the consumer price index. Consumer prices include rents, which went up by 7% according to the SSO data for 2009.

As the prices of imported raw materials fell, in 2009 the producer prices also went down by 6.5%. Observed by component, the fastest fall was registered in the prices of oil producers (28.2%) and basic metals (24.7%), thus contributing to the fall in the producer prices with -6.1 percentage points and -2.5 percentage points, respectively. On the other hand, 2009 witnessed the steepest increase in the electricity price of 17.1%, which acted towards increasing the production prices (contribution of 2.4 percentage points). In the last two months of the year, the prices of producers went up annually, largely due to the base effect (the prices of producers started falling in November 2008). Observing only the producer price index components, which correspond with the consumer price index, their fall in 2009 equaled 4.6%²⁸.

Figure 37

Inflation and PPI

(annual growth rates, in %)



Source: State Statistical Office and NBRM.

After the rapid price growth in the preceding year, the Southeast European countries in 2009 reported their substantial slowdown (average inflation of 2.3%). In this region, besides Macedonia, Kosovo and Bosnia and Herzegovina also reported negative inflation rates (2.4% and 0.4%, respectively). Other countries of the region registered low inflation rates, except for Serbia and Romania, which still face relatively high inflation (8.4% and 5.6%, respectively, mainly due to the depreciation of the national currencies). The Euro area, although registering a slight price growth over the year, in the second and the third quarter of the year reported a decrease in the price level.

²⁸ These include energy, and durables and nondurables for joint consumption. In 2009, the energy decreased by 10.6%, the durables for joint consumption went down by 0.5%, whereas the nondurables went up by 1.2%.

Table 7
Inflation in the Euro area and the Southeast European countries
(in %)

	Inflation (annual average rate of change)							
	2002	2003	2004	2005	2006	2007	2008	2009
<i>Eurozone</i>	2.3	2.1	2.1	2.2	2.2	2.1	3.3	0.3
<i>Southeast Europe</i>	8.8	5.2	3.8	4.6	4.9	4.2	8.4	2.3
Albania	1.7	3.3	2.2	2.0	2.5	3.1	3.4	2.2
Bosnia and Herzegovina	1.0	0.6	0.4	3.8	6.1	1.5	7.5	-0.4
Bulgaria	5.8	2.3	6.1	6.0	7.4	7.6	12	2.5
Montenegro	16.4	6.8	2.2	2.4	2.9	4.2	8.5	3.4
Croatia	1.7	1.8	2.1	3.3	3.2	2.9	6.1	2.4
Kosovo	-	-	-1.1	-1.4	0.7	4.3	9.4	-2.4
Macedonia	1.8	1.2	-0.4	0.5	3.2	2.3	8.3	-0.8
Romania	22.5	15.3	11.9	9.0	6.6	4.9	7.9	5.6
Serbia	19.5	10.0	11.0	16.1	11.8	6.8	12.9	8.4

Source: Eurostat and national statistical offices.

2.3 Labor market and wages

The favorable developments registered on the labor market continued in 2009, in spite of the deterioration in the real economy. Thus, same as in the preceding year, 2009 witnessed further growth in the employment and fall in the unemployment. Given the growth in the overall labor (increase of 9,351 persons relative to 2008) and lower number of unemployed persons (by 11,536 compared to 2008), the number of employed persons went up by 20,887 or 3.4%, on average. The employment growth, given the increase in most of the economic sectors, mostly reflects the larger number of employees in the trade and in the sectors of public administration and defense, education and health.

Figure 38
Labor market
(number of persons)

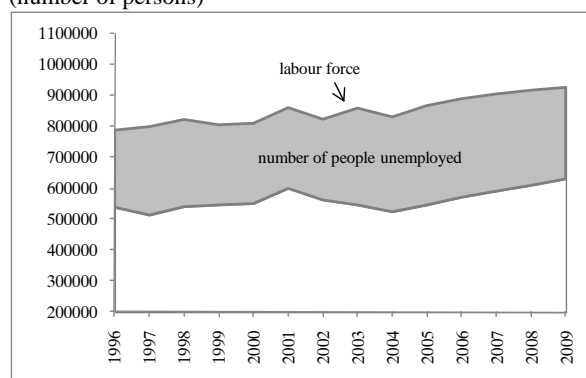
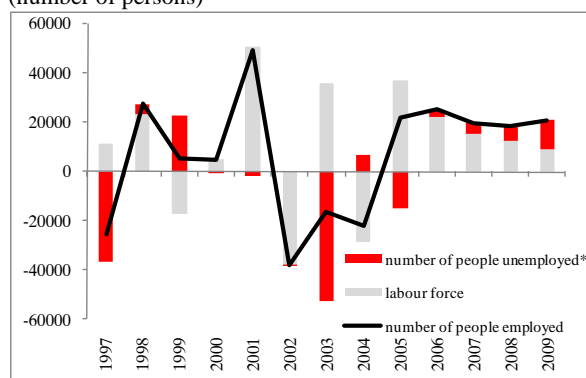


Figure 39
Employment growth
(number of persons)



*Positive growth of unemployed persons means lower unemployment, acting towards increasing the employment.

Source: SSO, Labor Survey.

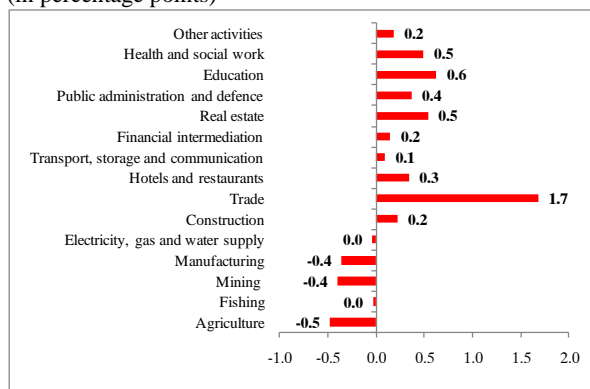
Such labor market conditions could hardly be explained, taking into account the generally lower domestic production and deterioration in the economy. One of the possible explanations is the certain time lag in the labor market adjustment to the change in the stage of economic cycle. This is partially illustrated with the fact that the first signal for the possible labor market adjustment in Macedonia is the slowdown of the quarterly growth of employment in the third quarter of the year, and its decrease in the fourth quarter²⁹ (6438 persons, or 1% lower employment in the fourth quarter compared to the preceding year). These developments, however, did not make the

²⁹ The analysis of quarterly employment growth uses seasonally-adjusted data.

annual unemployment rate higher. On the other hand, most of the countries in the region already reported higher annual unemployment rate (see Table 8). Other potential explanation would be the transfer of a part of the employees from the informal to the formal sector. Although data, due to the nature of the research (survey research), should also include unemployment in the informal sector, it is possible that some of the employees in the informal sector, who previously claimed to be unemployed, start claiming to be employed after being transferred to the formal sector. Additional factor could be the uncertainty regarding the strength and duration of the effects of global crisis, which resulted in initially temporary interruptions of the engagements of employees. However, considering the features of the Macedonian economy (high level of informal economy and high share of long-term, i.e. structural unemployment in the total unemployment) it is exceptionally difficult to identify real reasons behind the positive developments on the labor market amidst contraction of the economic activity.

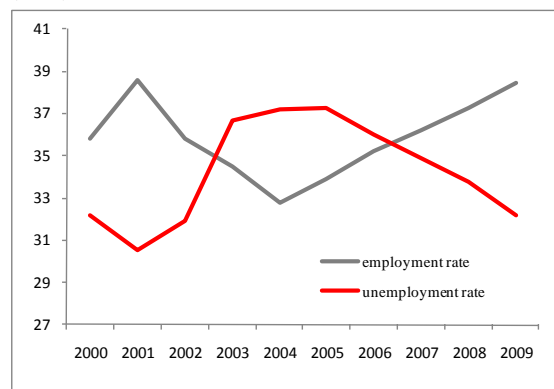
The increase in overall employment is accompanied with the increase in employment in almost all economic activities. Activities that reported lower number of employees include agriculture (by 2.4%), mining (by 36.3%) and manufacturing industry (by 1.7%). Observing by activity, the trade is considered the major contributor to the growth, reporting an increase in employment of 10,208 persons (11.8%). The significant increase in employment in the trade reflects the growth of the added value in this activity, and the moderate increase in the personal consumption in 2009. In addition, remarkable employment growth was also registered in the public administration and defense, health and education, which cumulatively account for 43% of the growth of overall employment.

Figure 40
Employee contribution to the overall employment growth, by activity
(in percentage points)



Source: SSO, Labor Survey.

Figure 41
Employment rate and unemployment rate
(in %)



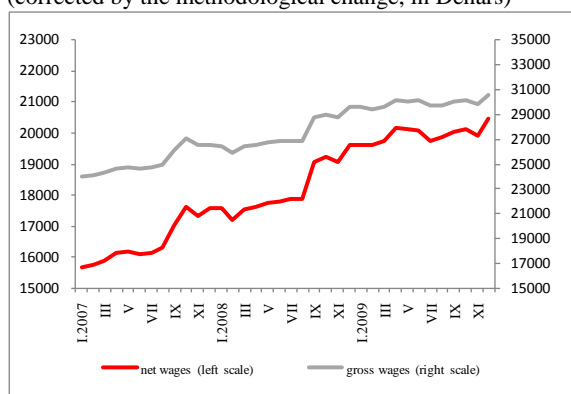
The favorable developments registered on the labor market in 2009, continued the uptrend of the employment rate and the downtrend of the unemployment rate which started in 2004. Thus, in 2009, the employment rate equaled 38.4%, compared to 37.3% in the preceding year, whereas the unemployment rate reduced from 33.8% in 2008 to 32.2%.

Employment growth in 2009 was accompanied with higher labor price (measured through the average paid wages) in all economic sectors. Yet, the significant increase of the average wage in 2009 compared to 2008, is mostly due to the transmission effect of the increase in the public sector wages in September 2008. The new wage growth, measured through the monthly changes in 2009, is relatively modest, illustrating certain adjustment of this labor market segment to the deteriorated economy.

In 2009, the nominal average net and gross wages³⁰ registered an annual growth of 9.8% and 9.2%, respectively. The annual growth largely reflects the increase in the wages of public sector in September 2008, with a wage growth being also registered in the private sector. Thus, in 2009, wages reported only a modest growth compared to the previous two years, showing some adjustment to the contracted economic activity. The monthly dynamics of wages in 2009 was not constant. In fact, nominal net wages went up in the first four months of the year, followed by a three-month downward trend, after which they resumed increasing from August to the end of the year, except for November 2009. The average monthly growth rate of the nominal net wages in 2009 equaled 0.4%, relative to 1% in 2007 and 2008. Furthermore, the new increase in the net and the gross wages in 2009, measured through the wage growth in December 2009, compared to January 2009, equaled 4.4% and 3.5%, respectively.

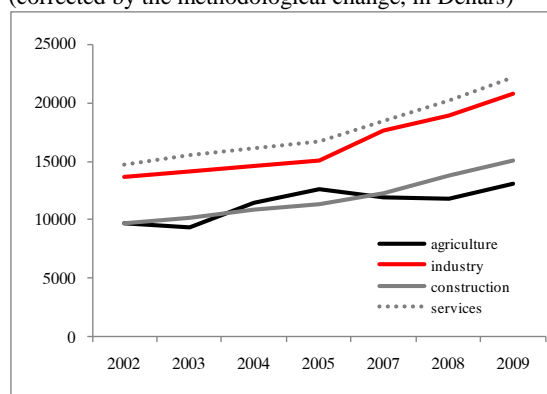
The mild price cut during the year resulted in higher real annual growth of the average paid wages, compared to the nominal ones (growth of 10.6% and 10.1% in the corrected net and gross wage, respectively), reflecting the increase in the real purchasing power of the economic agents in 2009.

Figure 42
Average nominal net and gross wage
(corrected by the methodological change, in Denars)



Source: SSO and NBRM calculations.

Figure 43
Nominal net wages, by sector
(corrected by the methodological change, in Denars)



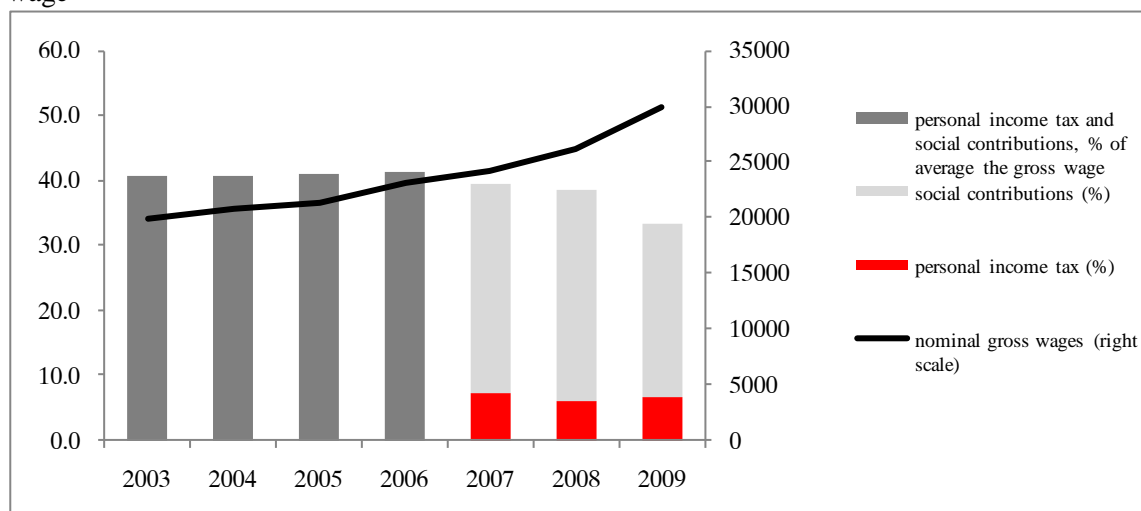
Slower nominal growth in gross wages in 2009 compared to the growth of net wages was due to the changes in the social contributions system³¹. In 2009, the contribution rates were reduced, bringing about a decrease in the total encumbrance of the gross wage with contributions, from 32.5% in 2008 to 26.6% in 2009. These measures also mean lower costs for engaging a manpower, which should lead to a higher employment rate by new recruitments, but also by transferring a part of the employment from the informal to the formal sector.

³⁰ According to the SSO data, the average nominal paid net and gross wages in 2009 went up by 24% and by 14.1%, respectively. Due to the change in the method of calculating the wages in 2009 (concept of gross wage, i.e. inclusion of the board and transport allowances in the income tax base), in order to reach higher level of annual comparability of data, a correction was made by assuming that the wage in December 2008 was at the level of the wage in January 2009, and for the months prior to December 2008, this amount was derived by applying the official historical monthly growth rates of wages, as published by SSO.

³¹ The changes in the social contribution system pertain to reduction of the social contributions and health insurance contributions in the period from 2009 to 2011. In 2009, the pension insurance contribution was reduced from 21.2% in 2008 to 19% in 2009; the health insurance contribution reduced from 9.2% to 7.5%, and the employment contribution reduced from 1.6% to 1.4%. The additional contribution for professional health insurance of 0.5% will become compulsory, i.e. since 2009 it has been included in the group of compulsory social contributions. Starting from 2009, the water supply contribution of 0.2% is no longer calculated.

Figure 44

Nominal gross wages and percentage share of the income tax and social contributions in the gross wage*



*For the period prior to 2007, due to the progressive income tax rates, the share of income tax and contribution duties in the total taxes could not be separated.

Source: SSO and NBRM calculations.

Wages in Macedonia, in spite of the accelerated growth in the last four years, are still amongst the lowest in the region. The highest net wages in 2009 were paid in Slovenia and Croatia. Macedonia reported almost identical level of net wages with Serbia and Romania and higher wages compared to those paid in Bulgaria. On the other hand, Macedonia is among the countries, together with Bulgaria and Montenegro, which reported faster annual growth of nominal net and gross wages³². Also, although Macedonia is the only state which reduced the contribution duties compared to the preceding year, it still belongs to the group of countries with highest share of these taxes in the gross wage.

³² Wages in Serbia and Romania in 2009 went down, primarily due to the depreciation of their national currencies. Additional contributor to the fall in wages in Serbia was the methodological change made in early 2008.

Table 8
Wages by country

		2008	2009**	nominal increase of wages, in %	real increase in wages, in %	personal income tax and contributions, % of the average gross wage	
						2008	2009
Macedonia	average gross wage (in euros)	429	487	13.6	14.6	38.6	33.3
	average net wage (in euros)	263	325	23.6	24.6		
	unemployment rate (in %)	33.8	32.2				
Slovenia	average gross wage (in euros)	1391	1439	3.4	3.4	35.3	35.4
	average net wage (in euros)	900	930	3.4	3.4		
	unemployment rate (in %)	4.4	5.7				
Croatia*	average gross wage (in euros)	1044	1050	0.5	-1.9	31.4	31.1
	average net wage (in euros)	717	723	0.9	-1.5		
	unemployment rate (in %)	8.4	9.0				
Bulgaria	average wage (in euros)	264	299	13.3	10.5		-
	unemployment rate (in %)	5.7	6.5				
Bosnia and Herzegovina	average gross wage (in euros)	565	615	9.0	9.4	32.0	34.2
	average net wage (in euros)	384	405	5.5	5.9		
	unemployment rate (in %)	23.4	24.1				
Serbia	average gross wage (in euros)	516	475	-7.9	-15.1	28.3	28.1
	average net wage (in euros)	370	341	-7.7	-14.8		
	unemployment rate (in %)	14.7	17.4				
Montenegro*	average gross wage (in euros)	609	642	5.5	2.1	31.8	28.1
	average net wage (in euros)	415	462	11.2	7.6		
	unemployment rate (in %)	16.8	18.9				
Romania	average gross wage (in euros)	460	446	-3.1	-8.2	26.5	27.5
	average net wage (in euros)	338	323	-4.4	-9.5		
	unemployment rate (in %)	5.8	6.7				

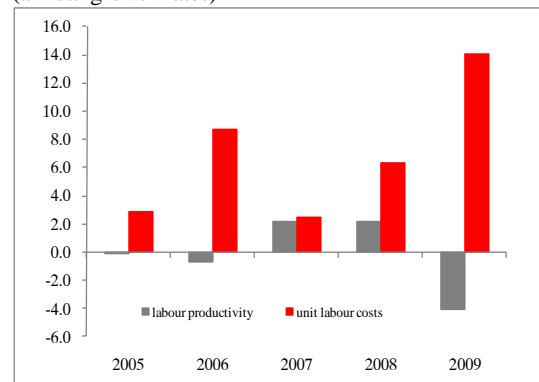
*Wage calculated as January - November 2009 average.

**The unemployment rate for 2009 for each country is an average of the rates in the first three quarters of 2009, except for Macedonia, where the unemployment rate presents the average of all four quarters.

Source: State statistical offices and central banks of the respective countries.

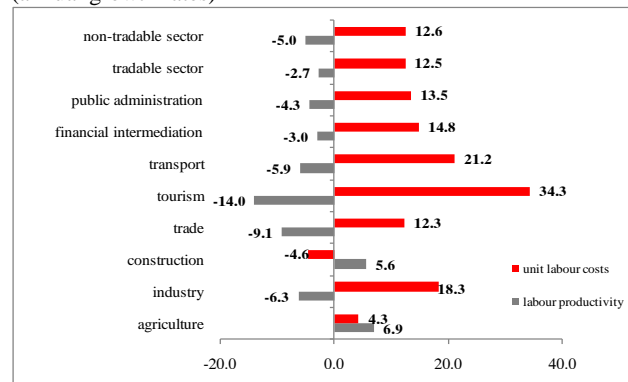
Contracted economic activity and higher employment led to a negative annual growth of labor productivity of 4%. Lower productivity was registered in all economic sectors except for the agriculture, due to the cut in the number of employees, and the construction, due to the substantial increase in the added value. Such development is not typical only for Macedonia, that is, the productivity contracted in most of the developed countries³³ where the labor market showed certain adaptability, but with significantly lower pace compared to the contraction in the economic activity.

Figure 45
Labor productivity and unit labor costs
(annual growth rates)



Source: SSO and NBRM calculations.

Figure 46
Labor productivity and unit labor costs, by sector
(annual growth rates)



³³ The only countries which reported higher productivity were Spain and the USA (Consensus Forecast, March, 2010).

The upward trend of the unit labor costs continued in 2009, in a faster pace. In environment of lower labor productivity and increase in the average gross wages, the nominal unit labor costs in 2009 went up by 14%³⁴ (6.4% in 2008). The fastest growth was registered in the tourism, which also reported the sharpest fall in the productivity, whereas lower costs were registered only in the construction. The higher unit labor costs are not expected to have larger transmission effect on the inflation on a short run (given the lower domestic demand). Yet, if it is not offset by adaptation, such as by downward correction of employees and/or wages, there is a risk the higher costs to affect the final prices. The increase in unit labor costs could have adverse effect on the competitiveness of the domestic economy, by increasing the prices of export products, considering that the unit labor costs in the tradable sector³⁵ in 2009 increased by 12.5%. On the other hand, unlike the significant growth in the first nine months of the year, in the last quarter, the unit labor costs in the tradable sector went down (quarterly annual rate of decrease of 3.9%) as a result of the improved labor productivity in this sector. Typical for most of the developed countries and some of the transitional economies was the upward trend of unit labor costs. Thus, the unit labor costs in the Euro area went up by 5.8%, given the increase in all developed economies (Consensus Forecast, March 2010). Among transitional economies, which are a part of the European Union, faster growth was registered in Bulgaria (10.6%), Poland (9.3%), Romania (9.1%), Slovenia (9.3%) and Slovakia (7.3%)³⁶. The higher unit labor costs in Macedonia compared to other countries most probably results from the employment growth, and the increase in the gross wages.

Figure 47
Labor productivity, by country
(annual growth rates)

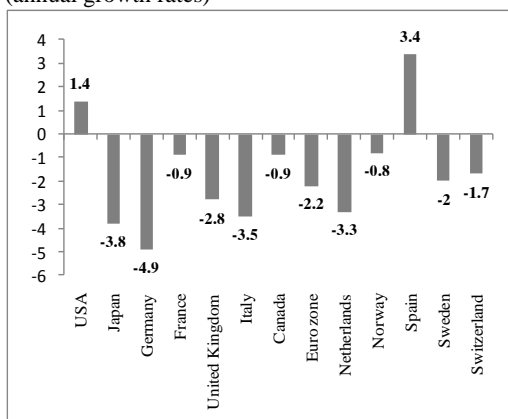
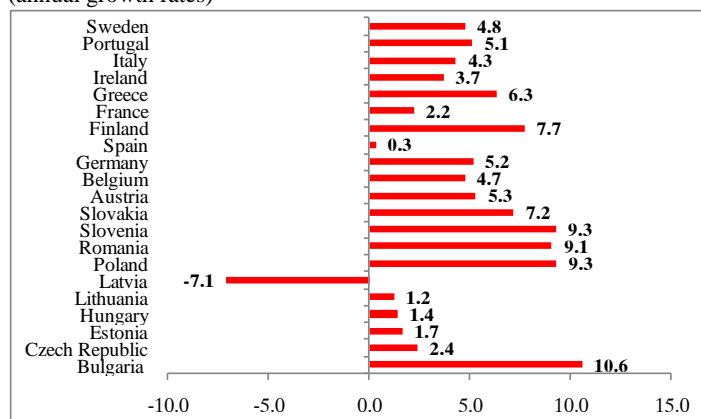


Figure 48
Unit labor costs, by country
(annual growth rates)



Source: European Central Bank (statistical database) and Consensus Forecast (March, 2010).

2.4. External sector

2.4.1. Balance of payments

The globally unfavorable economic conditions had remarkable transmission effects on the balance of payments in 2009. The trends reversed during the year, with the existence of two sub-periods being relevant to mention. The first period pertains to the first quarter of the year, when the crisis reflected a fast and rapid contraction in the external demand and deteriorated expectations of the economic agents for the stability of domestic currency. The deteriorated trade deficit (faster fall of the exports, and slower response of the imports), along with the negative income and the lower private transfers resulted in double broadening of the negative gap in the current account in this period,

³⁴ Productivity and unit labor costs for the overall economy have been calculated by using data on the GDP, on the total number of employed, from the SSO Labor Survey and on the average gross salaries.

³⁵ Tradable sector includes the sectors of agriculture, hunting and forestry, fishing, mining and quarrying, manufacturing industry and electricity, gas and water supply sector.

³⁶ Data on Euro area have been taken from Consensus Forecast, March, 2010. Data on transition economies have been taken from the statistical database of the European Central Bank.

compared to the same period of 2008. The trends started reversing in the second quarter, when the import demand started adjusting to the contraction in the domestic and the global economic activity and when the psychological pressures significantly alleviated. Thus, to the end of the year, the current account deficit reduced to 7.3% of GDP, and registered an annual decrease of 5.8 percentage points of GDP.

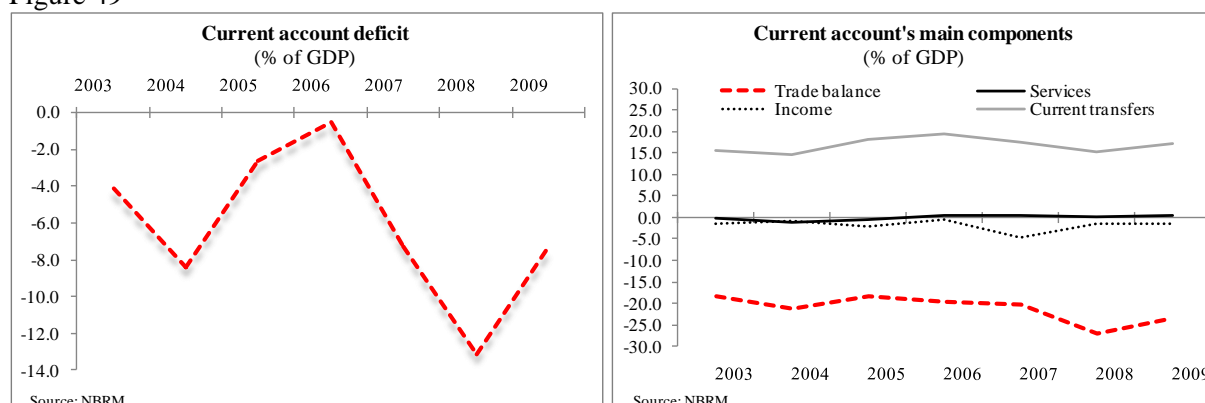
The lower liquidity in global terms and the restraint from new investments, in general, decreased the capital inflows. In the first five months of the year, capital inflows accounted for 1.1% of GDP, and were not sufficient to cover the negative gap in the current account, which led to a considerable decrease in the foreign reserves of 5.2% of GDP. At the end of the second quarter of the year, the considerable decrease in the current account deficit and the stabilization of the economic agents' expectations abated the pressures on the foreign exchange market. Additionally, this period also witnessed higher inflows channeled through the capital and financial account (total net inflows of 7% of GDP from June to December 2009), ensuring a growth of the foreign reserves of 6.3% of GDP in the June - December period.

The crisis cast a light on the structural weaknesses of the domestic economy and the high exposure to global price changes. In 2009, the relevance of the *high imports concentration* came to the surface in only several manufacturing sectors (metal manufacturing and textile sector - with a low added value) dependent on external demand, the *high energy dependence of the country* from imports and the *conditionality* of trade upon *changes in the prices of energy and metals on the international stock markets*. The exposure of metal manufacturing sector to changes in prices of metals on the global stock markets, in environment of their permanent fall, led to a contraction of this export segment and of the trade surplus. This adversely affected the trade balance and the current account. On the other hand, contracted economic activity, and therefore, lower exploitation of production capacities resulted in lower quantitative import of electricity and gas, which along with the fall in the import price of electricity, oil and gas resulted in contraction of the deficit in the energy balance. In spite of the positive implications on the trade balance and the current account, this also illustrated the high energy dependence of the Macedonian economy and its exposure to changes in the energy price.

2.4.2. Current account

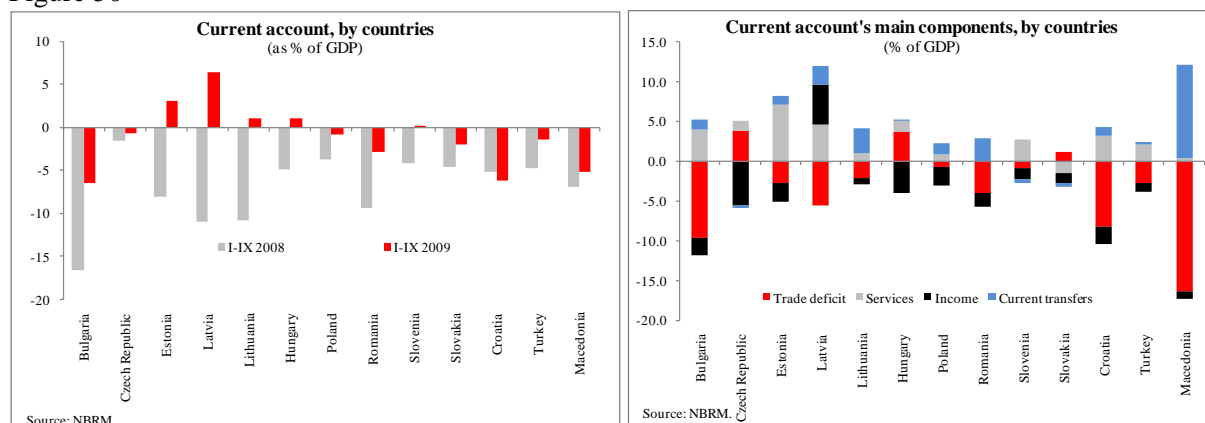
In 2009, the deficit in the balance of payments current account totaled Euro 483.3 million, or 7.3% of GDP, compared to the current account deficit of 13.1% of GDP in 2008. The current transactions deficit narrowed by 5.8 percentage points of GDP mostly due to the substantial narrowing of the negative gap in the foreign trade of 3.5 percentage points of GDP and the growth in the net inflows based on private transfers of 1.9 percentage points of GDP. However, the developments in the external sector were changing during the year. Thus, given the lower external effective demand and export prices, the trade deficit increased by almost 20% in the first quarter of the year. At the same time, the uncertainty regarding the intensity and nature of the transmission of the global crisis to the domestic economy had adverse effects on the expectations of the domestic agents. The deterioration of expectations led to an increasing demand for foreign currencies, which influenced the current account by reducing the private transfers. Hence, in the first three months of 2009, the current account worsened significantly, with the deficit registering an annual growth of 99.6%. The trends started reversing in the second quarter. The import demand started adjusting intensively, and the more stable and better expectations made the private transfers growing. Thus, in the first quarter, the trade deficit and the current account deficit narrowed significantly, registering an annual decrease of 19.8% and 79.8%, respectively in the April - December 2009 period.

Figure 49



Comparative analysis of the balance of payments current account with some of the new EU member states (enlargement in 2004 and 2007) and the EU candidate countries, in the first three quarters of the year³⁷ shows a trend of contraction of the negative balance (except for Croatia), and even a current transaction surplus in some countries. Major driver of the decrease in the deficit in all observed countries is the improvement of the trade balance, i.e. contraction of the trade deficit, or even the surplus reported by some countries (Czech Republic, Hungary and Slovakia). Such current account developments basically reflect the faster decrease in the imports compared the exports. The contraction of the economy and lower domestic demand in these countries decreased the import demands, which translated into significant correction of the external unbalances. Macedonia registered the highest trade deficit (16.4% of GDP in the first three quarters), compared to other countries which reported trade deficit of 4.1% of GDP on average. On the other hand, such high trade deficit was largely offset by the net inflows from current transfers (11.9% of GDP), compared to the average of 1.5% of GDP of the observed group of countries.

Figure 50

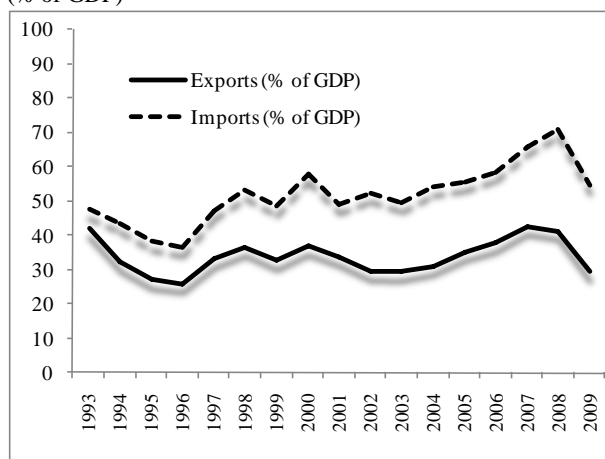


2.4.3. Foreign trade

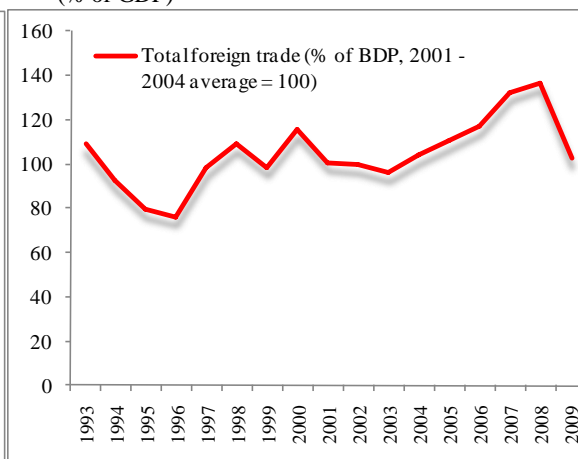
In 2009, total foreign trade decreased by Euro 1,792 million, on annual basis, and reduced to 83.5% of GDP (112.7% of GDP in the preceding year). The slower international trade reduced the foreign trade almost to the average level from 2001 to 2004.

³⁷ Last available data.

Figure 51
Exports and imports
(% of GDP)

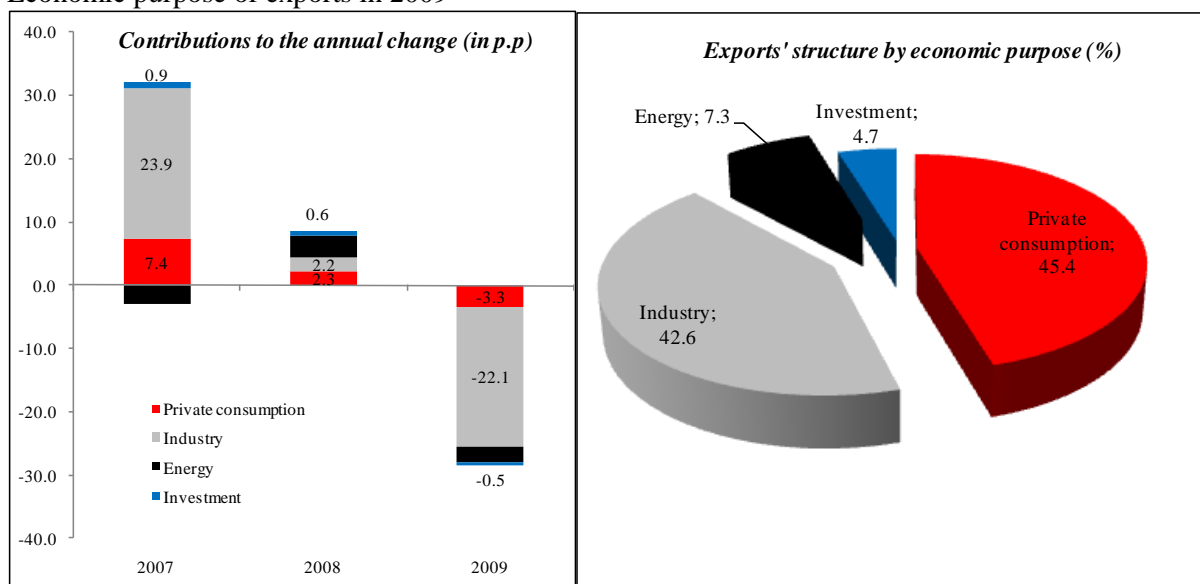


Total foreign trade
(% of GDP)



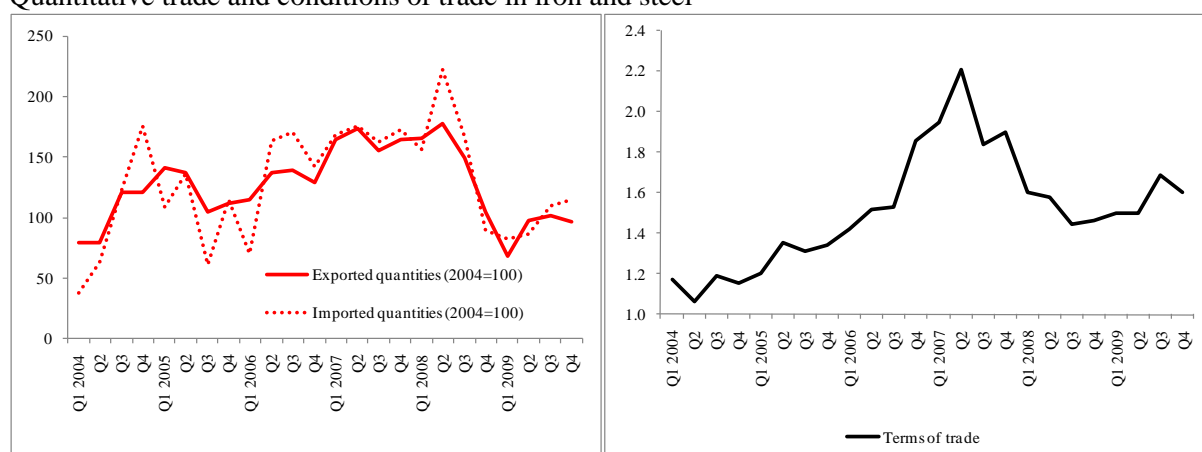
The lower global demand brought about substantial exports contraction, which reduced to Euro 1,925.2 million, i.e. 29% of GDP (average share of 40% of GDP in the last three years). Most of the exports fall, or roughly 78% is due to the lower exports of industrial products, while only a small portion accounts for the lower private consumption in the economies of our trading partners and the export of oil.

Figure 52
Economic purpose of exports in 2009



Two thirds of the exports fall result from the annual fall of the export of iron and steel (by 56%), thus proving the sensitivity of the domestic economy to the high level of export concentration. The lower quantitative demand of iron and steel, caused by the fall in investment activity of our trading partners and cut of metal prices on the international stock markets had their effect on the value of this export segment. With the first "wave" of the crisis and the continuous deterioration of the trade conditions, the export of these metals started decreasing, touching the bottom in the first quarter of 2009. In spite of the signs of recovery to the end of the year, the quantitative export of iron and steel remained at the level registered in 2004.

Figure 53
Quantitative trade and conditions of trade in iron and steel



Source: SSO and NBRM calculations.

Other part of the export fall is due to the lower export of oil and oil derivatives, wearing apparel and metal ore and metal scrap. Export of oil and oil derivatives contracted by 33.4% on annual basis, given the lower export price and exported quantity. Export of wearing apparel, which is the second most important export category, dropped annually by 13.4%, given the lower consumption in the economies of our trading partners. Export of metal ore and metal scraps plunged by 38.7% on annual basis, which is a low-base effect of the external demand and the base effect of the preceding year, when the reopened mines in the domestic economy resumed operating in full capacity, registering high exports.

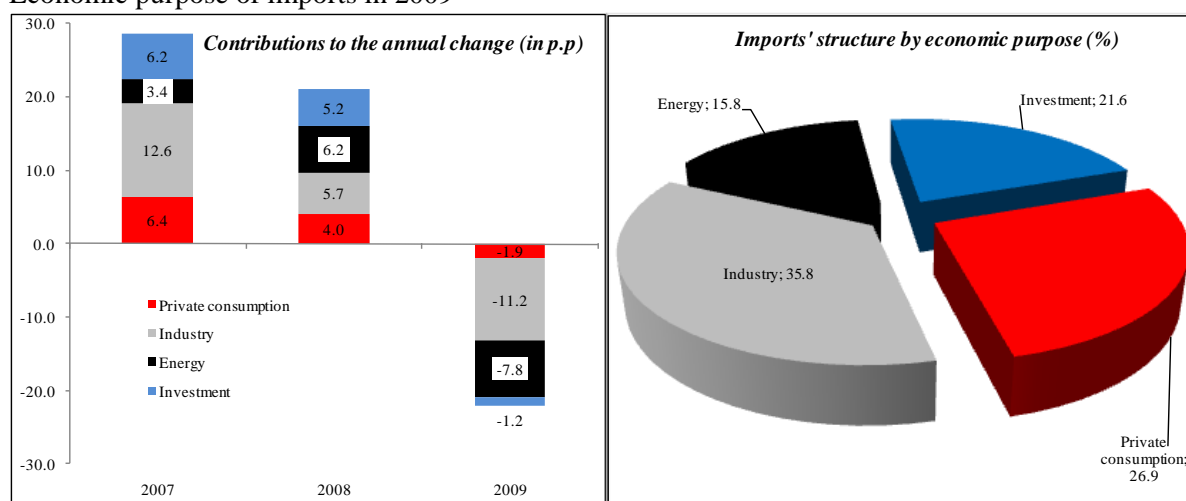
Table 9
Import and export of most important categories according to SITC

EXPORTS of goods	2008	2009	2009/2008 contributions		IMPORTS of goods	2008	2009	2009/2008 contributions	
	in millions of euros		change (%)	(%)		in millions of euros		change (%)	(%)
Total	2689	1925	-28.4	90.5	Total	4643	3616	-22.1	80.8
Iron and steel	868	381	56.1	63.8	Iron and steel	505	215	-57.4	28.2
Metalliferous ores and metal scrap	150	92	-38.7	7.6	Metalliferous ores and metal scrap	173	80	-53.8	9.1
Oil and oil derivatives	205	136	-33.4	9.0	Oil and oil derivatives	627	444	-29.2	17.8
Electric energy	1	4	4 times	-0.4	Electric energy	235	89	-62.0	14.2
Clothing	483.7	418.6	-13.4	8.5	Clothing	60	53	-11.4	0.7
Food and live animals	210	202	-3.5	1.0	Food and live animals	424	402	-5.2	2.1
Road vehicles	24	16	-33.0	1.0	Road vehicles	302	212	-29.7	8.7

Source: SSO

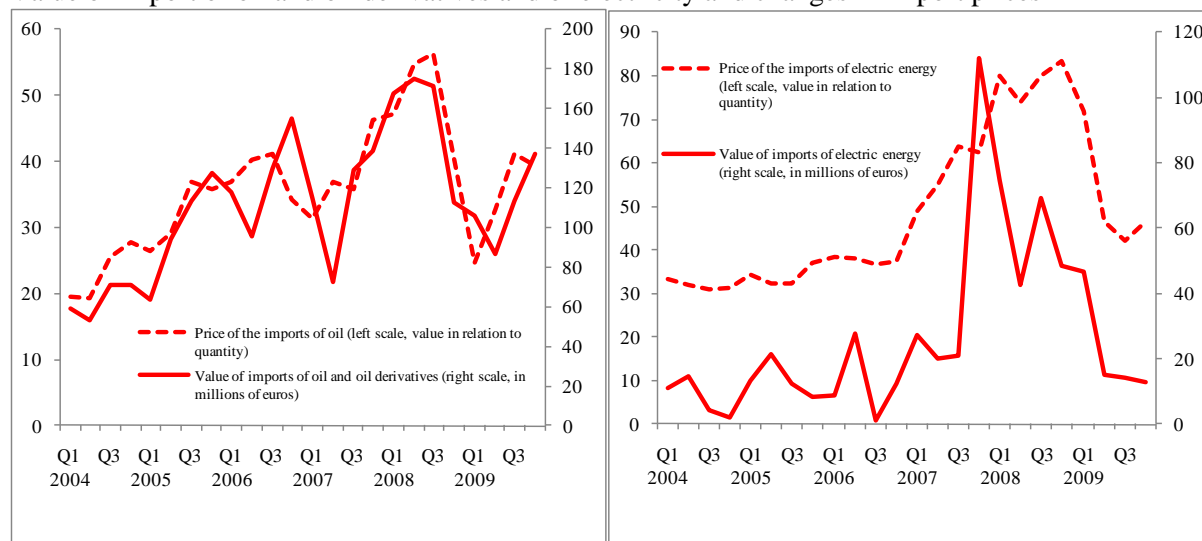
In 2009, the imports reduced to Euro 3,615.8 million, i.e. to 54.5% of GDP (65% of GDP average share in the preceding three years). Decrease in imports, unlike the decrease in exports, was dispersed in several sectors. Effects of crisis, which hit the exports in a very short time lag, brought about a decrease in the import of both raw materials and manufacturing supplies. Thus, half of the fall in the value of imported goods is due to the lower import of industrial supplies necessary for the production, i.e. the decreased import-export component. Import of iron and steel registered a fall, which was almost identical to the fall of the exports (by 57.4% on annual basis), and the imports of metal ore and metal scraps reduced in the same pace (by 54% on annual basis).

Figure 54
Economic purpose of imports in 2009



The remaining portion of the import decrease, i.e. about one third, is due to the fall in the imported energy component. Contraction of economic activity and lower level of exploitation of industrial facilities led to lower import of electricity and gas (by 62% and 32% respectively, on annual basis). However, the import of electricity (besides the lower demand, and therefore, a 46,1% annual fall in the imported quantities) was also a result of the lower import price and higher domestic output of electricity. Additionally, the rapid reduction of oil price on the international stock markets, which spilled over the import price of oil and oil derivatives, had a downward effect on their imported value (fall of 29.2% on annual basis). During the year, the gradual downward adjustment of the household consumption and the investment activity resulted in lower import of joint consumption goods and investment products (by about 6%).

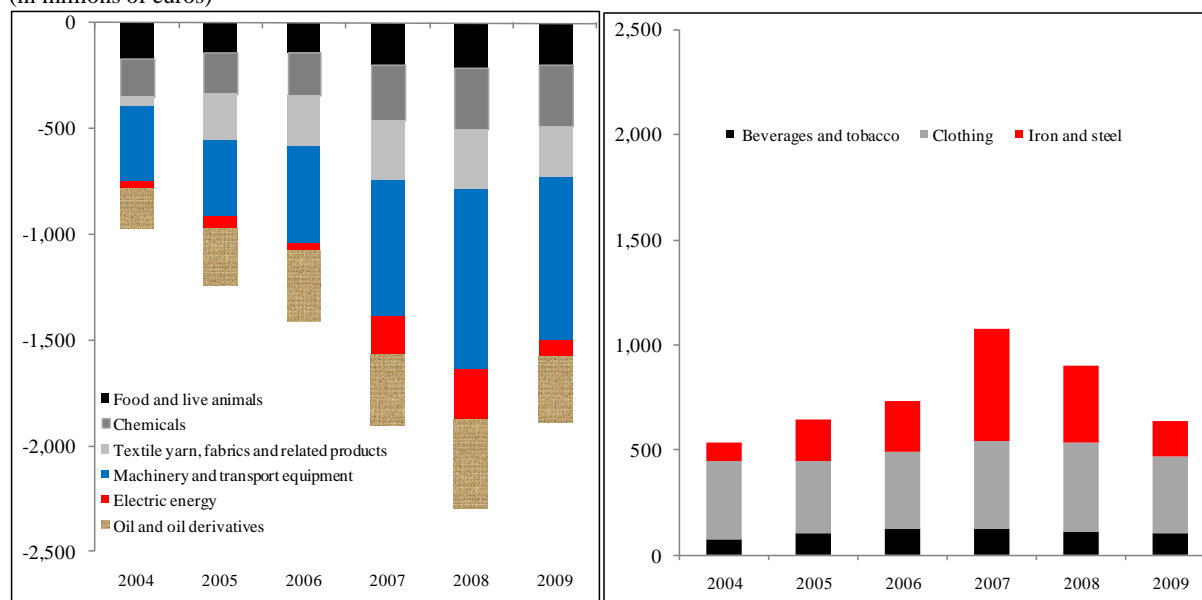
Figure 55
Value of import of oil and oil derivatives and of electricity and changes in import prices



Faster contraction of the import demand compared to the export demand in 2009 was a reason behind the narrowing the negative trade balance (by Euro 263.7 million on annual basis). Foreign trade deficit reduced to 25.5% of GDP (30% of GDP in the preceding year). Greatest contributor to the improvement of trade imbalance was the trade in electricity, where the deficit reduced by Euro 149 million, on annual basis. Second driver of the improved trade balance was the trade in oil and oil derivatives, where the deficit narrowed by Euro 114 million on annual basis. These improvements were also accompanied with lower deficit of road vehicles (by Euro 82 million on

annual basis), which is an effect of the larger restraint from consumption and lower lending. On the other hand, negative contribution to the overall trade balance was made by the lower surplus in the trade in iron and steel, and wearing apparel (by Euro 196 million, and by Euro 58 million, respectively, on annual basis).

Figure 56
Balances of trade categories according to SITC in 2008 and 2009
(in millions of euros)



2009 witnessed significant contraction in the trade deficit with the developing countries and increase in the trade deficit with the European Union. Trade deficit with the developing countries went down by Euro 446 million. Most of this contraction is explained with the halved trade deficit with Russia by Euro 260 million, which is a result of the lower import of crude oil. Lower trade deficit with the EFTA countries (by Euro 111 million), which primarily refers to the lower import of electricity from Switzerland also contributed to the fall of the total trade deficit. Trade deficit with the European Union increased by Euro 166 million, on annual basis. Most of this deterioration comes from the trade deficit with Greece (Euro 105 million, compared to the surplus of Euro 11.4 million registered in the preceding year), due to the worsened trade in iron and steel. The trade balance with Italy also worsened, due to the lower export of iron and steel. Deficit of roughly Euro 20 million was registered with Bulgaria (compared to the surplus of Euro 32 million), as an effect of the lower exports of metal ores and of iron and steel. On the other hand, the trade deficit with Poland decreased considerably due to the lower import of iron and steel. Trade surplus with the neighboring countries went down by Euro 154 million on annual basis. Most of this decrease results from the lower trade surplus with Kosovo, largely due to the lower value of the export of oil derivatives.

Table 10
Imports and exports by trading partners

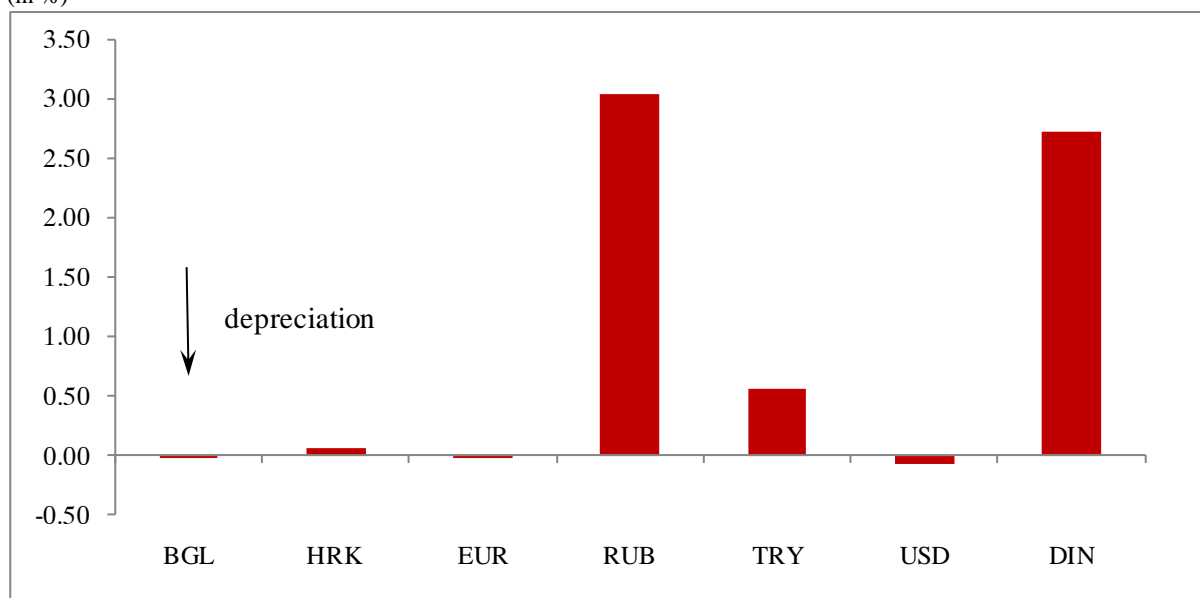
EXPORTS	2008	2009	2009/2008 contributions		IMPORTS	2008	2009	2009/2008 contributions	
	in millions of euros		change (%)	(%)		in millions of euros		change (%)	(%)
Total	2689	1925	-28.4	100	Total	4643	3616	-22.1	0
European Union	1599	1082	-32.3	67.6	European Union	2236	1886	-15.7	0.0
Other developed countries*	62	25	-60.6	4.9	Other developed countries*	217	205	-5.8	0.0
EFTA	12	14	14.1	-0.4	EFTA	202	92	-54.2	0.0
Western Balkans	957	716	-25.2	31.7	Western Balkans	515	426	-17.0	0.0
Developing countries**	57	64	12.7	-1.1	Developing countries**	1426	967	-32.2	0.0
Underdeveloped countries	2	25	11.9 times	-3.2	Underdeveloped countries	48	39	-19.0	0.0

2.4.4. Price competitiveness

Real effective exchange rate (REER), as an indicator for the change in the price competitiveness of the economy, registered a moderate appreciation in 2009, showing lower competitiveness. Annual appreciation is typical for REER, deflated by all three deflators, consumer price index, unit labor cost index and producer price index. Such REER dynamics was primarily determined by the changes in the nominal exchange rates. In 2009, the average Denar NEER was appreciating permanently, and the average annual appreciation equaled 5.9%. Such change could be explained with the slower depreciation of the Denar / US Dollar exchange rate compared to the exchange rate of the Russian Ruble / US Dollar and Serbian Dinar / US Dollar.

Figure 57

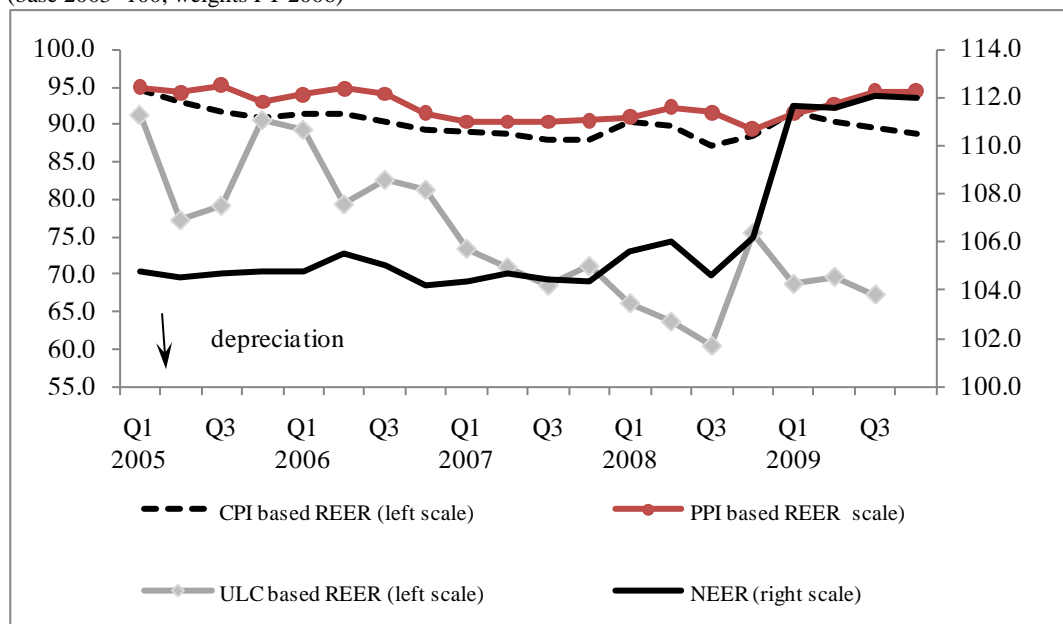
Contribution to the change in the Denar NEER*
(in %)



*Aggregated weight is used for Euro from the weights of the Euro area countries included in the REER calculation.
Source: National Bank of the Republic of Macedonia.

The influence of the annual NEER appreciation was partially offset by the increase in the relative price index (higher foreign prices, and lower domestic prices), which enabled mild annual appreciation of 1.2% of the average CPI-deflated Denar REER. The trend of appreciation of the Denar REER was typical during the entire year, with the fastest change registered in the third and the first quarter, due to the significantly faster appreciation of the Denar NEER compared to the increase in the relative price index.

Figure 58
Denar REER and Denar NEER indices
(base 2003=100, weights FT 2006)



Source: National Bank of the Republic of Macedonia.

Appreciation-related developments were registered in PPI-deflated REER, particularly in the second half of the year. Since the beginning of the year, the Denar NEER appreciation was largely offset by the increase in relative price index which enabled insignificant appreciation of PPI-deflated REER in the first and the second quarter. In the third quarter, the growth in relative price index started decelerating, and registered an annual fall in the last quarter, which contributed to acceleration of the REER appreciation trend in this period. In such environment, the Denar REER, PPI deflated, reported an average appreciation of 2.4% in 2009 compared to the preceding year. **Observing the Denar REER calculated on the basis of unit labor cost index, the appreciation was constantly intensifying during the year, and the first three quarters³⁸ compared to the same period of the preceding year reported an average appreciation of 8.1%.** Such change is a mixed effect of the NEER appreciation and the decrease in relative price index (faster growth of domestic unit labor costs compared to foreign ones).

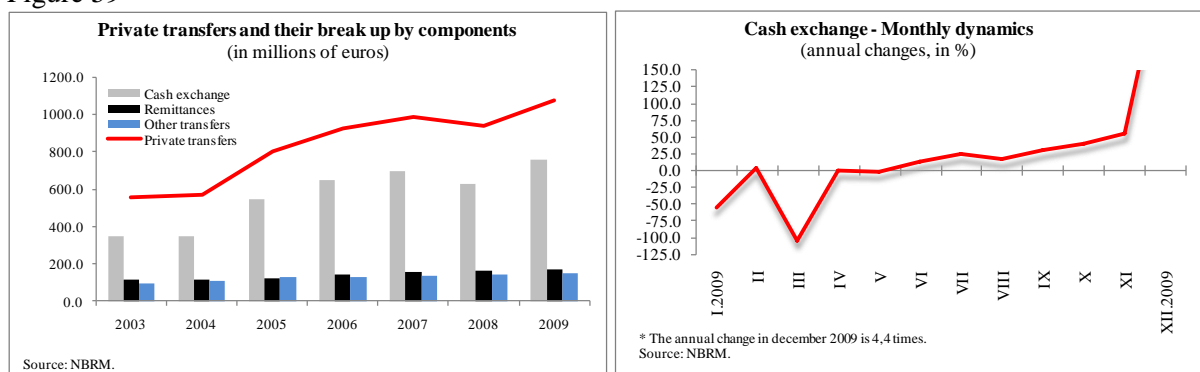
2.4.5. Other current account components

In 2009, the trade in services improved the current account balance. Thus, this category reported a surplus of Euro 28 million, which is by 6.5 times larger net inflows on annual basis. Improvement in net inflows from services mostly results from lower net outflows from traveling, i.e. reduced private and official trips of residents abroad, which corresponds with the general uncertainty and restraint. Lower net outflows from transport services caused by the significant decrease in the foreign trade also contributed to the above improvement. On the other hand, lower external demand also meant lower demand for services, lowering the surplus in construction services, i.e. lower construction activities of domestic companies abroad. **In 2009, category of income reported net outflows of Euro 91.7 million, which is almost unchanged level compared to the preceding year (deficit of Euro 90.9 million in 2008).** However, certain changes could be registered from structural aspect, primarily pertaining to the investment income structure. Thus, direct investment income registered lower net outflows, which given the higher annual amount of paid dividend fully result from the higher reinvested and undistributed profit on annual basis (by 4.4 times). These developments were offset by lower net inflows to the income from portfolio investments (lower returns from foreign reserves invested in securities, due to lower interest rates) and higher income from other investments

³⁸ Last available data.

(i.e. lower inflows from interests on deposited foreign assets of the central bank and commercial banks on accounts abroad, given the fall of returns on these instruments).

Figure 59

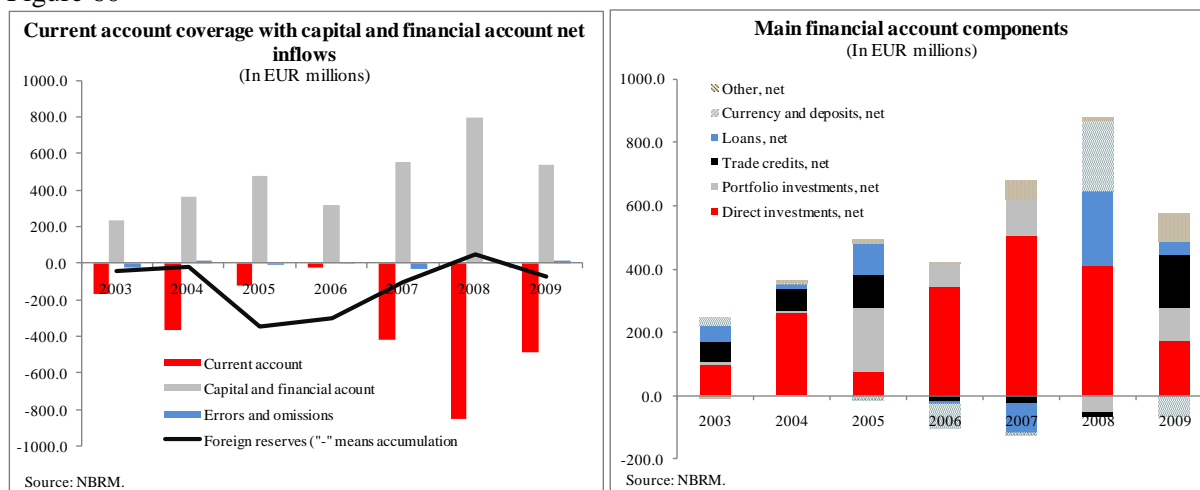


After the moderate fall in 2008, in 2009 the net inflows from *current transfers* went up by 15% on annual basis, reaching Euro 1,131.4 million. Hence, given the annual growth of current transfers and narrowed the negative trade balance, the *trade deficit / current transfers coverage ratio* in 2009 equaled 72.9%, which is an increase of 16.7 percentage points compared to 2008. Observing current transfers, net inflows from private transfers made the largest contribution to the annual growth rate, with Euro 1,077.6 million. Annual growth of private transfers, given the relatively stable growth rate of 5.3% of official remittances and other transfers was mainly due to the annual increase in net cash. Net inflows based on cash totaled Euro 756.3 million, which is by 19.9% more on annual basis. Dynamics of net cash during the year was primarily driven by the expectations of domestic entities. High level of uncertainty followed by the global recession and psychological pressures on the stability of domestic currency resulted in a significant fall in net inflows through this channel in the first quarter of the year. Monetary measures undertaken for preserving the stability of domestic currency, and the first signals for improved economic performances of global economy than expected, resulted in considerable improvement of perceptions and in growth of net inflows from cash private transfers in the second half of the year.

2.4.6. Capital and financial account

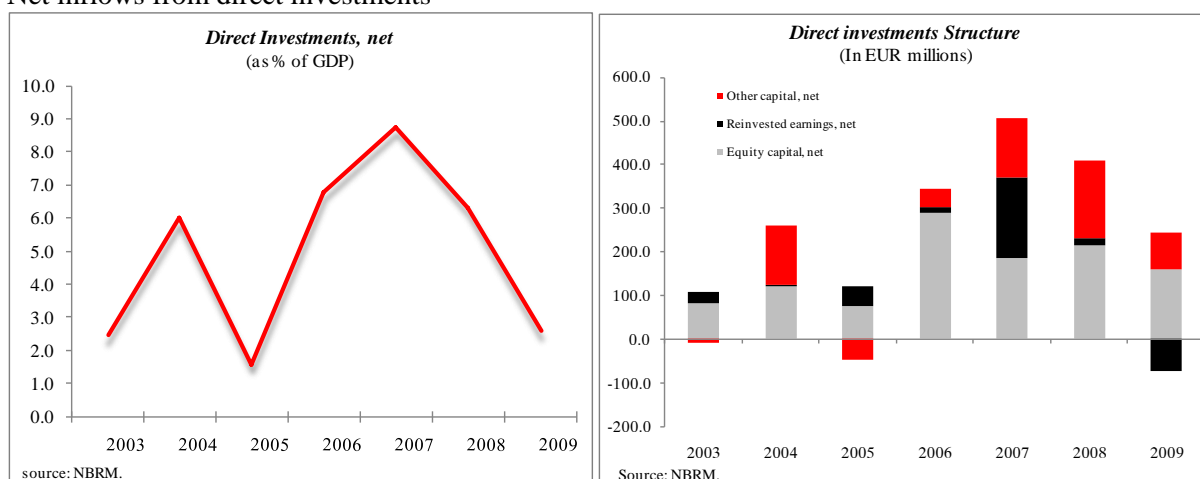
In 2009, capital inflows in less developed economies were significantly lower, with evident risk aversion, insufficient liquidity, lower trust and investors' preferences to invest their available assets in their own economies. In such environment, in 2009, net inflows from capital and financial account in the Macedonian economy reduced by 33% on annual basis, totaling Euro 535.5 million. Net inflows decomposition shows that most of them are direct investments, trade credits, government borrowing on international Eurobond capital market, assets provided by SDR allocation from the IMF quota, and additional inflows were also generated from the net borrowings from abroad.

Figure 60



In 2009, total direct investments stood at Euro 171.9 million (or 2.6% of GDP), which is an annual decrease of 58%. However, analyzing the direct investment structure it could be noticed that such change in investments is driven by the *decrease in reinvested profit from previous years* (net outflows of Euro 73.5 million and 38% contribution to reducing the direct investments), due to the lower amounts of paid dividend. The intensity of *decrease in net inflows from intercompany debt* was the same (by 51.5%), due to the higher repayments of used credits from parent companies and higher claims on credits extended to parent companies. Such changes in the direct investment structure show that, amidst recession, the existing investors fulfill their need of additional financial assets by withdrawing dividends and credits from their branches. On the other hand, the decrease in investments in new equity was less intensive (26.4% on annual basis), primarily due to the developments in the first half of the year. On the other hand, in the second half of the year, the average amount of investments equaled only 19.5% of the average investments in the first half, reflecting the response of these capital flows to the unfavorable changes in the global environment. Analyzing the distribution by country, in 2009 most of the direct investments come from Austria, the Netherlands and Slovenia (overtaking a telecommunication investment from Greece).

Figure 61
Net inflows from direct investments*



*Pertains to direct investments, net, i.e. to direct investments in the country and investments abroad. Value of the latter is insignificant.

Portfolio investments in 2009 are additional source of funding the current account deficit, and net inflows on this basis totaled Euro 104.3 million. Inflows fully result from the Eurobond issued by the government in the amount of Euro 175 million. By insulating the effect of the

Eurobond, it could be noticed that the portfolio investment balance is negative, reflecting the larger investments of domestic institutional investors in equities and debt securities on the international financial markets. Impeded access to external sources of funding, as well as the lower needs for additional funding could be perceived through the dynamics of borrowing. Thus, **net inflows based on external borrowing registered a significant annual decrease (of 80.8%)**. Given the stable level of repaid liabilities on long-term credits, the lower used funds result primarily from the lower external long-term borrowing of the private sector. On the other hand, net short-term borrowing moves to opposite direction, i.e. opposite the net outflows (Euro 44.2 million) in the preceding year, and in 2009 this category reported net inflows in the amount of Euro 14.6 million (predominantly short-term borrowing of the banking sector).

2.4.7. Gross external debt

In 2009, net borrowing of the Macedonian economy totaled Euro 1,365.6 million or 20.6% of GDP and compared to the end of the preceding year, it surged by 49.7% or 6.6 percentage points of GDP. The increase in external net debt comes from the additional external debt of the domestic economic agents. The effect of the higher debt on the net debt position of the domestic economy was partially offset through the increase in gross external demand (mainly due to the larger short-term claims of the banking sector based on currencies and deposits).

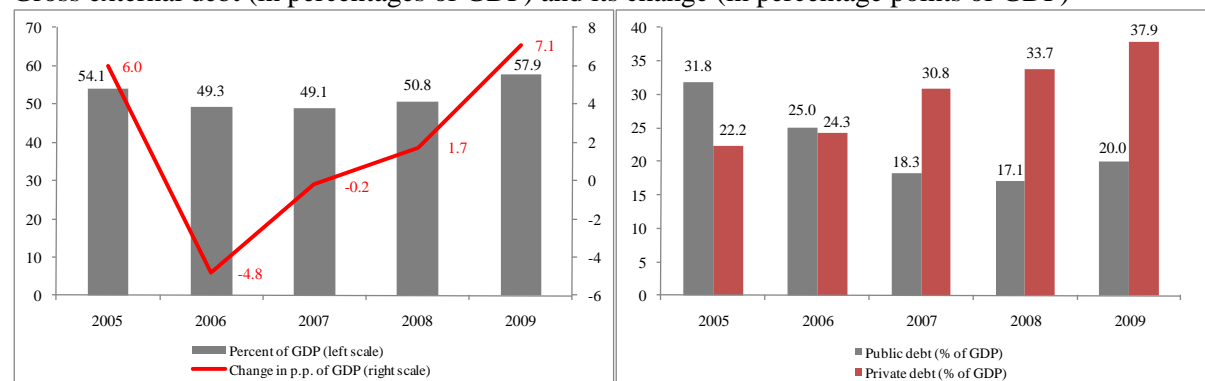
Table 11
Dynamics of external debt

	2005	2006	2007	2008	2009	2005	2006	2007	2008	2009	2005	2006	2007	2008	2009
	in millions of Euro					in absolute amounts					annual changes				
											in %				
Gross external debt	2,528.2	2,503.4	2,841.1	3,304.2	3,839.4	448.1	-24.8	337.6	463.1	535.3	21.5	-1.0	13.5	16.3	16.2
General Government	1,282.8	1,065.6	897.7	906.3	1,055.8	266.4	-217.3	-167.9	8.6	149.5	26.2	-16.9	-15.8	1.0	16.5
Monetary Authorities	62.8	52.0	9.0	9.2	71.7	7.3	-10.8	-43.0	0.1	62.6	13.1	-17.2	-82.7	1.6	683.7
Banks	192.0	269.9	387.9	384.1	467.7	68.8	77.9	118.0	-3.8	83.7	55.8	40.6	43.7	-1.0	21.8
Other Sectors	721.0	786.7	1,115.7	1,321.9	1,417.7	120.6	65.7	329.0	206.2	95.8	20.1	9.1	41.8	18.5	7.2
Direct investment: Intercompany lending	269.6	329.3	430.8	682.7	826.4	-14.9	59.7	101.5	251.9	143.7	-5.3	22.2	30.8	58.5	21.0
Gross external claims	2,026.2	2,427.4	2,634.9	2,392.1	2,473.8	496.2	401.2	207.5	-242.8	81.7	32.4	19.8	8.5	-9.2	3.4
General Government	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Monetary Authorities	1,040.5	1,327.0	1,416.3	1,361.2	1,366.9	375.8	286.5	89.3	-55.1	5.7	56.5	27.5	6.7	-3.9	0.4
Banks	635.9	668.3	648.1	390.6	496.7	16.3	32.4	-20.2	-257.4	106.1	2.6	5.1	-3.0	-39.7	27.2
Other Sectors	253.9	336.5	447.4	507.0	431.3	56.2	82.6	110.9	59.6	-75.7	28.4	32.5	32.9	13.3	-14.9
Direct investment: Intercompany lending	95.9	95.6	123.1	133.3	178.9	47.9	-0.3	27.5	10.2	45.6	99.8	-0.3	28.8	8.3	34.2
Net external debt	502.0	76.0	206.2	912.1	1,365.6	-48.1	-426.0	130.1	705.9	453.5	-8.7	-84.9	171.1	342.4	49.7

Source: NBRM.

In spite of the restricted financial flows on the international capital market, due to the lower trust and high restraint, the gross external debt in 2009 registered an increase which is significantly sharper compared to the preceding year. Thus, on December 31, 2009, the gross external debt totaled Euro 3,839.4 million (57.9% of GDP), which is an increase of 16.2%, or 7.1 percentage points of GDP compared to the end of the preceding year.

Figure 62
Gross external debt (in percentages of GDP) and its change (in percentage points of GDP)



Source: NBRM.

Higher external debt results from the new borrowing of both public and private sector, contributing with 40.1% and 59.9%, respectively, to the growth of the gross debt. At the end of 2009, the external debt of the public sector equaled 20% of GDP (increase of 2.9 percentage points of GDP compared to the preceding year), with the growth being fully concentrated in the third quarter. The increase in public external debt mainly results from the higher government borrowing. This interrupted the trend of decreasing the external debt of the government sector (as a share of GDP) typical for the previous three years, when given the low deficit and budget surplus, the needs for new borrowing were insignificant, with early repayment of the debt being made to international financial institutions. These factors, together with the larger government presence on the domestic financial market ensured the decrease in the government external debt in this period. In 2009, when the budget deficit increased and a need was created for additional sources of funding the budget spending, a Eurobond was issued on the international capital market³⁹, increasing the debt exposure of the government abroad. The debt of monetary authority also went up (by 0.9 percentage points of GDP) due to the SDR allocation.

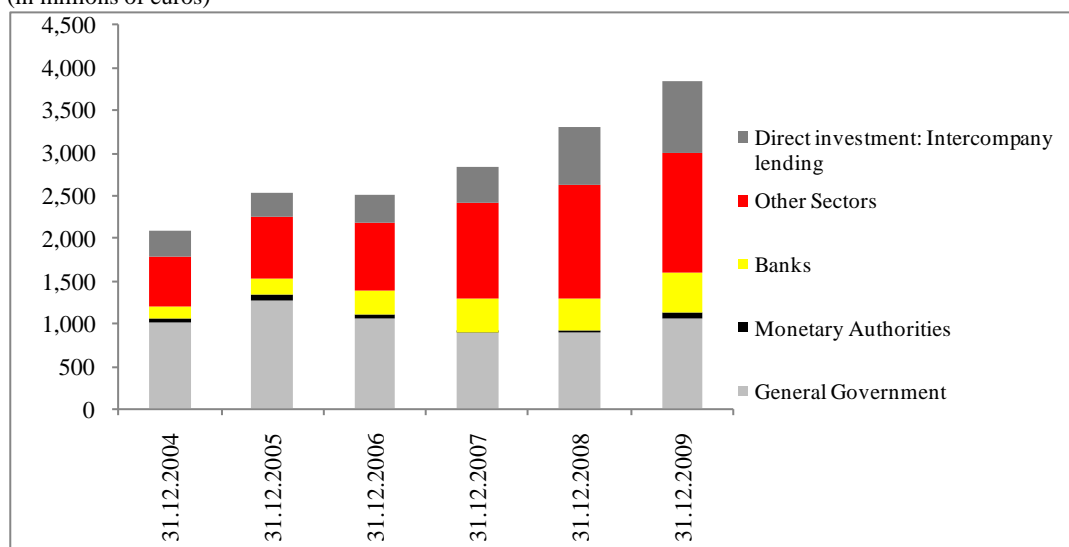
The external debt of the private sector in 2009 went up by 4.2 percentage points of GDP and reached 37.9% of GDP. The growth in private external debt basically reflects the higher intercompany debt (higher long-term liabilities to direct investors) and increase in the external debt of other sectors in the economy⁴⁰ and the banking sector. Hence, in spite of the generally weaker global financial position of the corporate sector, yet, the financial flows from the parent companies did not dried up in 2009, although their intensity was considerably weaker compared to the previous year. Also, the debt of other sectors went up, primarily reflecting the higher debt based on short-term commercial credits. The higher banking sector's external debt results from the increase in liabilities on loans and nonresidents' deposits, which could partially be explained with the high interest spread between domestic and foreign returns on savings.

Taking into account the changes in the level of indebtedness of some sectors, 2009 witnessed changes in the sector structure of the debt. Thus, the share of other sectors in the gross debt of 36.9% went down by 3.1 percentage points, mostly resulting from the lower share of loans. Moreover, 27.5% of the structure of gross external debt pertains to government sector, which is an increase in the share of 0.1 percentage point compared to the end of the preceding year, reflecting the higher debt based on long-term securities, i.e. inflows from the Eurobond. In addition, the share of *intercompany debt* in the external debt increased by 0.9 percentage points, and equal 21.5%. Such developments reflect the higher long-term lending to branches by parent companies.

³⁹ On July 8, 2009, the Government of the Republic of Macedonia issued the second Eurobond worth Euro 175 million that falls due on January 8, 2013, with interest rate of 9.875%.

⁴⁰ This category includes nonbanking financial intermediaries, nonfinancial trade companies, households and nonprofit institutions.

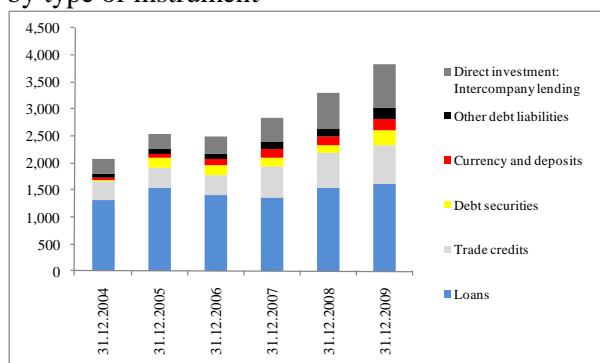
Figure 63
Structure of gross external debt with respect to the basic institutional sectors
(in millions of euros)



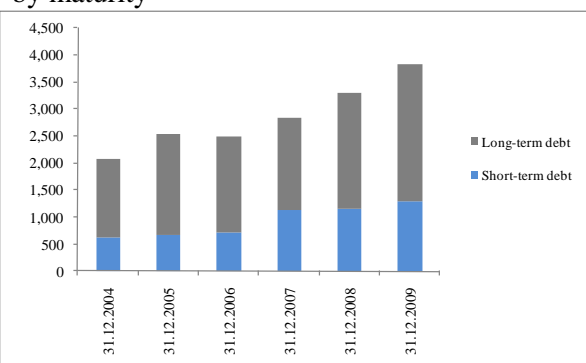
Source: NBRM.

Analyzing the debt instruments, at the end of 2009, most of the gross debt is composed of loans, and with respect to maturity, long-term debt is prevailing. Thus, the share of loans equals 42.3%, registering an annual fall of 4.5 percentage points, compared to December 31, 2008. Loans between associated companies and commercial credits follow with structural share of 21.5% and 18.6%, respectively. Analyzing the maturity, most of the gross external debt (66.1%) is long-term debt, which is by 18.4% higher, primarily reflecting the higher government debt through bonds.

Figure 64
Structure of gross external debt
by type of instrument



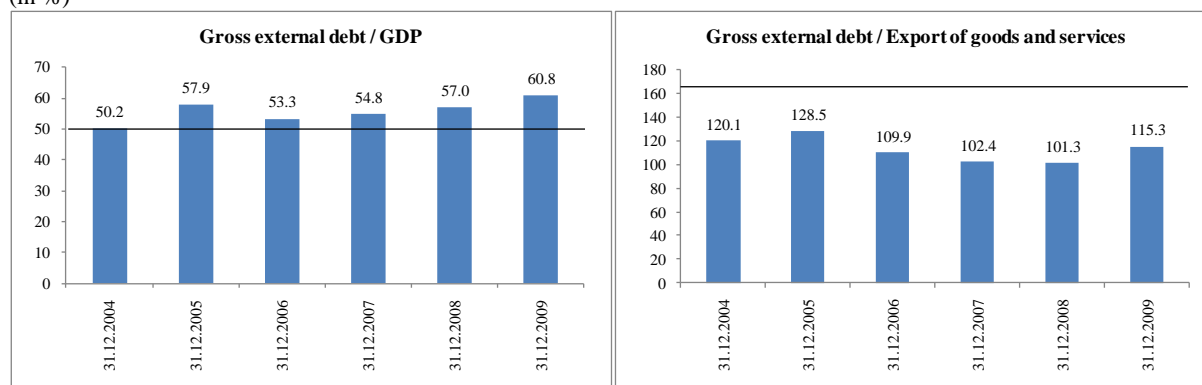
by maturity



Source: NBRM.

Although various external debt indicators provide various understanding for the level of external debt of the Macedonian economy, yet, this area deserves a favorable grade. Thus, according to the gross external debt / exports ratio, the external debt of the Republic of Macedonia is low. Unlike this indicator which shows moderate indebtedness, the share of gross external debt in GDP shows a debt which is higher than moderate (by 10.8 percentage points), which however, is not significantly higher excess compared to the preceding year.

Figure 65
External debt indicators
(in %)



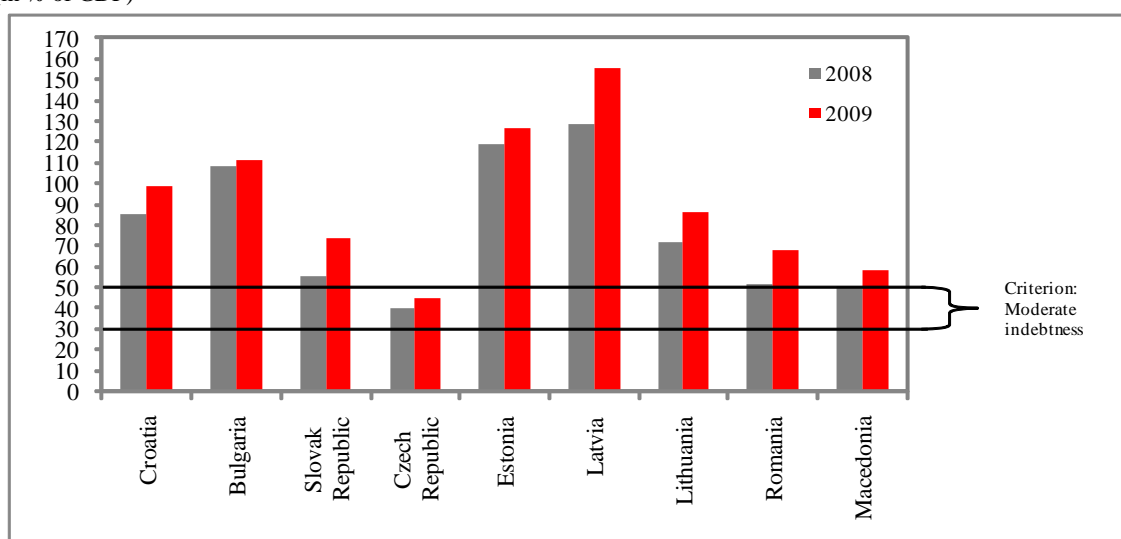
Criterion: Moderate indebtedness 30-50%

Criterion: Lower indebtedness 0-165%

According to the World Bank Methodology, three-year averages are taken for GDP and export of goods and services.

Comparative analysis of some Central and Southeast European and Baltic countries regarding the share of gross external debt in GDP shows that on December 31, 2009, most analyzed countries reported higher external debt on gross basis compared to the end of the preceding year. Thus, at the end of 2009, this indicator for all analyzed countries was higher relative to December 31, 2008, which in case of Estonia and Latvia reflects the fall in GDP, and other countries, besides the lower GDP, were under the influence of the increase of external financing, as well.

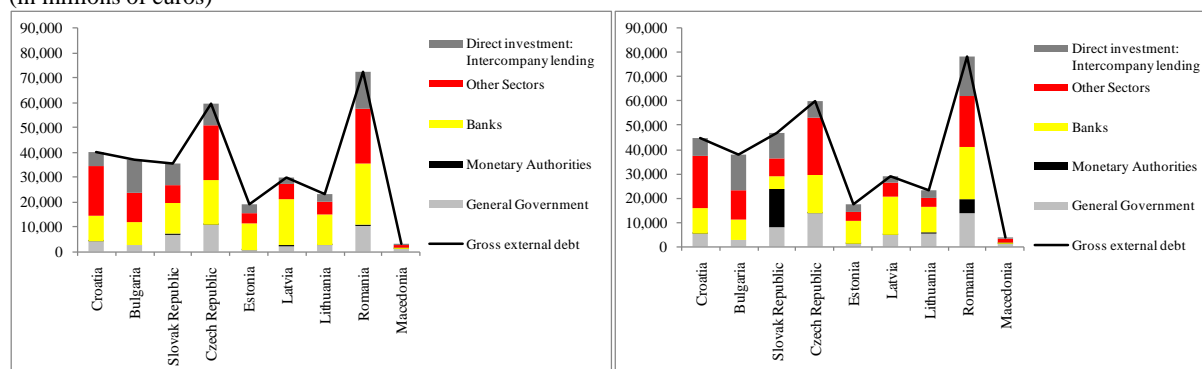
Figure 66
Comparative analysis of GDP
(in % of GDP)



Source: NBRM and data from the websites of central banks on gross external debt and Eurostat, on GDP.

Observing the external debt structure of the analyzed countries at the end of 2009, most of the external financing in Croatia, Czech Republic and Macedonia is a debt of other sectors in the economy, whereas the Baltic countries reported a predominance of the debt of the banking sector. The gross government debt is the greatest contributor to the increase in the external debt in Lithuania and Czech Republic, and the debt of the monetary authority is the largest contributor in Slovakia and in Romania (due to the agreement on multilateral financial arrangement with IMF, EU and other financial institutions).

Figure 67
Comparative analysis of the structure of gross external debt and its integral components
(in millions of euros)



Source: NBRM and data from the websites of some central banks

2.5. Public finances

Given the steep contraction of the global economic activity, 2009 was characterized with robust fiscal support of economies, and accordingly, significant increase in budget deficit in global terms. Fiscal position in Macedonia followed this path, with the intensity of deterioration of budget balance being significantly lower. This ascertainment largely pertains to the comparison with the fiscal positions of more advanced economies. In this group of countries, the fiscal sets for stimulating economic activities were robust, resulting in significant increase in budget deficits.

Table 12
Budget deficits by country
(% of GDP)

	2005	2006	2007	2008	2009
Germany	-3.3	-1.6	0.2	0.0	-4.2
France	-2.9	-2.3	-2.7	-3.4	-7.0
Netherlands	-0.3	0.5	0.2	0.7	-3.8
Greece	-5.2	-2.9	-3.7	-7.7	-12.7
Spain	1.0	2.0	1.9	-4.1	-12.3
Italy	-4.3	-3.3	-1.5	-2.7	-5.6
Portugal	-6.1	-3.9	-2.6	-2.7	-6.9
Czech Republic	-3.6	-2.6	-0.7	-2.1	-6.0
Slovenia	-1.4	-1.3	0.0	-1.8	-5.9
Slovakia	-2.8	-3.5	-1.9	-2.3	-5.3
Romania	-1.2	-2.2	-2.5	-5.5	-7.2
Bulgaria	3.2	3.5	3.5	3.0	-0.8
Turkey	-0.6	0.8	-1.0	-2.2	-5.5
Serbia	1.6	1.5	0.5	-1.7	-3.2
Albania	-3.4	-3.3	-4.8	-7.9	-8.6
Macedonia	0.2	-0.5	0.6	-1.0	-2.7

Source: Eurostat, central banks, Ministries of Finance and IMF (IMF, World Economic Outlook Data, October 2009), National Bank of Greece (NBG, Monthly Macroeconomic Outlook, January 2010).

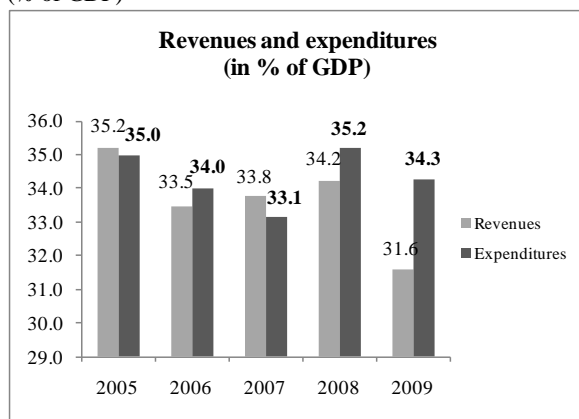
In 2009, the budget deficit made up 2.7% of GDP, which is by 1.7 percentage points higher compared to the preceding year. Compared to the plan⁴¹, the deficit is by minor 0.1 percentage points lower than planned, given the lower income (by 7.2%) and expenses (by 6.8%). After the low deficit in the preceding year, and the surplus in the 2005-2007 period, 2009 witnessed

⁴¹ Refers to the second budget revision, see the text below.

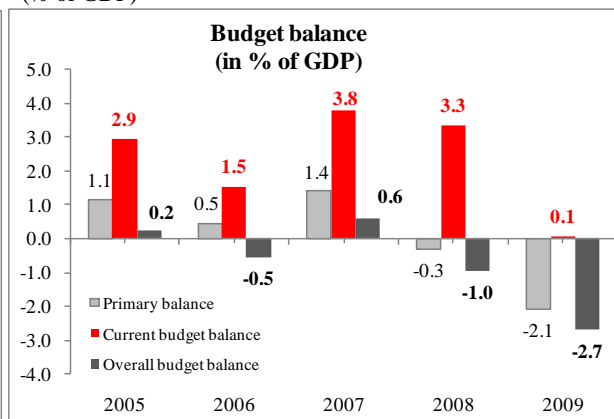
higher deficit in the primary budget balance⁴², of 2.1% of GDP, whereas the current budget deficit⁴³ registered an insignificant surplus (of 0.1% of GDP) given the slightly higher current income than expenses.

Figure 68

Budget income and expenses
(central government and funds)
(% of GDP)



Primary, current and total balance
(central government and funds)
(% of GDP)



Source: Ministry of Finance of the Republic of Macedonia and NBRM calculations.

Considerable uncertainty and risks surrounding the effects of the global crisis on the domestic economy resulted in several revisions of the projected growth rates for 2009. Also, the performances, particularly in the first part of the year diverged from projections, creating a need of revision of the projected budget parameters during the year. Global crisis, although with a certain time lag, hit the domestic real sector, decreasing the tax revenues in the fiscal sector. In such environment, fiscal consolidation was a must, by narrowing the magnitude of public expenses. Thus, considering the 10% decrease in tax revenues in the first quarter than projected, the **first budget revision** was made in June 2009 (within the third set of anti-crisis measures), which also included the effect of the profit tax release as a part of the anti-crisis measures of the Government in November 2008. Alongside the decrease in budget revenues (by 6.6%), the expenses were corrected similarly (decrease in import spending and capital expenses), which helped the budget deficit remain at 2.9% of the newly projected GDP (real growth of 1%⁴⁴). Taking into account the GDP data for the first two quarters which indicated a contraction of economic activity and failure of GDP growth projections, and subsequently, the budget revenues, October 2009 witnessed the adoption of the **second budget revision**. According to this revision, the budget deficit was projected to equal 2.8% of the revised GDP (fall of 0.6%). On the revenue side, the greatest correction was made in tax revenues, primarily VAT and import duties, in line with the decrease in domestic demand and the imports, whereas the expense side registered more substantial cut of capital expenses (projects with below 30% delivery and projects with dominant import component, and less EBRD funds for the Road Fund). Each quarter of the year reported a budget deficit, registering no significant oscillations during the year, unlike the preceding two years characterized with high concentration of budget consumption in the last quarter of the year.

⁴² Primary budget balance is a difference between the total income and total expenses corrected by interest payments.

⁴³ Current budget balance is a difference between the current income (tax revenues, contributions and nontax income) and current expenses.

⁴⁴ Projections underlying the Budget. The assumed economic growth rate in the first budget projection equaled 5.5%.

Table 13
Consolidated budget (central government and funds)

	2008	2009	Annual change 2009/2008	Contribution to annual growth
	in millions of denars		in %	in %
TOTAL REVENUES	136,411	128,498	-5.8	100
Taxes and Contributions	115,103	109,860	-4.6	66
Tax Revenues (SRA)	295	269	-8.8	0
Taxes	76,559	70,754	-7.6	73.4
Personal Income Tax	8,696	8,710	0.2	0
Profit Tax	8,579	4,434	-48.3	52
VAT	36,173	35,173	-2.8	13
Excises	14,276	14,533	1.8	-3
Import Duties	6,275	5,229	-16.7	13
Other Taxes	2,560	2,675	4.5	-1
Contributions	38,249	38,837	1.5	-7
Pension and Disability Insurance Fund	25,586	26,281	2.7	-9
Employment agency	1,790	1,848	3.2	-1
Health fund	10,873	10,708	-1.5	2
Non Tax Revenues	18,400	16,402	-10.9	25
Non Tax Revenues (SRA)	7,160	6,859	-4.2	4
Profit of Public Financial Institutions	5,546	3,807	-31.4	22
NBRM	1,289	1,161	-9.9	2
Asset Management Agency	260	132	-49.2	2
Other Property Income	10	3	-70.0	0
Interest on Deposits with NBRM	182	111	-39.0	1
Dividends	3,805	2,400	-36.9	18
Administrative Taxes and Charges	1,858	1,897	2.1	0
Health co-payment	390	312	-20.0	1
Other Administrative Taxes and Charges	561	514	-8.4	1
Other Nontax Revenues	942	1,265	34.3	-4
Road Fund Fees	1,943	1,747	-10.1	2
Capital Revenues	1,390	1,167	-16.0	3
Foreign Donations	1,327	833	-37.2	6
Revenues from repayment of loans	191	237	24.1	-1
TOTAL EXPENDITURES	140,222	139,393	-0.6	100
Current Expenditures	120,160	125,965	4.8	-700
Wages and Allowances	20,827	22,699	9.0	-226
Goods and Services	18,745	16,220	-13.5	305
Transfers	77,942	84,601	8.5	-803
Transfers (SRA)	1,283	1,505	17.3	-27
Social Transfers	58,104	61,742	6.3	-439
Pension and Disability Insurance Fund	33,366	36,455	9.3	-373
Employment Agency	1,626	2,271	39.6	-78
Social Benefits	3,990	4,305	7.9	-38
Health Care	19,122	18,711	-2.1	50
Other Transfers	18,488	21,296	15.2	-339
Refugees	67	58	-13.4	1
Interest	2,646	2,445	-7.6	24
Domestic debt interest	943	1,011	7.2	-8
Foreign debt interest	1,702	1,434	-15.7	32
Capital Expenditures	20,062	13,428	-33.1	800
Investment in Fixed Assets	13,468	9,453	-29.8	484
Capital Transfers	6,594	3,975	-39.7	316
BUDGET BALANCE	-3,811	-10,895		
FINANCING	3,811	10,895		
Inflow	10,788	18,939		
Privatisation Receipts	1,652	0		
Foreign Loans	2,672	13,040		
Deposits	3,328	-274		
Domestic borrowing	3,038	6,098		
Sell of Shares	97	75		
Outflow	6,977	8,044		
Repayment of Principal	6,977	8,044		
Foreign	1,879	2,356		
Domestic	5,098	5,688		

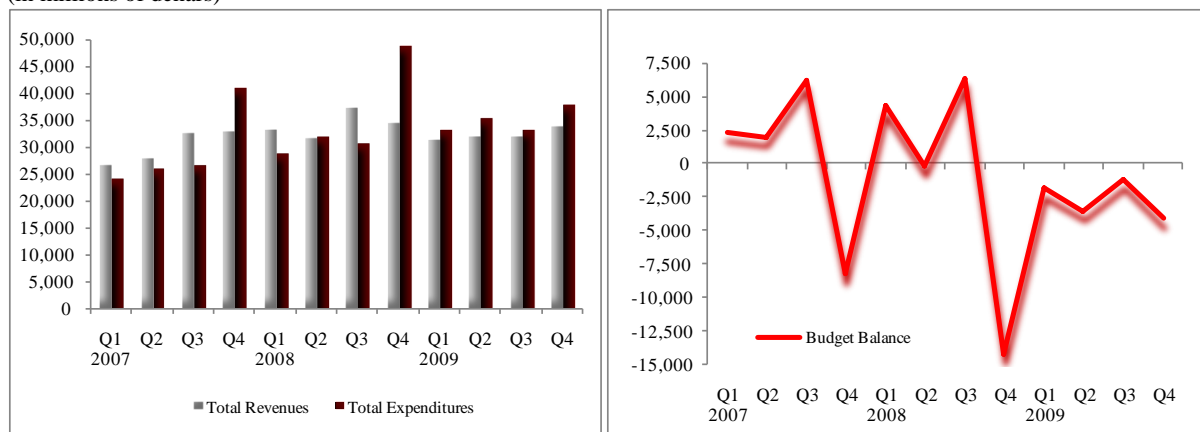
* Accounts for own revenues

Source: Ministry of Finance of the Republic of Macedonia.

In 2009, total budget revenues stood at Denar 128,498 million, which is by 5.8% less compared to the preceding year. Thus, their share in GDP equaled 31.6% (decrease of 2.6 percentage points). The annual fall mostly results from the lower tax revenues, particularly taxes levied on the profit and turnover of goods and services. Substantial decrease was also registered in nontax revenues, whereas the reform of integrated collection of contributions by IRS resulted in higher revenues from contributions.

Figure 69

Quarterly distribution of budget revenues and expenses and of budget balance
(in millions of denars)

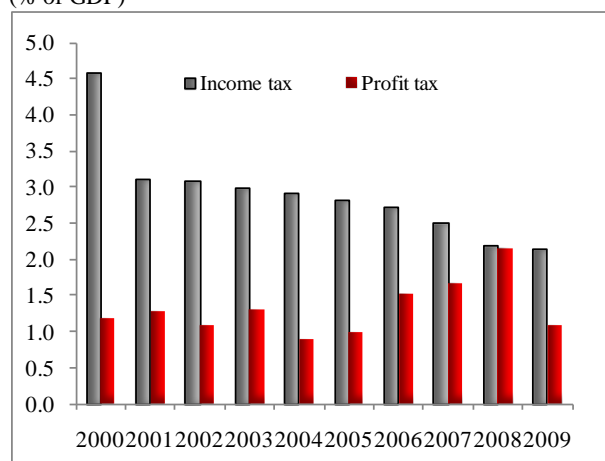


Source: Ministry of Finance of the Republic of Macedonia.

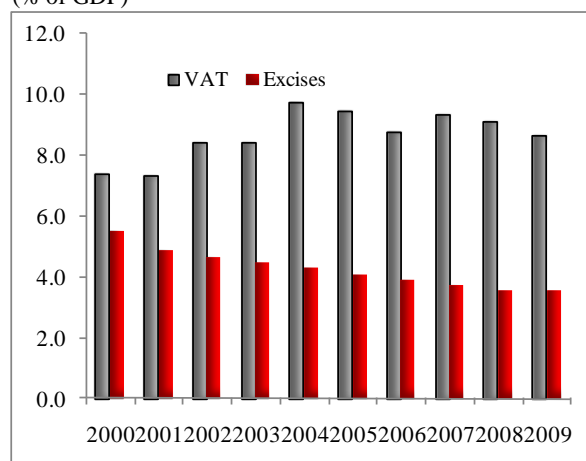
Contracted economic activity and anti-crisis measures for mitigating the crisis brought about 7.6% annual decrease in tax revenues (contribution of 73.4% to the fall in total revenues). Thus, the fastest decrease was registered in the **profit tax** revenues, contributing with 71.4% to the reduction of tax revenues. The decrease in profit tax revenues largely reflects the tax release effective since the beginning of the year as a part of the first set of anti-crisis measures, in order to preserve the corporate liquidity amidst unfavorable economic developments. Law amendments released the companies from paying tax on undistributed profit generated in the current year⁴⁵. To take into account the effects of this measure, in June 2009, the Government made the first budget revision, where this item was subject to the largest decrease compared to the initial plan (similar level was projected with the second revision). Yet, the generation of profit tax revenues was lower (86.5% of the projected with the second revision).

⁴⁵ "Official Gazette of the Republic of Macedonia" no. 159/2008 (Article 36-d). "Taxpayer shall be released from the obligation to pay tax on undistributed profit generated for the current year. Undistributed profit shall be the difference between the total income and total expenses of the taxpayer in amounts as defined by accounting regulations and accounting standards less paid tax specified in the tax balance. Amount distributed as dividends and other profit distributions, whether in monetary or nonmonetary form shall be taxed at payment."

Figure 70
Income tax revenues
(% of GDP)



Goods and services tax revenues
(% of GDP)



Source: Ministry of Finance of the Republic of Macedonia and NBRM calculations.

The contraction in the domestic economy was primarily determined by the lower personal and investment consumption, which brought about a decrease in VAT revenues (annual fall of 2.8%). Such decrease in VAT revenues is due to the lower trade turnover⁴⁶ and fall in the imports. Additionally, the annual fall in the total imports (by 22.1%), along with the effect of gradual decrease in customs rates, which is in line with the Agreement with the World Trade Organization (WTO) and the Stabilization and Association Agreement with the EU⁴⁷, and due to the anti-crisis measures of the first set which included additional decrease of some customs duties⁴⁸, contributed to the annual decline in customs revenues of 16.7%.

Other tax revenues and contributions registered an annual increase. Excises reported an annual increase of 1.8%, which is a result of higher revenues from excises on oil derivatives and tobacco products (by 3.5% and 3.1%, respectively, on annual basis), whereas the vehicle excise revenues went down (by 19.5%). Personal income tax revenues remained almost the same as in the preceding year. Gross wage concept⁴⁹ was introduced on January 1, 2009 which includes board and transport allowances, making the tax base higher. This reform tightens the control and collection of personal income tax and contributions. The introduction of this reform triggered the contribution rate cut⁵⁰, which means lower coverage of the tax base. However, as a result of the integrated collection of contributions by IRS, and the stricter control of taxpayers, the paid-in contributions increased by 1.5% compared to 2008.

⁴⁶ Source: SSO Total retail and wholesale turnover in 2009 was by 6.2% lower compared to 2008.

⁴⁷ "Official Gazette of the Republic of Macedonia" no. 146/2008, Decision on harmonizing and amending the Customs Tariff for 2009. Average non-weighted rate in 2009 equaled 8.99% (9.26% in 2008).

⁴⁸ "Official Gazette of the Republic of Macedonia" no. 160/2008, Law on amending the Law on Customs Tariff. This measure reduced or abolished customs duty rates for raw materials and machines for total of 498 groups of products of the customs tariff, of which the customs duties for 286 groups of products being fully abolished, and for the remaining 212 groups, they reduced partially. These amendments were made in line with the needs of the business community, and the Law allowed for decrease in customs duty rates for many sectors affected by the global financial crisis. Of total of 498 groups of products which registered a decrease in customs duty rates, 33.5% are products intended for metal manufacturing industry, 24.7% are products intended for textile industry, 11.8% are products intended for agricultural sector, 8.8% are products intended for printing industry, 7% are products intended for pharmaceutical industry, 3.4% are products intended for chemical industry, 3% for the IT sector, 2.2% for the wood industry, 1.6% for the construction industry, 0.8% for the railway industry, 0.4% for the glass industry, 0.4% for the food industry, 0.2% for the leather industry, 0.2% for the electronic industry and other with 1.6% (products intended for various industries).

⁴⁹ "Official Gazette of the Republic of Macedonia" no. 16/2008, Law on amending the Law on Payment of Wages in the Republic of Macedonia.

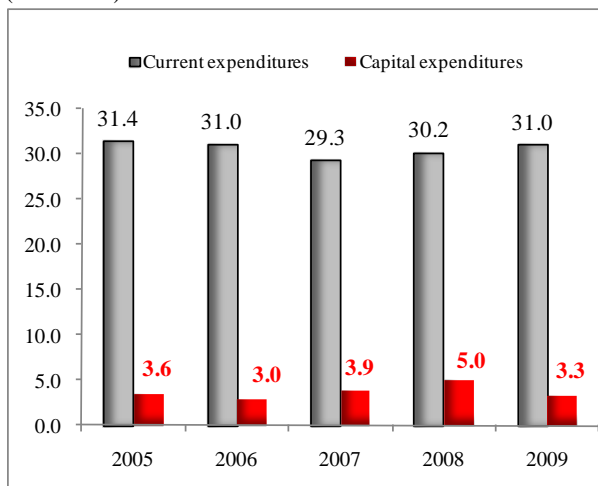
⁵⁰ Pension insurance contribution reduced from the existing 21.2% in 2008 to 19% in 2009; the health insurance contribution reduced from 9.2% to 7.5%, and the employment contribution reduced from 1.6% to 1.4%. The additional contribution for professional health insurance of 0.5% became compulsory, i.e. starting from 2009 it was included in the group of compulsory social contributions. Starting from 2009, the water supply contribution of 0.2% ceased to be calculated. This means that the encumbrance of gross wage with contributions reduced from 32.7% in 2008 to 28.4% in 2009.

Nontax revenues registered an annual fall of 10.9% given the decrease in each quarters except for the second, when a large partially state-owned company paid the dividend. On annual basis, however, the dividend paid went down by roughly 37% compared to the preceding year (paid in the third quarter), which is a major factor for the lower nontax revenues. **Capital revenues and foreign subsidies** also registered an annual fall, which, in fact, are items that showed the poorest effectuation of the plan (70% and 30%, respectively).

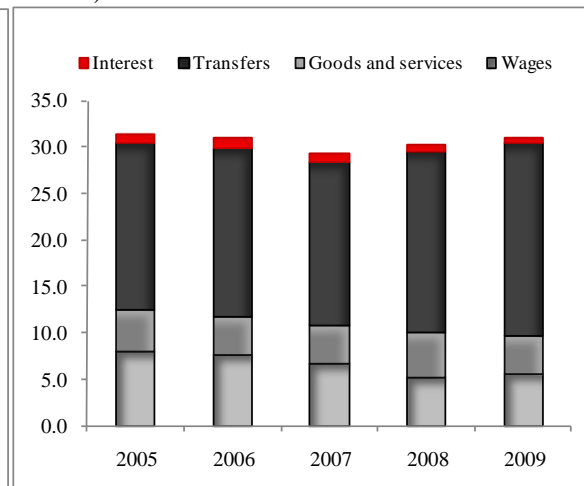
Total budget revenues in 2009 were valued at Denar 139,393 million, which is almost the same as in the preceding year (fall of 0.6%). In terms of GDP, budget spending declined by 0.9 percentage points, constituting 34.3% of GDP. Negative dynamics of revenues during the year resulted in less funds available for spending than initially projected. Thus, the first budget revision decreased the total expenses by 6%, with more significant decrease being made in the capital expenses (by 19%); with the second revision, the capital expenses were further decreased by 19%. Such government investment policy arises from the legal decrease in expenses for projects with effectuation lower than 30% in the first half of the year, and the deferral or slower delivery of projects with predominant import component.

Figure 71

Distribution of expenses
(% of GDP)



Distribution of current expenses
(% of GDP)



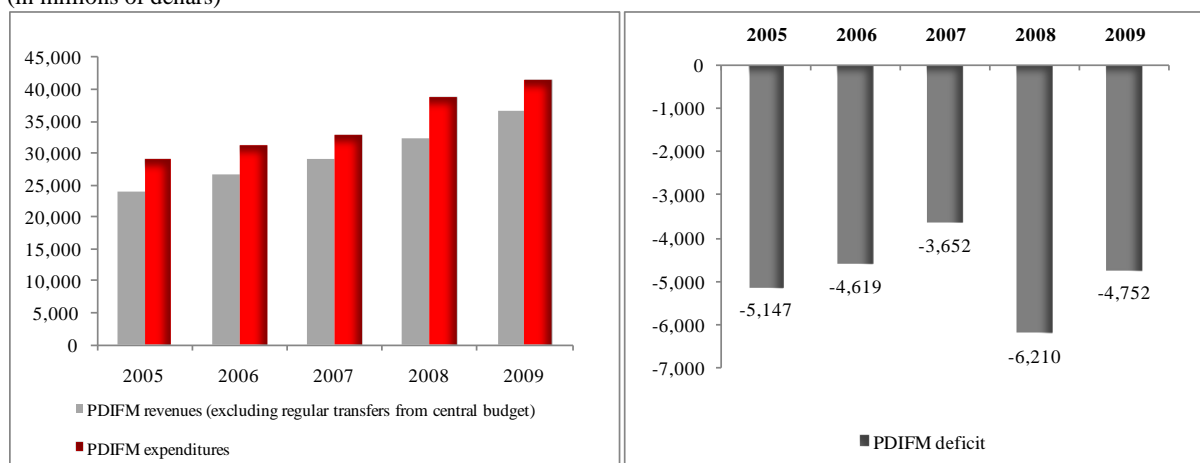
Source: Ministry of Finance of the Republic of Macedonia and NBRM calculations.

Although the total expenses registered a marginal decrease, the current expenses reported an annual growth of 4.8%. Such growth primarily reflects the increased transfers (by 8.5%), which constitute a dominant item in the total expenses with 61% (56% in 2008). Moreover, wage and compensation costs also went up (by 9%). Conversely, goods and services costs and interest payments went down (by 13.5% and 7.6%, respectively), on annual basis.

The annual growth of transfers almost solely results from the higher payments for social transfers (contribution of 54.6%) and payments for other transfers (contribution of 42.1%). Within **social transfers**, payments for pensions registered the fastest annual increase, which is a result of the compliance of pensions and the increase in number of pension beneficiaries⁵¹. Higher costs of the Employment Agency made their contribution to the increase in social transfers, reflecting the regular and timely payment of compensations for unemployed persons, and the larger support of active employment measures, implementation of self-employment project and engagement of unemployed force for public works.

⁵¹ Source: Pension and Disability Insurance Fund of Macedonia. Pension compliance was made in 2009 from January 1, 2009 by 3.5% and from July 1, 2009 by 2.02%.

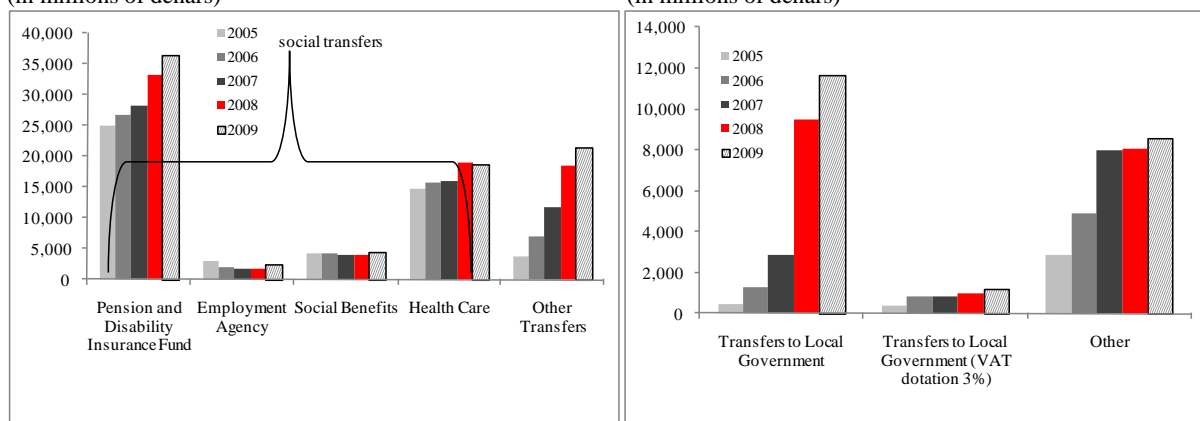
Figure 72
Pension and Disability Insurance Fund of Macedonia
(in millions of denars)



Source: Ministry of Finance of the Republic of Macedonia.

The increase in other transfers results mostly from higher amounts transferred to local governments in the form of block donations for financing the conferred responsibilities⁵², in accordance with the higher number of municipalities which entered the second phase of decentralization (from 62 to 68 municipalities), and due to the effect of increase in the education wages⁵³. Besides the above categories, the further support of the agricultural sector was moving to the same direction.

Figure 73
Distribution of transfers
(in millions of denars)



Source: Ministry of Finance of the Republic of Macedonia.

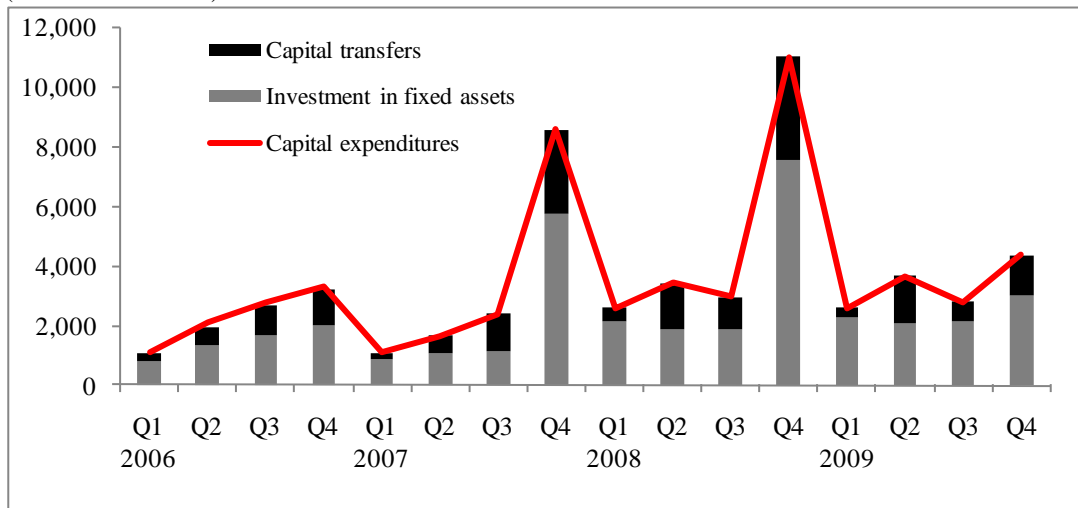
In 2009, **wage and compensation** costs registered an annual increase of 9%, due to the higher wage and increase in the number of employees in the public administration. Higher wage costs in 2009 reflect the transmission effect of the increase in wages of employees in the public administration in September 2008, which provided a higher level of average wage in 2009 compared to the preceding year, whereas the planned 10% wage increase in September 2009 was not effectuated. Apart from this, new employments arising primarily from the Euro integration process and the Ohrid agreement,

⁵² In July 2007, the Government made a decision to finance the costs for compensations and wages of the employees in four sectors of the local public administration (education, social policy and children protection, culture) through block-donations at municipalities that met the respective criteria.

⁵³ The increase in wages in primary and secondary education according to the agreement signed with SONK (increase in board allowance from Denar 2,300 to Denar 3,200).

contributed to the increase in the number of employees in public administration⁵⁴. In 2009, current expenses intended for **goods and services** registered a poor realization compared to the plan (85%), which is by 13.5% less relative to the preceding year.

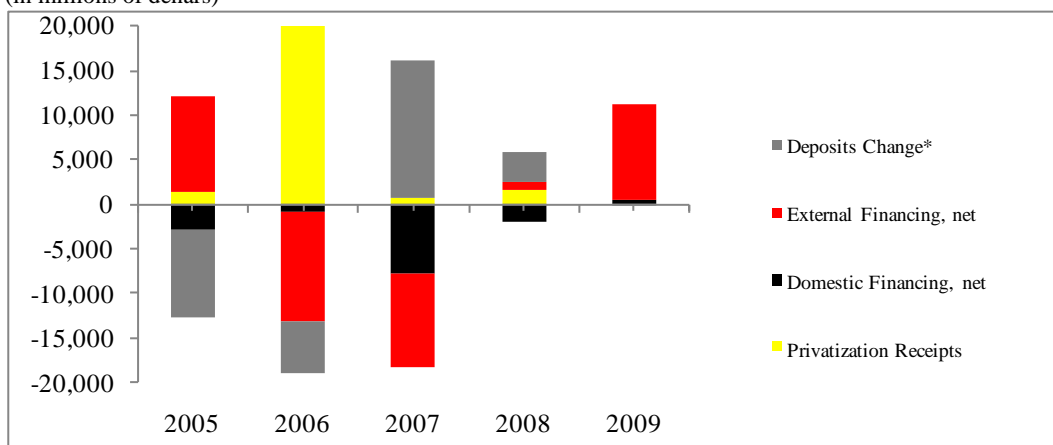
Figure 74
Quarterly distribution of capital expenses
(in millions of denars)



Source: Ministry of Finance of the Republic of Macedonia.

In 2009, the announced acceleration of capital spending failed to happen, taking account of the contracted economic activity and lower income. Thus, the capital spending was by one third lower compared to the preceding year, and most of their fall (or 61%) arises from the decrease in investments in fixed assets. Lower public investments, particularly those with predominant import component⁵⁵, had their effect on the import of investment goods, which also registered an annual fall of about 7%. Furthermore, although the two budget revisions made the largest downward correction of capital spending, yet, the investments in fixed assets registered the weakest performance compared to the plan (62.7%).

Figure 75
Financing the budget balance
(in millions of denars)



*positive change - deposit withdrawal, negative change - deposit accumulation.

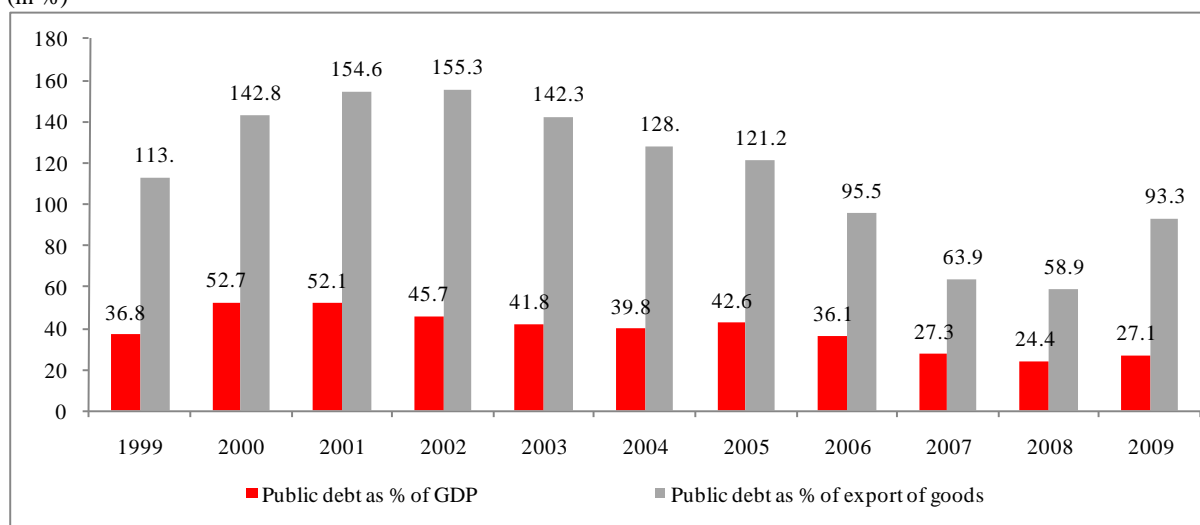
Source: Ministry of Finance of the Republic of Macedonia.

⁵⁴Source: SSO. According to the Labor Survey and NBRM calculations, the number of employees in public administration in the sectors of public administration and defense, education, health and social works and other utility services went up by 6,229 in 2009 compared to 2008.

⁵⁵ Source: Ministry of Finance, Amendments to the Budget of the Republic of Macedonia for 2009 (second revision)

Most of the budget deficit funding in 2009 was made through external net borrowing. The structure of sources of funding, however, was changing during the year. Thus, in the first half of the year, the external net borrowing was low. Notwithstanding the mobilization of assets on the financial market, the domestic net borrowing was negative, in line with the higher paid principal of structural⁵⁶ and continuous⁵⁷ bonds (regular payment based on bond for old foreign currency savings in April and denationalization bonds in June). Accordingly, the funding in this period was primarily made through the withdrawal of deposits with the NBRM. In environment of decrease in available funds, and given the lower performance of income than expected, *in July 2009, the Government borrowed funds from abroad by issuing a Eurobond in the amount of Euro 175 million.* In addition, further funding, particularly in the last quarter, was secured through domestic borrowing on the primary government securities market.

Figure 76
Public debt
(in %)



Source: Ministry of Finance of the Republic of Macedonia.

A yearlong trend of decreasing the public debt was interrupted in 2009. With the new borrowings, at the end of 2009 the total public debt⁵⁸ stood at 1,796.8 million, and compared to the preceding year it rose by Euro 211.6 million (or by 13.3%). In terms of GDP, public debt in 2009 increased by 2.7 percentage points compared to 2008 making up 27.1% of GDP⁵⁹, which is in line with the public debt management strategy⁶⁰. Most of the annual growth of public debt (88%) reflects the higher debt to foreign creditors, which increased its structural share in the total debt (by 2.1 percentage point). Most of the external debt is a central government debt based on issued Eurobond in the amount of Euro 175 million, whereas the remaining debt of the central government and the public enterprises are funds withdrawn from the World Bank, the EBRD and other creditors. The increase in the domestic debt results from the central government debt⁶¹ (annual rise of Euro 26.2 million), given the higher sale of treasury bills, partially offset by the payment based on structural shares (primarily payment of Bonds for old foreign currency savings).

⁵⁶ Structural bonds are long-term securities issued by the government in the reform process of restructuring the economy. These include bonds for denationalization, for old foreign currency savings, for privatization of Stopanska Banka, for selective credits. These securities are not issued on regular basis, i.e. they are intended for already known owners and are not of market nature.

⁵⁷ Continuous bonds are long-term government securities intended for the public and issued on regular basis at auctions.

⁵⁸ According to the amendments to the Law on Public Debt ("Official Gazette of the Republic of Macedonia" no. 88/2008) of July 2008, the calculation of the public debt is complied with the statistics of the government finances (of IMF), which, besides the debt of central government, funds, municipalities and public enterprises, also includes the NBRM debt. However, due to this analysis, public debt is considered only the debt of fiscal authority, excluding the debt of the monetary authority.

⁵⁹ GDP for 2009 follows the NBRM projection from January 2010.

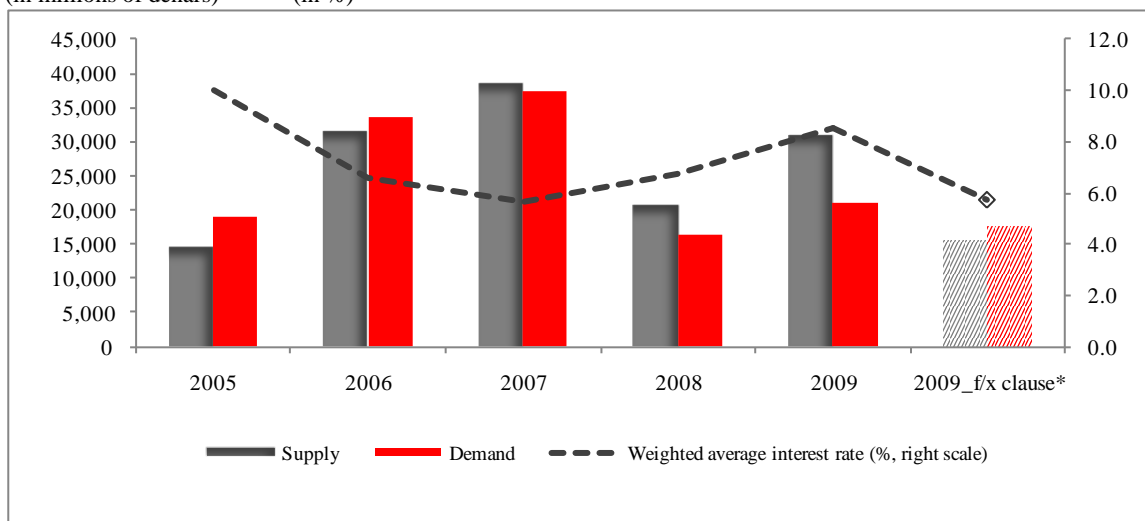
⁶⁰ Source: Ministry of Finance, "Public Debt Management Strategy of the Republic of Macedonia for 2009 to 2011 period" published in June 2009.

⁶¹ Domestic debt of central government includes structural and continuous securities.

Higher needs for budget funding in 2009 also caused movements on the primary market of government securities. In 2009, the performance of this market reached 7.8% of GDP, compared to 3.5% of GDP in 2008. The increase in the primary securities market operations reflects the increase in both supply of and demand for securities⁶² by 2.2 times and 2.3 times, respectively, compared to the preceding year. The market reported the most intense motion in the first half of the year, when the interest rate on bills with all maturities increased⁶³. Besides, in June 2009, the government started issuing currency indexed treasury bills. Thus the total supply of government securities (both currency indexed and non-indexed) exceeded the total demand by roughly 20%, with realization of over 80% of the demanded amount.

Figure 77

Total supply and demand for treasury bills and average weighted interest rate
(in millions of denars) (in %)



*"ci" refers to currency indexed treasury bills.

Source: NBRM and Ministry of Finance of the Republic of Macedonia.

Higher supply of than demand for government securities arises from the trends in the first half of the year, when the total supply exceeded the demand by 1.4 times, whereas in the second half, the demand exceeded the supply (by 5.7%). Taking into account the general environment of uncertainty, the preferences for short-term investments were evident during the year. One-month bills, issued in March and April 2009 were more attractive, with the demand exceeding the supply by almost 15%. On the other hand, the demand for two-year bond issued in February 2009 was low (the supply equaled Denar 250 million, with a coupon rate of 8.5%, while the demand was only Denar 10 million). The lower demand for government securities, particularly with longer maturities, partially reflects the macroeconomic uncertainty in the first half of the year which reported pressures for domestic currency depreciation. In such circumstances, and in order to increase the investors demand, in June 2009, the government started issuing a new instrument - currency indexed treasury bills. Although the offered interest rate on these bills was lower than the rate on non-currency indexed treasury bills, yet, the demand for these instruments, in each maturity (3-, 6- and 12-month) was high. Thus the total demand for currency indexed treasury bills exceeded the supply by roughly 14%, indicating the propensity of investors to invest in securities free of currency risk. Besides these government securities, April 2009 witnessed the issue of the Eight issue of denationalization bonds⁶⁴, in total amount of Euro 23 million, with a coupon rate of 2% p.a., and maturity of 10 years.

⁶² Government securities include treasury bills, two-year and three-year bonds, with the bonds having a minimum share.

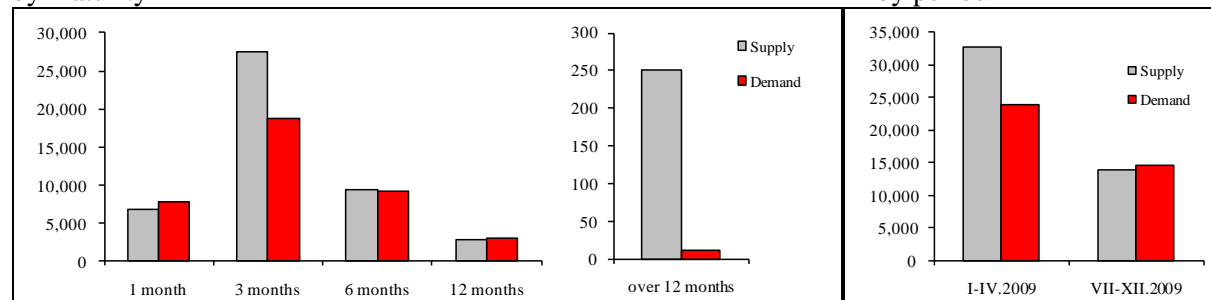
⁶³ Most of the government securities auctions conducted in the first half of 2009 were interest rate tender auctions.

⁶⁴ This issue of denationalization bonds includes all effective decisions on denationalization to December 31, 2008, where bonds were given as compensation. The nominal value of denationalization bond is the amount given to the claimant on the basis of denationalization as indemnification. Bonds are registered and in Euro, and are unrestrictedly transferable, and the nominal value of one bond equals one Euro.

Figure 78

Total supply of and demand for government securities (currency indexed and non-currency indexed)
(in millions of denars)

by maturity



Source: NBRM and Ministry of Finance of the Republic of Macedonia.

Annex 1

Anti-crisis fiscal measures

To abate the effects of the global economic recession, governments in many countries adopted sets of anti-crisis measures, including the Republic of Macedonia. **The first set of anti-crisis measures** was adopted in November 2008, with the total amount of fiscal stimulus to the domestic economy with this set of measures being valued at Euro 330 million. These measures were oriented towards companies with distorted liquidity and accumulated inherited problems, and to companies showing good performance. Measures included profit tax incentives, reduced customs duties and social contributions, reduced taxes for the farmers, etc.

Moreover, the Government adopted a eight-year Program for Realization of Infrastructure Projects as a **second set of measures**, in a total amount of roughly Euro 8 billion. It included projects in the field of road and railway infrastructure, energy sector, housing construction, environment, sports infrastructure and other capital projects. On the short run, the implementation of this Program will stimulate the economic growth, by supporting the construction sector, while on the long run, it will improve the competitiveness of the Macedonian economy.

The third set of anti-crisis measures, adopted in April 2009 included 70 anti-crisis measures oriented towards three segments:

1. **Budget revision** - change in revenues and expenses in line with the revised macroeconomic projections and the new circumstances. Most significant measures directed towards decreasing the budget spending within this segment include temporary ban on new employments in the public administration in 2009, control of employments through the agencies for temporary employments, deferral of the 10% increase in wages, cut of current expenses by 16%, on average, continuation of the ban on nonproductive expenses to the end of the year, decrease of current and capital expenses of public enterprises, recommendation for decreasing the outlays for the local administration, etc.
2. **Credit support to companies, i.e. direct support to small- and medium-size companies of the export sector and other sectors of the economy.**
The set of these measures includes four economy supporting programs:
 - Program for co-financing and guarantees for long-term investment credits and subsidizing interest rates;
 - Program for co-financing and guarantees for credits for working capital and subsidizing interest rates;
 - Program for subsidizing interest rates on short-term credits for working capital; and
 - Guarantees Program.

3. Other measures to support companies including:

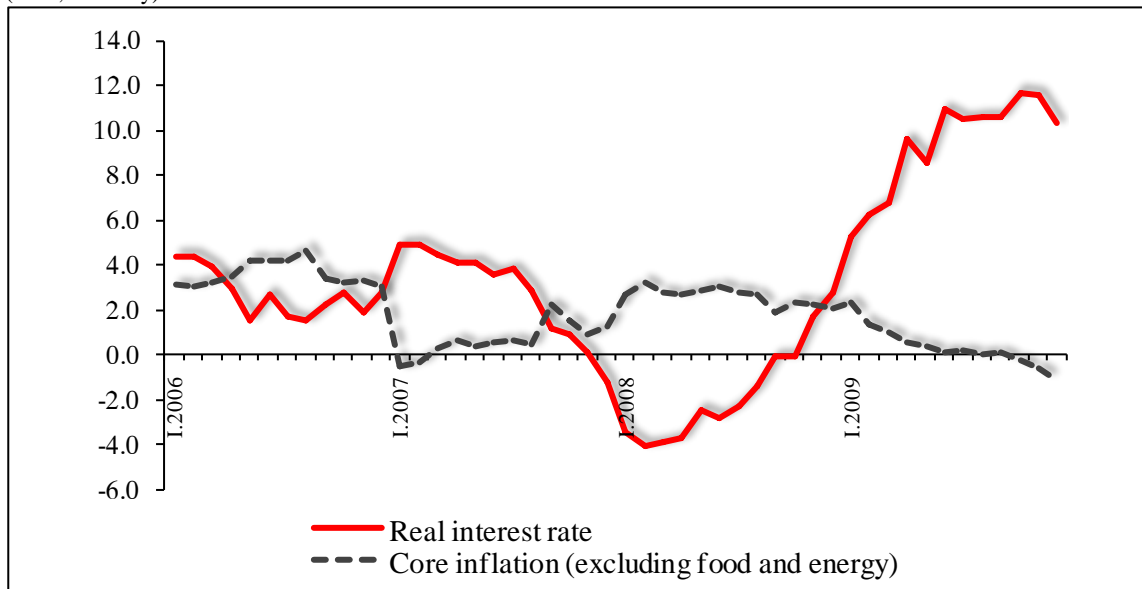
- 54 measures to simplify customs operations and prompt flow of goods at borders, within the II stage of the Regulatory Guillotine;
- accepting a dozen of measures proposed by chambers of commerce.
- accepting a part of the measures to support transporters.

III. Monetary policy

The monetary policy in 2009 was carried out in an environment of apparent risks and constant uncertainty about the transfer effects of the global financial and economic crisis on the domestic economy. The monetary implications of the crisis' first effects were serious depreciation pressures on the domestic currency. These pressures were concentrated in the first half of the year, when in conditions of growing trade deficit and negative expectations of the domestic entities, the demand for foreign exchange was continually exceeding the supply. In such circumstances and in conditions of strategy of fixed foreign exchange rate, in the first five months of the year the NBRM intervened on the foreign exchange market with a net sale of foreign currency. Such flows caused also monetary reaction by raising the basic interest rate and the banks' reserve requirement rate. Thus in March the basic interest rate went up from 7% to 9%, while in May Decision on increasing the banks' reserve requirement rate in foreign currency from 10% to 13%, and banks' liabilities with FX clause from 10% to 20% was adopted. **The monetary measures, as well as the better and less uncertain forecasts for the world economy since the beginning of the second half of the year, contributed for significant stabilization in the expectations and return of confidence in the Denar stability.** This, together with more intensive adjustment of the import demand and the positive trends with the capital flows enabled change in the movements on the foreign exchange market in the second half of the year, with the NBRM intervening with a purchase of foreign exchange from June till the end of the year. The positive movements in the second half of the year exceeded the expectations, and together with the estimates for stable external position in the following period created a room for monetary policy relaxation. At the end of November 2009, the basic interest rate of the NBRM went down by 0.5 percentage points.

The undertaken monetary measures in 2009 enabled maintenance of the foreign exchange rate stability. The reaction of the domestic entities to the negative shock since the beginning of the crisis in 2008 and in the first half of 2009, with conversion of the savings from domestic into foreign currency, showed that Macedonian economy still characterizes with tendency for managing with foreign exchange in conditions of uncertainty. On the other hand, the change in the negative trend in relatively short period and the new continuous monthly growth of the Denar deposits since August, emphasize the positive effect of conducting prudent monetary policy on the stabilization in the expectations. The maintenance of the foreign exchange rate stability, in conditions of significant external shocks, once again showed its significance for the Macedonian economy and prevented creation of larger internal and external misbalances.

Figure 79
Interest rate on CB bills and core inflation
(in %, annually)

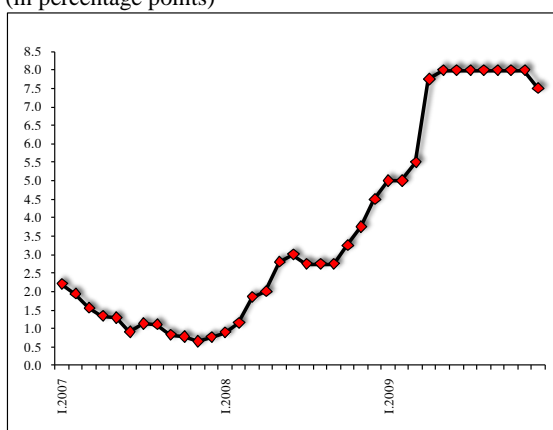


*Current month relative to the same month of the preceding year.

Source: National Bank of the Republic of Macedonia and State Statistical Office.

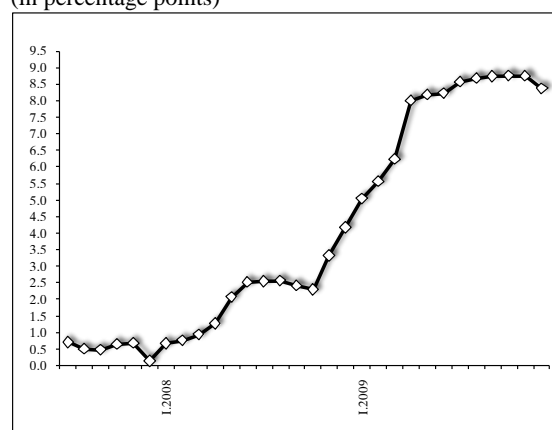
The price stability in 2009 was preserved, with the return of the core inflation into a zone of moderate positive changes being registered, after more apparent positive changes in 2008. On the other hand, the total inflation was negative (-0.8%), primarily as a reflection of the external factors. Namely, the severe change in the trends relative to 2008, mostly arises from the downward adjustment of the oil and food prices on the international market, which were the main inflation generator in the previous year. In 2009, under the influence of the global demand, the energy and food prices transformed into a source of apparent disinflationary tendencies in global terms and in the domestic economy.

Figure 80
Interest rate spread between the CB bills - 28 days and the ECM reference interest rate
(in percentage points)



Source: National Bank of the Republic of Macedonia, European Central Bank (www.ecb.int) and Central Bank of the Netherlands (www.statistics.dnb.nl).

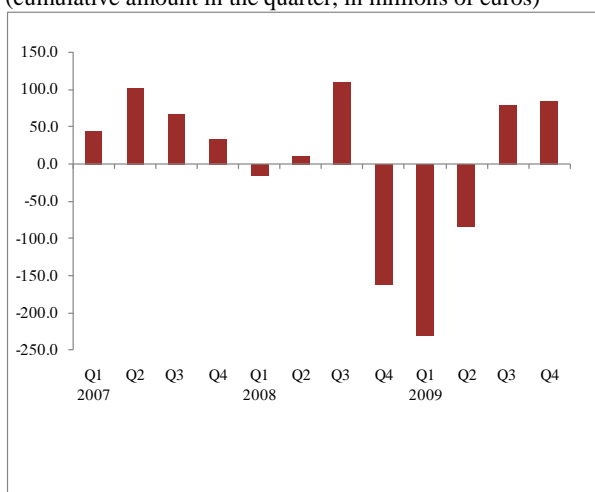
Figure 81
Interest rate spread between SKIBOR-one month and EURIBOR-one month
(in percentage points)



Different strategy layout of the monetary policies of the NBRM and the European Central Bank (ECB) was the reason for different monetary reaction to the global crisis blows. The divergent movements in the policies resulted in the widening of the interest rate spread between the yields based on domestic and foreign financial instruments. Higher yields of the

domestic financial instruments contributed to the decrease in the propensity for conversion of the domestic currency into a foreign currency and stabilization in the movements on the foreign exchange market in the Macedonian economy. ECB, as well as most central banks in the developed countries, reacted on the first blows of the recession, in the last quarter of 2008, with a monetary policy relaxation. Such an ECB reaction was motivated from the need for stimulation of the aggregate demand, and enabled by the significant calming down of the inflationary pressures in the Euro area. In the first half of 2009, ECB additionally lowered the basic interest rate in four turns and in May it reduced to 1%, a level that remained unchanged until the end of the year. The monetary policy relaxation had adequate reflection on the interest rate dynamics on the European Money Market, which in 2009, had generally a downward trend. Contrary to ECB, the basic interest rate adjustment of the NBRM was conditioned by the movements on the foreign exchange market, which despite the opening of the negative production gap and the stabilization of the inflation, imposed a need for monetary policy contraction in March in order to maintain the stability of the domestic currency. Such monetary reaction transferred to the domestic money market, stimulating growth in SKIBOR⁶⁵ in the second quarter. This interest rate continued to be maintained on stable level, close to the basic interest rate until the end of the year. In such conditions, the interest rate spread between the core interests of NBRM and ECB of 2.6 percentage points, as it equaled on average in 2008, reached 7.2 percentage points, on average, in 2009, which is close to the interest rate spread between the one-month SKIBOR and the one-month EURIBOR, which equaled 7.8 percentage points, on average (compared to 2.1 percentage points, on average in 2008).

Figure 82
NBRM interventions on the foreign exchange market with banks
(cumulative amount in the quarter, in millions of euros)

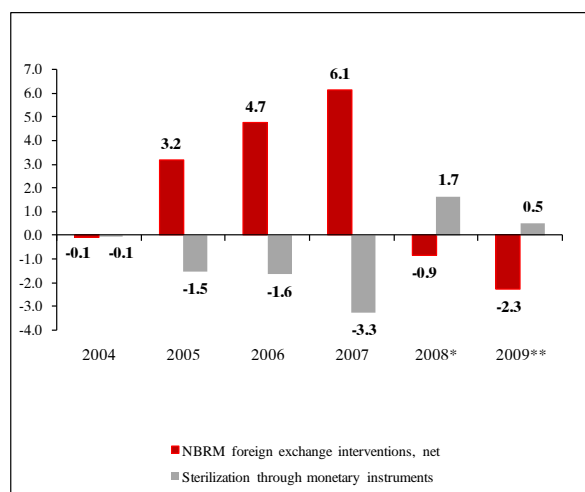


*Preliminary data for GDP.

**Estimated data for GDP.

Source: National Bank of the Republic of Macedonia.

Figure 83
Foreign exchange transactions and sterilization
(share in GDP, in %)



In 2009, the NBRM interventions on the foreign exchange market had synchronized dynamics with the changes in the macroeconomic trends in the economy. Since the beginning of the year, as a result of the depreciated global demand, given simultaneous slower adjustment of the domestic demand, the balance on the trade account continued to deteriorate, which in combination with the lower volume of capital inflows from abroad caused intensive depreciation pressures on the domestic currency. The foreign market destabilization was significantly influenced also by the worsen expectations of the economic agents regarding the stability of the foreign exchange rate (especially apparent in the period of the presidential and local elections in March), which stimulated higher propensity for management with foreign assets. This can be perceived through the significant increase in the demand for foreign exchange on the foreign exchange and the currency exchange market and

⁶⁵ Interbank interest rate for selling Denar deposits, calculated from the quotations of the reference banks.

the intensive growth in the banks' foreign assets in the first quarter. **Such movements resulted in strong pressure on the foreign reserves and extensive NBRM interventions on the foreign exchange market towards net sale of foreign assets, which equaled about 5.1% of the GDP, cumulatively, in the first five months of the year. The first changes in the trends on the foreign exchange market were evident in June, when NBRM commenced intervening with a net purchase of foreign assets.** The stabilization in the expectations and intensified adjustment of the import demand enabled positive gap between the supply of and the demand for foreign exchange. **In such conditions, the interventions with purchase of foreign assets continued to the end of the year, acting towards liquid assets creation.** Analyzed on annual basis, through the NBRM interventions on the foreign exchange market (net-sale of foreign assets in the transactions with banks), in 2009 liquid assets in the total amount of 2.3% of the GDP were withdrawn, which had adequate reflection on the dynamics of the monetary instruments, through which liquidity of 0.5% of the GDP was created. Analyzed by the dynamics, the annual change of the CB bills towards liquidity creation in the banking system is almost completely due to the intensive drop in the CB bills in the first quarter. Namely, the especially high risks evident in this period stimulated the demand for foreign exchange, which resulted in significantly lower interest of the banks to invest in CB bills. The increase in the basic interest rate in the NBRM and the interventions by increasing the reserve requirement allocation rate contributed to the stabilization in the expectations, with the banks once more focusing their interest on the CB bills. Thus in the remaining three quarters of the year, the influence of the CB bills was in conformity with their core function of liquid assets withdrawal.

Table 14
Flows of liquidity creation and withdrawal*
(in millions of denars)

	Balance as of 31.12.2008	Changes by quarters				Total	Balance as of 31.12.2009
		Q.1	Q.2	Q.3	Q.4		
Banks' liquidity (banks' account with the NBRM)	10,288	-1,465	458	3,331	1,632	3,957	14,245
<i>Liquidity creation</i>						3,975	
1. Net foreign assets	90,953	-13,706	-4,076	15,825	4,250	2,293	93,246
2. Net domestic assets	-59,866	8,708	4,090	-12,146	-305	347	-59,520
<i>of which:</i>							
CB bills	-17,451	10,542	-2,745	-2,975	-3,233	1,589	-15,862
Compulsory deposit with NBRM	-1,528	1,288	-84	55	99	1,358	-170
Foreign exchange deposit with NBRM	0	-602	-2,233	217	1805	-814	-814
Government Denar deposits with NBRM	-9,208	-3,236	8,959	1,946	-1,236	6,434	-2,775
Government Foreign currency deposits with NBRM	-3,126	671	495	-10,037	2,080	-6,791	-9,917
Other items, net	-29,871	43	-303	-1,349	156	-1,453	-31,324
3. Currency in circulation	17,601	2,955	436	-246	-1,810	1,335	16,266
<i>Liquidity withdrawal</i>						-18	
1. Banks' cash in vaults	3,198	577	8	-101	-503	-18	3,216

* Positive change - liquidity creation; negative change - liquidity withdrawal.

Source: National Bank of the Republic of Macedonia.

The dynamics of the government Denar deposits with the NBRM during the year was primarily conditioned by the availability of the sources of financing of the budget balance, which was negative almost during the entire year. Thus in the first half of the year, the registered budget deficit was almost completely financed from domestic sources of financing, with the first quarter being dominated by the Treasury bills, and in the second quarter the financing fell on the government Denar deposits with the NBRM. From a flow of liquidity withdrawal in the first quarter, in the second quarter the Government represented dominant flow of liquid assets creation. The financing structure of the budget balance changed significantly in the third quarter, when inflows based on the Eurobond were realized (in the amount of Euro 175 million), which enabled high rise in the government foreign currency deposits with the NBRM. The government Denar deposits in this quarter went down, but in significantly smaller volume in comparison with the second quarter, and in the last quarter they augmented, acting towards liquid assets withdrawal. **Annually, the government Denar deposits with the NBRM declined, thus acting towards liquid assets creation in the banking system. The**

liquidity creation was carried out also through the currency in circulation, which followed the common seasonal dynamics during the year, but registered a decrease on annual basis.

Table 15
NBRM survey
(in millions of denars)

	Balance as of	Changes by quarters				Total	Balance as of
	31.12.2008	I	II	III	IV		31.12.2009
Reserve money ^{1/}	31,087	-4,998	14	3,679	3,945	2,640	33,727
Currency in circulation	17,601	-2,955	-436	246	1,810	-1,335	16,266
Banks' account with NBRM	10,288	-1,465	458	3,331	1,632	3,957	14,245
Banks' cash in vaults	3,198	-577	-8	101	503	18	3,216
Net foreign assets	90,953	-13,706	-4,076	15,825	4,250	2,293	93,246
Foreign assets	91,908	-13,711	-4,292	19,634	4,269	5,899	97,807
Foreign liabilities	955	-6	-217	3,809	19	3,606	4,561
Net domestic assets	-59,866	8,708	4,090	-12,147	-304	348	-59,520
1. Credit to banks, net	-18,965	11,230	-5,062	-2,703	-1,329	2,136	-16,829
- credit	14	2	0	0	0	2	16
-instruments ^{2/}	-18,979	11,228	-5,062	-2,703	-1,329	2,134	-16,845
2. Net Government position with NBRM	-11,030	-2,564	9,454	-8,095	870	-335	-11,365
-Claims on Government	1,304	1	0	-4	26	22	1,327
-Government deposits	-12,334	-2,565	9,454	-8,090	844	-357	-12,692
3. Other items, net	-29,871	43	-303	-1,349	156	-1,453	-31,324

1/ Without reserve requirement on foreign currency deposits.

2/ It includes CB bills, compulsory deposit with NBRM and foreign currency deposit with NBRM.

Source: National Bank of the Republic of Macedonia.

At the end of December 2009 compared to the end of the preceding year, the reserve money⁶⁶ went up by 8.5%, which in conditions of annual decrease in the demand for cash is completely due to the higher level of the banks' liquid assets. Thus the banks' Denar liquid assets registered high annual increase of 38.5%, which is a combined effect of the increase in the total deposit potential of the banks (as a basis for reserve requirement allocation) and higher reserve requirement for the banks' liabilities with foreign currency component, which became effective since July 2009⁶⁷. Analyzed from the aspect of the NBRM balance sheet, the higher level of reserve money, annually, was dominantly determined by the net foreign currency assets of the NBRM. Namely, the realized high inflows based on issued Euro bond in July and the allocation of SDR in August and September, together with the registered net purchase of foreign exchange on the foreign exchange market by the NBRM in the second half of the year, completely neutralized the effects of the high net sale of foreign exchange on the foreign exchange market by the NBRM in the five months of the year. The increase in the net foreign assets of the NBRM was contributed by the banks' reserve requirement in foreign currency, as well as the foreign currency deposit, as new instrument of the NBRM. Although with significantly lower volume, the net domestic assets, also represented flow of reserve money creation, mainly as a reflection of the lower level of monetary instruments.

3.1. Monetary instruments

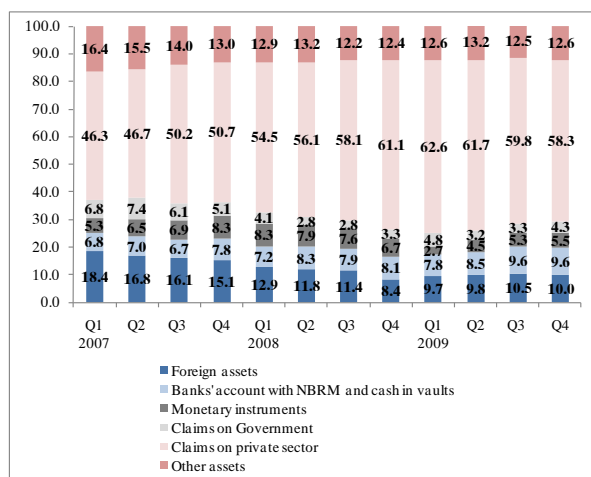
In 2009, the changes in the monetary instruments layout were directed towards maintenance of the foreign exchange rate stability, i.e. the price stability. The changes in the macroeconomic trends conditioned a multidirectional reaction with the monetary instruments in the first and the second half of the year. Thus in conditions of increasing external misbalance since the beginning of the year, for the purpose of redirecting the Denar liquidity from the foreign exchange market and calming down of the domestic currency depreciation pressures, **on March 26, 2009 the NBRM adopted a decision on increasing the interest rate of the basic monetary instrument (CB bills) from 7% to 9%.** The change in the interest for CB bills in the first quarter, when the demand

⁶⁶ It pertains to the reserve money without reserve requirement on foreign currency deposits. By inclusion of this component, and in conditions of higher reserve requirement of the banks' liabilities in foreign currency, the increase in the reserve money in December 2009 compared to the end of the previous year is higher and it equals 12.4%.

⁶⁷ In conformity with the NBRM Decision on reserve requirement dated May 2009, part of the amount obtained by applying the reserve requirement rate of the liabilities in foreign currency is allocated in Denars..

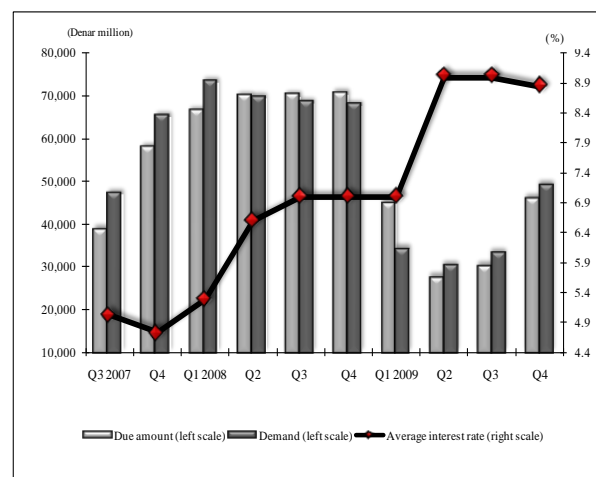
for CB bills was lower by 23.6% compared to the due amount, signaled significant increase in the banks' interest for foreign exchange. The same can be perceived also through the changes in the structure of the banking book, where in the first quarter significant drop in the share of the monetary instruments in the banks' total assets was registered, for the account of other financial instruments (government securities⁶⁸, placements with the private sector and foreign assets with foreign commercial banks). In such conditions, in environment of evident negative expectations for the foreign exchange rate, the attractiveness of the CB bills increased with the rise in the interest rate. In the second quarter, the demand for CB bills was higher by 10% compared to the due amount, which transferred to the foreign exchange market through calming down of the pressures for depreciation of the domestic currency. The interest for investment in CB bills by the banks continued to maintain on a relatively high level also in the second half of the year, which can be explained, to certain extent, with the lower propensity of the banks to expose to risks during a period of reduced economy and uncertainty about the future movements, as well as the exclusively low yield from the foreign assets in foreign banks. Annually, the CB bills represented a flow of liquidity creation in the banking sector in the total amount of Denar 1,589 million. **With the improvement of the situation and the forecasts for both global and domestic economy, which had positive effect on the external position and expectations, on November 30,2009 NBRM adopted a decision on reducing the CB bills interest rate from 9% to 8.5%.**

Figure 84
Structure of the banks' total assets
(end of period, in %)



Source: National Bank of the Republic of Macedonia.

Figure 85
Due amount, demand and interest rate on CB bills
(averages in the quarter)



In May 2009, NBRM adopted a decision on increasing the reserve requirement allocation rate on the banks' liabilities in foreign exchange and Denar liabilities with FX clause. For the purpose of banks' adjustment to larger allocation of reserve requirement, gradual increase was made, i.e. in July the liabilities rate in foreign currency went up from 10% to 11.5% and the liabilities rate in domestic currency with FX clause from 10% to 20%, and in August the liabilities rate in foreign currency augmented from 11.5% to 13%. Part of the amount obtained as a result of the higher reserve requirement allocation rate in foreign currency is allocated in Denars. Simultaneously, the amendments to the decision on the reserve requirement enabled the banks to use fully the reserve requirement assets allocated in Denars for satisfying their daily liquidity needs. Additionally, amendments to the Decision on managing banks' liquidity risk were made, thus enabling banks to include their placements in the NBRM instruments, except to the allocated reserve requirement in Euros, in meeting the required minimal level of Denar or foreign currency liquidity. Such changes were directed towards distimulation of the demand for foreign exchange. Namely, also though the basic interest rate partially stabilized after its increase in March, however, the NBRM interventions

⁶⁸ In the first quarter of 2009 the Ministry of Finance increased the value of the individual auctions of Treasury bills, with in March new financial instrument in form of one-month Treasury bills in Denars being introduced.

were directed towards net sale of foreign assets also in April and May. The effects of the adjusted behavior of the economic agents were evident in the second half of the year, when trend of foreign assets accumulation by the banks⁶⁹ ceased, and when the process of currency conversion of the households' savings from domestic into foreign currency began to lose its intensity.

At the end of the calculation period, the bank in 2009 allocated, on average, 2.7% over the reserve requirement (in Denars)⁷⁰, which is close to the average registered in the previous year (3.8%). In conditions of constant maintenance of the liquidity in the banking system on satisfactory level, no Lombard credits in 2009 were used⁷¹. With the increase in the basic interest rate, the interest rate on Lombard credits incremented from 8.5% to 10.5% in March.

In January 2009, NBRM widened the set of instruments by introducing auctions of banks' foreign currency deposits with the NBRM. The instrument was primarily aimed at diversification of the instruments offer in the domestic economy, enabling fulfillment of the minimal level of liquid assets⁷². Thus in conditions of unstable movements on the international financial markets and growing risk, the domestic banks were enabled to reduce the credit risk through investments in foreign currency deposits with NBRM. The interest rates on the foreign currency deposits placed with NBRM are equal to the interest rates on the deposits placed with the central banks in the Euro area, in the international financial institutions or to the yields arising from the Treasury bills of the Euro area member states. The auctions of the foreign currency deposits in 2009 were held according to the "volume tender" principle (unrestricted) and interest rates that reflect the movements of the yields in non-risk bearing instruments on the international financial markets. However, out of the four offered maturities (1, 3, 6 and 12 months), during the year, the banks were interested in placement of foreign currency deposits with NBRM with maturity of one month, while in November, one transaction with maturity of up to three months was realized, with total amount of Euro 13.3 million being withdrawn through this instrument, on a cumulative basis.

Annex 2

Chronology of the measures undertaken by NBRM in 2009

01 January 2009

1. The Decision on managing bank' liquidity risk, adopted on December 25,2008 was enforced, introducing requirement for the banks to maintain certain minimal level of liquid assets for covering the liabilities that fall due in the following 30 and 180 days, separately in Denars and in foreign currency.

February 01,2009

The Decision on the foreign currency deposit with the National Bank (adopted on December 25,2008) which in conditions of unstable movements on the international financial markets and growing risks, the domestic banks were enabled to reduce the credit risk through investments in foreign currency deposits with NBRM.

⁶⁹ Lower banks' propensity for accumulation of foreign assets in the second half of the year can partially be explained with the amendments to the Decision on managing banks' liquidity risk (from May 2009) which enable banks to include their placements in NBRM instruments, except the allocated reserve requirement in Euros, in the fulfillment of the required minimal level of Denar and foreign exchange liquidity.

⁷⁰ The period for maintaining (fulfilling) the banks' reserve requirement covers the period from the 11th in the current month to the 10th in the following month. The excess pertains to funds allocated to the banks' accounts with NBRM over the reserve requirement period.

⁷¹ Collateralized short-term credits for overcoming the temporary liquidity problems of the banks, entering the monetary instruments group - available instruments ("standing facilities").

⁷² In conformity with the Decision on the banks' liquidity management ("Official Gazette of RM" no. 162/2008).

March 26,2009

NBRM adopted a decision on increasing the interest rate on the CB bills from 7% to 9%.

March 26,2009

NBRM adopted a decision on increasing the interest rate on the Lombard credit from 8.5% to 10.5%.

May 28,2009

The NBRM Council adopted new Decision on the banks' reserve requirement and Decision on amending the Decision on managing banks' liquidity risk. The Decision on the reserve requirement enabled increase in the reserve requirement allocation rate for the banks' liabilities with foreign currency component, which became effective in July 2009 (increase in the liabilities rate in foreign currency from 10% to 11.5% and liabilities rate in domestic currency with FX clause from 10% to 20%), i.e. August 2009 (increase in the liabilities rate in foreign currency from 11.5% to 13%). Part of the amount obtained by applying the reserve requirement allocation rate for liabilities in foreign currency is met in Denars. Simultaneously, the Decision enabled the banks full use of the assets of the reserve requirement allocated in Denars for satisfying their daily liquidity needs. The amendments to the Decision on managing banks' liquidity risk enables banks to include their placements in NBRM instruments, except to the reserve requirement in Euros, regardless whether they are placements in Denars or in foreign currency, in the calculations of the rates for determining the necessary minimum of Denar or foreign currency liquidity.

October 15,2009

NBRM adopted a Decision on amending the Decision on the reserve requirement, prescribing the remuneration rate on the reserve requirement in Euros to equal 0.01%, annually.

November 30, 2009

NBRM adopted a decision on decreasing the interest rate on the CB bills from 9% to 8.5%.

November 30, 2009

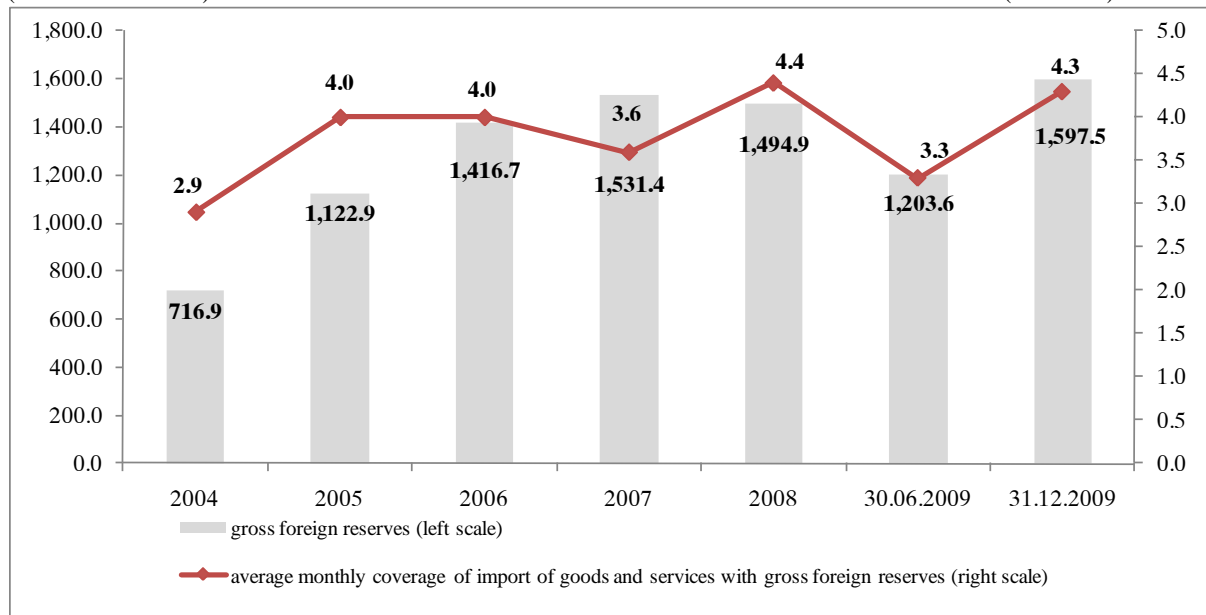
NBRM adopted a decision on decreasing the interest rate on the CB bills from 10.5% to 10%.

3.2. Foreign reserves and foreign exchange rate

On December 31,2009, the foreign reserves stock equaled Euro 1,597.5 million, which is an increase of Euro 102.6 million compared to the end of the preceding year. This level ensures coverage of the import of goods (f.o.b.) and other services for the period of 4.3 months of the following year. During the year, the foreign reserves were evidently variable and conditioned by several factors, such as the movements in the external sector, changes in the expectations of the economic agents and the reaction to the monetary and fiscal policy. In the first half of the year the foreign reserves registered a continuous decrease, which meant also larger external sensitivity of the economy, while in the second half of the year the foreign reserves moved upward.

Figure 86

Gross foreign reserves and monthly coverage of the import of goods (f.o.b.) and services from the following year with gross foreign reserves*
(in millions of euros) (in months)



*data pertaining on the import of goods (f.o.b.) and services from the following year for the period 2005 - 2009 are given according to the realized amounts, while for 2010 they are projected.

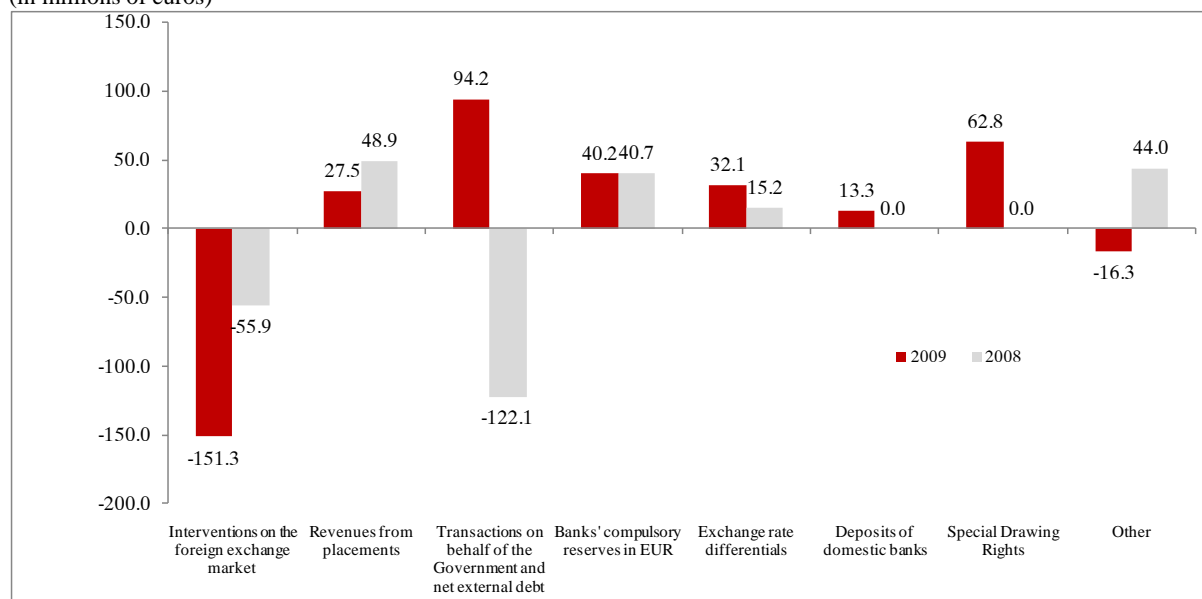
Source: National Bank of the Republic of Macedonia.

The NBRM interventions on the foreign exchange market in 2009 with net sale of foreign exchange significantly influenced on the change in the foreign reserves, and contributed to the maintenance of the stability of the nominal exchange rate. Although analyzed on annual basis, the NBRM interventions on the foreign exchange market acted towards foreign reserves reduction, however, in the second half of the year, they represented a flow of the foreign reserves growth. From the aspect of the foreign exchange rate, after the initial decline to the level of Denar 61.4 per one Euro in November 2008 (from Denar 61.2 per one Euro as it equaled, on average, in the January - October 2008 period), in the first quarter of 2009 the foreign exchange rate of the Denar relative to the Euro, maintained almost in continuity on this level. In such conditions, in order to maintain balance on the foreign exchange market and preserve the stability of the foreign exchange rate, in the first five months of the year the NBRM intervened with significant net sale of foreign assets in the total amount of Euro 333.9 million, or 5.1% of the GDP. The changes in the monetary policy made in March and May contributed to ease the pressures on the foreign exchange market until the end of the second quarter. In the second half of the year characterized with stable movements on the foreign exchange market and NBRM interventions towards net purchase of foreign assets. The Denar exchange rate relative to the Euro stabilized and in the second half of the year it equal Denar 61.2 per one Euro, on average. During the entire 2009, the average foreign exchange rate of the Denar relative to the Euro on the foreign exchange market equaled Denar 61.3 per one Euro, which is identical to the average registered in the preceding year. On the currency exchange market, average of Denar 61.5 per one Euro was traded, which compared to the average registered in the previous year is minimal depreciation of 0.1%.

Figure 87

Factors of change of the gross foreign reserves in 2008 and 2009

(in millions of euros)



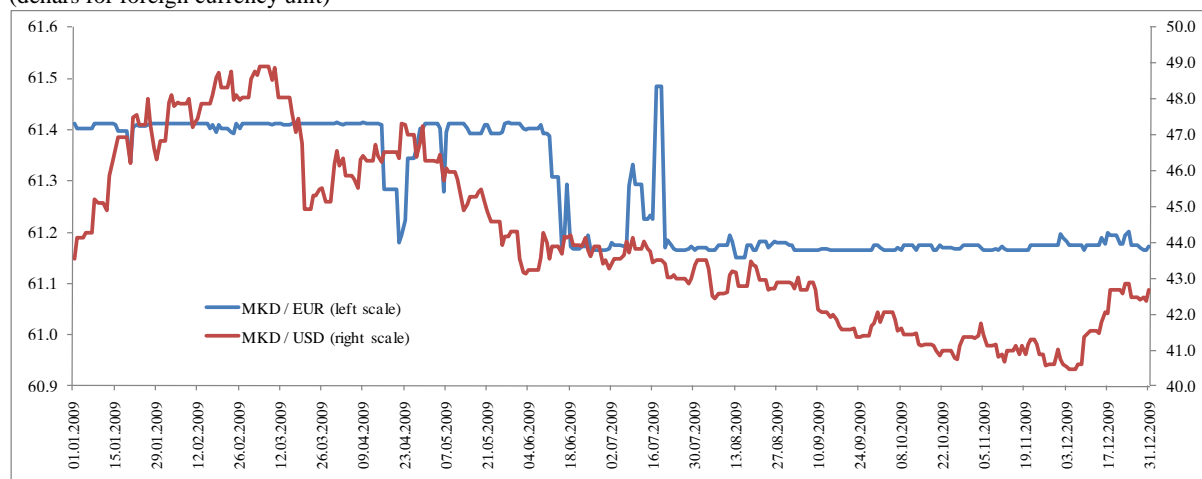
Source: National Bank of the Republic of Macedonia.

In 2009, the general appreciation of the Euro relative to the US Dollar had adequate reflection on the Denar foreign exchange rate relative to the US Dollar. Despite the variability, the tendencies were directed to the strengthening of the value of the domestic currency relative to the US Dollar, with the highest value being reached at the beginning of December 2009. In such conditions, the average Denar foreign exchange rate relative to the US Dollar on the foreign exchange market in December 2009 equaled Denar 41,81 per one US Dollar, which is an appreciation of 8.6% compared to December 2008. However, in comparison with the average registered in 2008 (which equaled Denar 41.9 per one US Dollar), in 2009 the value of the Denar relative to the US Dollar declined (on average by 5.3%, annually), with Denar 44.1 per one US Dollar on average being traded. Such change is due to the significantly higher value of the US Dollar compared to the Euro in the second half of 2008. Similar movements were registered also on the currency exchange market, where Denar 44.2 per one US Dollars were traded, on average.

Figure 88

Nominal foreign exchange rate of the Denar relative to the Euro and the US Dollar on the foreign exchange market

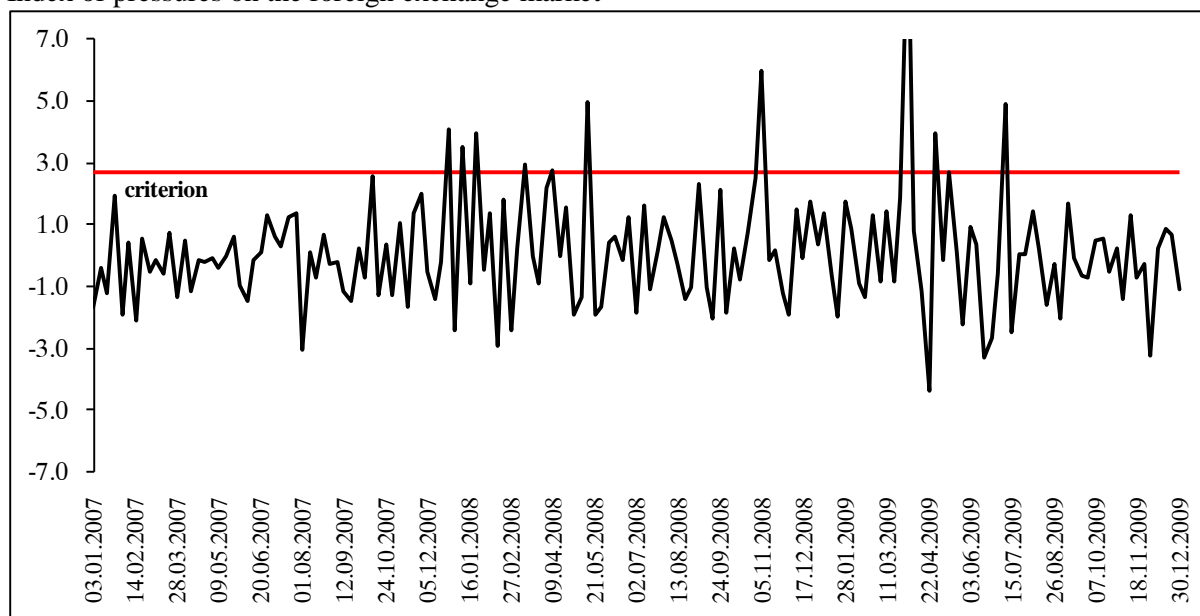
(denars for foreign currency unit)



Source: National Bank of the Republic of Macedonia.

According to the FX market pressure index⁷³, the signals for the pressures on the foreign reserves were concentrated in the first half of the year, when the critical threshold has been overcome in three occasions (out of the total 52 observations). A signal for pressures on the foreign exchange market was registered also in July 2009, which is due to the change in the level of the foreign exchange rate. However, the largest portion of the signals arises from the pressures for depreciation of the domestic currency, while only one of the signals reflects the rise in the basic interest rate of the NBRM as a result of the pressures on the foreign exchange market (in March by 2 percentage points, which became effective on the first CB bills auction held in April).

Figure 89
Index of pressures on the foreign exchange market*



*Value over the criterion (2.69), means pressure on the foreign exchange market.

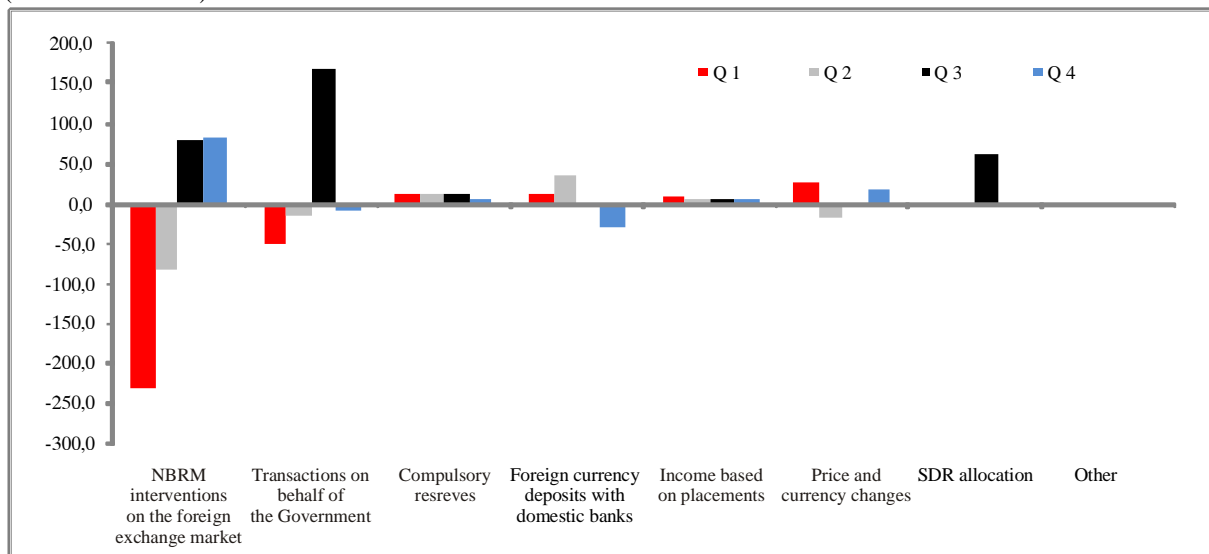
Source: National Bank of the Republic of Macedonia.

Significant contribution towards increase in the foreign reserves accounts for the Government foreign currency deposits with the NBRM, especially after the debiting with the Eurobond on the international financial market. The inflows based on the Eurobond were realized in July 2009, in the total amount of Denar 175 million and until the end of the year they mostly retained on the foreign exchange account of the Government with the NBRM, which was significant support to the foreign reserves. However, also by isolating this effect and the effect of the outflows for regular servicing of the liabilities based on external debiting, the dynamics of the foreign exchange outflows from the Government's account in 2009 points to smaller pressure of the public consumption on the misbalance in the balance of payments, compared to 2008. This corresponds to the changes in the total budget expenditures, which in 2009 went down annually by 0.6%, compared to 2008, when annual increase of 19.4% was registered. The position of the foreign reserves was additionally intensified with the SDR allocation⁷⁴ in August and September, with total amount of Euro 62.8 million.

⁷³ EMP index is composite of the percentage changes in the interest rate on the CB bills, the nominal Denar-Euro exchange rate and the foreign exchange transactions of the NBRM, i.e. $EMP_{mk} = \alpha\% \Delta ER_{mk/eur} + \beta \Delta MMIR - \lambda\% \Delta (FXT / MO)$, where $R_{mk/eur}$ is nominal foreign exchange rate MKD/EUR, MMIR is the average weighted interest rate of the CB bills and FXT/MO is the correlation between the NBRM interventions on the foreign exchange market and reserve money. The exceeding of the critical threshold points to pressures on the foreign exchange market, which are manifested through larger NBRM interventions on the foreign exchange market, larger changes in the interest rates, as a respond to the movements on the foreign exchange market, or larger changes of the nominal foreign exchange rate.

⁷⁴ Special Drawing Rights.

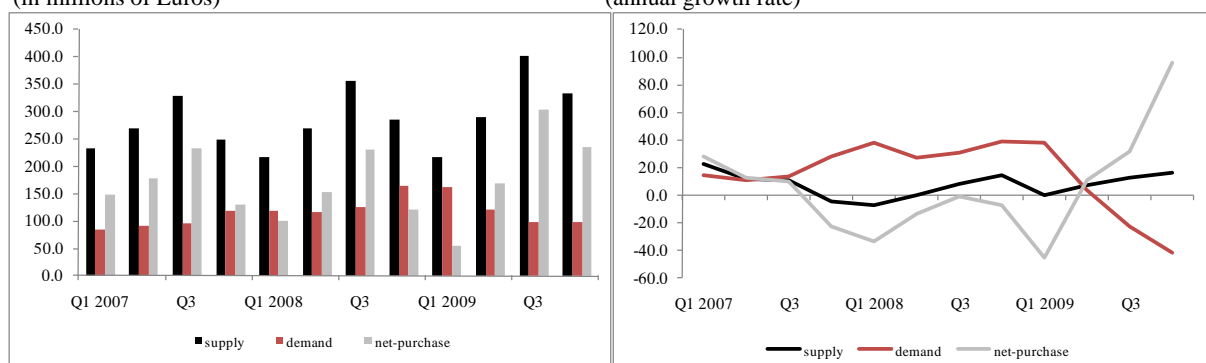
Figure 90
Quarterly distribution of the factors of change of the gross foreign reserves in 2009
(in millions of euros)



Source: National Bank of the Republic of Macedonia.

The macroeconomic movements in the Macedonian economy in 2009, as well as the changes in the global ambient also in the expectations of the domestic entities, reflected directly on both the foreign exchange and the currency exchange market. Thus since the beginning of the year, in conformity with the unfavorable trends in the external sector and deteriorated expectations of the domestic entities, the level of the net purchase of the currency exchange operations maintained low, and in March, for the first time since 2001 net sale of foreign assets on the currency exchange market was realized. Namely, in this period, in conditions of larger uncertainty about the impact of the effects of the crisis and simultaneous maintenance of the elections in March, the psychological pressures with the households intensified. This resulted in higher preferences for conversion of the Denar assets in foreign currency, which was reflected through the higher demand and lower supply of foreign exchange on the currency exchange market. The constant NBRM interventions with sale of foreign exchange on the foreign exchange market and increase in the basic interest rate in March resulted in stabilization also on the currency exchange market in April, when new net purchase of foreign assets was registered. The same tendency continued until the end of the year, with usually, the highest net purchase being registered in July and August. For the entire 2009, net purchase of foreign exchange in the amount of Euro 763.8 million was registered, which is an increase of 26.7% compared to the previous year, while the realized turnover reached Euro 1,721.9 million (annual rise of 4%).

Figure 91
Dynamics of the components on the currency exchange market
(in millions of Euros) (annual growth rate)

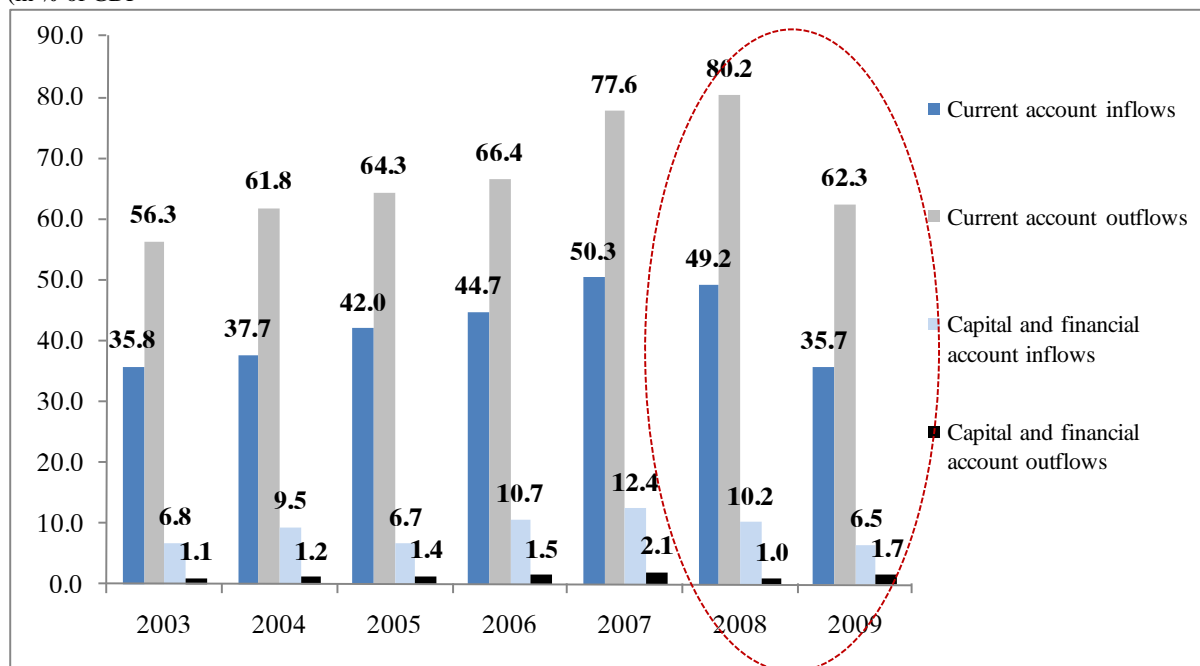


Source: National Bank of the Republic of Macedonia.

On the currency exchange market, in 2009 turnover in the amount of Euro 6,137.9 million was registered, which is a decrease of 10% compared to the previous year. The turnover of the "banks-enterprises" segment registered an annual decrease, given the registered drop also on the side of both the demand and the supply of the foreign exchange. Such movements correspond to the changes in the flows in the balance of payments, related to the trade and financial transactions of the enterprises. Thus compared to the previous years, when the value of the realized transactions of the corporate sector with other countries was generally increasing, in 2009 it registered a decrease, which had adequate reflection on the foreign exchange market.

Figure 92

Dynamics of the flows in the balance of payments related to the transactions of the corporate sector* (in % of GDP⁽¹⁾)



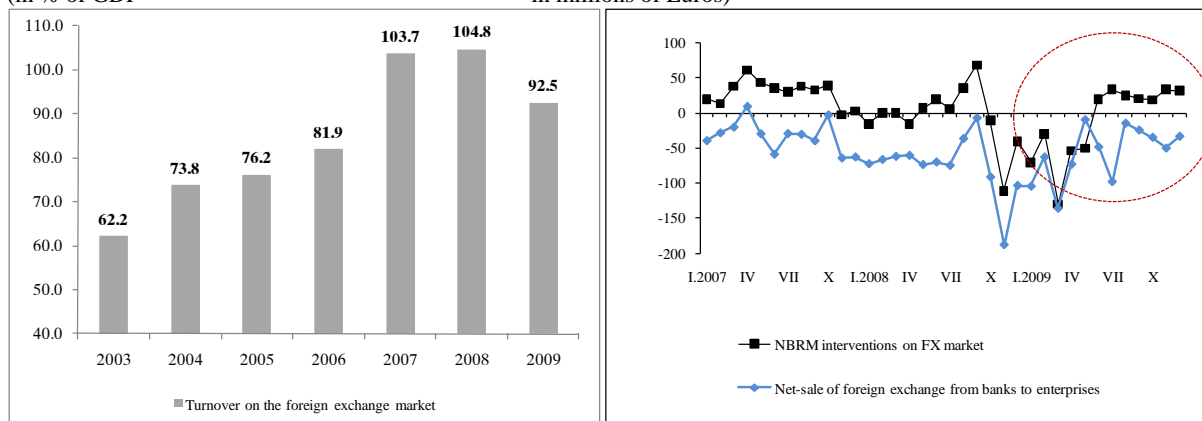
*Inflows based on export of goods (f.o.b.), inflows based on export of transport services and other services (without government and other personal, cultural and recreational services), inflows based on income from direct investments, income from portfolio investments of other sectors and income from other investments of other sectors; the outflows from the current account include: outflows based on import of goods (f.o.b.), outflows based on transport services and other services (without government and other personal, cultural and recreational services), outflows from income from direct investments, income from portfolio investments of other sectors and income from other investments of other sectors; incomes from capital and financial accounts include: income based on direct investments, net, liabilities based on portfolio investments of other sectors, liabilities based on other investments of other sectors (without loans and currencies and deposits) and utilization of short-term and long-term loans by other sectors; outflows from capital and financial account include: assets based on portfolio investments of other sectors, assets based on other investments of other sectors (without loans and currencies and deposits) and repayment of loans by other sectors.

⁽¹⁾ Preliminary data on GDP for 2008 and estimated data for GDP for 2009.

Source: National Bank of the Republic of Macedonia.

Consequently, in 2009, the banks realized net sale of foreign exchange with other private sector in the amount of Euro 687.4 million, which is less by 24.3% compared to 2008. However, the reduced export and the late adjustment of the import demand, the decrease in the private transfers and the capital inflows, as well as the higher propensity of the banks to strengthen the foreign currency position since the beginning of the year (partially due to the NBRM Decision on managing banks' liquidity risk) in the first five months of the year resulted in a lack of foreign exchange on the foreign exchange market' interbank segment, which imposed a need of NBRM interventions towards net sale of foreign assets.

Figure 93
 Movements on the foreign exchange market
 (in % of GDP¹) (in millions of Euros)



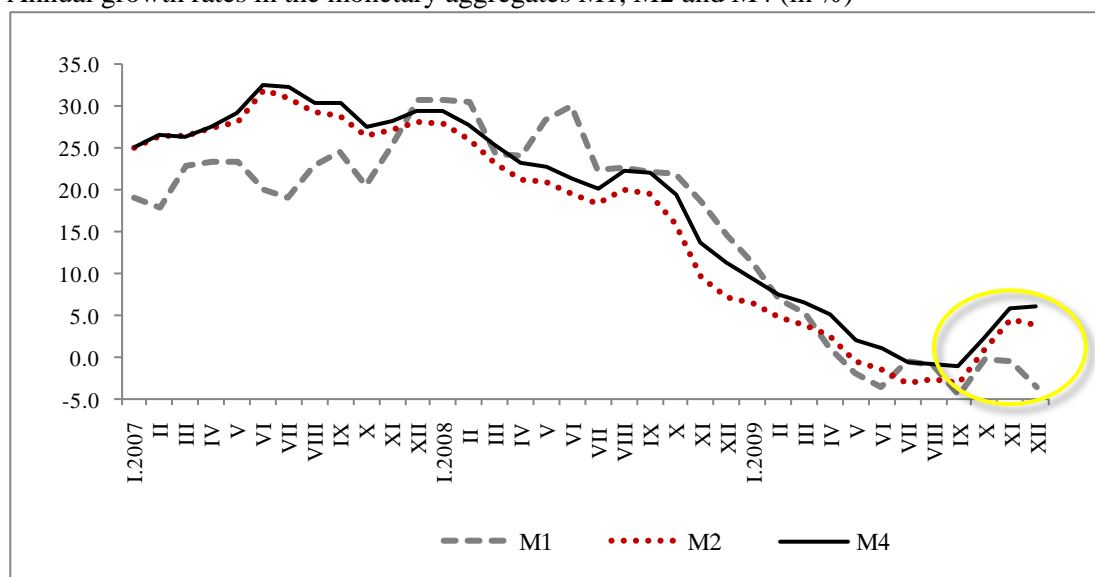
¹ Preliminary data on GDP for 2008 and estimated data for GDP for 2009.

Source: National Bank of the Republic of Macedonia.

3.3. Monetary aggregates

In 2009, the change in the trends in the real and external sector, as a result of the global crisis, had apparent transmission effects also on the monetary growth. Thus the annual growth in the broad money supply M4 at the end of the year equals 6%, which is the lowest growth rate in the last six years. The growth impediment in the money supply was especially evident in the first half of the year, which corresponds to the movements in the real sector, with the position of the balance of payments in this period and still present uncertainty and lower propensity for saving in the banking system being registered. Simultaneously, the structure of the currency portfolios continued to change towards higher significance of the foreign exchange saving. In the second half of the year the expectations significantly stabilized, the current account deficit plunged and capital inflows increased. These positive trends meant also new acceleration in the growth in the money supply and the banks' deposit potential, as well as moderate change in the currency structure especially in the last quarter of 2009.

Figure 94
 Annual growth rates in the monetary aggregates M1, M2 and M4 (in %)

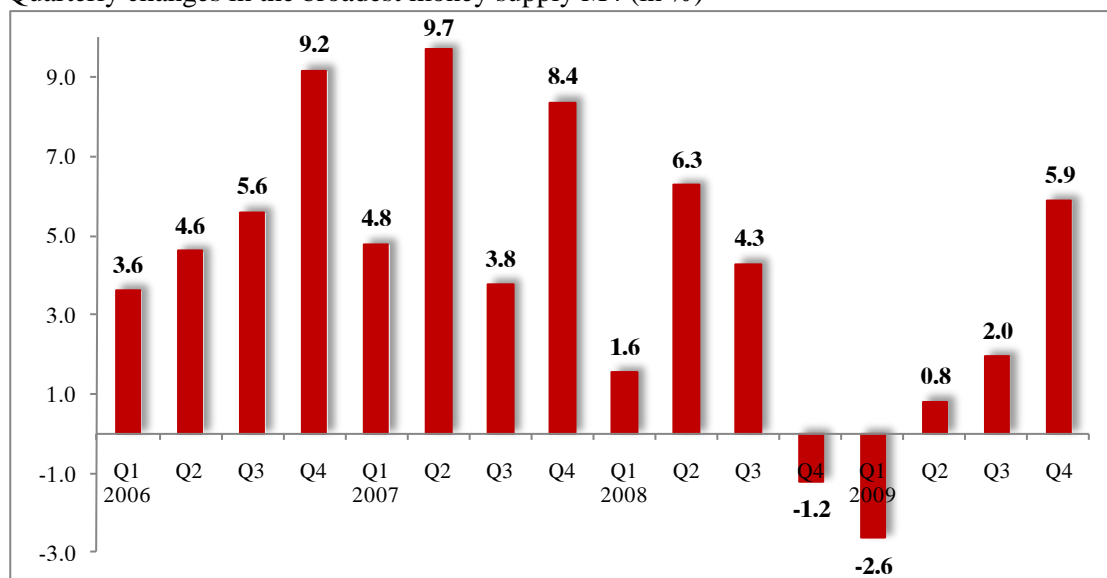


Source: National Bank of the Republic of Macedonia.

During the year, the broadest money supply was under the influence also of additional factors with one-time effect on the banks' assets. Thus in April and October, funds from the households' deposit accounts based on the regular installment of the bond for old foreign exchange saving were transferred. In May, part of the banks' deposit potential was redirected to the budget due to the payment of larger amount of a dividend to the Government. Additional funds from the enterprises' accounts were withdrawn in July, given a transfer of deposits of a resident to a non-resident⁷⁵. The funds remained in the domestic banks in form of Denar deposit with FX clause until December, when repatriation of larger amount of dividend to foreign investor was made.

Figure 95

Quarterly changes in the broadest money supply M4 (in %)



Source: National Bank of the Republic of Macedonia.

The analysis of the annual growth rates of the broadest money supply shows a continuing downward trend until the third quarter, and in September a decrease of 1.1% was registered. The consequences from the decrease in the economic activity and deterioration on the external account on the broadest money supply was felt mostly in the first quarter of 2009, when quarterly decrease in the money supply was registered, mainly as a result of the decrease in the enterprises' demand deposits. The improvement in the macroeconomic trends enabled quarterly growth in the money supply in the following period. In the last quarter, high quarterly inflow of new savings in the banks (as well as continuing trend of acceleration in the annual growth rates) was registered, which is combined effect of the better expectations of the domestic entities and the favorable changes in the external sector.

⁷⁵ Monetary statistics does not include the non-residents' deposits in the money supply.

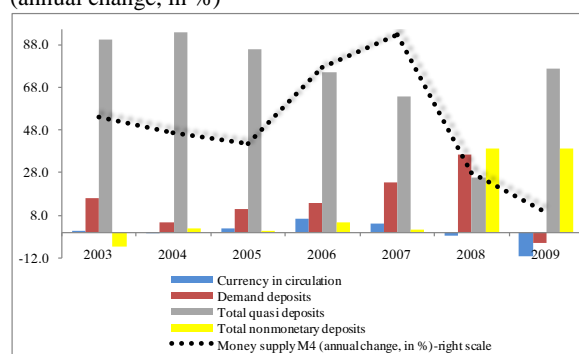
Table 16
Components of the monetary aggregates
(in millions of denars)

	31.12.2008	annual change		Share in total	Contribution		31.12.2009	annual change		Share in total	Contribution
	godina	(december					31.12.2008)	in growth	vo milioni		
	in million	%	%	%	%		denari	vo milioni	%	%	%
Currency in circulation	17,601	-307	-1.7	9.0	-1.6		16,266	-1,335	-7.6	7.8	-11.4
Demand deposits	36,518	7,170	24.4	18.7	36.3		35,957	-561	-1.5	17.3	-4.8
M1	54,119	6,863	14.5	27.7	34.8		52,223	-1,897	-3.5	25.2	-16.2
Quasi denar deposits	49,584	-6,015	-10.8	25.4	-30.5		45,735	-3,849	-7.8	22.1	-32.8
Quasi foreign currency deposits	75,182	11,084	17.3	38.5	56.1		88,025	12,843	17.1	42.5	109.4
M2	178,885	11,932	7.1	91.5	60.4		185,984	7,098	4.0	89.7	60.5
Nonmonetary denar deposits	7,990	3,318	71.0	4.1	16.8		8,791	801	10.0	4.2	6.8
Nonmonetary foreign currency deposits	8,650	4,492	108.0	4.4	22.8		12,488	3,838	44.4	6.0	32.7
M4	195,525	19,742	11.2	100	100		207,262	11,737	6.0	100	100

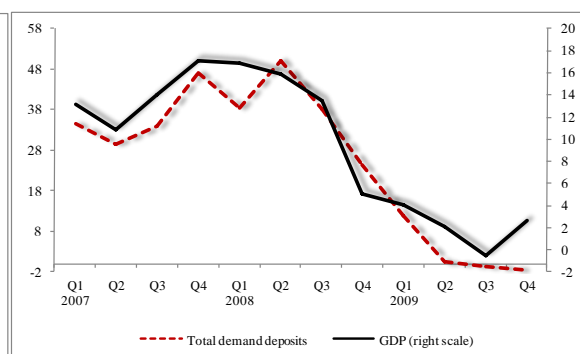
Source: National Bank of the Republic of Macedonia.

From the aspect of the money supply's individual components, the most liquid monetary aggregate M1 (which includes the cash foreign currency and transaction deposits) registered a downward trend in 2009 and at the end of the year it registered an annual decrease of 3.5% (since May continuing negative annual growth rates were registered). The decrease in the demand for assets for transaction purposes corresponds to the reduced activity in the domestic economy. On the other hand, in conditions of a growth in the total money supply, the negative trend of the money supply M1 signalizes also possible change towards smaller propensity for saving and investments, in conditions of evidenced uncertainty. Such changes can be explained also with the rise in the interest rates, i.e. the higher yields from the saving. With respect to the savings, in 2009 although both the short-term and the long-term deposits had positive contribution to the increase in the money supply, the short-term saving dominate (share of 7.6% in the increase in M4). However, the increase also in the long-term saving, which continued also in 2009, despite the present risks and the uncertainty about the future flows in the economy in 2009 should also be emphasized.

Figure 96
Share of the main components in
the growth in the money supply M4
(annual change, in %)



Nominal GDP in the total demand deposits

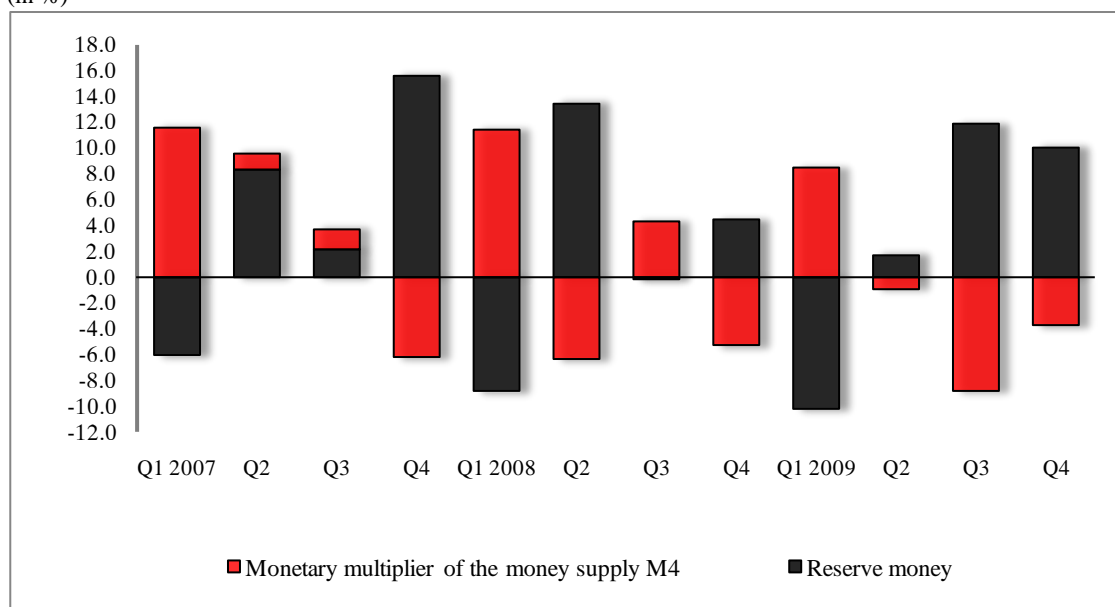


Source: National Bank of the Republic of Macedonia.

Annually, in 2009 the average monetary multiplier equals 4.8%, compared to 5% in the previous year. The monetary multiplication dynamics in 2009 varied, with an upward trend in the first half and trend of slowing down in the second half of the year being registered. Thus in the first half of 2009 the monetary multiplication accelerated, as a result of the decrease in the reserve money. Significant withdrawal through net sale of foreign exchange by the NBRM in this period was registered, which was not fully compensated through the monetary instruments and the net position of the Government. In the second half of 2009, the monetary multiplication slowed down, in conditions of higher level of reserve money, given the rise in the reserve requirement allocation rate (in July monthly increase in the reserve money of about Denar 5 billion was registered, as a single effect of the rise in the banks' requirement for allocation of reserve requirement).

Figure 97

Decomposition of the quarterly growth rate of the money supply M4
(in %)

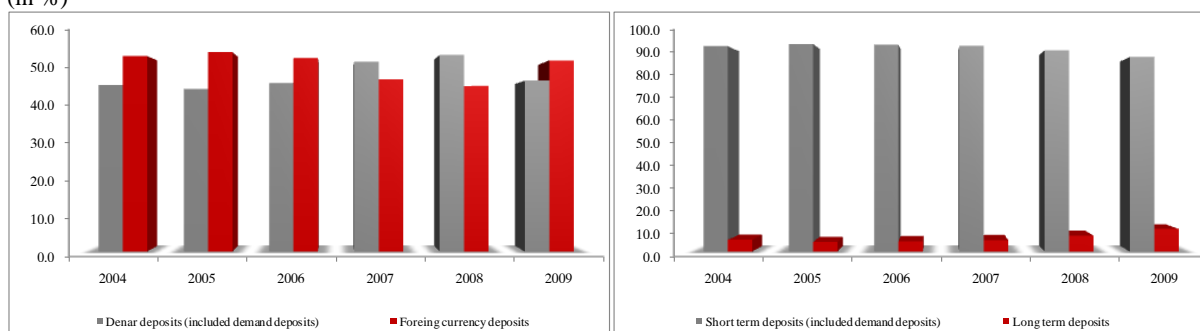


Source: National Bank of the Republic of Macedonia.

In 2009 the annual growth rates of the deposit potential of the banking system was registered, as a consequence of the reduced economic activity. Thus the annual growth rate of the total deposit potential (with demand deposits) in December 2009 equals 7.1%, compared to 12.4% in the previous year. In the first half of the year, deposit base contraction was registered, in conditions of reduced economic activity, significant decrease in the capital inflows in the economy and worsened perceptions of the domestic entities. The first two factors resulted in lower amount of funds on the corporate sector' transaction accounts, as a factor for banks' deposit potential reduction in this period. In the second half of 2009, the import demand adjustment, the inflow of the private transfers and the revival of the capital inflows contributed to the improvement in the deposit base movements, especially apparent in the last three-month period of the year.

Figure 98

Share of the main components in the total deposits (annual average)
(in %)



Source: National Bank of the Republic of Macedonia.

In 2009 the euroization trend, which commenced in the last months of 2008, intensified, given the simultaneous decrease in the saving in domestic currency. Thus the investments in foreign currency proved as preferred instrument for depositors' protection in conditions of negative shocks in the economy. Thus the euroization degree (assets substitution measured through the share of the foreign currency deposits in the total money supply) in December 2009 equals 48.5%, compared to 42.9% in the preceding year. The affinity for having assets in foreign currency available for the

purpose of protection from currency risk was especially apparent in the first half of the year. Thus during the year, decrease in the dominant role of the Denar deposits in the total deposits was registered, and in December 2009 their share in the deposit banks equaled 46.4%, compared to 52.1% in December 2008. The gradual stabilization in the expectations of the economic agents in the second half of the year contributed to the slower decline in the Denar deposits, given the simultaneous slowing down of the growth in the foreign currency deposits. Thus in August partial return of the confidence in the domestic currency and consequently, continuing monthly increase in the Denar deposits was registered. At the end of December, the Denar deposits registered a decrease of 4.6% (compared to the average decrease of 9.4% in the first three quarters of the year), while the foreign currency deposits augmented annually by 19.9%.

Table 17
Structure of the private sector's total deposits of the (in millions of denars)

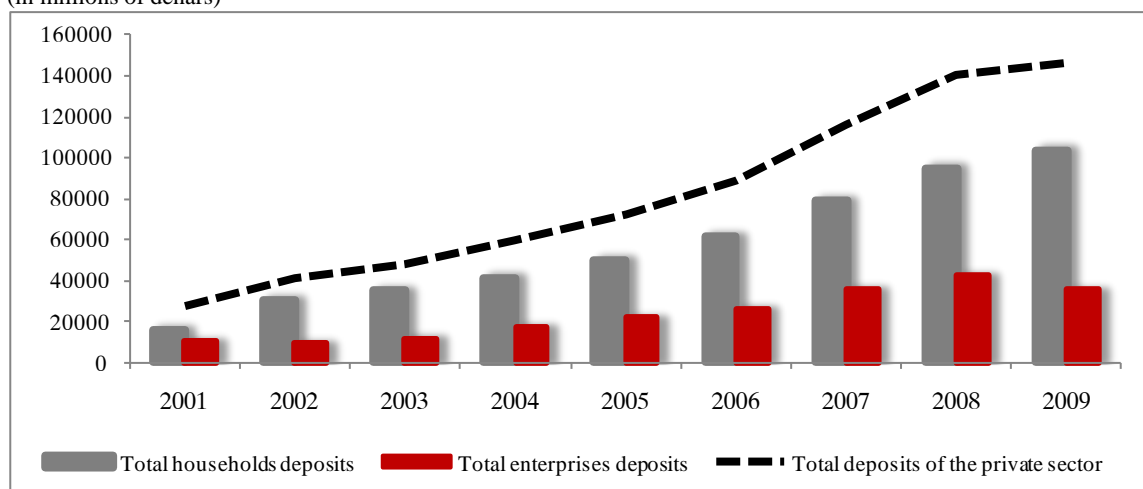
	31.12.2008		annual change (december 2008/december 2007)		Share in total deposits (31.12.2008)	Contribution in growth	31.12.2009		annual change (december 2009/december 2008)		Share in total deposits (31.12.2009)	Contribution in growth
	in millions denars	in millions denars	%	%	%	in millions denars	in millions denars	%	%	%		
Total deposits of the private sector	175,130	19,261	12.4	100	100	187,586	12,456	7.1	100	100		
Time structure												
Demand deposits	33,724	6,382	23.3	19.3	33.1	32,547	-1,177	-3.5	17.4	-9.4		
Quasi deposits	124,766	5,069	4.2	71.2	26.3	132,071	7,305	5.9	70.4	58.6		
Nonmonetary deposits	16,640	7,810	88.4	9.5	40.5	22,969	6,329	38.0	12.2	50.8		
Currency structure												
Denar deposits	91,298	3,685	4.2	52.1	19.1	87,073	-4,225	-4.6	46.4	-33.9		
Foreign currency deposits	83,832	15,576	22.8	47.9	80.9	100,513	16,681	19.9	53.6	133.9		
Sector structure												
Enterprises	61,891	4,683	8.2	35.3	24.3	52,563	-9,328	-15.1	28.0	-74.9		
Households	107,841	13,746	14.6	61.6	71.4	124,414	16,573	15.4	66.3	133.1		

Source: National Bank of the Republic of Macedonia.

From the aspect of the total deposits' maturity structure, in 2009 a trend of deceleration of the annual growth rates also of the short-term and long-term deposits was registered. Thus the annual growth rate of the short-term⁷⁶ and the long-term deposits in December equals 3.9% and 38%, respectively. Both the short-term and the long-term deposits had almost equal contribution to the creation of the new deposit potential (with a share of 49.2% and 50.8%, respectively in the annual growth in the total deposits). The stimulating interest rate policy of the banking sector that commenced in 2008 in order to create more stabile deposit base continued also in 2009, which contributed to the continuing rise in the propensity of the private sector to save on a long-term basis, despite the present uncertainty of the economic movements. Thus the long-term deposits had significant contribution to the creation of the new deposit base, and their share in the total deposits in December 2009 reached 12.2% (compared to 9.5% in December 2008).

⁷⁶ It also includes the demand deposits.

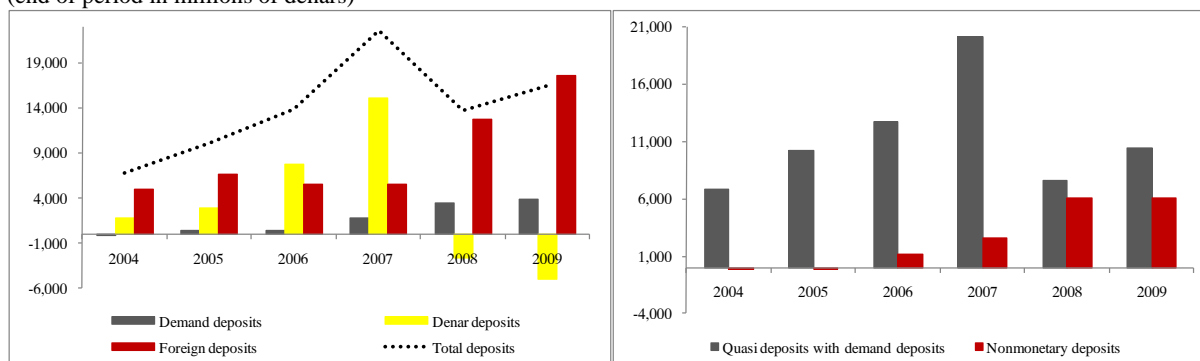
Figure 99
Average deposits of the private sector without demand deposits
(in millions of denars)



Source: National Bank of the Republic of Macedonia.

Observed from the aspect of the sectors, in 2009 a continuing increase in the households' deposits (with demand deposits) was registered, which proved the short-term and not very strong negative psychological effect of the global crisis on the depositors' confidence. Annually, the households' deposits augmented from 15.4% (increase of 12.8% of the households' deposits without demand deposits). The total new saving of the households in 2009 exceeds the amount of the new saving in the banking system in 2008. The rise in the households' deposits was supported by the still poor reaction on the labor market to the crisis, where in 2009 no worsening in the conditions was registered. Namely, the nominal wages continued to grow, with the unemployment downward trend still being registered. However, the dynamics of the currency exchange operating (i.e. return on the assets withdrawn through the cash foreign currency into the system in part of 2008) can be one of the explanations for larger marginal change in the saving. Also, in conditions of a growth in the available income and lower consumption, the higher level of deposits signalizes higher propensity for saving. The main feature for the households' deposit base in 2009 is the households' affinity to save in foreign currency, as a form of protection of the financial assets value. However, in the last quarter of 2009, the expectations stabilized, which contributed to the re-orientation of the households to save in domestic currency. From the aspect of the annual changes, in December 2009 the Denar deposits dropped annually by 2.5%, while the foreign currency deposits went up by 27.9%.

Figure 100
Annual change in the main components of the households' deposits
(end of period in millions of denars)



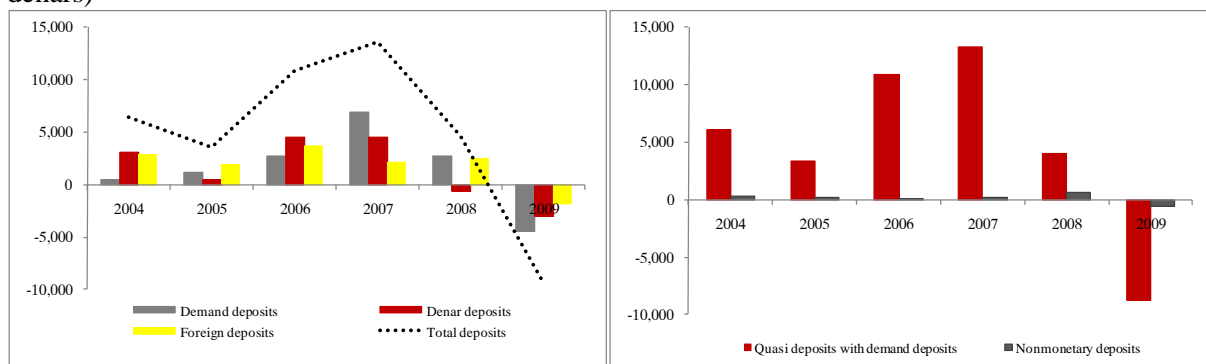
Source: National Bank of the Republic of Macedonia.

The movements in both real and external sector during the year, as a consequence of the global economic trends resulted in a decrease in the deposit base of the corporate sector. On

annual basis, the corporate deposits decreased by 15.1% (decrease of 12.4% of the enterprises' deposits without demand deposits). The trend of decrease in the enterprises' deposits was present during the entire year. Additional funds from the enterprises' accounts were withdrawn also through the payment of dividend of one larger company to the Government (in May), as well as through the transfer of funds from a resident's deposit to a non-resident's deposit (in July). The lower credit activity, the reduced economic activity, the decrease in the export, as well as the limited sources of financing, mostly contributed to the decrease in the funds on the transaction accounts, through which large part of the enterprises' base was withdrawn (contribution of 47.7% in the decrease in the total corporate deposits). With the stabilization of the flows in the last quarter of the year, the level of the enterprises' deposits also stabilized. On annual basis, all types of deposits registered a decrease (decline in the Denar and the foreign currency deposits of 17.8% and 9.3%, respectively, and negative changes of the short-term and long-term deposits of 11.6% and 26%, respectively).

Figure 101

Annual change in the main components of the corporate sector's deposits (end of period in millions of denars)



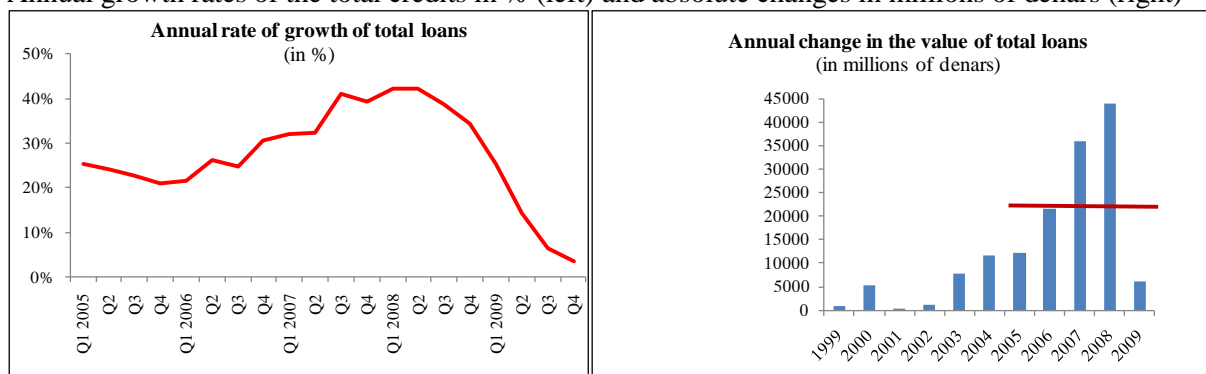
Source: National Bank of the Republic of Macedonia.

3.4. Bank placements

The global financial and economic crisis significantly decelerated the activity on the domestic market in 2009. In conditions of downward adjustment of both the credit supply (given lower saving and worsened banks' expectations) and demand (given lower preferences for new debiting, in conditions of uncertain future income and restraint from the consumption), the annual growth rate of the total deposits in 2009 reduced only to 3.5%, which is the lowest growth rate since 2002. The increase in the credits in the economy in 2009 represents only about 18% of the average credit growth in the preceding three years.

Figure 102

Annual growth rates of the total credits in % (left) and absolute changes in millions of denars (right)

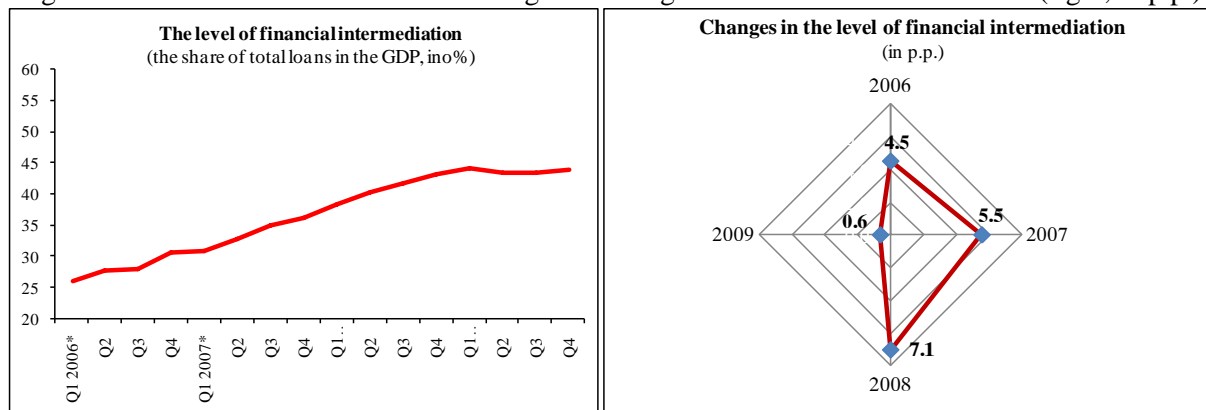


Source: NBRM.

In conditions of such a deceleration of the credit growth, in 2009 the degree of financial intermediation stagnated, compared to its relatively large deepening in the three previous years. The financial intermediation degree, measured through the total credits in the GDP, in 2009 equaled 43.9% and remained almost unchanged compared to the previous year (minimal growth of 0.7 p.p.) compared to 2008 when that growth equaled 7.1 p.p. The slowing down of the credit growth rates terminated the so-called "credit expansion", a phenomenon characteristic for the economies in transition, which had relatively low degree of financial convergence.

Figure 103

Degree of financial intermediation and change in the degree of financial intermediation (right, in p.p.)



*Preliminary data for GDP.

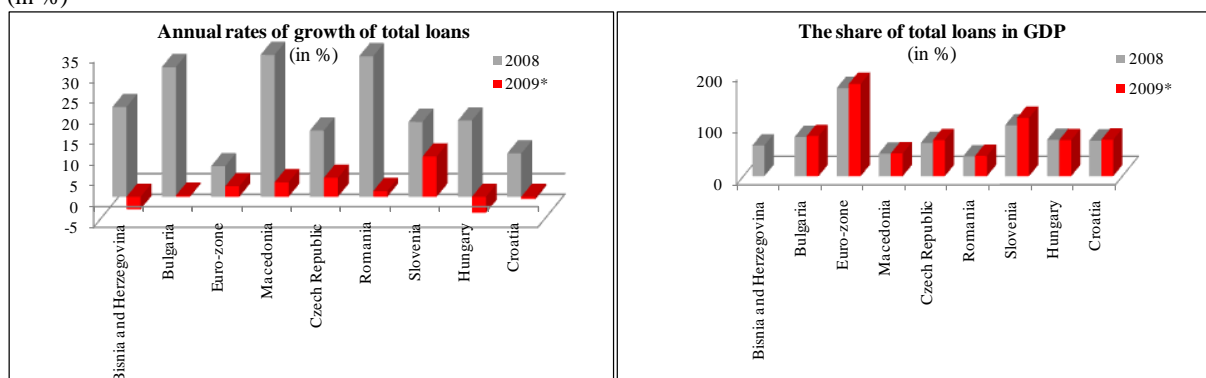
**Estimated data for GDP.

Source: NBRM and SSO.

Significant deceleration in the credit activity is characteristic also for the credit market in many other countries. Such trends are evidenced also in the Euro area, where despite the significant liquidity support by the ECB, the credit activity continually slowed down during the year. The poor confidence in the markets, the deteriorated perceptions and the future expectations of the banks, as well as the smaller demand are factors that triggered such trends. Similar movements were registered also with more developed former economies in transition, as well as with the countries in the region. In conditions of lower credit growth and credit activity reduction, the degree of growth in the financial intermediation also slowed down. Thus all of the analyzed countries registered an annual increase in the degree of financial intermediation, compared to the previous experience of intensified financial deepening.

Figure 104

Annual growth rates in the total credits in 2008 and 2009 (left) and share of the total bank credits in GDP (right) by countries (in %)



*The datum pertaining to GDP in 2009 by countries is projection.

Source: EUROSTAT, web sites of individual banks, NBRM

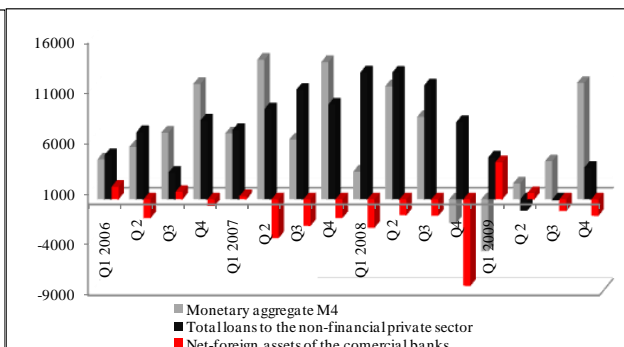
The adjustment of the banks' credit policy in 2009 corresponded to the changes in the macroeconomic trends during the year, the general expectations of the domestic entities and to the changes in the monetary policy. The first three quarters characterized with significant growth impediment and consequently stagnation in the credits quarterly change. The first three quarters are period within which evident perceptions of the banks for high risk were registered, given a decrease in the domestic economy and information on the still high uncertainty about the global economic movements. The reduced economic activity means also potential deterioration in the financial performances of the corporate sector, as well as possible worsening of the labor market conditions. This resulted in the banks' higher restraint regarding the credit activity, as a method to diminish the consequences of the asymmetric information problem (especially apparent in conditions of crisis) on their financial performances. Actually, in 2009 constant increase in the suspicious and contested claims of the banks was registered, an occurrence characteristic also for the financial systems of large number of economies. The on-balance sheets limitations, i.e. **significant contraction of the sources of financing**, also limited, to large extent, the capacity for new crediting during this period. The decrease in the demand for credits also acted in this direction, moved by the fear for the future available income, and thus smaller propensity for saving and new investments and smaller new debiting.

Figure 105
Share of the suspicious and doubtful claims in the total bank credits
(in millions of denars)



Source: NBRM.

Figure 106
Sources of financing
(in millions of denars)



After the credit activity had stabilized in the third quarter (preserving the same level as in the second quarter of the year), in the last quarter of the year, signals for moderate recuperation of the activities on the credit market emerged. The expectations were more stable and better, given the continuing information for better global perspectives. In direction of more stable expectation was also the decrease in the basic interest rate of the NBRM, as a signal for smaller risks in the future period. In such conditions, the trend of credit conditions contraction ceased. Also, given stable expectations about the foreign exchange rate and growth in the capital inflows, this period characterizes with moderate recovery of the deposit base. In the last quarter, the trend of decrease also of the demand for credits ceased, and for the first time from the beginning of the year, intensified demand for all types of corporate credits and certain types of households' credits was registered.

Table 18
Domestic credits of the deposit banks
(in millions of denars)

	Stock as of 31.12.2008	Stock as of 31.12.2009	Annual change		Contribution to the growth of total loans	
			in mill. of denars	in %	2008	2009
Total banks' placements	172150	178195	6045	3.5	100%	100%
In denars*	133679	139194	5515	4.1	82.4	91.2
In foreign currency**	38471	39001	530	1.4	17.6	8.8
Short-term	54298	53093	-1205	-2.2	35.2	-19.9
Long-term	105257	107386	2129	2.0	59.5	35.2
Non-performing loans	11077	15716	4639	41.9	3.8	76.7
Household sector	69460	71864	2404	3.5	42.7	39.8
in denars	65132	68053	2921	4.5	38.2	48.3
in foreign currency	4328	3811	-517	-11.9	4.5	-8.6
short-term	16392	17614	1222	7.5	9.6	20.2
long-run	48913	47105	-1808	-3.7	29.3	-29.9
non-performing loans	3695	5857	2162	58.5	3.5	35.8
Enterprises	102338	106155	3817	3.7	57.1	63.1
in denars	68211	71017	2806	4.1	44.0	46.4
in foreign currency	34127	35138	1011	3.0	13.1	16.7
short-term	37811	35423	-2388	-6.3	25.4	-39.5
long-run	56294	60164	3870	6.9	30.2	64.0
non-performing loans	7570	9859	2289	30.2	1.1	37.9

*The Denar credits include also the credits with FX clause.

**The foreign currency categories are estimated according to the current foreign exchange rate.

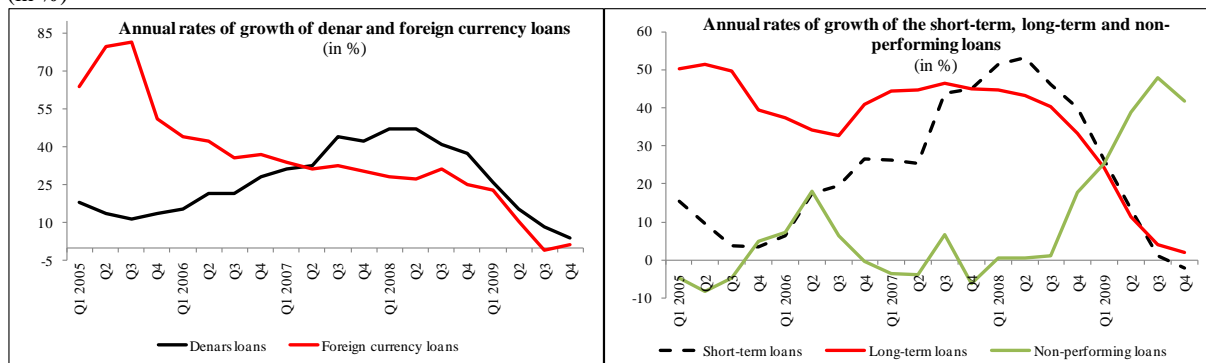
Source: NBRM.

From the aspect of the currency structure, 2009 characterizes with apparent preferences for Denar crediting⁷⁷, with almost the entire annual increase in the credits (91.2%) being generated from the currency component. However, the change in the propensity for Denar crediting was present also in the segment of crediting both the households and the enterprises. From the aspect of the second sector, such a tendency corresponds to the significant decrease in the foreign trade in 2009, as well as with the further increase in the external debiting of the corporate sector, despite the global crisis. The average contribution to the growth in the Denar credits in the total credit growth in 2008 equaled 81.4%, while in 2009 it reached on average 88.5%. On the other hand, the contribution of the foreign currency crediting to the total credit growth equaled on average 11.5% (18.6% in 2008), with the foreign currency crediting of households and enterprises having almost identical contribution to such annual movement.

⁷⁷ It also includes credits with FX clause.

Figure 107

Annual growth rates of credits from the aspect of the currency structure (left) and maturity structure (right) (in %)

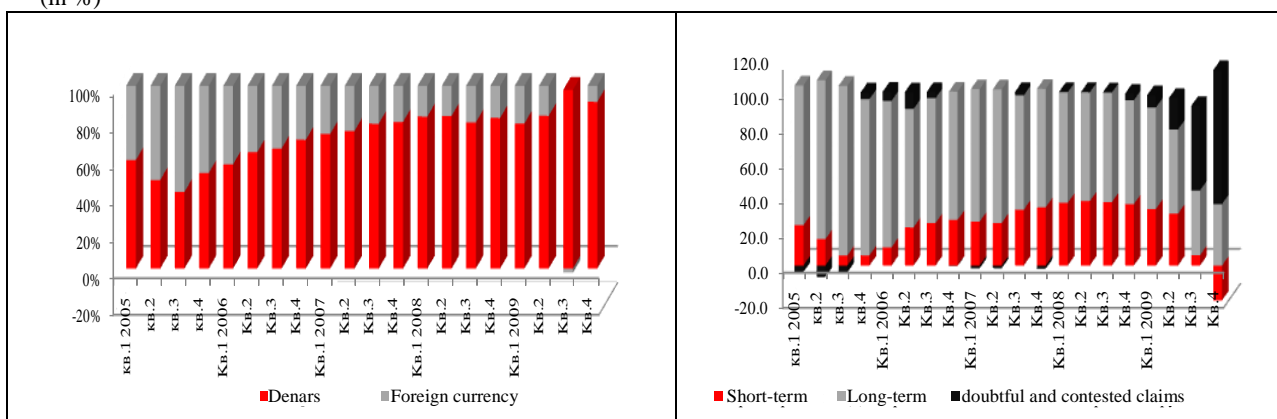


Source: NBRM.

Analyzed from the maturity aspect, the short-term credits contributed to the slowing down of the total credits' growth dynamics in 2009, which went down by 2.2% annually, while the long-term credits registered minimal increase of 2%. However, trends turnover in 2009 was registered. Thus for the first half of the year, slowing down in the growth dynamics of the long-term credits was evidenced. Such occurrence reflects the uncertain economic environment in the domestic economy, companies' restraint from investments in fixed assets, as well as the reduced households' consumption for durable consumption goods and real estate. In the second half of the year the trends changed, with the short-term credits being reduced more intensively relative to the long-term ones, registering negative growth rates. In conditions of reduced economic activity, the capacity for regular servicing of the liabilities decreased, and in 2009 intensive annual rise in the banks' suspicious and contested claims of 41.9% was registered. The most intensive growth was registered in the first nine months of the year, while in the last quarter their balance began to register gradual decline.

Figure 108

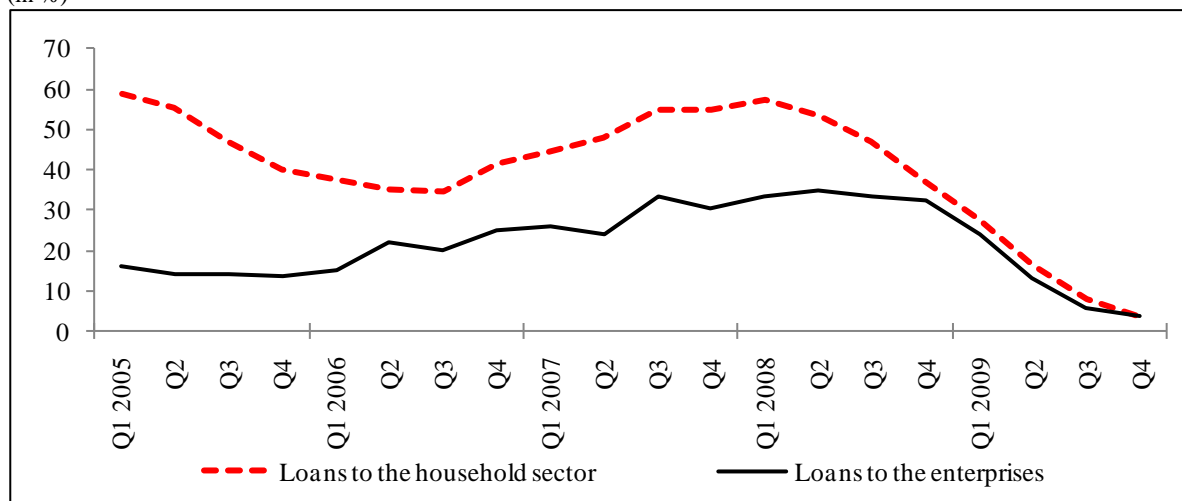
Contributions to the quarterly growth of the total credits from the aspect of the currency structure (left) and maturity structure (right) (in %)



Source: NBRM.

Opposite to the relatively higher annual growth rates of the households' credits, especially characteristic until the first half of 2008, 2009 characterizes with process of convergence of the annual growth rates of the households and the enterprises. Namely, the sector analysis shows more intensive deceleration of the households' credit dynamics, the annual growth rate of which reduced to 3.5%. Such changes resulted in an increase in the share of the credit growth of the corporate sector in the increase in the total credits in 2009 of 6.1 percentage point relative to 2008, thus reaching 63.1%.

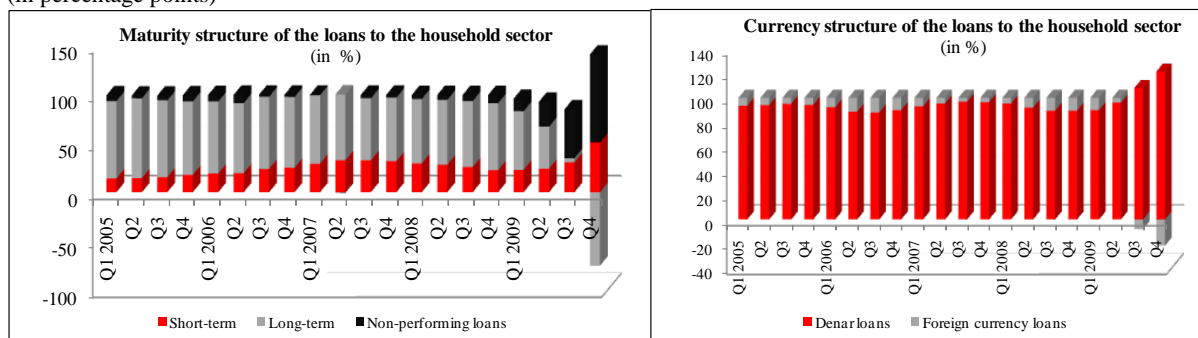
Figure 109
Annual growth rates of the credits from the aspect of the sector structure
(in %)



Source: NBRM.

The deceleration in the households' credit growth, which began since the last quarter of 2008, continued to intensify constantly during the first nine months of 2009. In the last quarter of 2009, the trend of constant decrease in the demand and the supply with the "households" sector was ceased. The higher costs for the banks financing, their on-balance sheet restrictions, the intensified risk and the banks' fear of unsuccessful foreclose, as well as the worsened perceptions for the credit worthiness of the households can be identified as the main limiting factors for the significant deceleration in the households' credit growth dynamics on the side of the supply⁷⁸. On the side of the demand for credits, the households' interest for additional debiting reduced more intensively, as a result of the higher uncertainty for the future anticipated income, which arises from the deteriorated perceptions for the economic movements in the country. However, remarkably lower interest of the households for debiting was evidenced with the housing and the consumer credits⁷⁹. However, in the last quarter of 2009 the households showed higher interest for additional debiting, i. increase in the demand for credits was registered, especially the housing and durable consumer goods credits.

Figure 110
Contributions to the quarterly growth in the households' credits from the maturity (left) and currency (right) direction
(in percentage points)



Source: NBRM.

Analyzed from the maturity aspect, in 2009 the annual growth rate of the households' credits is due primarily to the short-term crediting, which reflects the higher liquidity needs of the households. Despite the significantly lower growth dynamics compared to 2008, the short-term credits of the

⁷⁸ According to the Lending Surveys for 2009 - April July and October 2009 and January 2010, NBRM.

⁷⁹ According to the Lending Surveys for 2009 - April July and October 2009 and January 2010, NBRM.

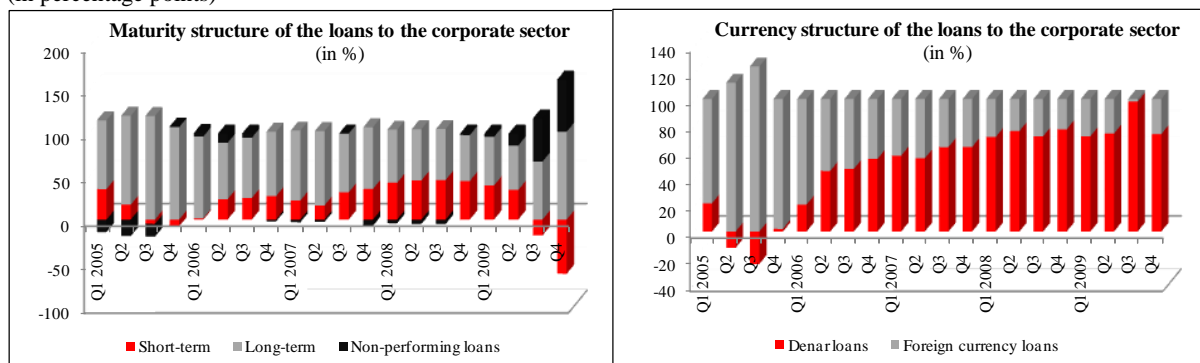
households registered annual growth rate of 7.5% in 2009, with a share of 50.8% in the total credit growth. The long-term households' credits went down annually by 3.7%, clearly indicating the evident effects of the uncertainty on the maturity structure of the new debiting. In 2009, significantly high annual growth of 58.5% accounts for the suspicious and contested claims. From the currency aspect, the banks were directed towards the Denar crediting of the households, which registered moderate annual growth of 4.5%, while the foreign currency credits plunged by 11.9%, annually.

Similar to the situation in the "households" sector, the growth dynamics of the credits with the corporate sector continually decreased in 2009, and their annual growth rate reduced to 3.7%. The reasons for the deceleration in the growth dynamics of the enterprises' credits, on the side of the supply⁸⁰ can be located in the higher risks of the banks, reflecting the uncertain economic situation in the country and accordingly, the worsened financial performances of the enterprises, worsened perceptions for the branch the enterprise belongs to and the fears for inability for foreclosure. The enterprises' adjustment relative to the economic crisis was in direction of their restraint from investment in fixed assets and working capital⁸¹, which acted also on the decline in the demand for credits.

Figure 111

Contributions to the quarterly growth in the enterprises' credits from the aspect of maturity (left) and currency (right)

(in percentage points)



Source: NBRM.

From maturity aspect, more apparent decrease was evidenced with the short-term enterprises' credits, which went down annually by 6.3%, compared to the long-term credits, where the growth rate reduced to 6.9%. In 2009, significantly high annual growth of 30.2% accounts for the suspicious and contested claims. From the currency aspect, the impeded growth in the crediting in foreign currency intensified, as a result of the lower foreign trade volume of the country due to the economic crisis which was felt by all trading partners. Thus the Denar crediting was more apparent, with annual growth rate of 4.1% and contribution to the increase in the total enterprises' credits of 73.5%.

3.5. Interest rates

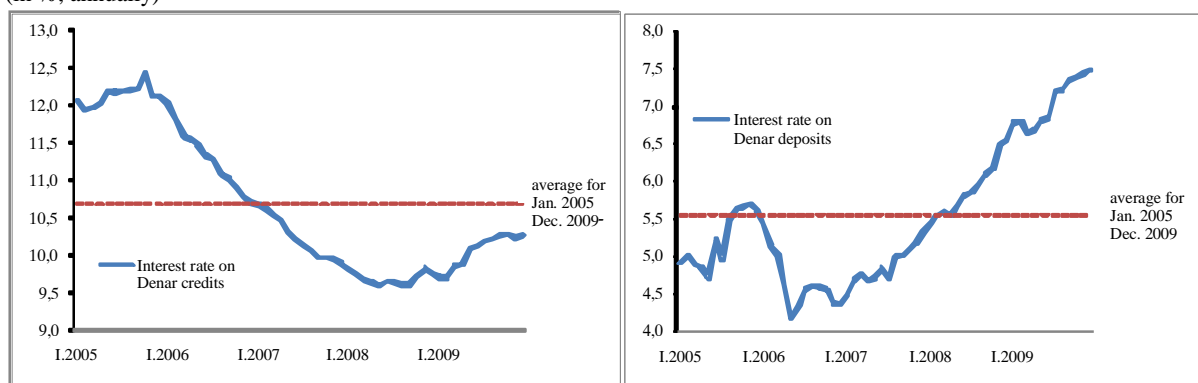
In 2009, tendency for tightening of the interest rate crediting conditions by the domestic banks and increase in yields from saving was evidenced. The average lending and deposit Denar interest rates registered an annual growth of 0.4 percentage points and 1.2 percentage points, respectively. The adjustment of the banks' interest rate policy is a reaction of several factors. **Firstly, the high degree of uncertainty and apparent risks** the banks faced with in their operating in 2009. **Secondly, the limited possibility of the banks for domestic financing through deposits and internally, through borrowings on the international markets.** **Thirdly, the undertaken monetary measures,** by increasing their basic interest rate and reserve requirement rate, which also acted

⁸⁰ According to the Lending Surveys for 2009 - April July and October 2009 and January 2010, NBRM.

⁸¹ According to the Lending Surveys for 2009 - April July and October 2009 and January 2010, NBRM.

towards increase in the interest rates. **Intensified increase in the deposit relative to the lending Denar interest rates contributed to the interest rate spread contraction.** The improvement in the trends in the domestic and the world economy at the end of the year stabilized the banks expectations, and also resulted in favorable movements in the banks' deposit base. This, together with the decrease in the basic interest rate of the NBRM at the end of November, depleted the pressures for further rise in the bank interest rates and influenced on the decrease in the interest rates on certain types of newly extended credits and newly accepted deposits, at the end of the year.

Figure 112
Lending and deposit interest rates of the bank
(in %, annually)



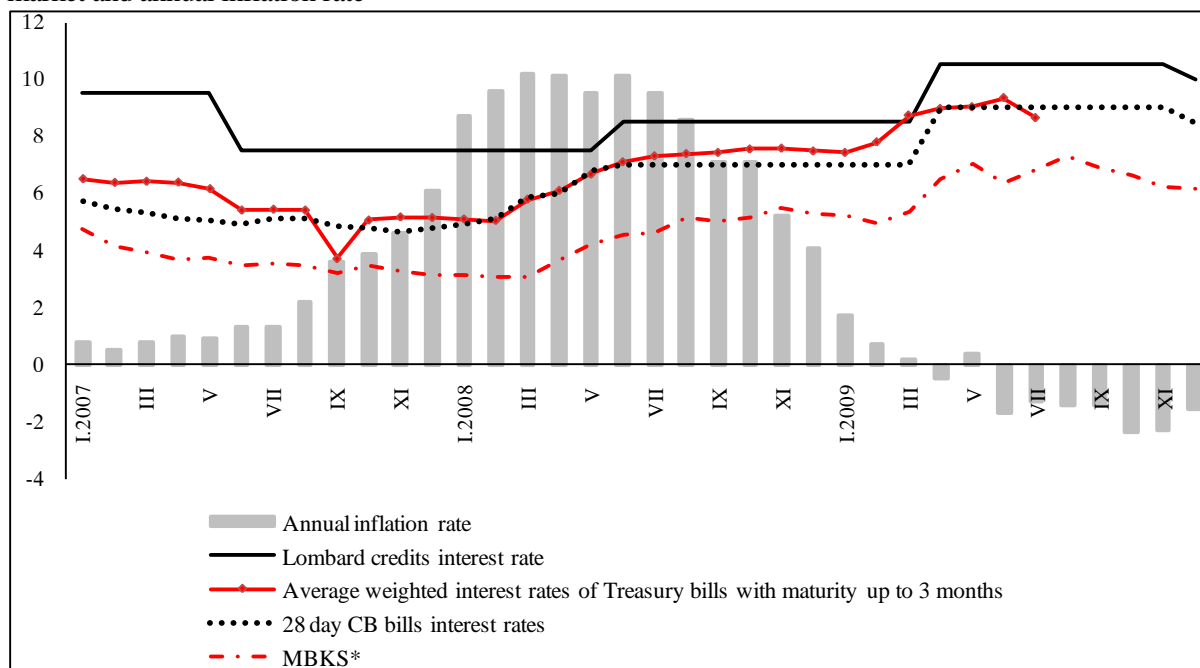
Source: NBRM.

The first segment affected by the increase in the basic interest rate of 2 p.p.⁸² was the interbank deposits market, where in April 2009 more significant monthly rise of the interbank interest rate (of 1.1 percentage point) was registered. Despite more apparent monthly variability, in 2009, MBKS registered an upward trend and it equaled 6.31%, on average (compared to 4.3% in 2008). The increase in the interest on the interbank deposit market can partially be explained by the remarkable uncertainty with the banks and the necessity of cautious liquidity management. However, with the gradual stabilization of the macroeconomic situation and the increased liquidity in the banking sector, as well as the changes of the monetary policy in the fourth quarter of the year, increase in the interbank trading and continuing downward adjustment of the MBKS on the interbank money market was registered.

⁸² On March 23, NBRM increased the interest rate on CB bills from 7% to 9%, with the higher interest rate began implementing since the first auction held in April 2009.

Figure 113

Short-term interest rates of the NBRM, interest rates on the money market, on the government securities market and annual inflation rate



*MBKS - interbank interest rate

Source: NBRM and the Ministry of Finance

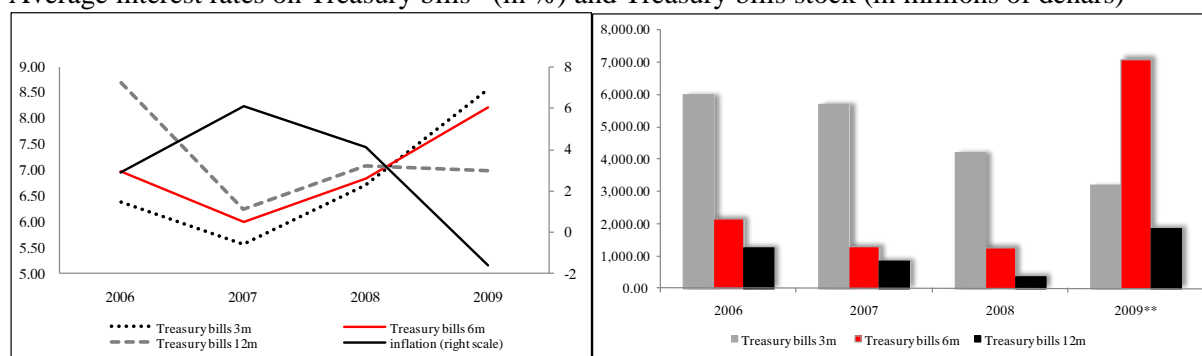
Upward movement of the interest rates in 2009 characterized also the Government securities market. In 2009, the interest rates on the three-month, six-month and the twelve month Treasury bills on this market equaled 8.59%, 8.23% and 7%, on average (compared to 6.71%, 6.85% и 7.09%, on average in 2008). Moderate upward movement of the interest rate also with the government bonds with two-year maturity was registered⁸³. **In conditions of intensified financial needs of the Government, especially in the first half of the year⁸⁴, in March 2009, one-month Treasury bills in Denars on the government securities market were introduced, with Treasury bills with maturity of three, six and twelve months being introduced in June 2009.** The financial instruments with FX clause attracted more significant interest, the demand for which in all maturities, on average, exceeding the supply, while the interest rates equaled 5.32%, 5.44% and 6.35%, on average, for three, six, and twelve months, respectively. The interest for Treasury bills with FX clause can be explained with the relatively attractive yields from such non-risk investment, which provides to the investors a complete protection from foreign exchange risk and improves the liquidity in conditions of crisis. This corresponds to the general behavior of the investors, which in conditions of vagueness are ruled by the so-called need for flight to safety and they are directed to the diversification of their portfolios by increasing the share of low-risk securities.

⁸³ In 2009, one auction of two-year government bonds were held, at which in conditions of significantly higher supply than demand, in case of a volume tender, the interest rate equals 8.5%.

⁸⁴ In July 2009, the Ministry of Finance issued an Eurobond, which influenced towards lower need for financing in form of government securities.

Figure 114

Average interest rates on Treasury bills* (in %) and Treasury bills stock (in millions of denars)



*The interest rates refer to the Treasury bills without FX clause.

**At the end of 2009 the stock of the three-month and six-month Treasury bills refers to the Treasury bills with FX clause. The stock with the twelve-month Treasury bills includes also the undue Treasury bills without FX clause.

Source: NBRM.

Table 19

Movements on the money market in Denars with FX clause in 2009

	Three-month Treasury bills with FX clause			Six-month Treasury bills with FX clause			Twelve-month Treasury bills with FX clause		
	Supply (in millions of Denars)	Demand (in millions of Denars)	Average weighted interest rate (%)	Supply (in millions of Denars)	Demand (in millions of Denars)	Average weighted interest rate (%)	Supply (in millions of Denars)	Demand (in millions of Denars)	Average weighted interest rate (%)
Q 1 2009									
Q 2 2009	650	1,327	5.25				1,350	2,332	7.00
Q 3 2009	2,200	1,959	5.40	2,100	2,866	5.38	900	484	5.70
Q 4 2009	3,180	3,180	5.30	5,000	5,376	5.50			

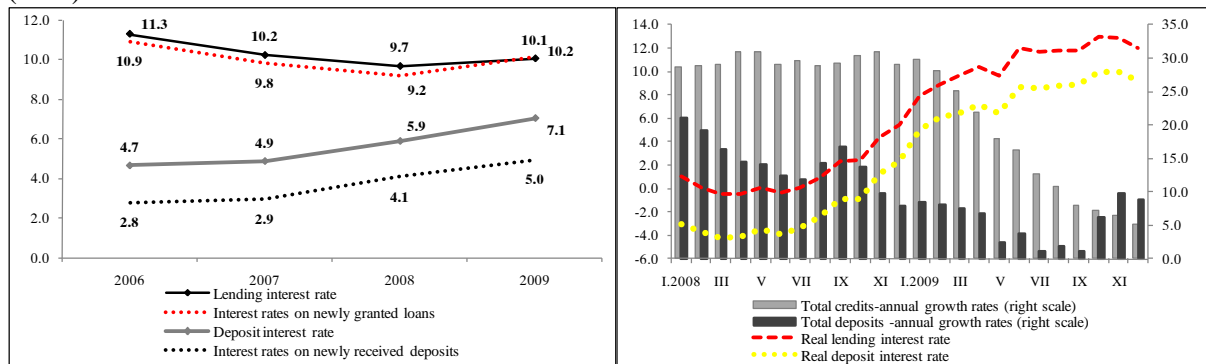
Source: NBRM.

The lending and the deposit Denar interest rates in the banking system in 2009 registered an increase, thus transmitting the unfavorable expectations of the banks and the unfavorable movements in their on-balance sheet positions on the private sector through larger financing costs, and higher saving yields. Commonly, the banks behavior in profiling the interest rate policy is moved by several factors: intermediation costs, such as the premiums for the interest rate, currency, credit and liquidity risk and operating costs; 2) changes in the macroeconomic indicators, such as the inflation rate and the economic growth and the changes in the monetary policy; and 3) structural factors, such as the degree of competitiveness, the size of individual banks and the banking sector development degree⁸⁵. Clear distinction between the degree of influence of the individual factors in certain period can not be made, having in mind their mutual close relationship and dependence. However, general conclusion is that in conditions of financial crisis, followed by extreme uncertainty and global recession, as the world experienced in the last two years, the mutual ties of individual risk factors strengthened, resulting in stronger effect on the banks' decisions. In the domestic banking sector in 2009, the negative perceptions and the banks expectations for the macroeconomic environment and its recurrent effects on the credit portfolio quality were especially apparent. In such an environment, in 2009 the lending and the deposit interest rates went up by 0.4 and 1.2 percentage points, on average. Consequently, the average lending and deposit interest rates equaled 10.1% and 7.1%. **The larger adjustment on the side of the deposit interest rates can be explained by the significantly limited sources of financing of the banks in this period and the need of deposit attraction as a long-term and stable source of financing.** The more attractive interest rate conditions in this market segment emerged also with the newly introduced bank products in 2009, created as a response to the growing competitiveness. On the side of the lending interest rates,

⁸⁵ See: A.Korelis "Financial structure, on-balance sheet interest rates and transmission mechanism of the monetary policy", 1994.

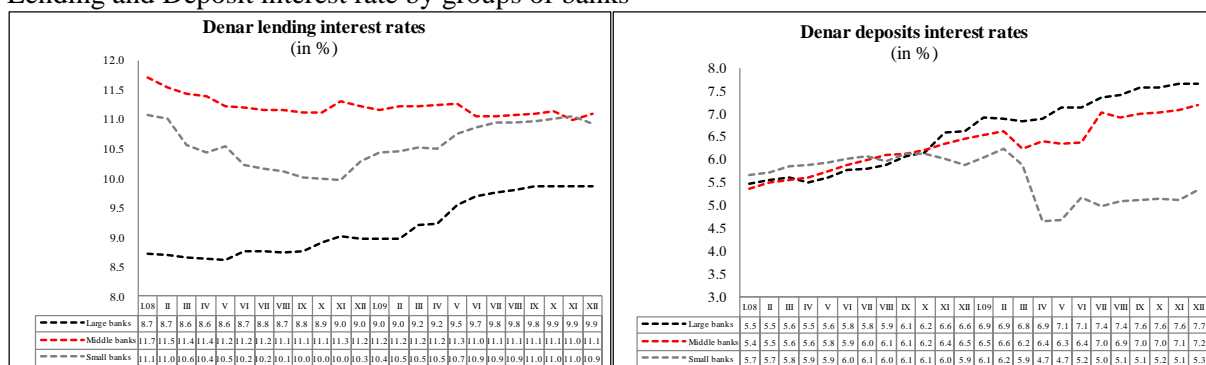
weaker adjustment probably arises from the importance of maintaining more stable longer-term relationship with the permanent clients. **However, significantly large transfer effect can be seen with the interest rate conditions of the newly approved credits, which augmented by one percentage point, on average (positioning at the level of 10.2%), which clearly implies conducting of more cautious policy regarding the new exposure of the banks⁸⁶.**

Figure 115
Denar lending and deposit interest rates and annual growth rates in the total credits and deposits (in %)



Source: National Bank of the Republic of Macedonia.

Figure 116
Lending and Deposit interest rate by groups of banks



Source: NBRM.

Analyzing the interest rate changes by sectors, the corporate sector characterizes with intensified rise in the interest rates, while the households registered higher increase with the deposit interest rates.

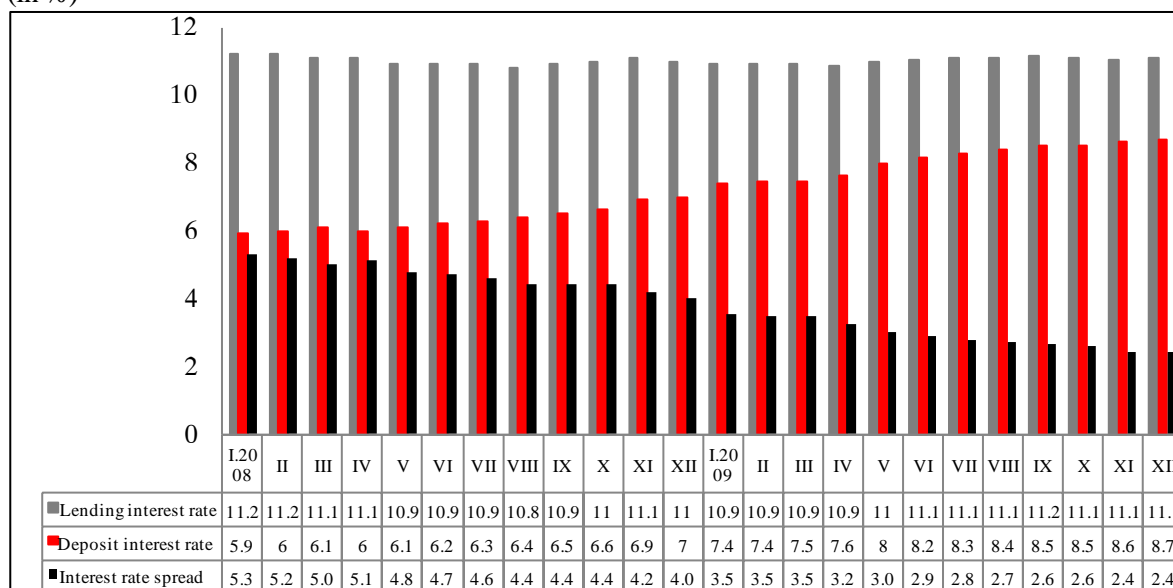
The price of the credits with the sector "households" remained unchanged on average in 2009 (11%). Moderate growth was recorded in the second half, as an effect of the higher risks and compensation of the higher deposit interest rates. **However, the movements with the interest rates on the newly extended credits indicate that in 2009 the banks perceived the credit exposure with households as significantly more risky, which caused increase in the risk premium and increase in the average weighted interest rate (from 11.2%, on average, in 2008 to 12.1% in 2009)⁸⁷. The interest rates on the households' Denar deposits registered continuing increase and on average**

⁸⁶ Actually, also the results from the conducted lending surveys which cover the period from the last quarter of 2008 and 2009, point to continuing contraction of the crediting terms (except to the last quarter), which is mainly due to the high risk degree the banks faced with and the higher financing costs.

⁸⁷ The uncertainty related to the labor market, the employment and the future income forced the banks to be more cautiously exposed to the households, accounting for possible direct effect of this factor on the households' credit worthiness. The analysis of the banks' answers in the lending surveys in 2009 points to the households' credit worthiness as one of the main factors for crediting terms contraction. Additional effects on the side of the supply are also the financing costs of individual banks and limitations in their on-balance sheet positions, as well as the expectations for the total economic activity.

in 2009 they equaled 8.1% (compared to 6.3% in 2008). Similar movements were evidenced with the newly accepted deposits, the average weighted interest rates of which surged by 1.4 percentage points, and equaled 5.3%, on average. The increase in the interest yields of the households' deposits was caused by the extreme significance of these deposits for the maintenance of the total deposit potential of the banks, especially in conditions when the corporate deposits registered negative trend in the movement during the year. In such movements of the lending and deposit interest rates, the interest rate spread for the "households" sector registered a decline and equaled 2.9 p.p. on average (compared to 4.7 p.p. in 2008).

Figure 117
Weighted Denar lending and deposit interest rate for households
(in %)



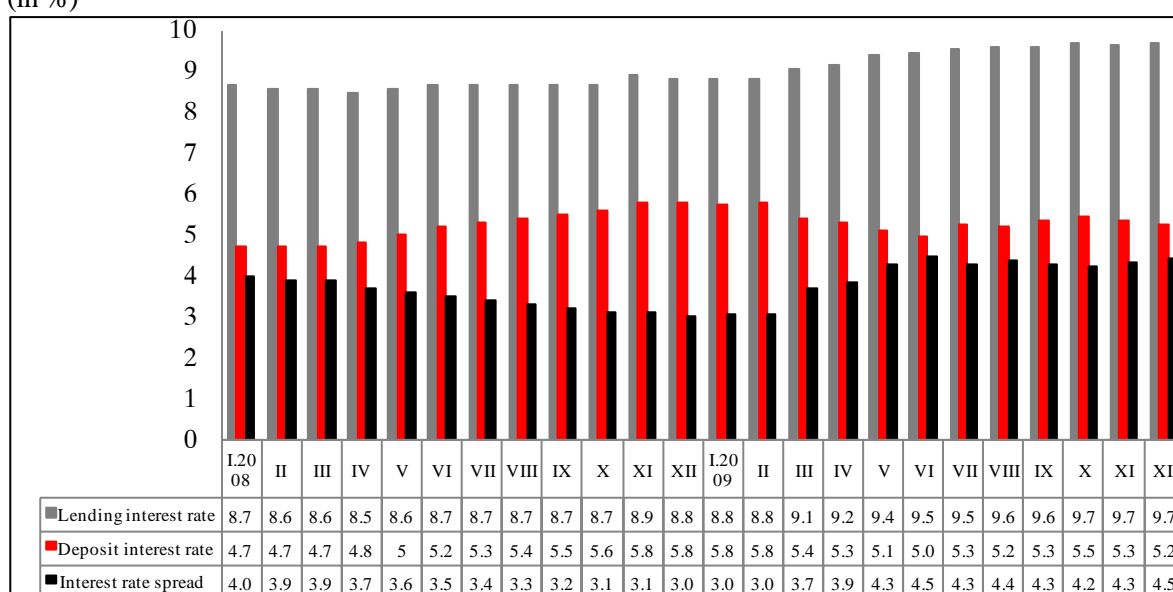
Source: NBRM.

Regarding the corporate sector, the lending interest rate went up by 0.7 percentage points, on average and it equaled 9.4%, while the deposit interest rate registered moderate increase (0.1 percentage point) and it equaled 5.4%, on average. Thus the interest rate differential with the enterprises went up by 0.6 percentage points and it equaled 4 p.p. In conformity with the results of the credit activity surveys, the banks' perceptions for the unfavorable future movements in the economy, but also within the individual activities they are exposed to, are the main factors for the increase in the risk premium with the enterprises. The banks point to the limitations arising from the costs related to the capital position as a factor with a secondary influence⁸⁸. Usually, the enterprises are far more sensitive to the factors that move the business cycle and react faster compared to the households, having in mind the direct effect on their profit position and the sources of financing. Namely, the financial position of the enterprises is typically procyclic, as a result of the procyclic component with the profits and the capital price, which in conditions of a crisis reduced the credit worthiness of the enterprises and deteriorates the credit demand quality. **In such conditions also the interest rates on the newly extended credits moved upwards, increasing, on average by 1.2 p.p. (and they equaled 9.7%).** Analyzed from the aspect of the dynamics, an increase was evidenced in April and May, which corresponds to the monetary changes. The deposit interest rates, besides their moderate increase, still maintained below the level registered in December 2008 (5.8%). Also the interest rates on the newly extended deposits moved upwards, given evident volatility, and on average they equaled 4.7%.

⁸⁸The qualitative information obtained from the conducted surveys correspond to the data pertaining to the banking sector, which point to deterioration in the indicator for non-performing loans/total loans (from 6.7% at the end of the 2008 to 9.3% in September 2009), and maintaining the indicator for the capital adequacy relatively stable (about 16.5%), high over the prescribed minimum.

At the end of the year, parallel to the signs for stabilization of both the domestic and the global economy, also signs of strengthening of the sources of financing of the banks were registered (primarily deposits), normalization of the banks' expectations and certain increase in the credit demand⁸⁹. The improved sentiment in the banking sector until the end of the year was transmitted in a decrease in the interest rates on certain types of newly extended credits. Also the decrease in the basic interest rate of the NBRM by 0.5 p.p. in November acted in that direction. However, the adjustment of the banks interest rate policy to the monetary reaction until the end of 2009 was not complete, which can be explained with the delay in the transfer of monetary signals, especially in conditions of still present uncertainty, as well as the known phenomenon of sticky prices, especially with the credit prices⁹⁰. However, with more optimistic forecasts for the future trends, as well as the anticipated effect of the monetary relaxation in the future period, banks reaction by moderate lowering of the credit price can be expected.

Figure 118
Weighted Denar lending and deposit interest rate for enterprises
(in %)



Source: NBRM.

Within the domain of the interest rates on the foreign currency credits and deposits, the movement of the international interest rates during the year, primarily the EUROBOR, contributed to the average reduction of the lending interest rate compared to the previous year. On the other hand, the changes with the deposit interest rate were under the dominant influence of the need for saving stimulation in conditions of high competitiveness on the foreign exchange market. Consequently, the first ones registered a decrease of 0.6 p.p. on average for 2009 and they equaled 7.4%, while the second ones augmented by 0.8 p.p. and equaled 3.3%, on average. Despite the average annual drop of the lending interest rates, however, the monthly analysis indicates that except in January and February, the interest rates maintained over the level registered in December 2008 (7.2%). This indicates that the adjustment with the lending interest rates to the lower EURIBOR was not proportional⁹¹, which probably reflects the higher risk premium, as well as the higher costs of the

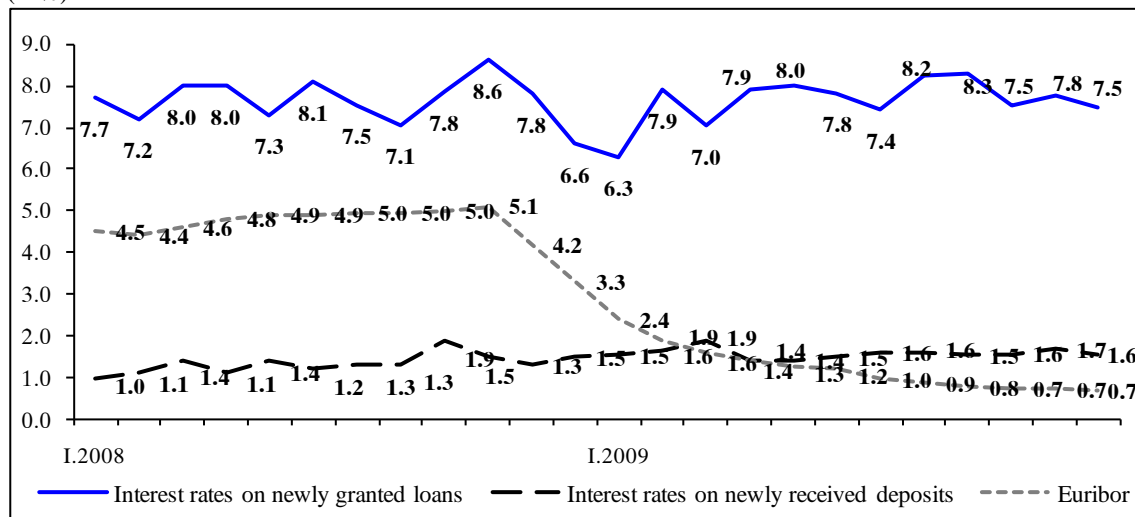
⁸⁹ Actually, also in the Banks' Lending Survey in the third quarter of 2009, opposite to the several previous surveys, the larger portion of the banks pointed to the slight decrease in the intensity of crediting terms contraction and stabilization of the drop with the credit demand and showed signs of more optimistic expectations for the following period. In the Survey pertaining to the fourth quarter, the banks pointed to the unchangeability in the crediting terms and higher demand, while the expectations for the following three-month period signalize also certain relaxation in the crediting terms, given further rise in the demand.

⁹⁰ Numerous researches point to an existence of certain asymmetry in the monetary changes transmission effects, with the lending interest rates fail to change very much in case of a decrease in the basic interest rate and the rates on the money market, while the deposit interest rates react in the same manner in case of monetary contraction (see, for an example: "Financial Structure and Interest Rate Transmission Channel of the ECB Monetary Policy, ECB Working Paper, no. 40 and "The Rigidity of Prices: Evidence from the Banking Industry", T.H.Hannan i A.N.Berger, 1991.

⁹¹ In 2009, the three-month EURIBOR decreased by 3.4 percentage points, on average.

sources of financing of the foreign currency credits. Regarding the newly extended credits, the interest rate remained unchanged, on average, relative to the average in 2008, with evident monthly variability being registered. The interest rate on the newly accepted deposits went up moderately by 0.2 percentage points and it equaled 1.6%, on average.

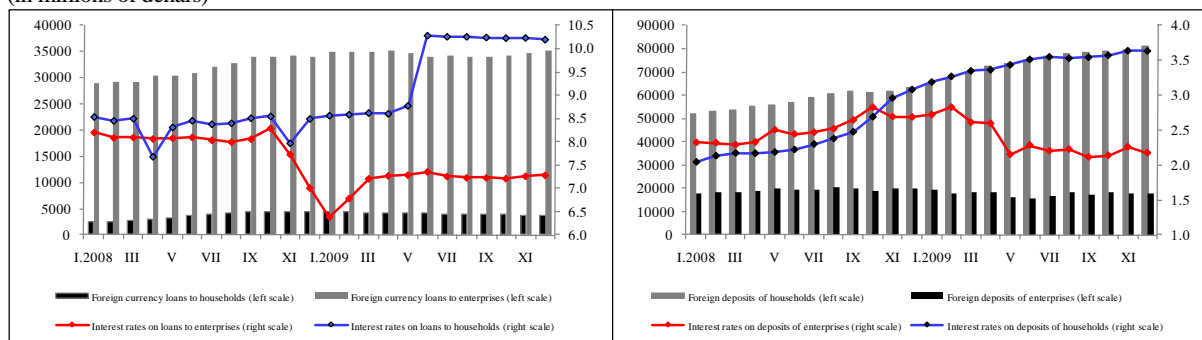
Figure 119
Foreign currency lending and deposit interest rate and three-month international interest rate EURIBOR
(in %)



Source: NBRM.

From the aspect of individual sectors, the corporate sector generally characterizes with a decline in the lending interest rates, with an increase in both lending and deposit foreign currency interest rates being registered with the households. Consequently, the interest rates on the corporate credits approved in foreign currency went down by 0.8 percentage points, on average, while the foreign currency deposits registered moderate decline (of 0.1 percentage point), with the interest rate equaling 2.4%, on average. With the households, the upward movement was almost identical in both the lending and the deposit interest rates (1.2 percentage points and 1.1 percentage point, respectively), and they equaled 9.6% and 3.5%, respectively, on average.

Figure 120
Monthly dynamics of the foreign currency credits and deposits of the private sector and lending and deposit foreign currency interest rate
(in millions of denars)



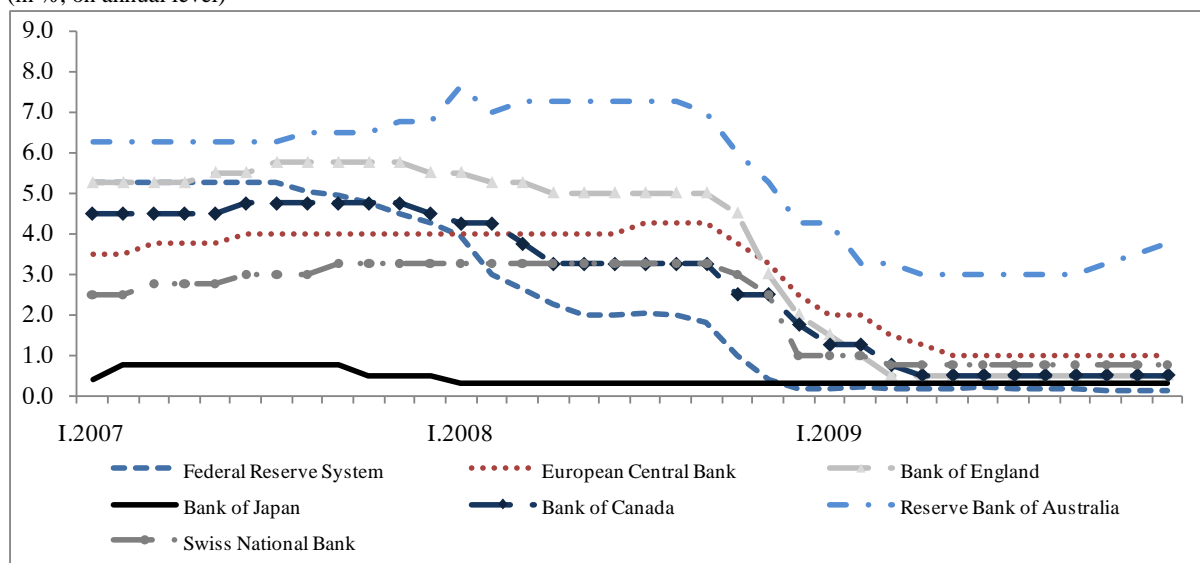
Source: NBRM

Annex 3**Conducting monetary policy during the global crisis in the developed countries relative to the developing countries**

The global crisis imposed difficult challenges for the central banks, forcing them to react differently from the method of conducting monetary policy in normal conditions. In conditions of crisis, despite the aggressive fall in the interest rates, the monetary authorities resorted to large scale reliance upon the so called balance sheet policy, i.e. policies based on more considerable change in the structure and volume of the balance sheet positions of the central banks. These was especially characteristic for the central banks of the developed countries, which in conditions of evident financial and economic shocks engaged all available instruments in function of stabilization of the financial markets and stimulation of the economic activity. On the other hand, in the developing countries, according to the characteristics and various macroeconomic context, the relaxation of the monetary policy was with smaller intensity so their central banks were generally focused on regulating the foreign currency liquidity in the domestic economies.

The implementation of the monetary policy by the central banks was usually performed through two types of instruments. First, through the short-term interest rate, i.e. the basic interest rate of the central bank, and with its adjustment the central bank signalizes the course of the monetary policy. Hence, the policy for signalizing the intentions of the monetary authorities is known as "interest rates policy". Second, through "liquidity management operations", or open market operations, through which the central bank regulated the level of liquidity in the banking system in order to maintain the market interest rate on the level consistent with the basic interest rate of the central bank. Therefore, this instrument has a technical role in the process of conducting the monetary policy, with single goal to enable practical implementation of the targeted changes in the interest rates. With such positioning of the monetary policy, which represents practice of more central banks when the economy functions normally, the central bank realizes its influence on the broader financial conditions in the country through defining the level of basic interest rate and indication of the future steps of the monetary policy in public. However, in certain specific situations, the efficient regulating of the financial conditions in the country can impose a need of more direct influence of the central bank through adjustment of its balance sheet. This can represent also an introduction and use of new non-standard instruments of the monetary policy, in function of controlling certain specific elements from the mechanism of monetary transmission, as well as for strengthening the effect which arises from the basic interest rates on the prices of the financial assets, on the income and costs of financing in the economy. As this type of operations basically result in considerable changes in the volume, the composition and the risk profile of the balance sheet of the central bank, in the literature they are known as "balance sheet policy of the central bank" (Borio and Disyatat, 2009). Therefore, the term "balance sheet policy of the central bank" pertains to the use of more types of measures, as the following: modification of instruments for regulating the liquidity in the financial system through introducing new non-standard instruments and broadening in the number of financial institutions which are directly related with the central bank, active usage of direct instruments (such as reserve requirements), conducting operations for ensuring foreign currency liquidity in the system, credit relaxation, as well as different types of quantity relaxation (such as direct purchase of Government securities, securities issued by the private sector etc.).

Figure 121
Dynamics of the basic interest rates in the developed countries
(in %, on annual level)



Source: web pages of respective central banks.

The intensive tensions on the financial markets and especially the escalation of the global financial crisis in September 2008 imposed a need for robust engagement of new measures of the monetary policy by the developed countries. Namely, this group of countries was in the firing line of the financial and later, the economic shocks as well, which was the reason for their central banks to react in direction of covering the shortages of liquidity in the financial system and calming the panic among the investors in the beginning of the crisis. For this purpose, the central banks basically used the standard monetary instruments for regulating the liquidity in the financial system, so with exception of the USA Federal Reserves System (which reacted immediately with drop in the interest rate), the other central banks did not perform more considerable relaxation of the interest policy (at the middle of 2008, ECB even reacted with rise in the basic interest as well, with inflation pressures that were still present). But, the situation drastically changed as a result of the events in September 2008. The bankruptcy of the "Lehman Brothers" and the interventions with government financial support of the "AIG" insurance company blocked the flows of liquidity to the financial and non-financial companies, additionally inhibiting the already weakened channels of monetary transmission since the beginning of the crisis. Simultaneously, the first signs of weakening of the activity in the real economy sector showed. The central banks responded to these changes by decreasing the basic interests and more robust interventions towards liquidity injection in domestic and foreign currency denomination in the domestic financial systems. Since the beginning of 2009, as the economic crisis was becoming more intensive and the inflation pressures were depleting, the relaxation of the monetary policy continued more intensively. The central banks decreased their interest rates to the lowest historical levels, reducing them near the effective threshold in certain countries, and part of them committed publically to their maintenance at that level within a longer period (USA Federal Reserves Systems, Bank of Canada). However, the conditions for evident impaired functioning of the channels of monetary transmission and the worsened situation the financial sector and the total economy were facing with in that period, clearly showed that the conventional monetary instrument, i.e. the interest rate, although undoubtedly efficient in the pre-crisis period, shall be not enough to overcome the crisis. In such conditions and facing the risk from exceeding the zero bound on interest rate, most of the central banks transferred the attention from interest rates, to "balance sheet policies" and renamed the so called measures for quality and measures for quantity relaxation of the liquidity terms⁹². Table 1

⁹² The measures for quality relaxation pertain to lowering the quality standards of the collateral required by the central bank instead of extending credits to banks. The quantity relaxation includes purchase of certain financial assets by the central bank, in order to influence its price. Accordingly, generally four measures were undertaken: 1) measures for systemic relaxation of the liquidity conditions, acting towards rise in the liquidity through mitigating the systemically significant liquidity shortages on the key money markets; 2) purchase of long-term Government securities, as well as measure acting towards drop in the long-term interest rates and mitigating the imbalances on the long-term

shows systematic review of the measures undertaken by the three large banks, USA Federal Reserves System (FED), the European Central Bank (ECB) and the Bank of England, in function of stabilizing the financial sector and stimulating the economy in 2009. As stated with Gerlach (Gerlach, 2010) most of these instruments represented an integral part of the operative frameworks of the monetary policy of the large central banks in the period before the crisis as well. Namely, the repo operations represent standard instrument of the central banks for ensuring liquidity for the financial system, so in the period before the crisis they were organized by the principle of relative short maturity dates (starting with over night and up to two weeks). The available lines of credits were also accessible for the banks in the pre-crisis period, so in conditions of normal distribution of the liquidity in the financial system, the commercial banks showed relatively small interest for use of this instrument. However, the global crisis imposed a need for an adequate adjustment of the positioning of these instruments, as well as of the terms for their usage.

Therefore, although representing standard instrument for obtaining liquidity for the financial sector, during the crisis the role of the repo operations was modified, so the central banks increased the volume considerably and prolonged the maturity of these operations (see more detailed with Borio and Nelson, 2008). The approach to the available credit lines was simplified, and the conditions for the collateral were largely liberalized. FED and the Bank of England reacted with introducing several new instruments as well, such as Term Auction Facility in USA. As shown in the table, as the crisis developed, all three central banks reacted with direct purchase of securities as well. Simultaneously, in function of relaxation of the international financial terms, the central banks were mutually covering the shortages of foreign currency liquidity through foreign currency swap operations.

Table 20
Selected measures of the large central banks in 2009

	March	June	September	December
	level, in billions of own currency units, end of month			
United States				
Federal Reserve System: Total assets	2,073	2,027	2,162	2,237
Repos and term auction credit	469	283	196	76
Standing facility lending	81	49	28	19
Other lending	249	165	85	62
FX swaps providing own currency	328	119	59	10
Securities	761	1,217	1,588	1,845
Euro area				
Eurosystem: Total assets	1,803	1,997	1,790	1,905
Repos	661	896	681	749
US dollar repos	166	60	44	1
Standing facility lending	1	0	0	1
FX swaps providing own currency	2	5	4	3
Covered bonds	0	0	14	29
United Kingdom				
Bank of England: Total assets	181	220	223	238
Repos	130	91	39	24
US dollar repos	10	2	0	0
Operational lending facility	0	0	0	0
Securities	15	99	154	190

Source: Gerlach Petra (2010), "The Dependence of the Financial System on Central Bank and Government Support", BIS Quarterly Review, March 2010

Although it is hard to measure precisely the effectiveness of the balance sheet operations, still the fact that they contributed for alleviating the liquidity tensions is indisputable, evidently improving the situation on the key markets. The start of the process of revival of the economic activity in the

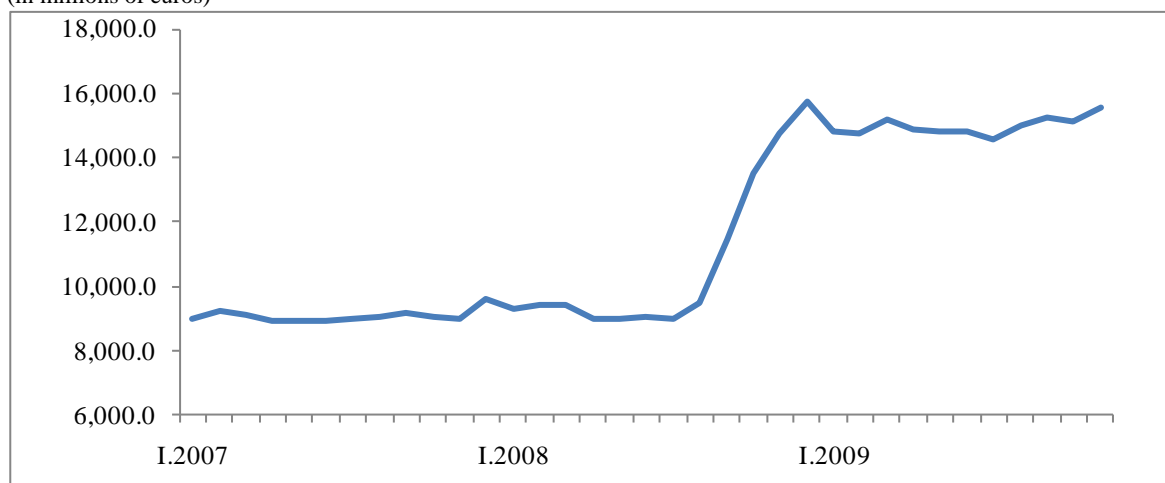
credit markets; 3) purchase of securities issued by the private sector for supporting the crediting on the key markets, in function of achieving macroeconomic goals ; and 4) operation for ensuring foreign currency liquidity, the primary function of which is not to mitigate the fluctuations of the foreign exchange rate, but to neutralize the shortage of foreign currency liquidity in the domestic economy.

third quarter, as a combined effect of the monetary interventions and large stimulative fiscal packages is in favor of the effectiveness of the markets. But, although it appeared that they were an effective instrument for mitigating the crisis situations, the balance sheet policies carry their own costs and risks. Thus, as the developed countries gradually started to overcome the recession, their central banks were facing new and not very easy challenge for creating adequate strategies which will ensure smooth and less painful overcome of the "crisis form" of conducting the monetary policy. Namely, the relaying on the balance sheet policies resulted in rise in the volume and modification of the structure of the balance sheet positions of the central banks, stressing the risks from higher financial costs for the central banks and prolonged hindered functioning of the channels of monetary transmission. The risk from non-optimal rise in the offer of money in the economy is also present, based on the evident expansion of the balances of the central banks and the monetary base, with effect in direction of triggering the pressures for inflation growth. With respect to the banking system, the prolonged maintaining of the robust monetary stimuli can cause two undesired effects: 1) undermining the competition in the banking sector; and 2) motivating the banks to delay the necessary balance sheet adjustments and underestimating the risks again in the process of adopting business decisions (Gerlach, 2010). Therefore, the need of an adequate and timely neutralization of the undertaken balance sheet operations is clear, which at the end of 2009, the large central banks have already started to implement. Simultaneously, considering the fact that the level of the interest rate close to zero is non-sustainable on long term, the central banks are expected to increase the interest rates. But, if the growth in the interest rate is too fast and uncoordinated it can suffocate the already weak economic recovery and can weaken additionally the balance sheet positions of the banking sector, especially if it corresponds with the inevitably required measures for fiscal consolidations. This clearly indicated the critical significance of the monetary and fiscal coordination for successful overcome of the crisis in the developed countries and the need for its elevation on a much higher level than the usual in the following period.

Figure 122

Dynamics of the aggregated balance sheet of the developed countries*

(in millions of euros)



* It pertains to the data on the balance sheet (assets plus liabilities) of: the USA Federal Reserves System, Bank of England, Bank of Canada, European Central Bank, National Bank of Switzerland, Bank of Japan and Reserve Bank of Australia. Source: Constructed variable based on data from IFS.

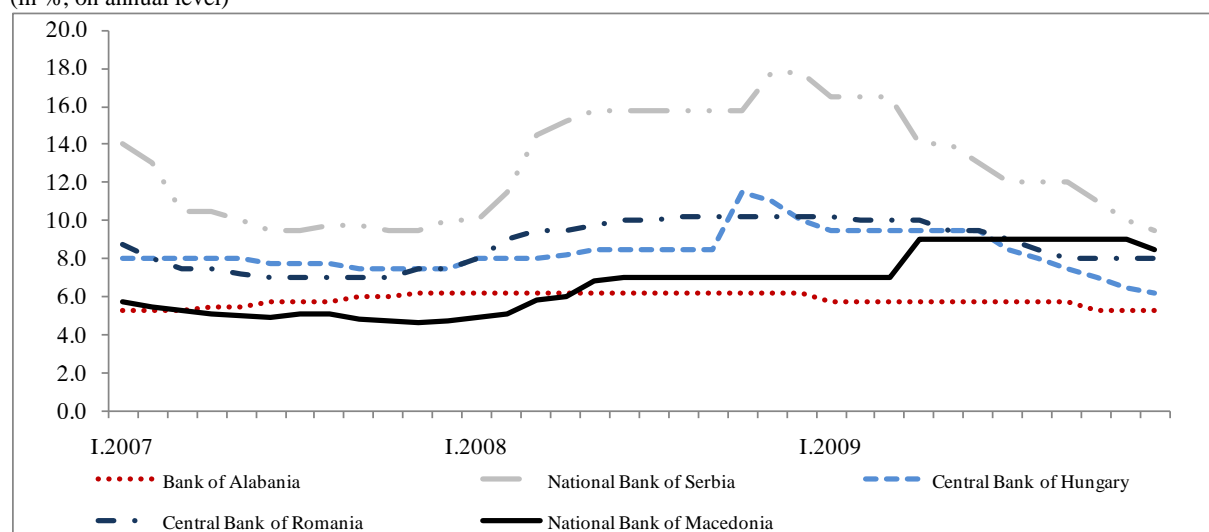
With respect to the developing countries, the measures that were undertaken by their central banks generally differed from those in the developed countries, both with respect to the time consolidation and to the type and intensity of the monetary reactions. Namely, as indicated by certain authors, the "EME central bank crisis measures differed from those of AEs in timing, type, and magnitude (Table 3). They started taking intervention measures at a much later stage and, overall, they eased monetary policy conditions less than did AE central banks. EME central banks focused largely on foreign exchange liquidity measures, as well as using both interest rates and direct instruments (e.g., adjustments in a reserve requirement framework) to ease conditions. The varied crisis response

measures of EME and AE central banks reflected different financial systems and the response to the global crisis. First, EME domestic financial sectors generally experienced less stress compared to those of AE countries. Second, EMEs, along with some AEs, faced acute shortages of foreign liquidity, mainly in U.S. dollars. Third, some EME central banks utilize direct instruments as a matter of course, and they relied on these during the crisis much more than did AE central bank" (Fujita *et al*, 2010, p. 17).

In conditions of relatively lower level of development and low integration of the financial systems in the global financial flows, the crises overflow in the developing countries started being noticed after the unexpected sharp restriction of the global liquidity conditions in September 2008. In this initial phase, the central banks of the developing countries were mainly focused to the neutralization of the imbalances on the foreign exchange market and mitigation of the pressures for depreciation of the domestic currency, considering the fact that in conditions of lower capital inflows and higher psychological pressure on the economic entities, their economies faced a lack of foreign currency liquidity. In this context, in most of the countries, the conditions of the already existing instruments for obtaining foreign currency liquidity were largely relaxed, and in some countries new tools in form of foreign currency repo transactions, credits and swaps were introduced. Depending on the situations, part of the central banks reacted in direction of facilitating the approach to liquidity in domestic currency as well. The reactions with drop in the interest rates came a bit later as a reaction to the started weakening of the economic activity and stabilization of the inflation expectations. However, the relaxation of the monetary policy was performed carefully and with considerably lower intensity, compared to the developed countries, so the level to which the interest rates were reduced, stayed high above the effective threshold of the interest rates. Namely, the risks from potential worsening in the external imbalance restricted the possibility for more aggressive contra-cyclic adjustment of the monetary policy in these countries. Thus, stimulated by the risk that the evident changes in the foreign exchange rate can result in additional destabilization of the economy, the countries with flexible regime of foreign exchange rate were concentrated mostly on prevention from higher depreciation of the domestic currency, whereas in the countries with regime of fixed foreign exchange rate, the interest policy of the central bank solely depended on the need of maintaining stable value of the domestic currency. Excluding the Bank of Israel, most of the central banks from the developing countries characterized with limited usage of balance sheet operations, so the rise in the balance sheet positions of their central banks was considerably lower as well relative to the developed countries.

Figure 123

Dynamics of the basic interest rates in the developing countries, from the area
(in %, on annual level)



Source: web pages of respective central banks.

In such conditions, it seems that the central banks of the developing countries were facing with lower challenges when leaving the adjustable conducting of the monetary policies in the crisis period. As the economic analysts indicate (Portugal, 2010), for these countries it is critically important to determine the real time for overcome and for withdrawal of the monetary stimuli, considering the fact that the prolonged maintenance of low interest rates after closing the negative production gap, can result in inflationary pressures and endangering of the financial stability in these countries.

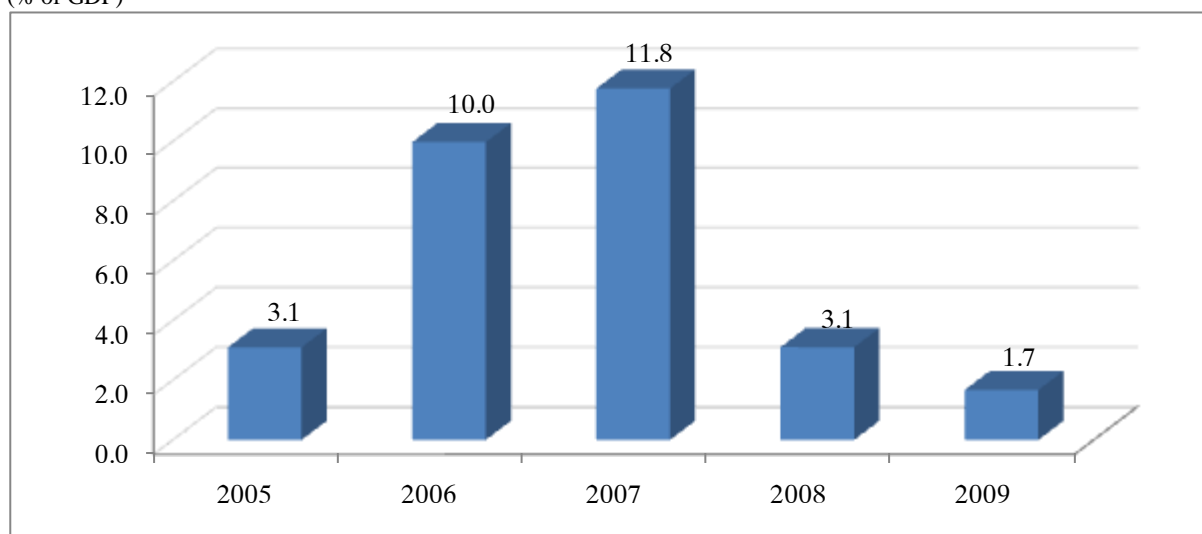
References:

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2. Baba et al (2009), "Overview: Risk Appetite Rebounds Stabilization Hopes", BIS Quarterly Review, June 2009.
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IV. Capital market

Turbulences on the global and regional financial markets in 2009 had transfer effect on the Macedonian stock exchange as well. The lack of trust with the market participants, the drop in the liquidity, higher volatility and unpredictability of the price developments were characteristic for the Macedonian capital market, which registered low volume of trading and variable price developments in 2009. Thus, after the large downward correction in the turnover and the prices in 2008, in 2009 the fall in the stock exchange trading continued, whereas the price index registered alternating rise and drop in the value. The first signs of revival emerged in the second half of the year, but only through upward developments in the price levels.

Figure 124
Stock exchange turnover by years
(% of GDP)



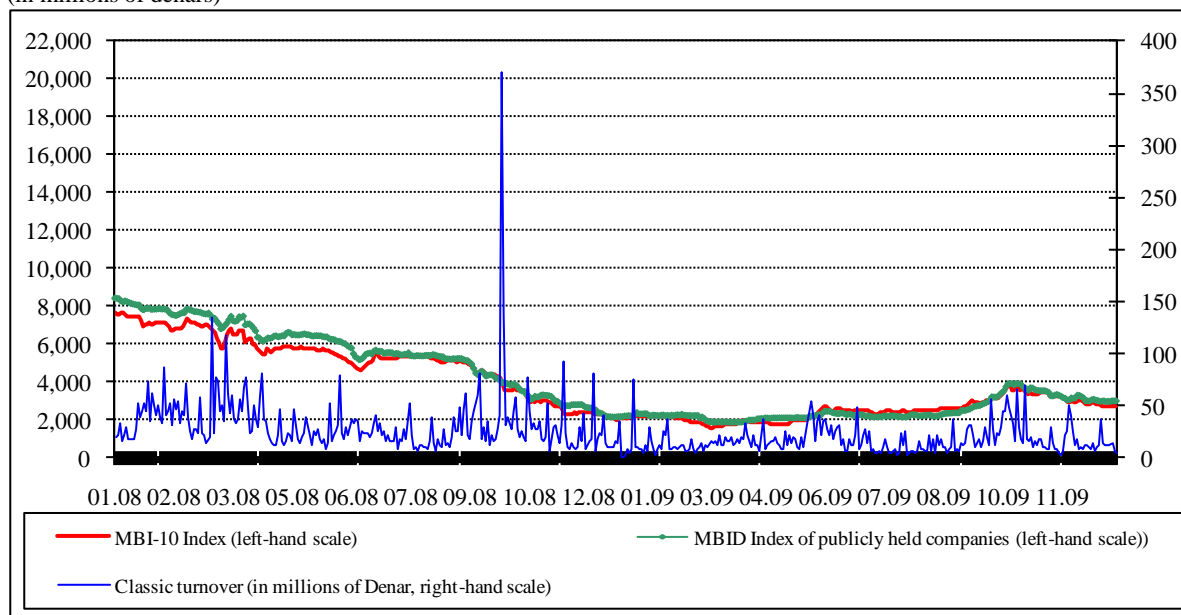
Source: Macedonian stock exchange AD Skopje and State Statistical Office of the Republic of Macedonia.

In 2009, the Macedonian stock exchange index (MBI-10) registered average drop on annual basis of 51.5%, with various dynamics being registered during the year. Thus, in conditions of evident uncertainty, at the beginning of 2009 its downward adjustment continued, so it registered new minimum⁹³ in March 2009. The first signals for certain revitalization of the activity on the Macedonian stock exchange emerged in the second quarter, parallel with their revival of the global and regional capital markets. This was a period within which the first expectations for moderate recovery of the global economy showed. Thus, during the year MBI-10 went up to a level which was by 2.5 times over the annual minimum, and it finished the year at a level which was by 1.7 times over the minimum for 2009. The fluctuations in the MBI-10, which resulted from the information that were received from the developed capital markets, were mostly due to the market shallowness as well. Namely, the low stock exchange turnover created situations when even a small activity on the side of the sale or purchase results in a larger deviation in the prices of certain shares. In 2009, the index of publicly held companies (MBID)⁹⁴ almost fully followed the fluctuations of MBI-10, ending the year at a level which was higher by 37.1% compared with 2008.

⁹³ In 2009, MBI-10 registered the lowest value on 10.03.2009 thus positioning at the level of 1.598,5 indexed points.

⁹⁴ Price non-weighted index, the components of which are determined having in mind the number of trade days and the realized turnover between two index reviews.

Figure 125
 MBI-10, MBID and stock exchange turnover realized with classical trade
 (in millions of denars)



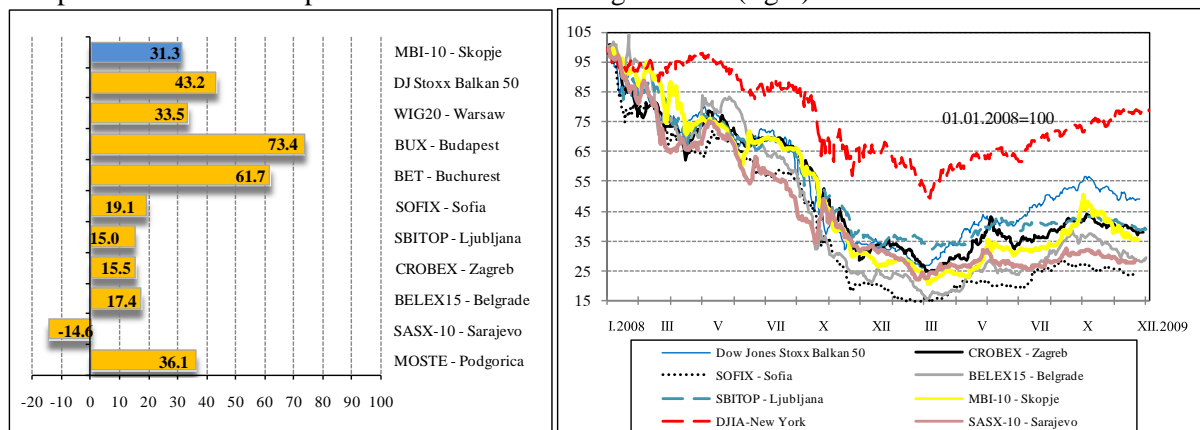
Source: Macedonian stock exchange AD Skopje.

The capital markets in the countries from South East Europe countries, as a result of the higher level of integration, were under stronger direct influence of the information which came from the developed capital markets. Therefore, after the larger share of the indices from the analyzed regional stock exchanges registered the lowest levels in the first quarter of 2009, development in upward direction was registered further this year. Besides the optimism for the leading world economies, the readiness of EU and IMF⁹⁵ for supporting these economies contributed considerably to the partial returning of the investors on the regional stock exchanges, whereas the macroeconomic indicators of these countries can not be indicated as a factor which influenced the changes in the capital market in this period. In conditions of evident instability of these stock exchanges, more certain upward trend can be expected only if the real sector stabilizes and if the macroeconomic indicators in individual economies improve. In 2009, the Hungarian BUX grew up considerably (rise of 73.4% at the end of 2009, relative to the end of 2008), followed by the Romanian BET (61.7%) and Montenegro MOSTE (36.1%). The Croatian CROBEX and the Slovenian SBITOP registered positive development of only 15.5% and 15%, respectively, whereas the Sarajevo SASX-10 deepened its fall by 14.6% relative to the level at end of 2008.

⁹⁵ Raiffeisen research, No. 33 and 34, April and July 2009.

Figure 126

Annual growth rates of the national and composite regional stock exchange indices⁹⁶ (left) and comparison of the development in the stock exchange indices (right)

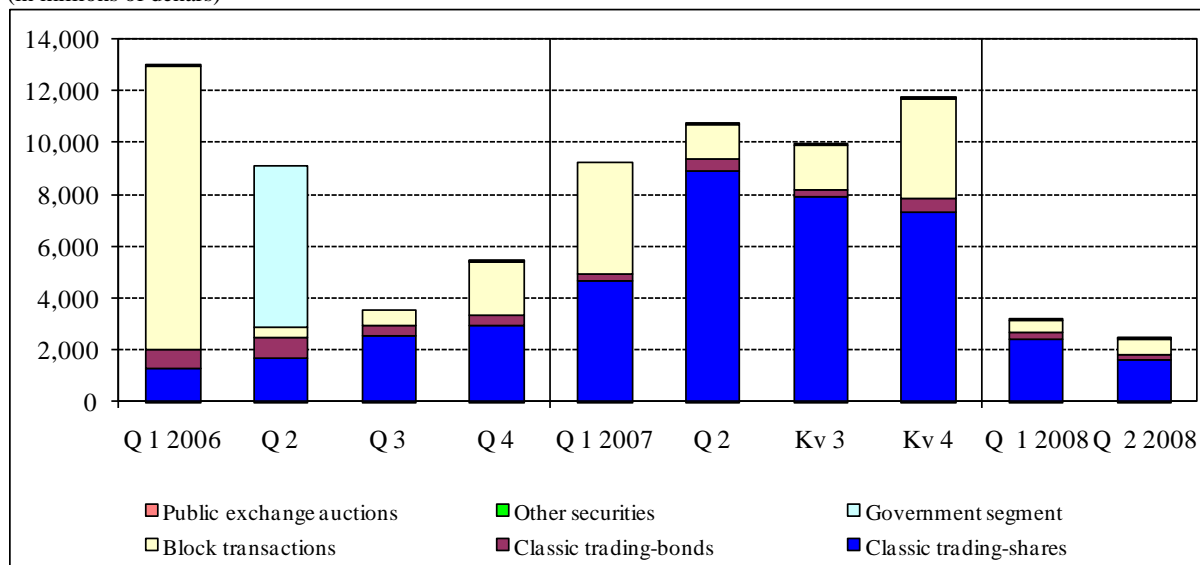


Source: Bloomberg, Macedonian stock exchange AD Skopje, national stock exchanges.

In 2009, the market lethargy and the lower activity were the main feature of the Macedonian capital market. Thus, in 2009 the total stock exchange trade amounted to Denar 6.7 billion, which represented drop of 45.6% compared with the previous year. All segments of the stock exchange registered trade fall. However, the high fall in the turnover reflected mostly the lower volume of classical trade with shares (decrease of 58.1%). Besides the fall, cyclic developments characterized the classical trade in this period, indicating also situation when the optimism of the investors, which returned on a very short period, disappears under the influence of negative information from the real sector. During the year, the trading with shares of companies from the banking sector, the steel industry and the pharmaceutical industry participated mostly in the classical share trade. The stock exchange turnover realized through bloc transactions registered annual drop of 37.2%. In conditions of fall in the economic activity, and subsequently lower anticipated company position, such developments on the stock exchange were expected. Simultaneously, the generally uncertain ambient, followed by chain of risks, motivated the investors to behave carefully and to direct the available assets towards less risky instruments. The rise in the interest rates of deposits and Treasury bills stimulated redirection of a share of the available assets towards these alternatives for investing, i.e. it represented an additional support of such strategy.

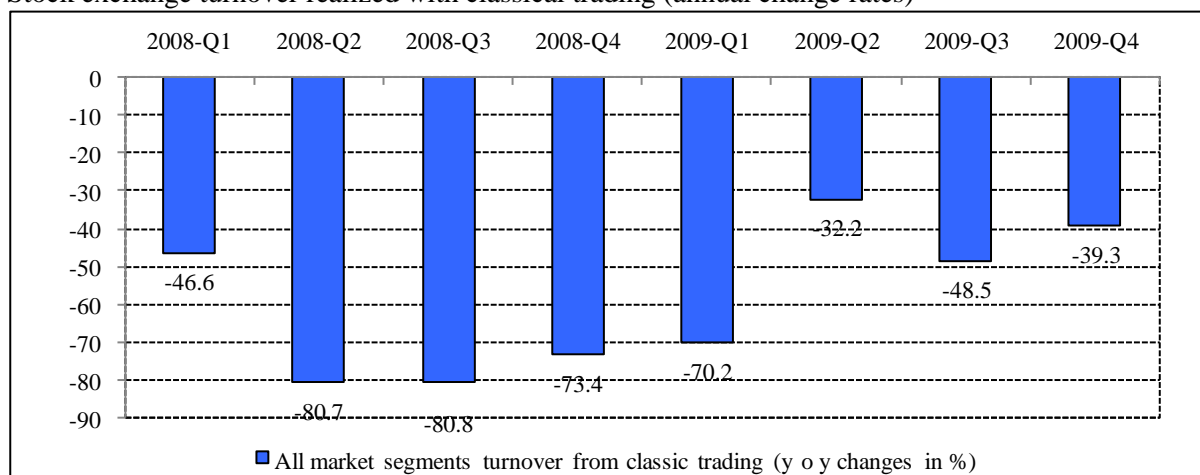
⁹⁶ "Dow Jones Stoxx Balkan 50" includes the shares of the 50 largest and most liquid companies from eight Balkan stock exchanges.

Figure 127
Structure of the stock exchange turnover⁹⁷
(in millions of denars)



Source: Macedonian stock exchange AD Skopje.

Figure 128
Stock exchange turnover realized with classical trading (annual change rates)



Source: Macedonian stock exchange AD Skopje.

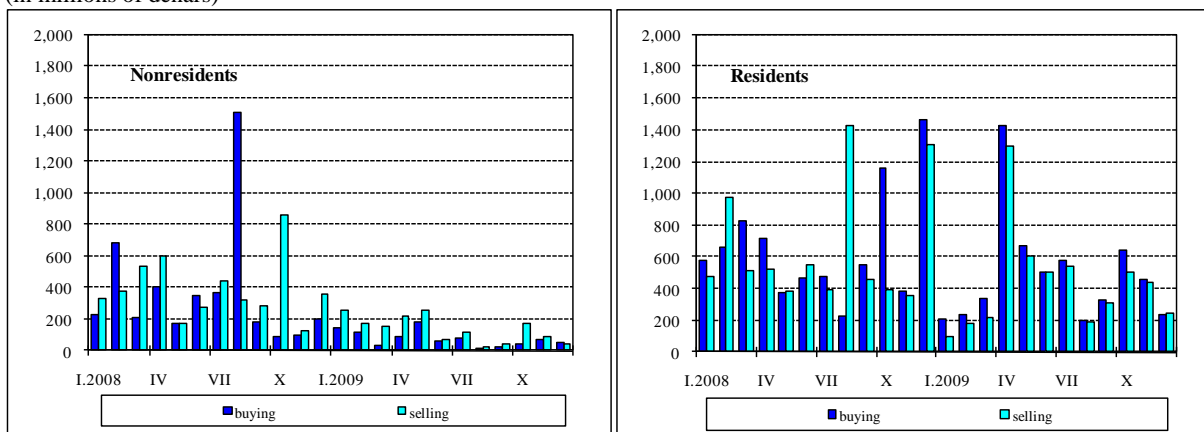
In 2009 the foreign investors had relatively small participation in the trade on the Macedonian stock exchange, both, on the side of purchasing and on the side of sale. On net basis, the foreign investors held back from investments in securities on the Macedonian stock exchange in

⁹⁷ **Classical trading** on the stock exchange implies trading through "BEST" (stock exchange electronic trading system) on the Macedonian stock exchange. The turnover realized with classical trading does not include the turnover realized on the public stock exchanges and the registered bloc transactions; **The public stock exchange auctions** are conducted on a special stock exchange segment within the "BEST". The subject of auctions is the state capital in form of shares in the joint stock companies in the Republic of Macedonia owned by the Republic of Macedonia and the Government authorities, which are sold by the authorized Government authorities, as well as the shares owned by the Pension and Disability Insurance Fund of Macedonia. Shares offered by the National Bank of the Republic of Macedonia, on a manner and terms defined by the law, can be subject of auction; **Bloc transaction** is a security transaction which is concluded with intermediation of one or more members of stock exchange out of the regular trading at "BEST". The bloc transaction can be concluded only with shares. The members of the stock exchange can conclude bloc transaction only if the value of bloc transaction amounts at least Denar 5.000.000.00. The price of the registered bloc transaction for the shares that are traded on the official and regular market on the stock exchange shall not deviate more than $\pm 10\%$ of the weighted average price of all transactions with these shares on the stock exchange in the last 30 calendar days, including the trading day of registration of the bloc transaction. If the shares which are traded on the official and regular market on the stock exchange, which are subject of bloc transaction, were not traded in the last 30 calendar days, including the trading day of registration of the bloc transaction, the price of auctions in the bloc transaction is freely created.

the amount of Denar 677.6 million. Such trends can be partially explained by the shallowness of the Macedonian capital market, which obstruct fast and low cost withdrawing from investments. In conditions of evident uncertainty and risks, such feature represents considerable restrictive factor. Simultaneously, the considerably lower liquidity, the preferences for investing in own economies, the pressure for withdrawal of assets of clients of the foreign institutional investors were also factors that were acting towards decrease in the participation of the foreign investors on the Macedonian capital market. At the end of the year, the foreign investors participated with 26.91% to the total principal of companies and 3.57% to the total nominal value of bonds (33.26% and 4.77%, respectively, at the end of 2008). The return of the foreign investors on the stock exchange was mostly determined by the liquidity on the global and regional stock exchanges, by the preferences for taking risks, the income which would arise from the domestic shares, as well as by the financial indicators for operating of the Macedonian companies. When the domestic investors are in question, the domestic natural persons in 2009 on net basis would withdraw of investments in the amount of Denar 381.2 million, whereas the domestic legal entities invested Denar 1.058,9 million on net basis.

Figure 129

Turnover on the stock exchange in 2009, by investors and direction of transactions
(in millions of denars)



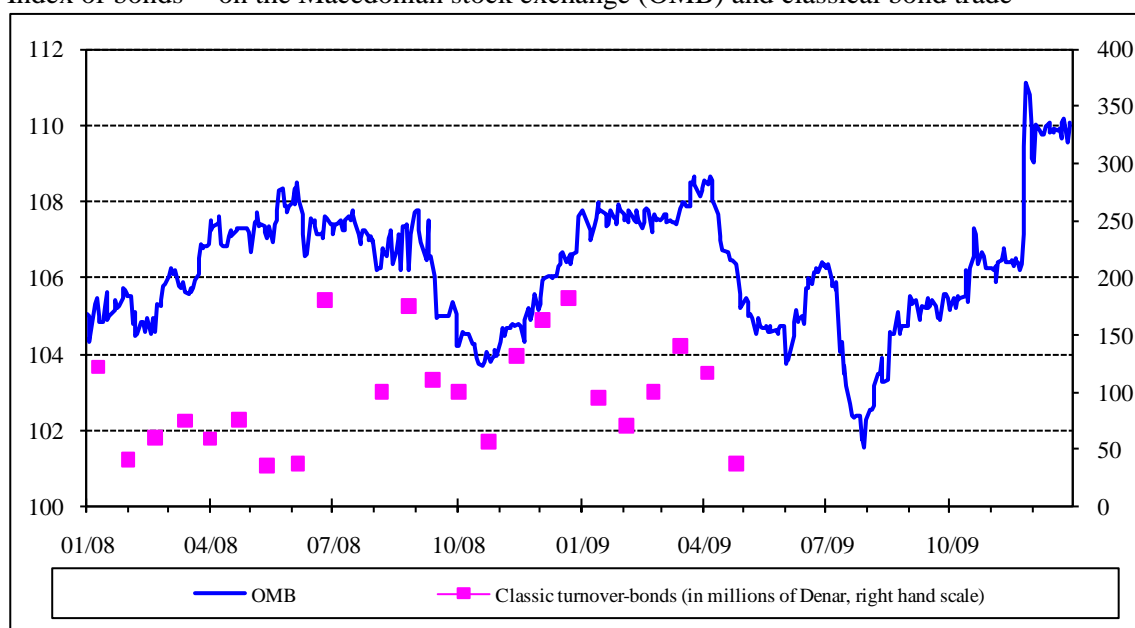
Source: Macedonian stock exchange AD Skopje and NBRM calculations.

The realized turnover with bonds on the official market⁹⁸ on the stock exchange in 2009 amounted to Denar 1.304,4 million and it went down by 10.3%, relative to the previous year. The bonds for denationalization from the eight issue were traded mostly (48.9% of the total turnover realized with bonds). During the year, the prices of the Government bonds had relatively broad range - from 73.1% (bond for denationalization from the eight issue) to 100% (Corporate bond of "Prokredit banka" AD Skopje and Corporate bond of "NLB Tutunska Banka" AD Skopje) of the nominal value. The index of bonds on the Macedonian stock exchange⁹⁹ (OMB) till the end of March swung around stable trend. In the period April-July, although with short periods of rise and stagnation, the index registered downward correction registering the minimal value for 2009 at the end of July. Since the beginning of the third quarter the trend changed, so till the end of the year this index positioned at the level of 110.1 index point, which represented rise of 2.3% relative to the end of the previous year.

⁹⁸ Listed securities are traded on the **official market on the stock exchange**. Listing of securities represents procedure of introduction of a security on the official market in accordance with certain criteria prescribed by the stock exchange and the liability for regular public disclosure of financial and non-financial information and data vulnerable to price change. On the official market there is a classification of **stock exchange listing** and **super listing**. The second segment on the stock exchange is the regular market where there is division: market of publicly held joint stock companies and free market. **The market of publicly held joint stock companies** is a segment where the non-listed securities are introduced issued by the joint stock companies with special responsibilities for notification, in accordance with the Law on Securities. Since 10.09.2009, the name of the market segment "market of publicly held joint stock companies" is changed in **market of joint stock companies with special responsibilities for notification**. **The free market** is the market segment where all other securities are traded except for the one being traded on the official market and the market of publicly held joint stock companies.

⁹⁹ The OMB index is composed of bonds for old foreign exchange savings and denationalization bonds of the 1st, 2nd, 3rd, 4th, 5th, 6th, 7th and 8th issue. The OMB is a price index weighted by the turnover, with a restriction according to which the share of none of the bonds within the index structure is not allowed to exceed 30%.

Figure 130
Index of bonds¹⁰⁰ on the Macedonian stock exchange (OMB) and classical bond trade



In 2009, transactions with Treasury bills in nominal amount of Denar 429 million were realized on the over the counter market (Denar 186.5 million in the previous year), as well as transaction with CB bills in nominal amount of Denar 340 million (opposite to Denar 1.665 million in 2008). The fall in the secondary trade can be partially related with the periodical character of the transactions on this market, where there was no continuous activity. Simultaneously, the lower secondary trade with CB bills corresponded with the lower stock of undue CB bills, the annual drop of which amounted to 9.1% in 2009.

¹⁰⁰ On April 6, 2009 the Macedonian stock exchange adopted a decision on listing of the 8th emission of denationalization bonds on the official market since April 9, 2009. The total amount of the emission is Euro 23 million, the nominal value of one bond is Euro 1. The date of due is June 1, 2019.

V. Other activities of NBRM

5.1. Payment system in the Republic of Macedonia

In 2009, the payment system in the Republic of Macedonia continued enabling smooth performance of the payment transactions. The NBRM, as the owner and manager of the Macedonian Interbank Payment System (MIPS), through which real time gross settlement is performed, successfully implemented its operational function in the payment system. Also, the other components of the payment system, the Clearing House "KIBS" AD Skopje, "Kasis" AD Skopje and the internal bank systems, through their functioning, contributed to stable, smooth and efficient performance of the payment transactions in the Republic of Macedonia.

In 2009, the National Payment Systems Council of the Republic of Macedonia was focused on the implementation of the Payment System Development Strategy of the Republic of Macedonia 2007-2011. The work groups of the National Payment Systems Council in 2009 identified all the rules and technical standards which are required to be implemented in the following period till the final joining of the Republic of Macedonia to the European Union. Through the National Council of Payment Systems of the Republic of Macedonia, complete cooperation and coordination with the institutions, which are indirectly and directly related with the payment system and in charge of implementation of strategic instructions, was performed.

5.1.1. NBRM's role in the payment operations

In the performance of its operative function, NBRM manages the settlement system - MIPS. In 2009, MIPS operated in a real time with accessibility of 99.98% of the envisaged working time during the entire year. Furthermore, the system processed 19.105 transactions a day on average, whereas the maximal number of transactions processed per day amounted to 64.467. Introducing the latest technical and technological solutions in the infrastructure of MIPS in 2009 resulted in absence of queuing resulting from technical reasons.

Participants in MIPS are the banks (including the NBRM), the clearing institutions, brokerage houses and Ministry of Finance. At the end of 2009, the total number of participants in MIPS equaled 25.

In 2009 the NBRM received and processed 4.412 execution orders and decisions on forced collection, out of which 952 were fully executed, whereas the other were partially or fully unexecuted, as a result of lack of funds with the debtors, delayed by the body that adopted them, or they were not complete because that they were either returned to the courts, or to the authorized executors to be finalized.

Within the authorizations for oversight of the payment systems, in 2009, NBRM performed off-site oversight on the internal payment system of banks and payment system of the clearing house through information received based on the Instructions on submitting data on performed activities in the payment operations.

In 2009, within the technical cooperation with the Central Bank of Nederland, an oversight was conducted over MIPS of the National Bank concerning the compliance with the seventh basic principle (Core Principle No. 7: "The system should ensure a high degree of security and operational reliability and should have contingency arrangements which shall in any case enable timely completion of daily processing"). Through the conducted oversight over its own payment system (MIPS), the National Bank fully accepted and implemented the "Responsibility B" in the implementation the Core Principles (Responsibility B: "The central bank should ensure that the systems it operates comply with the Core Principles").

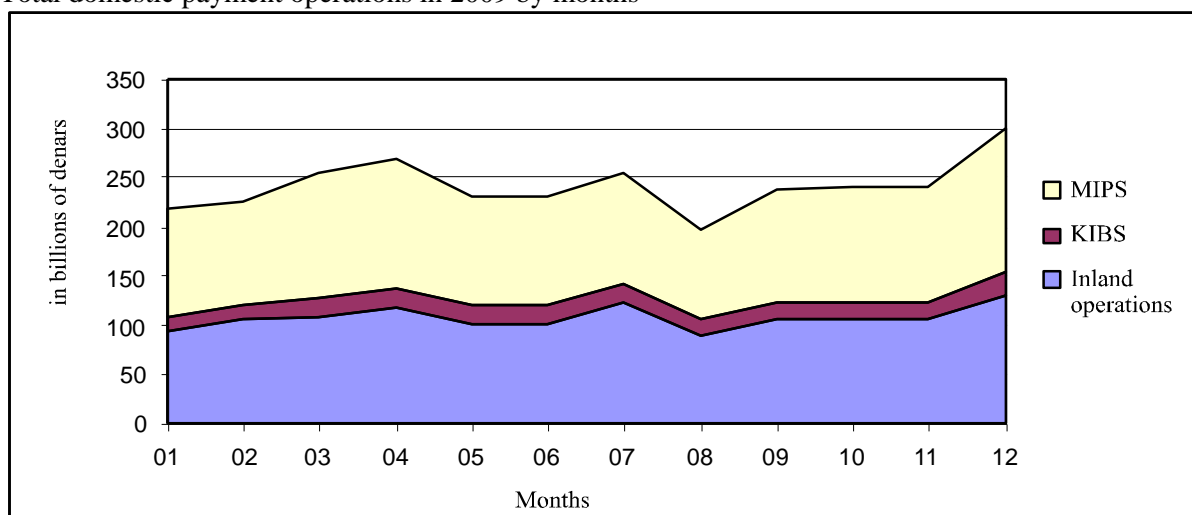
5.1.2. Indicators for the operations of the payment system in the Republic of Macedonia

In 2009, total 370.143 new accounts of natural persons and legal entities were reported in the Single Accountholders Registry with the careers of the payment operations in the Republic of Macedonia, and 36.308 accounts were closed, so the total number of opened accounts in the Single Accountholders Registry reached up to 3.293.371 at the end of the year. Holders of these accounts were 1.403.370 different entities (natural persons and legal entities), where 45.38% of them holding only one account, while the average number of opened accounts equaled approximately 2.35 accounts per entity.

At the end of 2009, the total number of registered blocked accounts amounted to 56.313. In 2009, 71.189 blockings were instigated, and in the same period 29.262 were unblocked, which represented 41.10% of the total number of initiated blockings.

In 2009, the executed payment operations totaled Denar 2,887.35 billion. The internal payment operations of banks (among accounts in a same bank) amounted to 44.2%, interbank payment operations realized through MIPS equaled 48.2% and 7.6% represented interbank payment operations realized through KIBS.

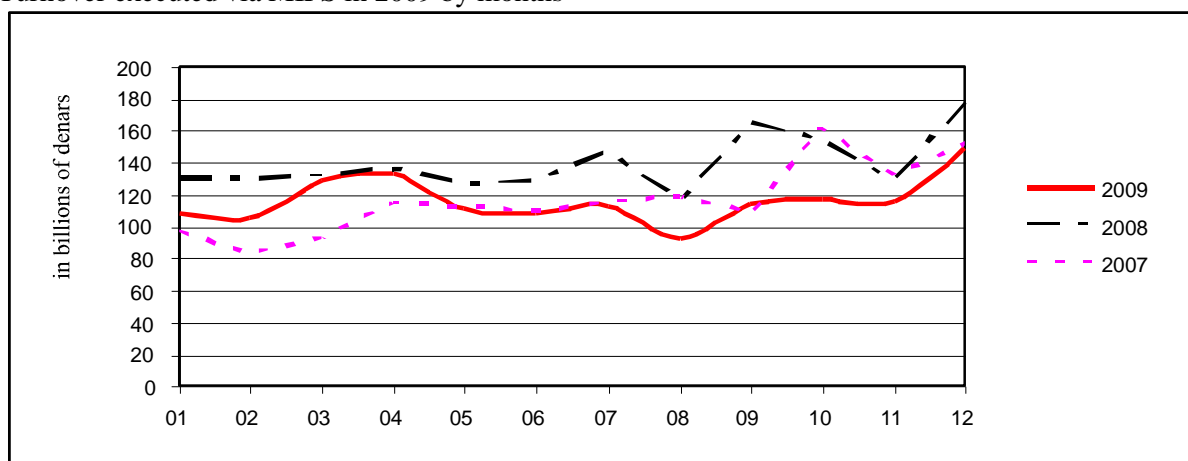
Figure 131
Total domestic payment operations in 2009 by months



Source: National Bank of the Republic of Macedonia.

The turnover realized via MIPS went down by 16.6% relative to the previous year. Out of the total turnover via MIPS, 54.1% represented interbank turnover realized by payment operations careers - banks, whereas 45.9% represented turnover realized by an order given by the Government institutions (NBRM, Treasury system), clearing and brokerage houses.

Figure 132
Turnover executed via MIPS in 2009 by months



Source: National Bank of the Republic of Macedonia.

In 2009, the total number of realized transactions in the domestic payment operations amounted to 49.204.300, out of which 9.6% were performed through MIPS, 33.8% through KIBS, and 56.6% were transactions performed through the internal clearing in the banks.

In 2009, the number of executed transactions went down by 3.8% relative to the previous year. Out of the total number of transactions via MIPS, 34.0% represented interbank transactions realized by payment operations careers - banks, while 66.0% represented transactions realized by an order given by the Government institutions (NBRM, Treasury system), clearing and brokerage houses.

5.2. Cash management operations

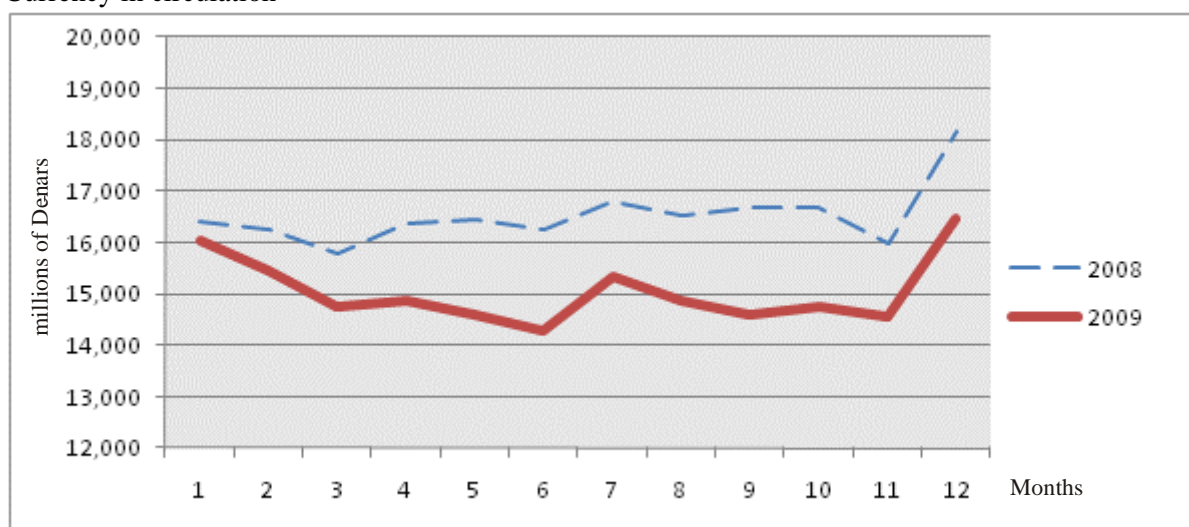
5.2.1. Currency in circulation

On December 31, 2009, the currency in circulation amounted to Denar 16.471 million¹⁰¹ and relative to the end of 2008 they registered drop of Denar 1.692 million or 9.3%.

With respect to the structure of the currency in circulation, on December 31, 2009, the banknotes participated with 97.7%, while the coins participated with 2.3%. Relative to 2008, the participation of the banknotes in the structure of the currency in circulation dropped insignificantly while the participation of the coins in circulation increased which was due to the new denominations of minted coins of 10 and 50 denars.

¹⁰¹ The currency in circulation excludes the money which are in commercial banks in the amount of Denar 3.011 million.

Figure 133
Currency in circulation



Source: National Bank of the Republic of Macedonia

Analyzing the value, the denominations of Denar 1000 and Denar 500 registered the largest participation. The denomination of Denar 1000 participated with 77.5% and the denomination of Denar 500 participated with 14.2% in the value of the banknotes in circulation (17.0% on December 31, 2008). The other denominations with lower denomination structure participated with 8.3% of the total value of banknotes in circulation.

The largest share of the value of coins accounts for the denomination of Denar 5 (37%) and Denar 2 (22%). In 2009, the participation of the new denominations of coins Denar 50 and Denar 10 in the value structure of the coins in circulation considerably rose (13.7% and 7.8%, respectively, relative to 1.0% and 0.4% in 2008). This increase resulted from the short period of existence of coins of only two months in 2008.

The structure realized through the number of pieces, showed participation of banknotes of 26.3% and of minted coins of 73.7% in the currency in circulation.

The largest participation according to the number of pieces accounted for the banknotes in denomination of 10, 100 and 1000 Denar. The denomination of Denar 10 participated with 45.7% (on December 31, 2008 with 44.1%), the denomination of Denar 100 participated with 16.2% (14.3% on 31.12.2008) and the denomination of Denar 1000 participated with 23.9% in the total number of pieces of banknotes (24.4% on 31.12. 2008).

The denomination of Denar 1 participated mostly in the quantities of coins in circulation (46.3%).

5.2.2. Supplying banks with cash

In 2009, the central vault of the National Bank and the subunits for handling cash in the Republic of Macedonia, issued Denar 31.3 billion in cash to banks, with 2.866 realized transactions (62.3 millions of banknotes and 13.8 millions of coins issued). Simultaneously, cash in the amount of Denar 32.6 billions was received from the banks, through 4.850 transactions. The analysis of the denomination structure of banknotes and coins indicated that when issuing and receiving, the denomination of Denar 1000 registered largest participation (35.8%, i.e. 35.5% respectively).

5.2.3. Banknote processing and destroying

In 2009, in the process of inspection of the quality of banknotes in circulation, in the central vault and the subunits for handling cash in the Republic of Macedonia all received banknotes were processed. Of the total processed banknotes, as a result of wearout and damage, 19.0 million banknotes were destroyed (relative to 25.5 millions of banknotes in 2008). The denominations of Denar 10, 50 and 100 participated mostly in the destroyed banknotes (74.0%). In 2009, all received denominations of Denar 1, 2, 5, 10 and 50 were processed out of which 96 thousands of peaces were destroyed. In 2009, as a result of wearout and damage, 144 thousands of banknotes were destroyed.

5.2.4. Expertise on suspicious / forged banknotes

Within its responsibilities as the only authorized institution, the National Bank performs the function of expertise on forged Denar banknotes. In 2009, the expertise showed total of 1460 forgeries discovered by the commercial banks or confiscated in Republic of Macedonia by the Ministry of Interior (MOI). Of the total number of discovered forged banknotes, in 2009 there was a change in the denomination structure relative to the previous year, i.e. this year the denomination of Denar 100 was most frequent, or 74.2% (of the total number of forgeries), different from 2008 when the denomination of Denar 1000 was most frequent. In 2009, the total value of the forged Denar banknotes amounted to Denar 386.180 participating insignificantly relative to the total value of the currency in circulation.

5.3. Internal audit

Through the realization of the Program of Activities in 2009, the Internal Audit Department fulfilled its ultimate task to improve the performance of NBRM activities, through systematic and regular assessments and improvement of the risk management, the internal control system and the managing processes. The process of achieving this goal was performed through giving an assurance to the managing bodies of NBRM that the risk management, the internal control systems and the managing processes, designed and implemented by the management, are adequate and that they function on a manner that enables to achieve the following goals: credibility and integrity of the financial and other information, compliance of the operations with the laws and bylaws, the internal policies and the operating procedures, safeguarding of assets, and rational and efficient resource employment.

The largest part of the regular activities pertained to the performance of regular audits, the performance of which was planned, not only with respect to the level of inherent, business risks, but also to the importance of the functions performed, the interval from the last audit performed, as well as the changes made in the operating processes. The audit reports provided an opinion on the adequacy of the established internal audit system, on which the NBRM management was regularly informed. Recommendations were given for overcoming the identified weaknesses, if any, presented in the audit reports together with the accomplishment of the given recommendations.

In 2009, 15 regular and 1 extraordinary audits were conducted, with the implementation of the recommendations given in the audit reports, which were to be completed by 2008, being closely monitored on a regular quarterly basis. The monitoring mainly showed that the recommendations were observed and implemented within the given periods. The audits of 31 work processes in NBRM in 2009, resulted in 57 recommendations for improvement of the internal control system.

Despite the regular activities, the internal audit also undertook some other activities aimed at improving its own operation quality and efficiency through commenced activities for implementation of the international internal audit standards. With respect to this, in 2009 the following was developed: adopting a new Rulebook for the Operations of the Internal Audit, implementing the Internal and External Program on assessment of the operating quality in the internal audit, developing methodology on risk assessment, as a starting point for the annual planning of the regular revisions, creating a new

form of audit report and introducing procedure for ranging the given recommendations with respect to their risk level.

5.4. Strengthening of the NBRM institutional capacity

Activities towards building institutional capacities through human resource development

In 2009, the National Bank continued with the activities on building the institutional capacity through developing the human resource management, through continuous performance of activities for professional development of staff and improvement of the employee qualification structure.

The professional development of staff was performed through realization of professional trainings in the country and abroad, as well as through co-financing of the upgrade of professional education for achieving higher qualification degree. Upgrades of professional education with special certificates were financed.

In 2009 the cooperation between the Central Bank of Nederland and the National Bank of the Republic of Macedonia continued in the field of technical assistance.

Professional trainings with foreign organizers

Table 21
Number of visited professional trainings

	2009
In the country	11
Abroad	66
Total	77

Table 22
Number of employees included

	2009
Number of employees included	68
Total realized professional trainings	77

The professional trainings visited by the employees in 2009 were realized based on annual training programs of the European central banks and other significant international institutions. Considering the tradition and the high level of organization of different trainings from all segments of the central banking, which is initiated by the stated organizers, the National Bank regularly sends its representatives on the events. Also, the possibility for exchange of experiences with other central banks, which are always available for direct contacts on such events, is considered to be a great advantage for our institution.

With respect to the organizers, most of the visited seminars in 2009 were organized by the International Monetary Fund (20.5%), by the German Central Bank (13%), Central Bank of Nederland (7.7%), Bank of England (6.4%), Central Bank of Austria (6.4%), followed by the seminars organized by the Bank for International Settlements - BIS - Financial Stability Institute - FSI (5.1%), and smaller share, but not less significant share of the total professional training for the employees pertains to the seminars organized by other central banks as: the Bank of France, Bank of Italy, Bank of Greece, National Bank of Serbia, Central Bank of Albania, as well as the ECB - European Central Bank etc.

The priority areas which were included in the professional training of employees in 2008 and 2009 are the following:

- Monetary economy (monetary policy, macroeconomic projection and central banking operations) which in 2008 participated with 35.5% and in 2009 with 37.2% to the total fund of realized professional trainings;

- Building of institutional capacity within the supervision (on-site and off-site), the participation of which ranged between 13.5% in 2008 and 15% in 2009, also registered small rise in 2009.

- Financial stability, banking regulation and methodologies with 8.7% for 2008 and 10.2% in 2009, was with higher participation by approximately 2%.

- Statistics, also registered rise of about 2%, i.e. from 7.3% in 2008 to 9% in the participation to the total fund for 2009.

- The following areas participated with smaller share to the total fund: central bank management, Euro-integration processes, internal audit, law, human resource management, cash management, finances and accounting, payment systems, information technology (although it registered growth in 2009 relative to 2008) and other.

It is significant to be mentioned that the larger number of professional training were envisaged for building the institutional capacities for fulfilling the most important functions of the central bank. Other areas were included in the realization of the professional training but with lower participation in the total fund of realized professional trainings.

Professional training organized by the National Bank

In 2009, events for professional training were organized indoors, within the National Bank or on other location in the country but organized by the National Bank. This method became more popular with respect to the fall in the costs for professional training of employees, thus enabling for higher number of employees, as target-group, to acquire new specific knowledge required for performing the tasks.

In 2009, total 196 employees from the National Bank participated on the seminars and workshops for professional training organized by the National Bank.

The events organized by the National Bank in 2009 which were in favor of the professional training of employees are stated below:

- **Regional Econometrics Seminar**
- **International seminar: Macro stress testing**
- **Trainings within the Nederland's grant**
 - "Quality of management, corporate management, process of risk management, the role of the audit and strategic risk management"
 - "Risks based supervision and global financial market, "Melt down"
 - "Liquidity risk management and market risks management"
 - "Econometric and statistic methods and financial risk measurement techniques"
- **Workshops for achieving business continuity**
 - Workshop "Risk Management"
 - Workshop "Preparing and realization of the process of testing the business continuity"
 - Workshop "Testing of plans for achieving business continuity"
- **Conference for payment systems and security settlement systems**
- **Organization of in-house computer training course**

In 2009, the Information Technology Department organized internal computer training course:

 - Seminar for the needs of the system administrators titled: Interconnecting Cisco Networking Devices (Part 1).
 - Apollo 13simulation for IT Service Management
 - Workshop - SharePoint Deployment Planning Service

Qualification structure of the employees in the National Bank

In the Table review given below, the data on the qualification structure for the last two years were shown. The trend of gradual **rise in the percentage of higher education profiles** was clearly

evident, for the account of the lower. The positive change within the university education continued in 2009 relative to 2008, and it rose by 2.02%, the number of MSc. rose by 16.66% relative to 2008, whereas negative values were registered in the drop of number of employees with elementary, high school and higher education.

Table 23

Qualification structure of the NBRM's employees (2007, 2008 and 2009)

Qualification structure	31.12.2008	31.12.2009	Change in 2009 relative to 2008
Total number of employees:	433	433	0%
1. University degree	198	202	2.02%
2. MSc.	30	35	16.66%
3. PhD	5	5	0%
4. Higher education	18	15	-16.66%
5. High school	164	160	-2.43%
6. High school - degree V	4	4	0%
7. Elementary education	14	12	-14.28%

The presented **qualification structure of the National Banks dated December 31, 2009** (Table 3) is showing that most of the employees in the National Bank are with finished university education. The total number of university education employees in the banks (including MSc. and PhD) participated with 55.88% in the total number of employees.

The participation of the high education with almost 40 % was due to the large number of employees in the Administrative and Technical Operations Department and the Banknotes Department as technical activities.

Other activities of NBRM in 2009

In 2009, the activities in function of improvement of the NBRM's library activities continued. In this context, besides the improvement of the operability of the library and the enriching of the library fund, other activities were undertaken during the year. Thus, in 2009, NBRM and the National University Library "St. Clement of Ohrid" signed a Contract for installation of program support COBISS and Contract on full membership of libraries in the library information system COBISS.MK. The goal of these activities was to enable integration of the NBRM Library in the single library and information system of Macedonia, through single organizational and information platform COBISS. In 2009 intensive activities for cooperation of the NBRM Library with the World Bank were undertaken in order to form joint informative center for development and the signing of the Memorandum of understanding between the two institutions is in the final phase. At the end of 2009 the NBRM Library obtained about 200 publications from the World Bank.

In 2009, activities for promotion of the design and functionality of the web page of NBRM were undertaken, and in the beginning of 2010 the new web page: <http://www.nbrm.gov.mk/> was launched.

In order to stimulate the scientific and research activities and to inspire the young staff potentials in the country to perform deep researches in the area of macroeconomics, significant for the Macedonian economy, NBRM in 2009 as well, for the third time, awarded the Annual award for best paper in the area of macro-economy to a young researcher.