

**National Bank of the Republic of Macedonia**  
MONETARY POLICY AND RESEARCH DEPARTMENT



**Recent Macroeconomic Indicators  
Review of the Current Situation**

April 2015

## Recent Macroeconomic Indicators

### Review of the Current Situation - Implications for the Monetary Policy

*The review of the current situation aims to give an overview of the recent macroeconomic data (December 2014 - March 2015) and to make a comparison with the latest macroeconomic projections (October 2014). This will determine the extent to which the current situation in the economy corresponds to the expected movements of the variables in the previous round of projections. The review focuses on the changes in external assumptions and performances of domestic variables and the effect of these changes on the environment for monetary policy conduct.*

**Generally, the global economic environment has not undergone major changes compared to the period of the last assessments. Uncertainties remain, yet the latest indicators suggest that some risks are reduced compared to the October projections.** This is especially true for the euro area, where recent indicators of growth point to performance which is higher (GDP growth of 0.3% in the fourth quarter, on a quarterly basis) than expected by the European Central Bank. At the same time, the high frequency indicators for the growth in the first quarter of 2015 are favorable for the time being. Favorable movements were observed also in the labor market, with a decrease in the unemployment rate in February to the level of 11.3%. On the other hand, March is the fourth month in a row that registered negative annual growth rate of inflation of 0.1% (although at a slower pace), as a result of the fall in oil and food prices, which is partially due to the depreciation of the euro. Registered inflation and expected inflation show that the probability of prolonged deflation will remain a key challenge for the monetary policy in the euro area, and the expected recovery of the economy is not yet sufficient for greater use of the potential of the economy and for reduction of this risk. **Observed from a viewpoint of the individual quantitative external environment indicators for the Macedonian economy, the assessments regarding the foreign effective demand registered minor changes relative to the October projection.** The new assessments indicate somewhat less intensive recovery of foreign demand in 2015, largely due to the weaker economic outlook of the neighboring economies, while the expectations for 2016 remained unchanged. Compared with the October projection significantly lower rates of **foreign effective inflation** are expected in the forthcoming period, **particularly in 2015**, mainly as a result of the revised expectations for the countries in the region, but also for other trading partners. **Changes in the expectations for the prices of primary products are divergent.** Latest developments and assessments for the **world oil prices** further indicate lower price levels of this energy source in relation to the October expectations, and accordingly, less pressure on inflation and terms of trade in 2015. Yet another rise in oil prices is expected in 2016, despite the expected stagnation in the October projections. Changes are registered also in the expected movement in **metal prices**, i.e. the average price of nickel for 2015-2016 has been revised downwards, while the price of copper has been revised upwards. Regarding the **food prices**, recent data on the prices of cereals point to higher price levels for these products, indicating somewhat higher import pressures through this channel on domestic inflation and terms of trade, compared with the October projections.

**The comparison between the latest macroeconomic indicators and their projected dynamics within the October round of projections does not indicate major deviations in the individual segments of the economy.** Published data on GDP for the fourth quarter are in line with the expected growth of the economy according to the October round of projections. Observing the sectors, generators of growth are construction and industry, while in terms of demand, the growth structure is similar to the previous quarter. As expected, domestic demand and exports are the main generators of growth, amid moderate growth in private consumption and investment and fast growth in export activity. Indicative high frequency data for the first quarter of 2015 point to further growth of the domestic economy, at probably a similar pace as in the previous quarter. When it comes to the movement of consumer prices, in March the annual decline slowed down significantly, amid slower decline in the prices of the energy component, stabilization of core inflation and growth in food prices. However, also in March, the inflation was moderately lower compared to the October projection. This,

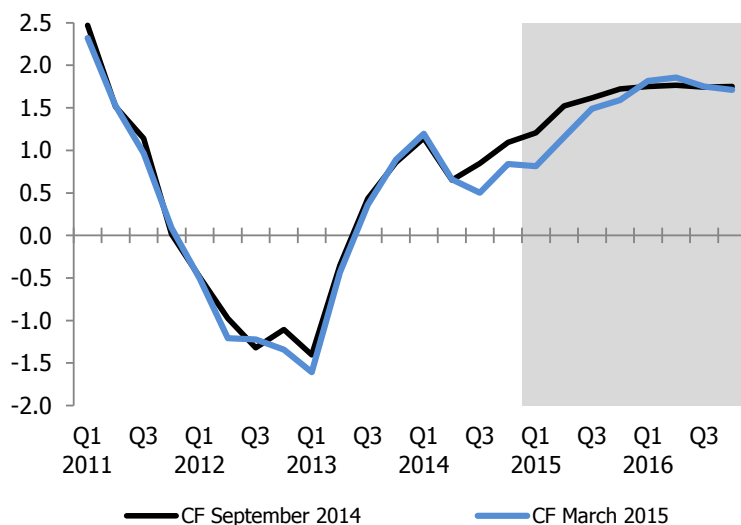
complemented by the changes in key assumptions for the prices of primary products, particularly the significant downward revision of the expected movement of energy sources, **generates downward risks related to the projected movement of domestic prices in 2015**. However, changes in the expectations about the prices of primary products indicate that the uncertainty about the future movement of these products is important, and the possibility of sudden changes in these categories is great. At the same time, the previously identified upward risk remains, attributable to the adverse weather conditions in the domestic economy, whose effect is still difficult to assess.

**The latest data on foreign reserves point to their decline since the beginning of the year (excluding the effects of price and exchange rate differences and changes in securities price).** Analyzing through the change factors, the reduction of reserves in this period is a result of transactions for the account of the government, with the greatest effect of the early repayment of the loan from the IMF, used within the Precautionary Credit Line. External sector indicators suggest that the data on the balance of payments for January 2015 point to the possibility of achieving a smaller current account deficit than expected for the first quarter of the year, while the financial transactions generated net outflows instead of the expected net inflows. Latest available data on foreign trade for the first two months still suggest a smaller trade deficit, as a combined effect of the good performance of the new companies and smaller pressures from energy imports, due to the lower than projected oil prices. Net purchase from currency exchange operations in the first quarter of 2015 gives a signal for increasing private transfers and better performances than projected, which is probably largely due to the high purchase of Swiss francs, after the Swiss National Bank abandoned the exchange rate target and the strong appreciation in mid-January. The analysis of foreign reserves adequacy indicators shows that they continue to move within a safe zone.

**In terms of monetary movements,** preliminary ten-day data on the credit market for March show relatively fast growth of total loans on a monthly basis, indicating a significant revival of the credit market after the relatively weaker performance since the beginning of the year. The new lending in March was equally distributed among households and the corporate sector. Against such background and realized higher than anticipated credit growth in 2014, the annual growth of total loans in March was 9.2%, which is above the October projection for the first quarter (8.5%). In terms of the deposit potential, preliminary data as of March show a monthly decline due to the fall in corporate deposits and deposits of other financial institutions. Deposits of households continued to grow at a similar pace as in the previous month. The annual growth of total deposits in March was slightly above the October projection, amid stronger growth in deposits in 2014 relative to the projection. The latest **EURIBOR assessments indicate its lower level in the 2015-2016 period, compared to the October projection.**

**The latest macroeconomic indicators and assessments do not point to major changes in the conclusions about the environment for conducting monetary policy and about the risks, compared to the assessments provided in the October projections.** Foreign reserves have dropped since the beginning of the year, which, if the impact of unforeseen factors is excluded (early repayment of the loan to the IMF) is generally in line with expectations. Foreign reserves adequacy indicators remain within the safe zone. Risks arising from the external environment remain unfavorable, even though those coming from the euro area are mitigated by the recent amendments to the ECB's monetary policy. Regarding inflation, as of March there was a significant slowdown in the annual decline in the general price level amid slower decline in the prices of the energy component and stabilization of core inflation, while food prices grew. However, inflation performances remained weaker than expected, which coupled with the significant downward revision of the world oil price for the forthcoming period reinforces the downward risks to the projection of the future dynamics of inflation. Indicators of economic activity for the first quarter of 2015 point to further growth of the domestic economy, at probably a similar pace as in the previous quarter. Regarding the credit market, preliminary data for March show an intensified lending activity compared with the first two months of the year, surpassing the October projection for the first quarter.

**Foreign effective demand**  
(annual rates of change in %)



Source: "Consensus Forecast" and NBRM calculations.

**In 2015, it is expected that foreign effective demand will increase by 1.3% ...**

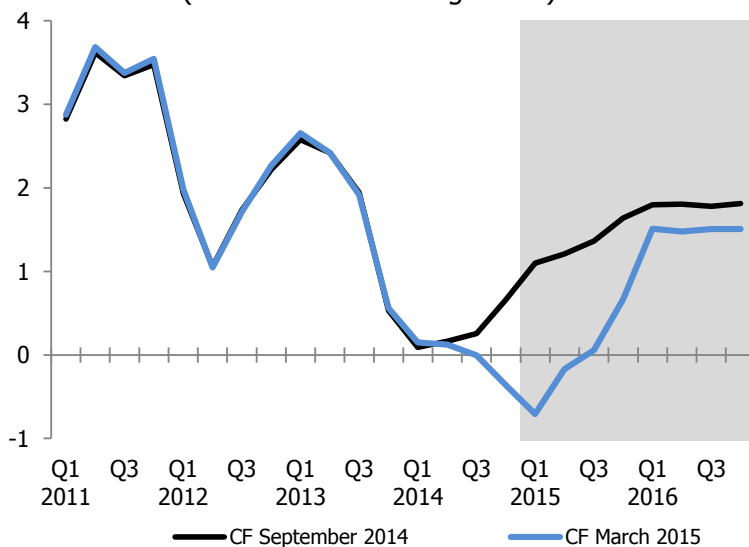
... which compared with the projection of October last year of 1.5% is a minimal downward revision ...

... made as a result of reduced estimates of the dynamics of economic activity with some of our major trading partners.

In terms of contributions of individual countries, most of the revision stems from the expectations of lower economic growth in the neighboring countries (Serbia, Bulgaria and Greece).

**On the other hand, the expectations for growth in foreign demand of 1.8% in 2016 were retained.**

**Foreign effective inflation**  
(annual rates of change in %)



Source: "Consensus Forecast" and NBRM calculations.

**According to recent estimates, it is expected that in 2015 international prices will be at the level of the previous year (inflation of 0%) ...**

... which is different from the October projection when foreign inflation of 1.3% was forecasted.

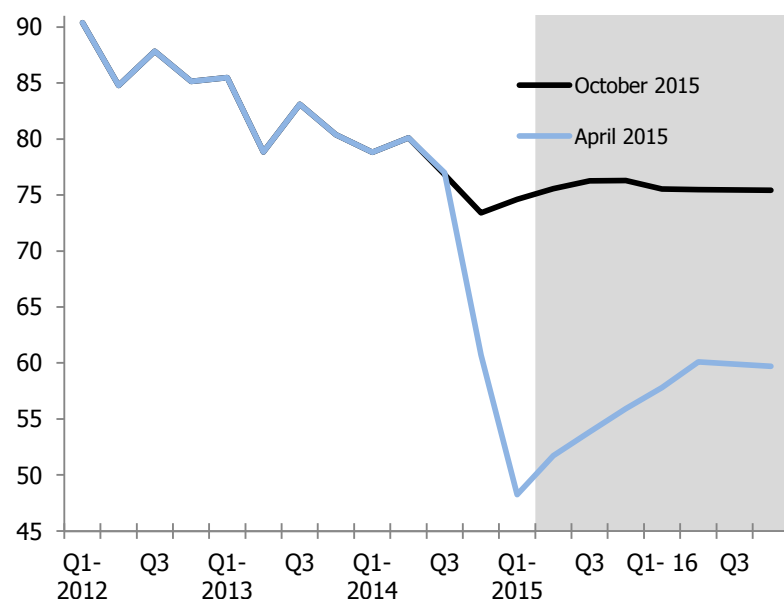
The significant downward revision is due to the expectations of much lower inflation rates in all of our major trading partners ...

... of which the largest cumulative contribution is expected to come from the downward revisions of inflation<sup>1</sup> in Germany, Serbia, Croatia and Bulgaria.

**Downward revision of the foreign effective inflation was made also for 2016, which is expected to be 1.5% versus 1.8% in the October projection.**

<sup>1</sup> Inflation in Serbia and Croatia has been adjusted for the changes in the exchange rate.

**Brent oil**  
(quarterly average, EUR/Barrel)



Source: IMF and NBRM calculations.

**Crude oil "Brent" is expected to register a significant decline in 2015, which will be much sharper than that expected in October ...**

... in circumstances of imbalance between fundamental price factors, i.e. continuous presence of a structural surplus of oil supply in the global market despite the slow growth in demand.

However, the upward movement of oil prices in the recent period indicates the presence of certain risks to this projection, such as possible faster growth in demand, temporary disturbances in the supply of oil due to geopolitical reasons or observations of market participants that oil prices have already reached the minimum level and start to adversely affect oil production in the USA.

**On the other hand, it is now expected that oil prices will rise significantly in 2016, as opposed to the October projection for minimum decline. However, the oil price level is expected to be about 20% lower than the price projected in October.**

**During the projections period, the revisions of metal prices were divergent.**

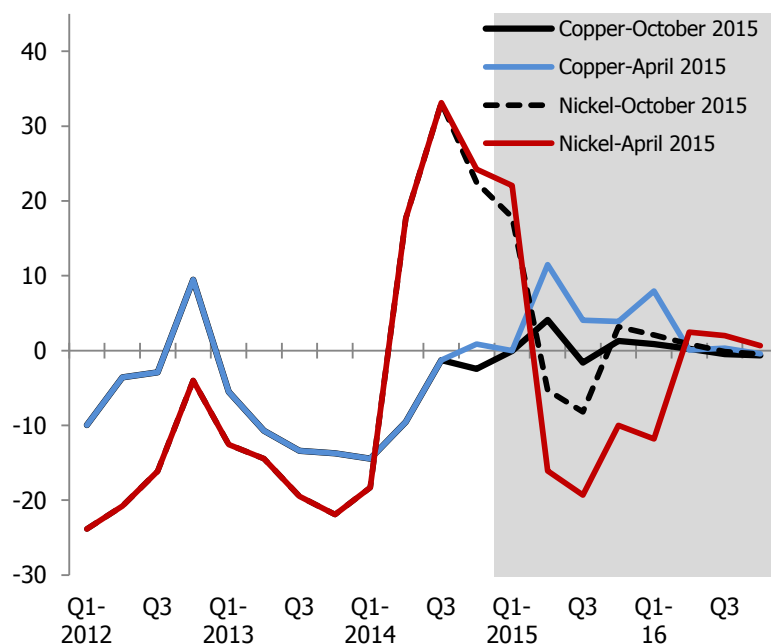
**Thus, now it is expected that in 2015 the price of nickel will decline, as opposed to the October estimate of growth ...**

... as a result of the increased inventories of this metal and lower demand ...

... while the price of copper has been revised towards faster growth ...

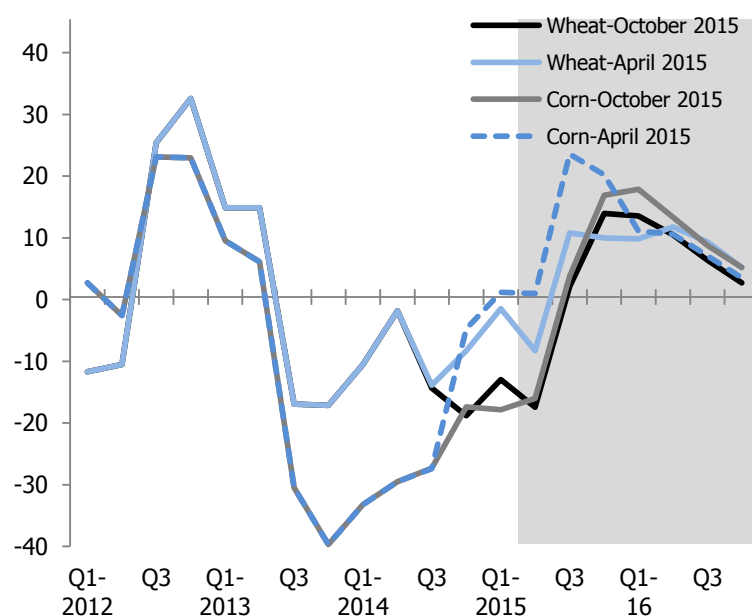
... amid mixed economic signals from China and the opportunity to pursue further stimulating government measures toward encouraging demand, on the one hand, and concerns about

**Nickel and copper prices in EUR**  
(annual changes in %)



Source: IMF and NBRM calculations.

**Wheat and corn prices in EUR**  
(annual changes in %)



Source: IMF and NBRM calculations.

possible disruptions on the supply side, on the other.

**In 2016, a reduction in the price of nickel and an increase in the price of copper is envisaged, versus the October expectations for minimal growth in the price of nickel, i.e. stagnation in the price of copper.**

**In 2015, an upward revision was made in the prices of primary food products compared to October estimates.**

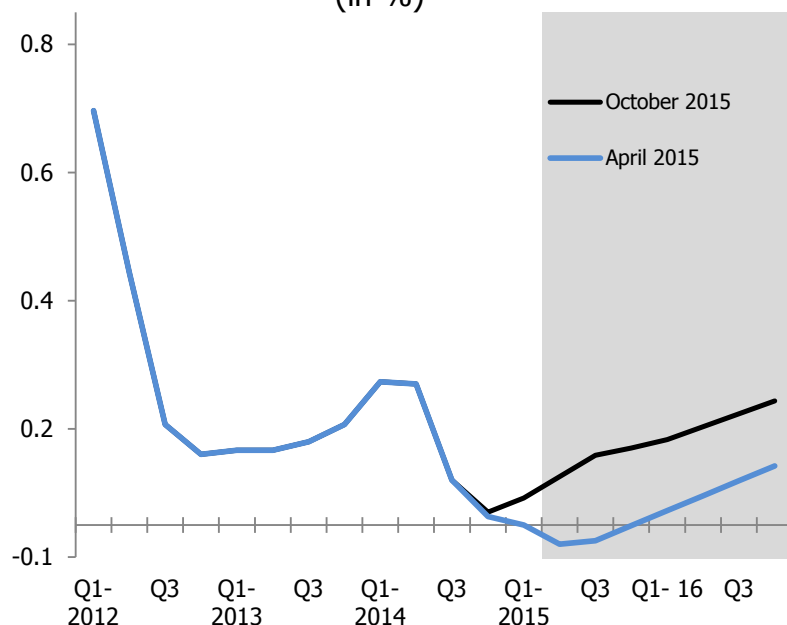
Thus, prices of wheat and corn are now expected to grow, as opposed to their projected decline in October ...

... despite the generally positive preliminary outlook for the production from the new harvest and the substantial inventories accumulated in the previous two seasons.

Given that if expressed in US dollars, the price of these products decreased, this shows that the upward pressures on prices in euros are largely associated with the projected increase in the value of the US dollar against the euro in 2015.

**Prices of primary food products are expected to grow also in 2016, at a pace which compared with October projection would be faster in the case of wheat and slower in the case of corn.**

### 1M Euribor (in %)



Source: "Consensus Forecast" and NBRM calculations.

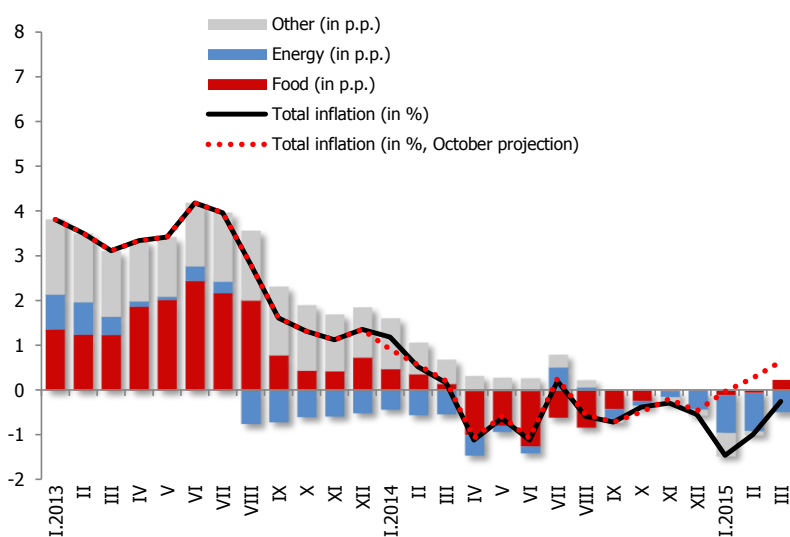
**It is estimated that throughout most of 2015, the one-month EURIBOR will be minimally negative, which first occurred in March 2015 and is a situation which historically has not been reported in the European money market until now ...**

... and which reflects the expectations of market participants for significant growth of excess liquidity in the euro system as a result of the implementation of the program of quantitative easing by the ECB, which began on 9 March 2015.

Since this program is planned to be implemented by the end of September 2016, or until inflation has stabilized below but close to 2%, a significant downward revision of the foreign interest rate is made, which is now expected to average -0.01% and 0.06%, respectively, in 2015 and 2016, versus 0.09% and 0.16% in the October projections round.

## Inflation rate

(annual impacts to inflation, in p.p.)



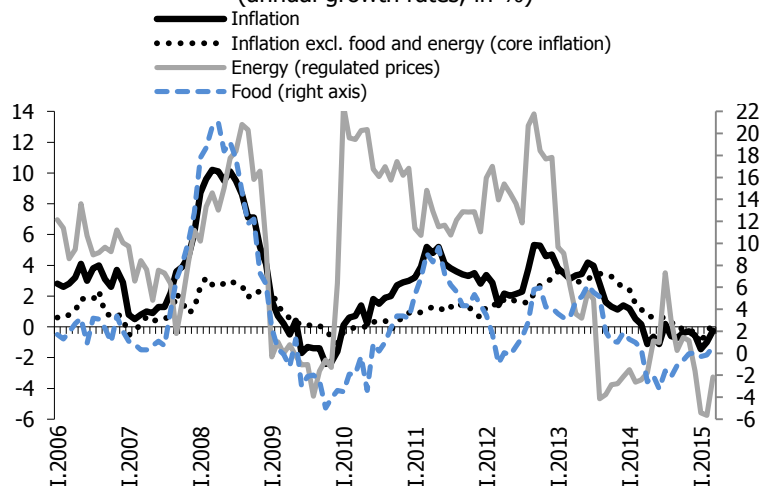
Source: SSO and NBRM.

**After the monthly decline in consumer prices in January and stagnation in February, in March 2015 there was a moderate growth in consumer prices of 0.5% ...**

... mostly due to the rise in the prices of transport (as opposed to their decline in February)<sup>2</sup>.

## Inflation and volatility of food and energy

(annual growth rates, in %)



Source: State statistical office and NBRM calculations.

**According to the monthly pace, in March the annual decline in consumer prices slowed down to 0.3%, compared to the decrease of 1% in February ...**

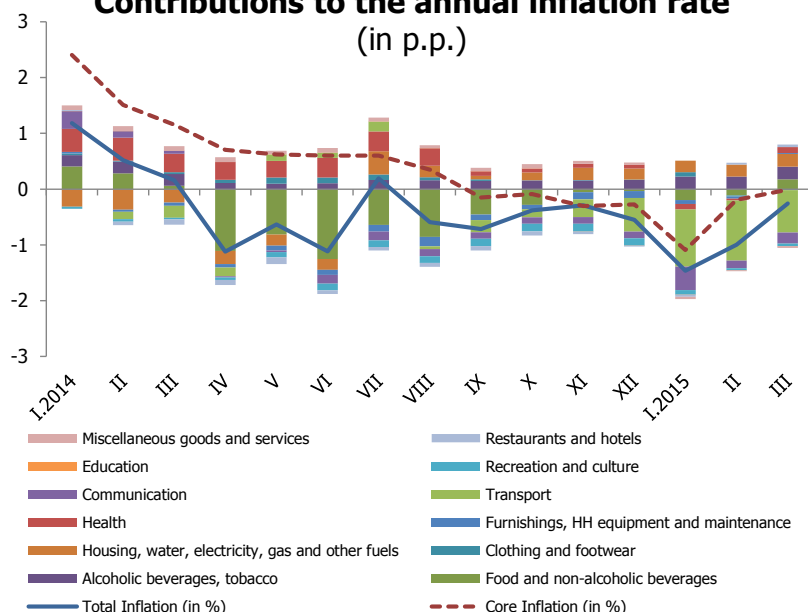
...which is a lower rate than expected in the October round of projections...

...amid downward deviation of the actual inflation from the projected one in the energy component, the core inflation and the food component.

<sup>2</sup> Categories with the largest individual contribution to the March price increase include liquid fuels and lubricants (monthly price increase of 9.5%) and fruits and vegetables (monthly price increase of 4.8% and 2.5%, respectively) .

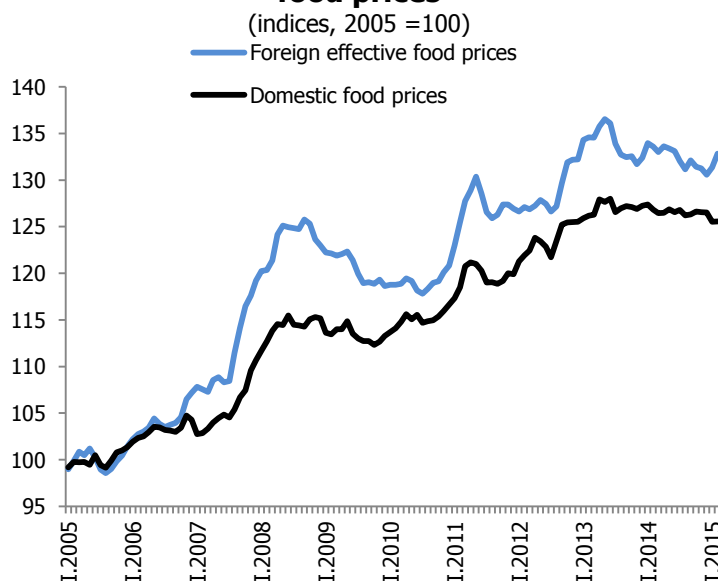


## Contributions to the annual inflation rate (in p.p.)



Source: SSO and NBRM.

## Foreign effective food prices\* and domestic food prices (indices, 2005 = 100)



\* Foreign effective food prices are calculated as weighted sum of food prices in countries that are major trade partners with Macedonia.

Source: State statistical office, Eurostat and NBRM calculations.

In March, **core inflation decreased slightly by 0.1%, on a monthly basis** (compared to February when a minor increase was registered)...

... while on an annual basis, after the deceleration of the annual decline in the first two months of the year, in March, core inflation remained unchanged.

In terms of structure, in March divergent movements in the prices of individual products within the core inflation were registered. The fastest price growth was recorded in alcoholic beverages and tobacco, while the sharpest decline was evident in consumer prices of communications.

**External input assumptions for 2015, which are included in the inflation projection, are revised in divergent directions.**

Thus, according to the latest assessments, lower **foreign effective inflation** is expected by the end of 2015.

Also, the assessments for **oil price** movement for 2015 have been downwardly adjusted...

... amid present imbalance between the fundamental factors, i.e. structural excess of oil supply in the global market amid slow growth in demand.

On the other hand, the latest assessments for the **prices of internationally traded primary food products**, expressed in euros, point to upward adjustment for 2015, compared with the October projection ...

...which, given the favorable movements in the fundamental factors, entirely reflects the appreciated value of the US dollar against the euro.

**Risks surrounding the projected movement of domestic prices in 2015 are mainly downward**, amid downward deviation of the actual compared to the projected movement of prices in March and significant downward revision of the expected movement of energy sources...

...despite the upward revisions of prices of cereals.

However, it should be emphasized that there is great uncertainty about the projected movement of world oil prices, given that the movement of these prices is sometimes conditioned by factors of temporary character. In addition, a factor that could create upward pressure on prices of early vegetables and cereals, and hence on the overall price level, are the floods that swept Macedonia at the beginning of the year.

In January 2015, the average **net wage** recorded a nominal annual growth of 2.3%...

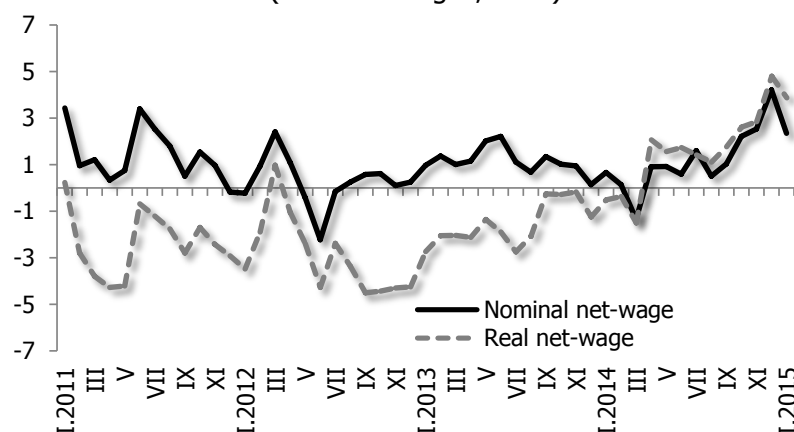
... which is a deceleration of growth of 1.9 percentage points compared to December.

Most of the sectors registered upward movements in the wages ...

... however, fastest growth was registered in the wages in construction and in part of the services sectors (health, education, "arts, entertainment and recreation" and "professional, scientific and technical activities").

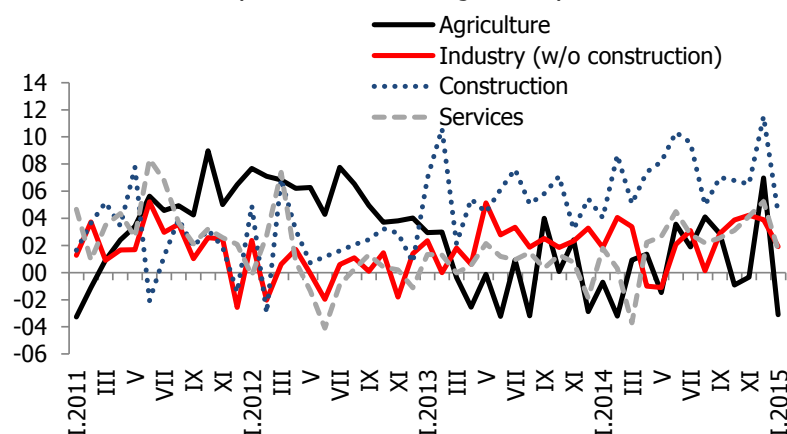
Downward movement was registered in the wages in agriculture, mining and some services.

**Average net-wage**  
(annual changes, in %)



Source: SSO.

**Average monthly net wage paid by sectors**  
(nominal annual changes, in %)



Source: SSO.

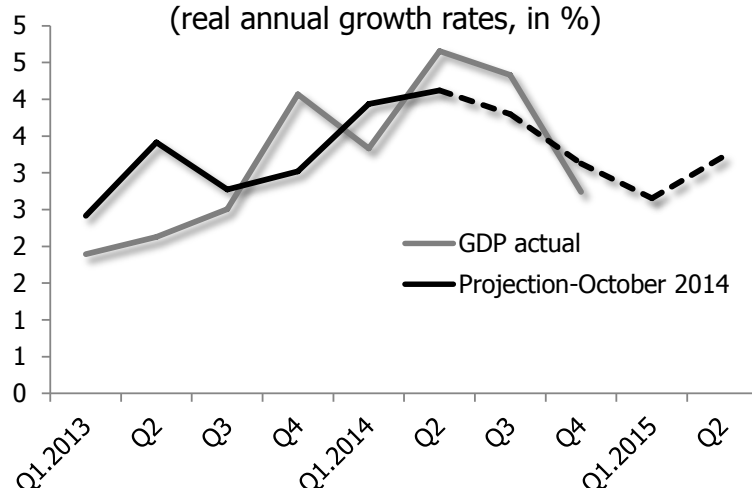
**The growth registered in the nominal wage is slightly higher than anticipated in the October projection (expected growth of 1.8% in the first quarter of 2015).**

Despite the sharper decline in consumer prices, the slowdown in nominal growth reflected in the movement of real wages, whose growth in January also slowed down to 3.9% (versus 4.8% in December)

...

...which was also higher than expected in the October round of projections.

**Gross domestic product**  
(real annual growth rates, in %)



Source: SSO and NBRM projections.

**In the fourth quarter of 2014, the real annual economic growth was 2.7%, and it was somewhat lower than expected according to the October projection (3.1%).**

On the **production side**, favorable movements were registered in almost all economic sectors, with the construction and industry giving the highest annual contribution to the growth of the economy...

... while **in terms of demand**, the increase in GDP is the result of growth in exports and higher domestic demand (amid growth in household consumption and investments) ...

... which was simultaneously followed by a surge in imports from abroad.

The high frequency data for the first quarter of 2015 indicate growth of the domestic economy, given the constant positive performance in most economic sectors.

In the period January-February 2015, **industrial production** registered an average growth of 2.1% ...

... with the manufacturing facilities in technological and industrial development zones (primarily the production of motor vehicles, trailers and semi-trailers), clothes manufacturing and energy sector being the sectors with the largest contribution to growth...

... while a significant decline in manufacturing was registered in mining and non-metallic minerals.

In the January - February period the growth of **trade** turnover continued ...

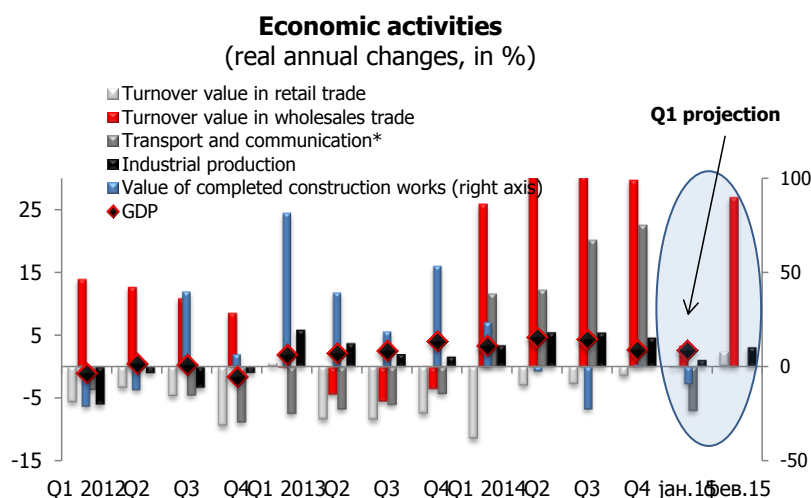
... amid further high real growth in the wholesales and in the trade with motor vehicles, as well as growth, albeit moderate, in retail trade, for the first time after the constant decline in real terms in the last seven quarters.

The positive economic growth is supported by the data on the turnover in **catering**, with the number of tourists in January registering more intensive growth in comparison with the annual growth registered in the fourth quarter.

On the other hand, the January data on the **transport sector** indicate a less favorable position compared to the fourth quarter of the year ...

... and similar movements are typical for the "**construction**" sector, which recorded lower value of completed construction works compared to the same period last year, despite the moderate growth recorded in the previous quarter.

**Available indicators of aggregate demand in most part also point to economic growth in the first quarter**



\*Simple average of annual growth rates of the different types of transport and the telecommunications.  
Source: SSO and NBRM calculations.

of 2015, which is consistent with the expectation in the October projection.

According to the high-frequency data on **private consumption**, its further growth is expected in the first quarter of 2015...

... amid accelerated annual growth in real wages and private transfers, as well as growth in pensions paid ...

... and continuing steady pace of growth in lending to households.

The growth of domestic production of consumer goods also points to growth in households' consumption, despite its decline in the previous quarter ...

... as well as the moderate real growth of retail trade for the first time after a constant real decline in seven consecutive quarters.

On the other hand, annual decline was recorded in the imports of consumer goods and net revenues from VAT.

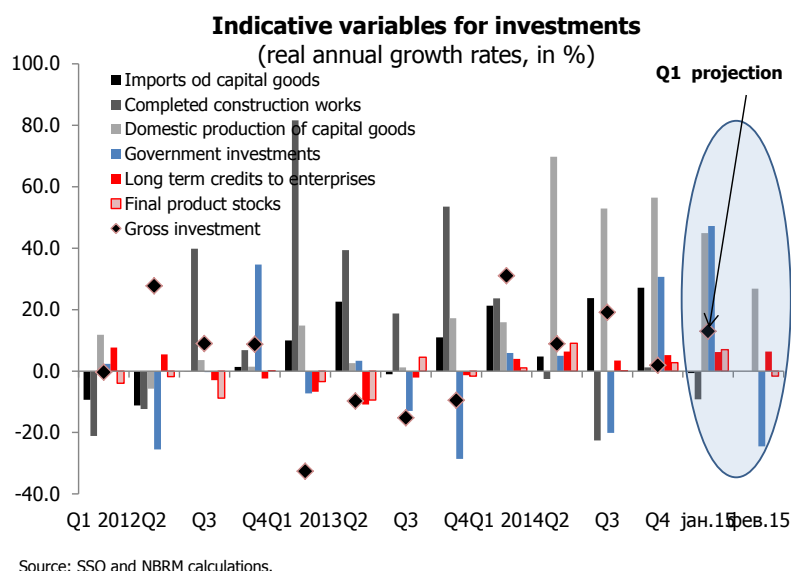
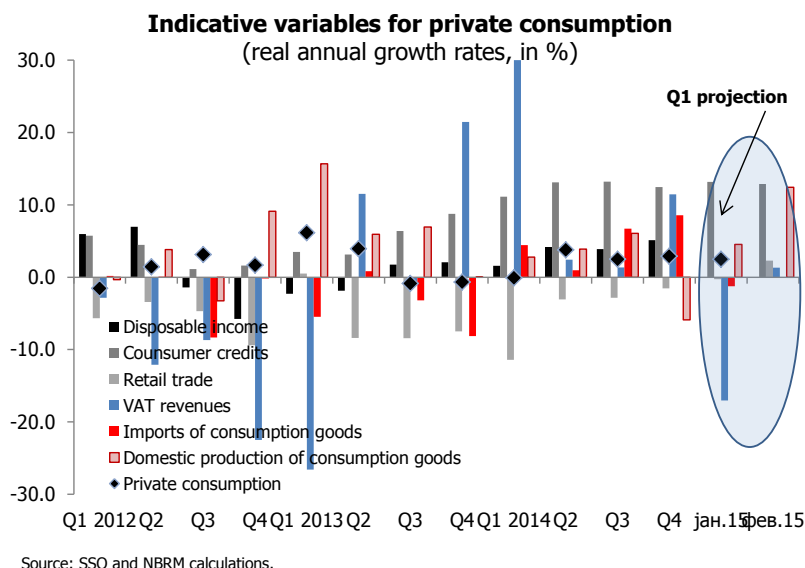
The latest indicators of **investment activity** send divergent signals, but generally indicate a possible moderate growth of investments in the first quarter ...

... amid faster growth of credit activity to the corporate sector and foreign direct investments ...

... and similar growth was registered also in the inventories of finished products.

High annual growth was observed in the domestic production of capital goods, but at a slower pace.

On the other hand, the data on **construction** (where a decline in the value of completed construction works in January was registered), **budgetary capital expenditures** (decline in the first two months of the year), and **imports of investment products** (small decline in



January, as opposed to the double-digit growth in the previous quarter) point to slower investment activity in the first quarter of the year.

Nominal data on **foreign trade** as of February 2015 show a significant narrowing of the trade deficit, as opposed to the expected expansion in the October projection ...

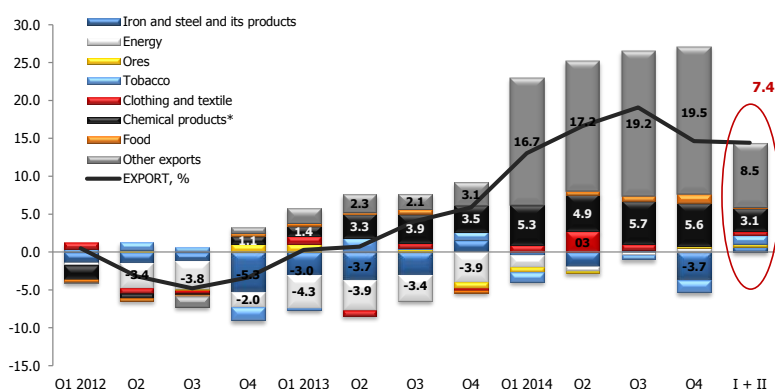
...given the high growth in exports and decline in imports of goods.

Budget performances in the first two months of the first quarter of 2015 indicate an increase in **public consumption**, contrary to the expectations for decline in the October projection ...

... amid an annual increase in the expenditures for wages and for goods and services.

## EXTERNAL SECTOR

**Exports by components**  
(contributions to the annual change, in p.p.)



Source: NBRM.

\* The following data depict the overall exports of one major export capacity in the free industrial zone.

In the first two months of 2015, **the foreign trade deficit registered significant annual contraction of 34.5%**, driven by the high annual growth of exports and the simultaneous reduction of import component...

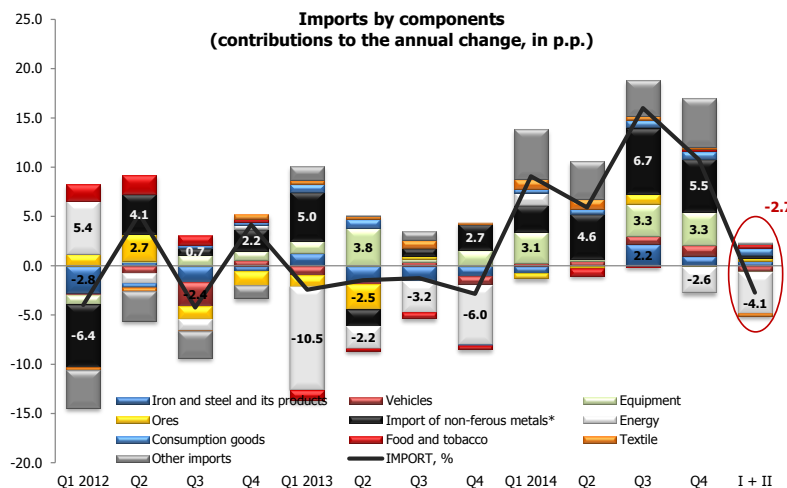
...which is contrary to the expected annual widening of the trade deficit in the first quarter, according to the October projection.

**Exports** of goods in January and February registered an annual growth of 14.4%, driven primarily by the improved export performance of the new facilities in the economy ...

... with a significantly lower but positive contribution of other export categories.

*Compared with the projection, exports realized in January and February were higher than expected for the first quarter. The positive deviation arises mainly from the improved export performance of the new facilities.*

**Imports by components**  
(contributions to the annual change, in p.p.)



Source: NBRM.

\* The following data depict the overall exports of one major export capacity in the free industrial zone.

**Imports** of goods in January and February fell by 2.7% on an annual basis as a result of the sharp decline in energy imports. The reduced energy imports reflect the effect of lower import prices of fuels amid a decline in the price of crude oil, and higher amounts of imported oil derivatives ...

... while other import categories made an insignificant contribution.

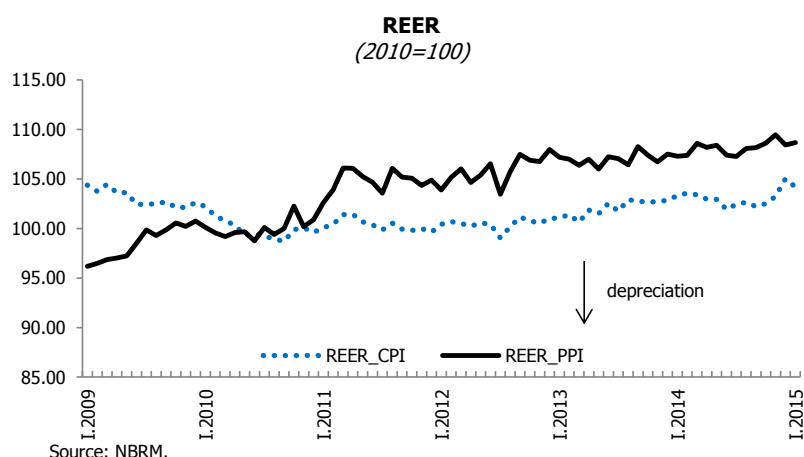
*Import performances in January and February were significantly lower than those projected for the first quarter of the year. The largest downward deviation is observed in energy imports, and in the import of vehicles, import of iron and steel and other imports.*



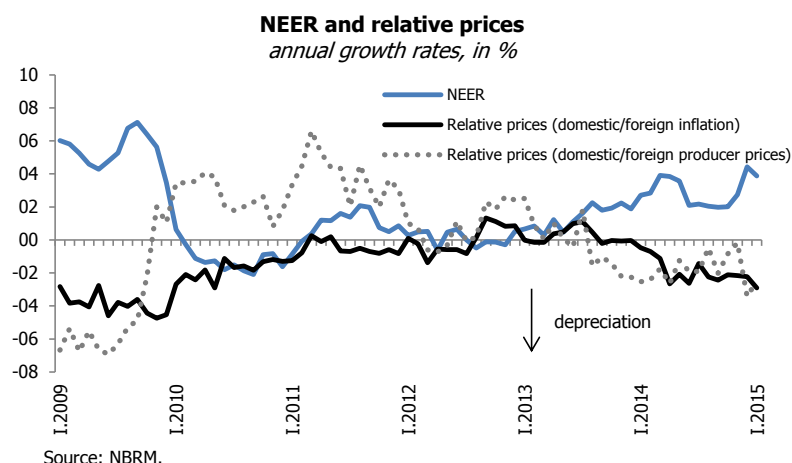
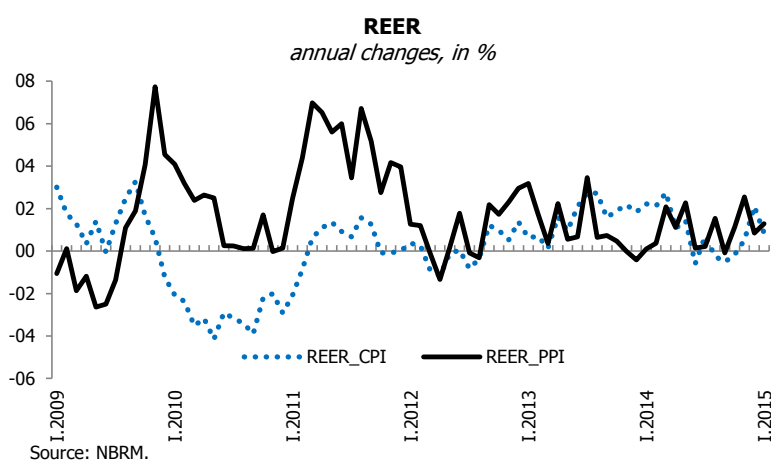
**Compared with the expectations and with the historical average, exports were higher, while imports were significantly lower in the period January-February, which suggests the possibility of accomplishing smaller trade deficit for the first quarter compared to the projected.**

The latest estimates for the movement of world stock prices of oil indicate more favorable movements in the current year and their deterioration in the next year, compared with the October projection. Namely, the price expressed in euros is expected to register a significantly sharper annual decline in 2015 and to be upwardly adjusted in 2016. Regarding metals, during the current and in the next year, on average, less favorable changes in the prices of nickel and more favorable movements in world prices of copper are expected.





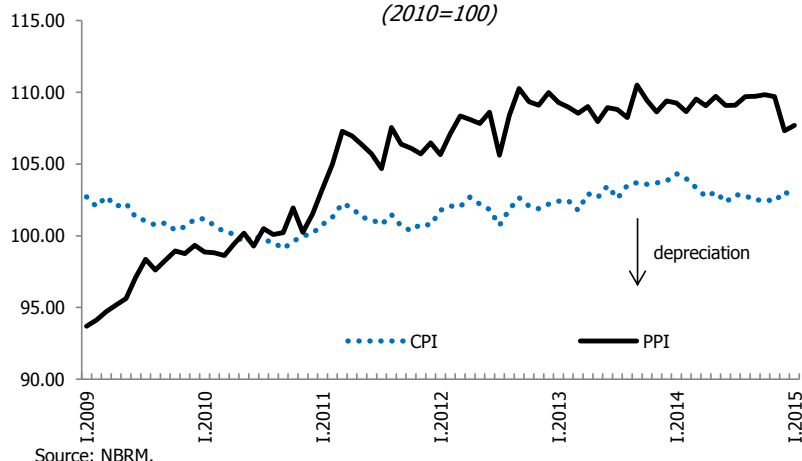
**In February 2015, price competitiveness indicators of the domestic economy continued to deteriorate moderately on an annual basis,** given the 1.5% appreciation of the REER deflated by consumer prices and the simultaneous 4.2% appreciation of the REER deflated by producer prices, compared to the same period last year.



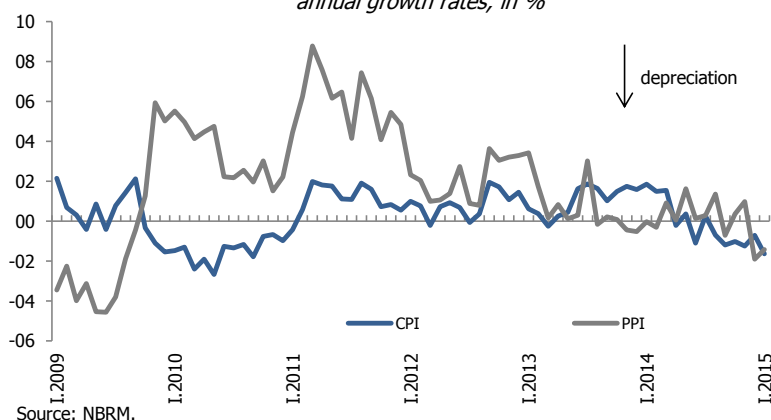
The annual appreciation of the nominal effective exchange rate (of 4%) was yet again driven by the depreciation of the Russian ruble and Ukrainian hryvnia against the denar, causing upward shifts in both REER indices. The relative consumer prices registered an annual decline of 2.5%, driven by the growth in foreign prices, as opposed to the decline of domestic prices. On the other hand, relative prices of industrial products recorded an annual growth of 0.2%, driven by the sharper decline in the foreign relative to the domestic prices of industrial products.

## EXTERNAL SECTOR

**REER, excluding primary commodities**  
(2010=100)

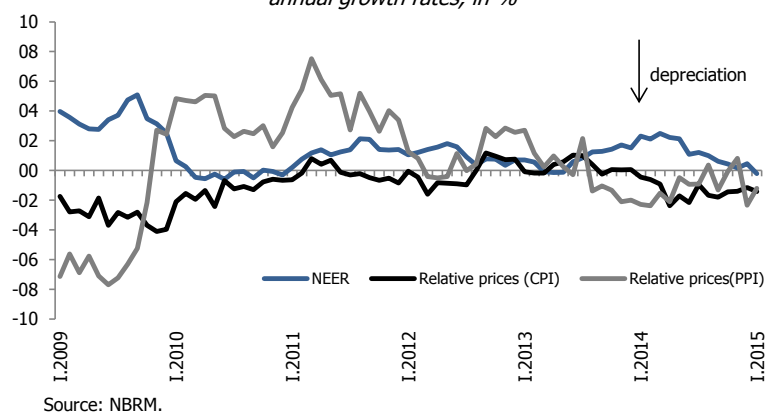


**REER, excluding primary commodities**  
annual growth rates, in %



The analysis of the movement of the REER indices, as measured using weights based on the foreign trade without primary products<sup>3</sup>, still indicates improvement in the price competitiveness of domestic economy. The index of the REER deflated by consumer prices and REER deflated by producer prices of industrial products depreciated annually by 2.1% and 0.1% respectively.

**NEER and relative prices, excluding primary commodities**  
annual growth rates, in %

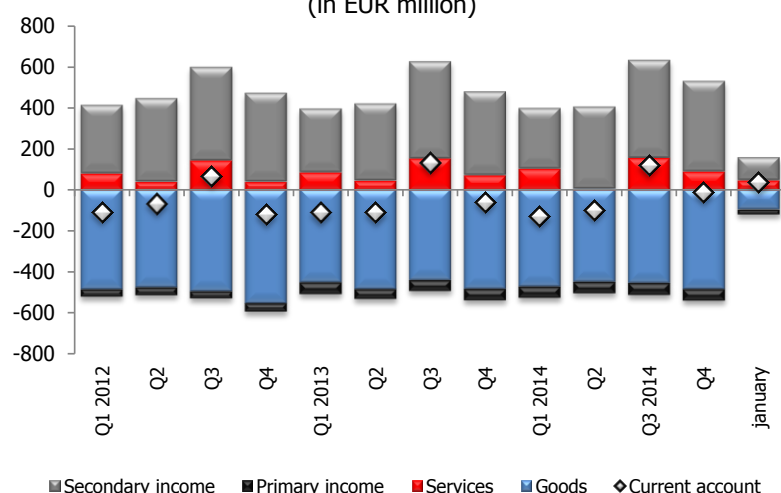


The improvement in both REER indices is a result of the NEER depreciation (of 1.3%). In the same vein is the annual decline in the relative prices of the costs of living (0.8%), compared to the annual growth of 1.2% observed in the relative prices of the producers of industrial products.

<sup>3</sup> Primary products that are not included in the calculation are: oil and oil derivatives, iron and steel, ores and imported raw materials for the new industrial facilities in the free economic zones.

## EXTERNAL SECTOR

**Main components of the current account**  
(in EUR million)

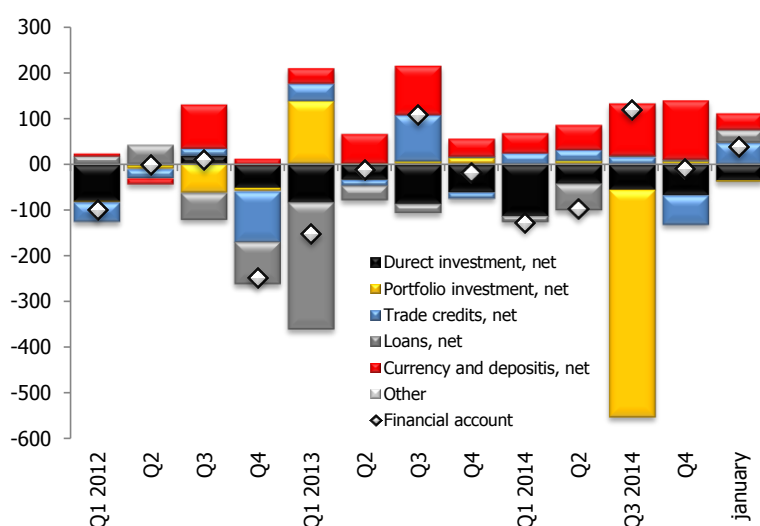


Source: NBRM.

**In January 2015, the balance of payments current account registered a surplus of Euro 37.8 million (or 0.4% of GDP), contrary to the expectations for a deficit according to the October projection...**

... with the improved performances being due mainly to the significantly lower deficit in the balance of goods and services, and also to the higher surplus in secondary income compared with expectations, given that the deficit in primary income is in line with the October projection.

**Financial account components**  
(in EUR million)



Source: NBRM.

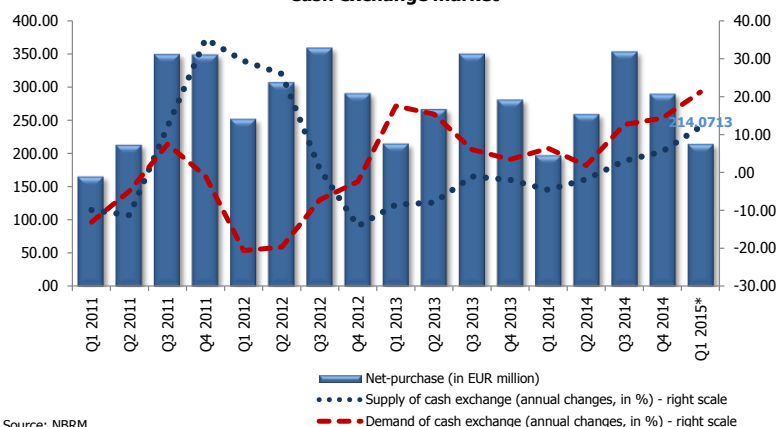
**In the first month of the year, the financial account registered net outflows of Euro 73.2 million (or 0.8% of GDP), instead of the net inflows expected for the first quarter of the year, according to the October projection<sup>4</sup>.**

Such deviations result from the realized net outflows in loans against the expected net inflows, and from the higher than expected net outflows in currency and deposits. Direct investments moved in line with the October projection, while trade credits acted in the opposite direction and registered net inflows, as opposed to the projected net outflows.

<sup>4</sup> According to the new methodology for compilation of the balance of payments (BPM6), the terms net inflows and net outflows denote net incurrence of liabilities and net acquisition of financial assets, respectively.

## EXTERNAL SECTOR

Cash exchange market



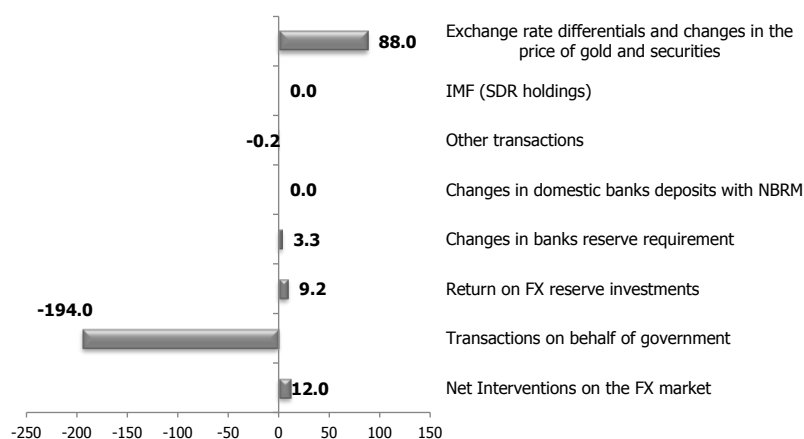
Source: NBRM.

Foreign exchange reserves  
(stock, in EUR million)



Source: NBRM.

Factors of change of the foreign reserves in the first quarter (in EUR million)



Source: NBRM.

Data on currency exchange operations as of March 2015 indicate significant further increase in the supply of and demand for foreign currency on an annual basis.

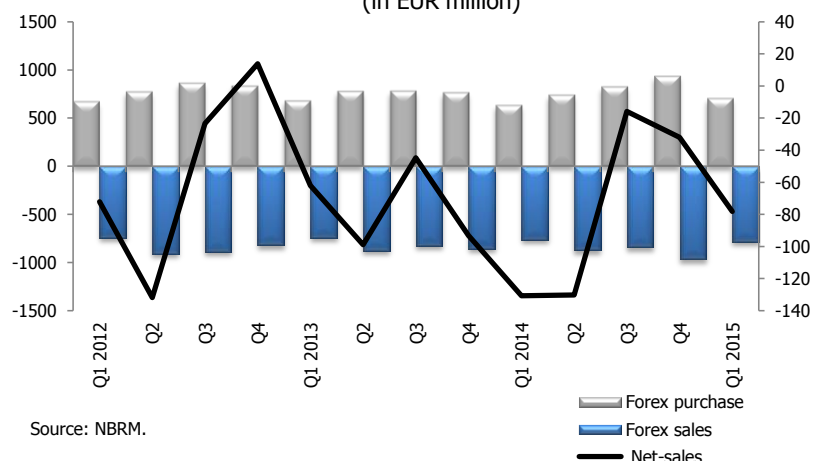
The net purchase in the foreign exchange market as of the first quarter of 2015 totaled Euro 214.1 million, which is an annual increase of 8.6%.

As of 31 March 2015, the gross foreign reserves stood at Euro 2,354.9 million, down by Euro 81.6 million compared to the end of the previous year. The reduction of foreign reserves is due to transactions for the government account<sup>5</sup>, with the currency changes and the changes in the price of gold and the net purchase of foreign currency in the foreign exchange market by the NBRM acting in the opposite direction.

<sup>5</sup>On 27 February 2015, the government made early repayment of the liabilities to the IMF, based on the Precautionary Credit Line (PCL), which decreased the foreign reserves by Euro 153.4 million.

## EXTERNAL SECTOR

**Foreign exchange market**  
(in EUR million)



In the first quarter of 2015, the **foreign exchange market** of banks reported a net sale of Euro 78.1 million, which is by Euro 52.7 million lower compared to the net sale registered in the same period last year. This annual change is a result of the faster annual growth in the supply (of 11.2%) than the growth in the demand for foreign currency (of 2.4%).

The analysis by sector suggests that better annual performances are mainly due to lower net sales of companies and higher net purchase of exchange offices.

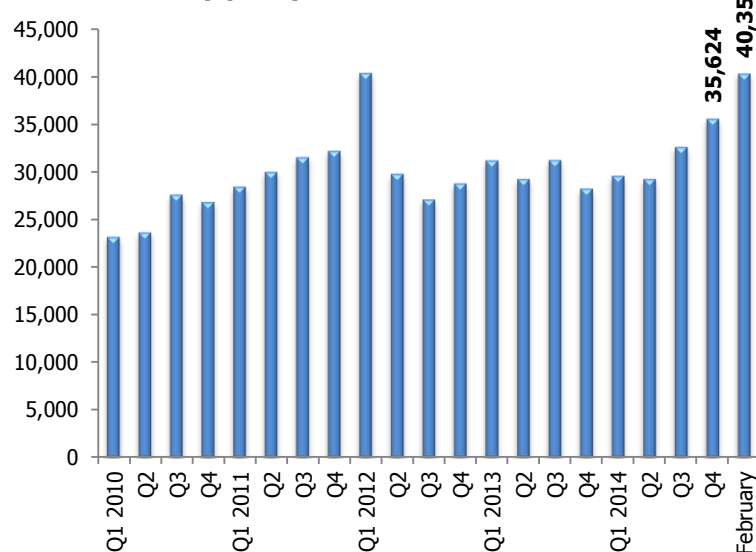
Data as of February show liquidity withdrawal through monetary instruments relative to December, but at a faster pace compared with the expectations for the first quarter within the October projection. However, the level of monetary instruments in February is similar to the projected balance for the end of the first quarter as a result of the performances at the end of 2014<sup>6</sup>.

Analyzing flows of creating and withdrawing liquidity (from balance sheet aspect) in February, net foreign assets of the NBRM declined relative to December, but at a faster pace compared with the expectations in the October projection. This decrease was fully realized in February due to early repayment of the loan from the IMF, used within the Precautionary Credit Line<sup>7</sup>. Consequently, total government deposits with the NBRM also registered more intensive decline compared with the projected pace for the first quarter.

Hence, with respect to the balance sheet, the divergence in monetary instruments, compared with the projection, corresponds to the divergence in reserve money, which in February dropped relative to the end of the year, despite the growth in the first quarter as projected in October.

According to the latest available data, in February, in the Budget of the Republic of Macedonia a deficit of Denar 2,378 million was registered. On a cumulative basis, for the first two months of 2015, the budget deficit amounted to Denar 4,583 million (or 0.8% of GDP<sup>8</sup>), representing about 25% of the projected budget deficit for 2015 in accordance with the Budget of the Republic of Macedonia. In terms of its financing, the budget deficit was mainly financed by

**Monetary policy instruments, in MKD million**



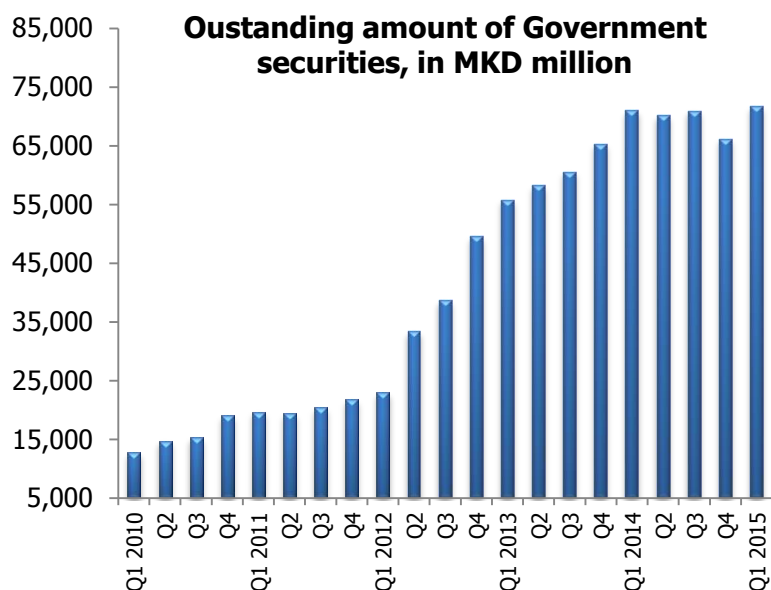
Source: NBRM.

<sup>6</sup>In the fourth quarter of 2014 lower level of monetary instruments compared with the projection was registered.

<sup>7</sup>On 27 February 2015, the government made early repayment of the liabilities to the IMF, based on the Precautionary Credit Line (PCL), in total amount of Euro 153.4 million. In January, net foreign assets of the NBRM grew mainly due to the relatively high foreign exchange gains (about Euro 70 million) as a result of the changes in the price of the US dollar and the Swiss franc.

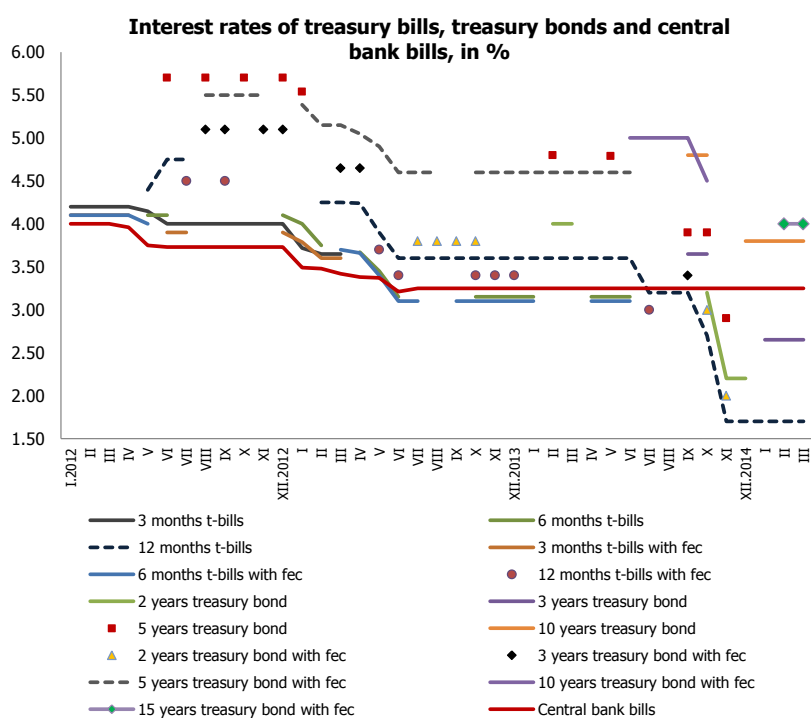
<sup>8</sup> According to the NBRM projection for the nominal GDP. The Ministry of Finance's budget deficit projection also equals 0.8% of GDP.

withdrawing deposits from the account with the NBRM, and to a smaller extent by a net-issuance of government securities.



Source: NBRM.

The stock of government securities on the domestic market as of March amounted to Denar 71,683 million, and compared to December 2014 it is higher by Denar 5,521 million.

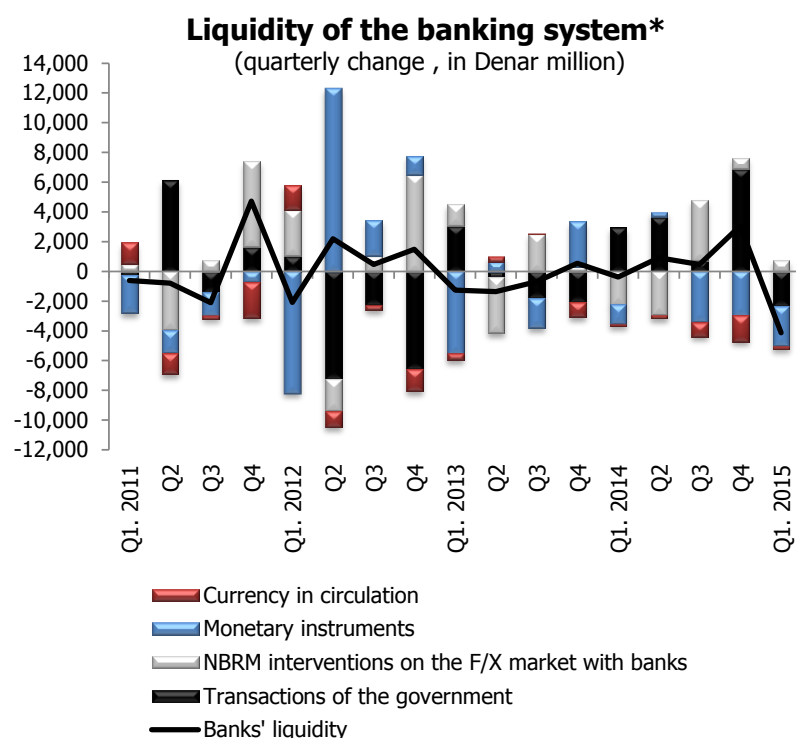


Source: NBRM.

Interest rates on government securities at the auctions held in March ranged from 1.25% and 1.7% for the 6-month and 12-month treasury bills, respectively, and 2.65% for the 3-year government bonds without foreign currency clause and 3.8% for the 10-year government bonds without foreign currency clause, to 4% for the 15-year government bonds with foreign currency clause. The interest rate on the issued 6-month treasury bills was lower than their last auction in June 2014 (interest rate of 3.15%) while the other interest rates remained unchanged.

Regarding the flows of creating and withdrawing liquidity, in March liquidity was predominantly created through monetary instruments. In circumstances of further solid level of CB bills, the liquidity created entirely arises from changes in the standing deposit facility with the NBRM. Government transactions

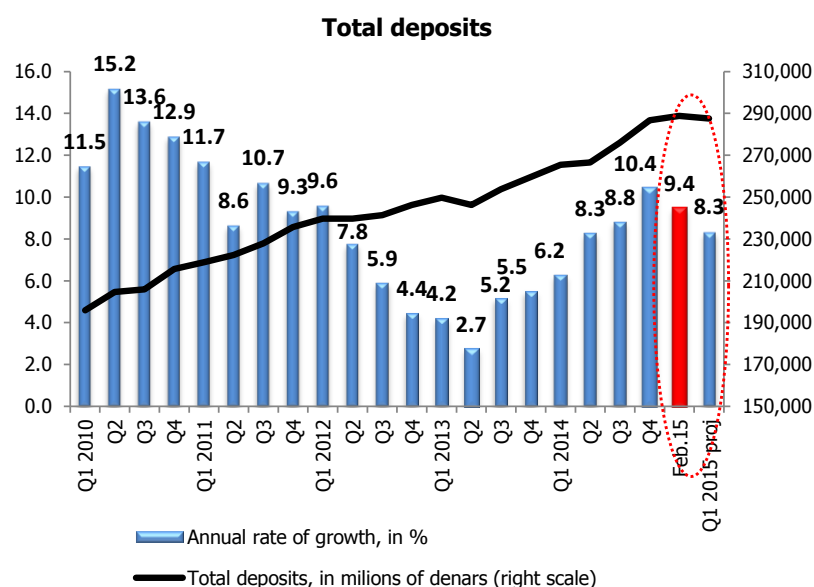
## MONETARY SECTOR



\*Positive change- liquidity creation, negative change- liquidity withdrawal.  
Source: NBRM.

(mainly through increased government Denar deposits with the NBRM) contribute to the withdrawal of liquidity, and currency in circulation also acts in the same direction. In the foreign exchange market, in the transactions with market makers, the NBRM made net sales of foreign currency, which acted toward further withdrawal of liquidity. Against such background, in March the total liquidity declined on a monthly basis.

Data as of February show more intensive decline of reserve money compared to the end of 2014, as a cumulative effect of the simultaneous reduction of currency in circulation and especially the total liquid assets of banks. These accomplishments are contrary to the expectations for quarterly growth of reserve money and its components in the first quarter, according to the October projection. Yet, the reserve money at the end of February is similar to the projection for the first quarter, mainly due to the performances at the end of 2014 (a higher level of reserve money than projected in December).



\*Includes demand money  
Source: NBRM.

In February, further expansion of the deposit base was registered. The increase was due primarily to the growth of household deposits, amid small contribution also of deposits of other financial institutions<sup>9</sup>. Corporate deposits continued to decline on a monthly basis, at a faster pace compared to the previous month.

**At the end of February, the annual growth rate of total deposits equaled 9.4%, which is above the growth of 8.3% projected for the first quarter of 2015.** In the period January-February, the growth of total deposits equaled around 43% of the growth projected for the first quarter. The total deposits were higher than the level projected for the first quarter of

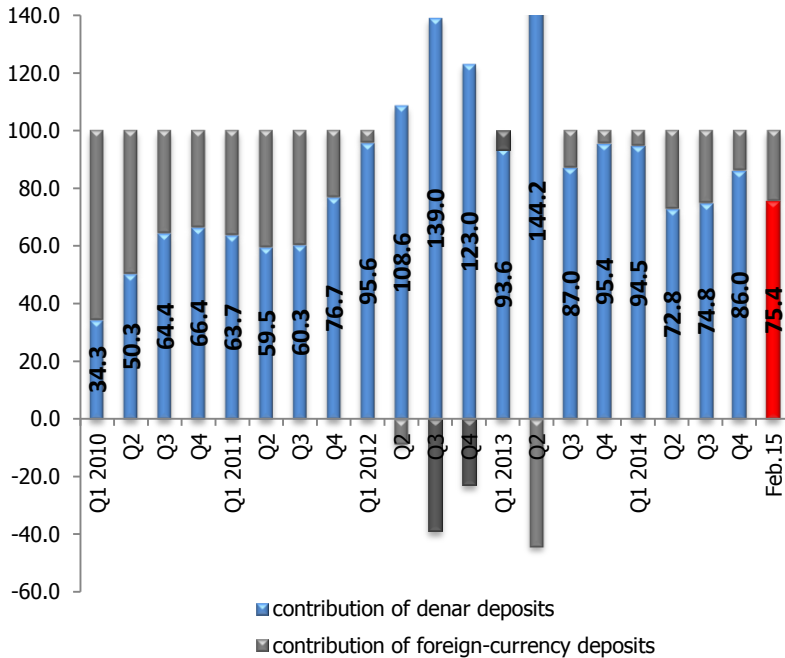
<sup>9</sup>Other financial institutions include investment funds, pension funds, insurance companies, investment funds management companies and pension funds management companies.



## MONETARY SECTOR

2015 according to the October projection, indicating a possible exceeding of the projected deposit base for the first quarter of 2015<sup>10</sup>.

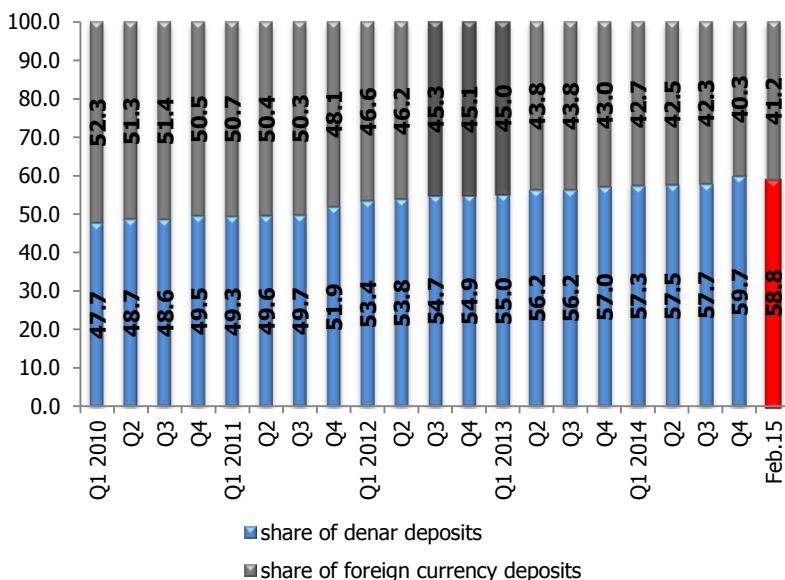
**Contribution of denar and foreign currency deposits to the annual growth of total deposits (in %)**



Source: NBRM.

\*Includes demand deposits.

**Share of denar and foreign currency deposits in total deposits (in %)**



Source: NBRM.

\*Includes demand deposits.

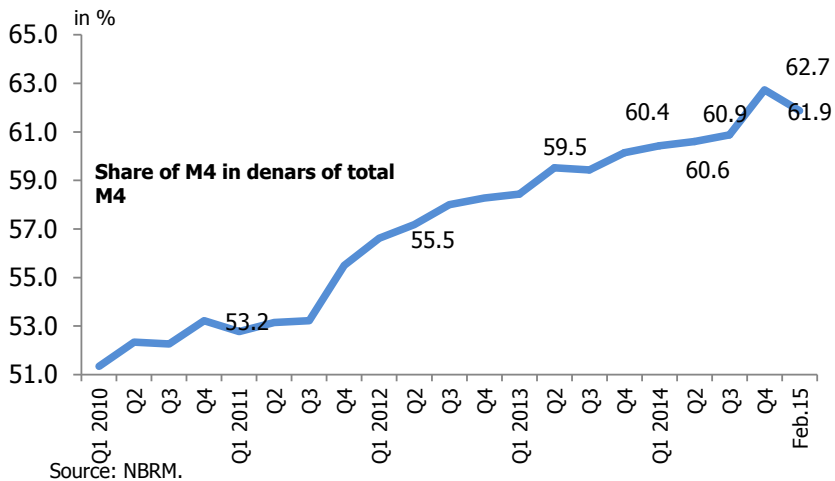
The annual growth of total deposits still stems mainly from the increased denar deposits, amid moderate positive contribution of foreign currency deposits. Also in February foreign currency deposits grew on a monthly basis, but at a slower pace compared to the previous month ...

...resulting in a slight increase of their share in total deposits.

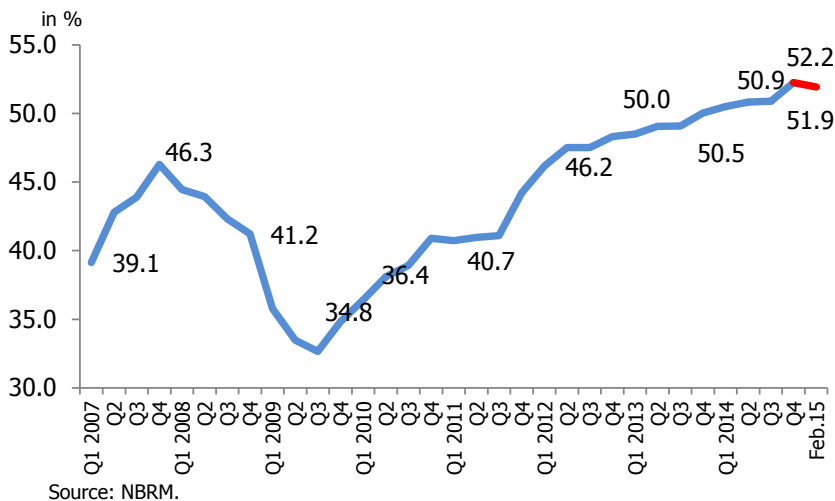
<sup>10</sup> The higher level of deposits in February compared to the projection is in large part explained by the performances at the end of 2014 when the achieved level of deposits was higher than projected.

## MONETARY SECTOR

**Share of denar M4 in total M4  
(in%)**



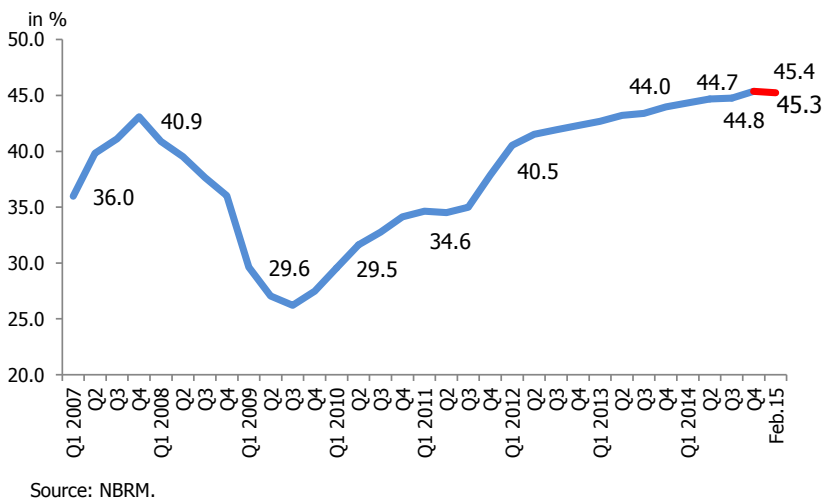
**Share of denar deposits in total household deposits, in %**



During February, twice higher monthly increase of total deposits of households was registered, compared to the previous month, which is dominated by the increased savings in domestic currency (versus their decline in January<sup>11</sup>) amid a small contribution also of foreign currency deposits. These developments have contributed to a moderate increase in the share of Denar deposits in total household deposits relative to January (accounting for 51.9%).

\*Includes demand deposits.

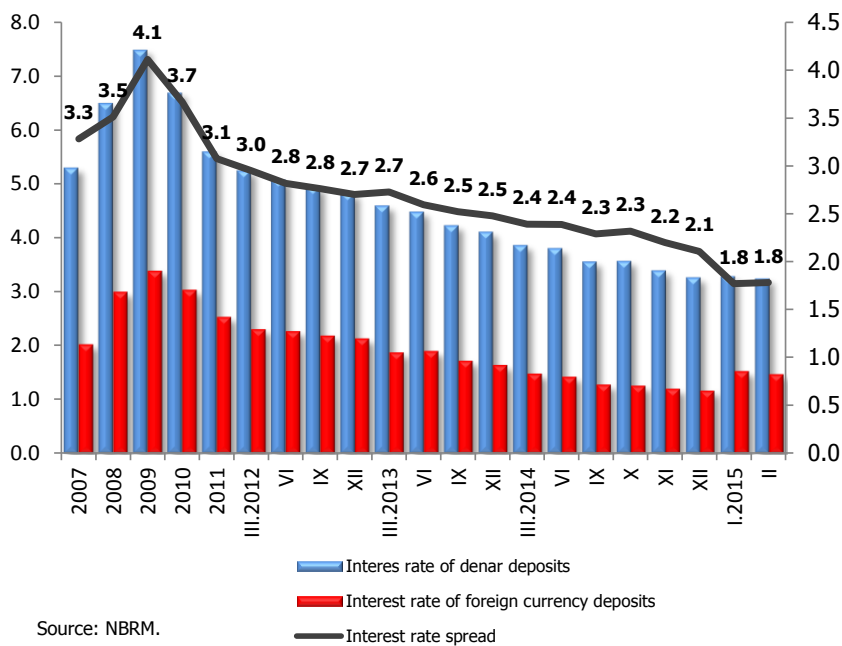
**Share of Denar deposits of households in total deposits of households (excluding demand money)**



<sup>11</sup> Household denar deposits went down in January due to the lower level of demand deposits, while time denar deposits registered a moderate monthly growth.

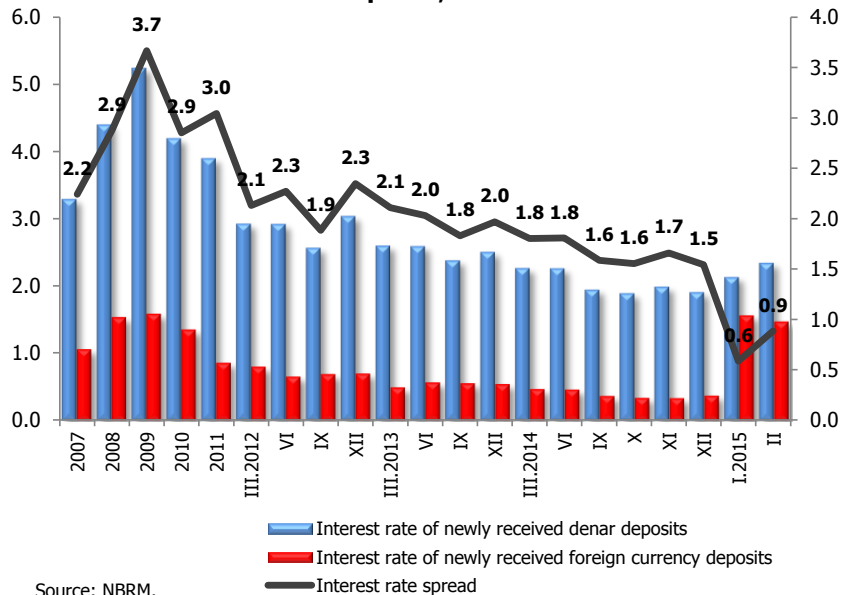
## MONETARY SECTOR

**Interest rates on denar and foreign currency deposits, in%**



During February the interest rate spread between denar and foreign currency interest rates<sup>12</sup> remained at the same level as in the previous month. Amid moderate rise in the interest rate on denar deposits and unchanged interest rate on foreign currency deposits, newly received deposits registered widening of the interest rate spread between them of 0.3 percentage points.

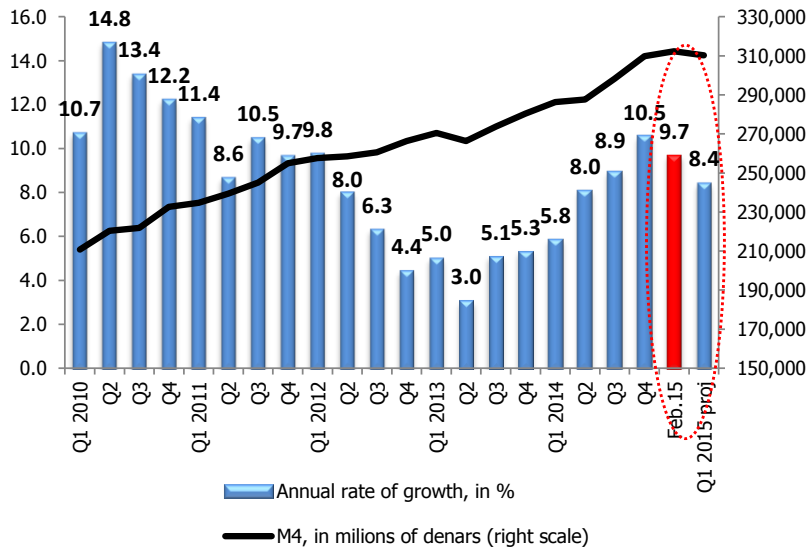
**Interest rates on newly accepted denar and foreign currency deposits, in %**



<sup>12</sup>As of January 2015, interest rate data of banks and savings houses have been collected under the new interest rate methodology, while data for the previous period were collected under the old methodology. For more detailed information see <http://nbrm.mk/default.asp?ItemID=950031C052DEF34CA7B5C69FD32E6C21>

## MONETARY SECTOR

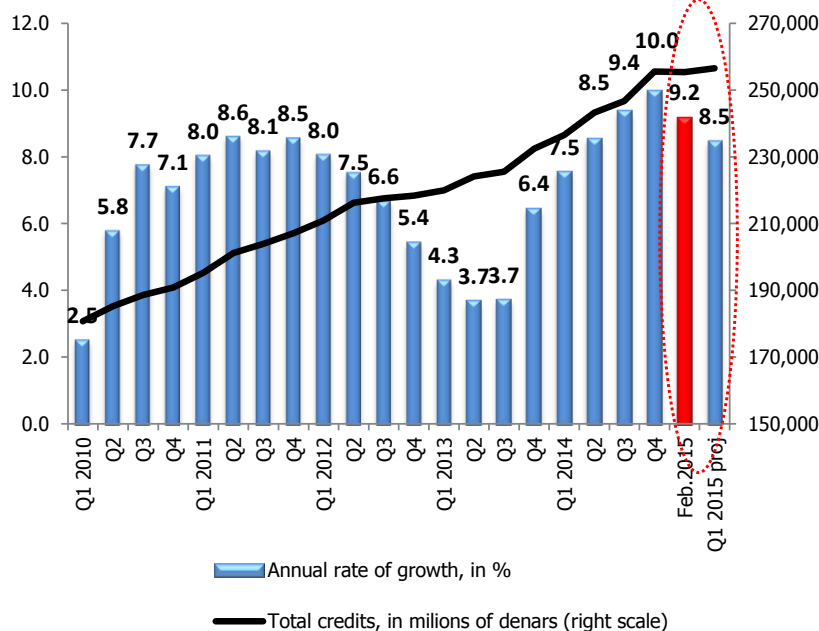
**Broad money, M4**



Source: NBRM.

According to the data as of February, the broad money registered a moderate growth compared to the previous month due to the increase in total deposits and the minor growth of currency in circulation. In the January-February period, the growth of money supply equaled around 47.6% of the projected growth for the first quarter. In February, the annual growth rate of the broad money equaled 9.7%, which is above the projection for the first quarter of 2015 (projected annual growth of 8.4%)<sup>13</sup>.

**Total loans**



Source: NBRM.

In February, total loans to the private sector registered a moderate monthly growth, after the decline in the previous month. This increase in credit activity is largely a result of the monthly growth of loans to households, amid small growth of loans extended to enterprises, as opposed to their decline in January.

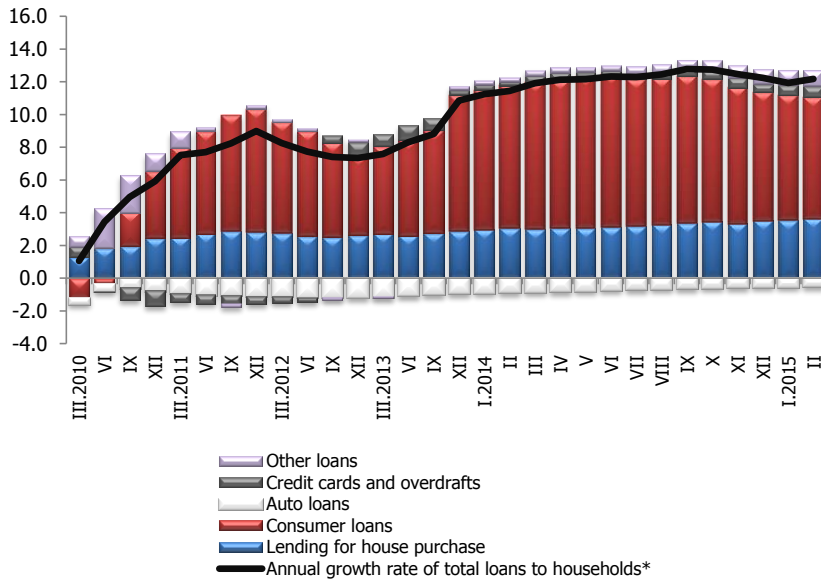
**At the end of February, the annual growth rate of total loans equaled 9.2%, which is above the annual growth of 8.5% projected for the first quarter of 2015<sup>14</sup>.** As of February, total loans registered a slight decline compared to the end of the previous year (as a result of the decline in January), while the October projection envisages quarterly growth of Denar 3,967 million.

<sup>13</sup> Also, the level of money supply as of February exceeds the projected level, mostly reflecting the faster growth of M4 than projected in 2014.

<sup>14</sup> The higher annual growth rate of total loans results from the increased lending activity as of end 2014.

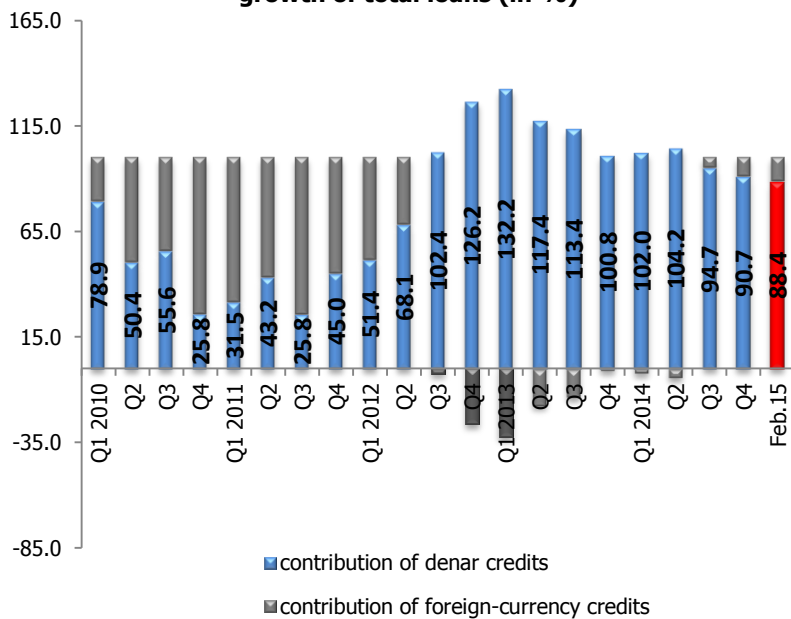
## MONETARY SECTOR

### Loans of banks and savings houses extended to households (contribution to the annual change in loans to households\*, in percentage points)



\*Total loans to households do not include loans to self-employed individuals.  
Source: NBRM.

### Contribution of denar and foreign currency loans to the annual growth of total loans (in %)

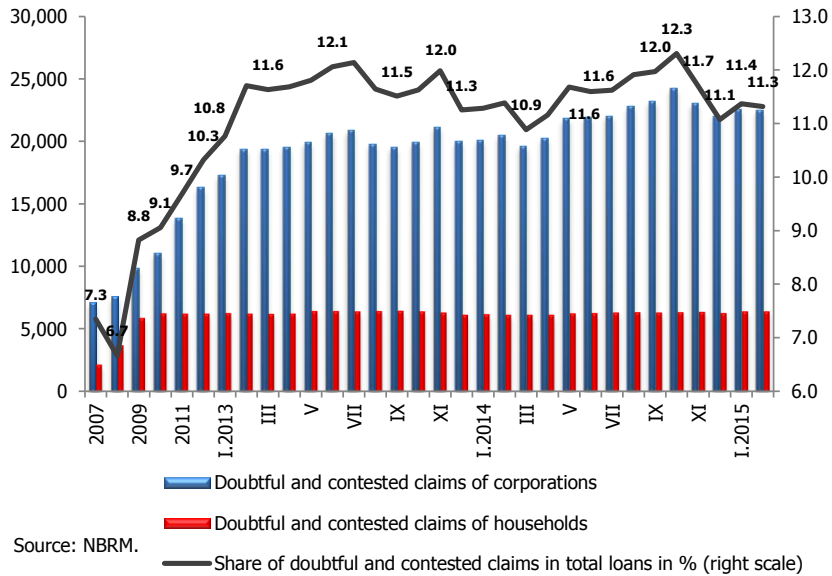


Source: NBRM.

The annual growth of total loans still mostly results from the growth of denar loans, amid moderate positive contribution of foreign currency loans.

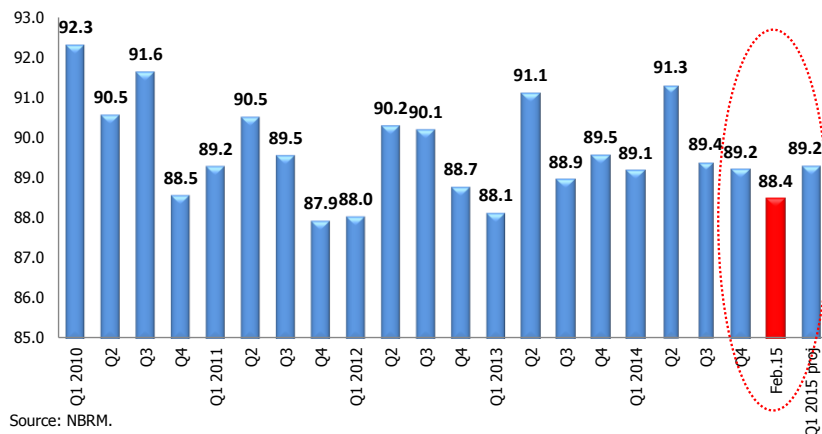
## MONETARY SECTOR

**Share of doubtful and contested claims in total loans, in %**



February registered an insignificant monthly decline of doubtful and contested claims, as opposed to their increase in the previous month. Thus the share of doubtful and contested claims in total loans was reduced to 11.3% versus 11.4% in January. On an annual basis, total non-performing loans further increased, at a slower pace compared to the previous month.

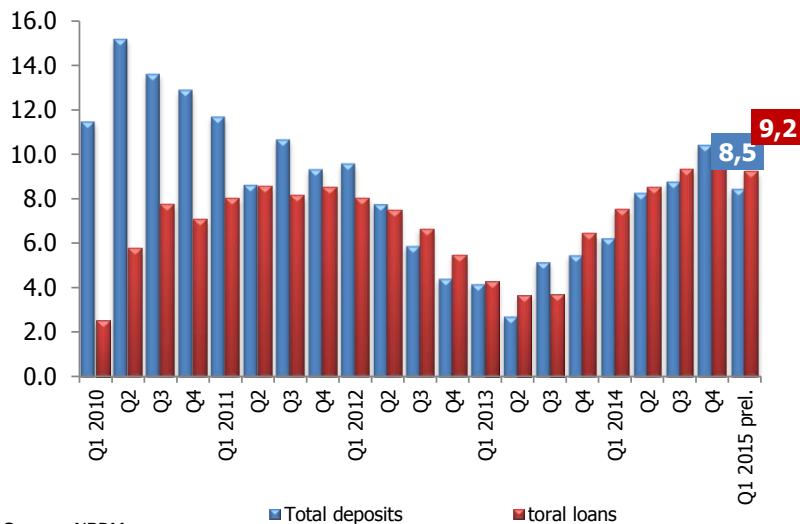
**Loan-deposit ratio, in %**



The utilization of deposit potential for lending to the private sector at the end of February remained at the same level as in the previous month, amid moderate growth of both components.

## MONETARY SECTOR

**Total loans and deposits, annual changes, in %**



Source: NBRM.

Preliminary ten-day data as of March 2015 show a decline in total deposits of 0.3% on a monthly basis, versus the increase registered in the previous month (of 0.3%). The decline in total deposits in March mainly resulted from the reduced saving of enterprises, which declined faster on a monthly basis compared to the previous month.

A decrease was registered also in the deposits of other financial institutions. Household deposits register an increase on a monthly basis also in March, with the same intensity as in the previous month. The structure of household savings shows further more intensive growth of denar deposits, which in March explain 70% of the monthly growth of the total household deposits. Preliminary data show growth of 1.2% in total loans in March on a monthly basis, which is faster in comparison with the previous month (0.4%). The increase of total loans in March was almost equally distributed between loans to households and loans to the corporate sector. **On an annual basis, total deposits and total loans rose by 8.5% and 9.2%, respectively in March.**

## **Annex 1 Timeline of the changes in the setup of the monetary instruments of the NBRM and selected supervisory decisions adopted in the period 2013 - 2015**

### **January 2013**

- A Decision amending the Decision on the reserve requirement (adopted in November 2012) came into force, allowing reduction of the reserve requirement base of banks for the amount of new loans to net exporters and domestic producers of electricity, as well as for the investments in debt securities in domestic currency without a currency clause, issued by the aforementioned companies. This decision fully exempts the banks from allocating reserve requirement for liabilities based on debt securities issued in local currency with an original maturity of at least two years. The Decision will apply throughout 2014, after which, depending on the results, the need for further application will be reconsidered.
- A Decision on reducing CB bill interest rate was adopted to cut the policy rate from 3.75% to 3.5%. At the same time, the interest rate on seven-day deposit facility and on overnight deposit facility was cut from 2% to 1.75% and from 1.0% to 0.75%, respectively.

### **March 2013**

- A Decision on credit risk management was adopted, which applies from 1 December 2013.

### **July 2013**

- A Decision on reducing CB bill interest rate was adopted to cut the policy rate from 3.5% to 3.25%. At the same time, the interest rate on seven-day deposit facility was cut from 1.75% to 1.5%.
- A Decision amending the Decision on reserve requirement was adopted, which reduces the reserve requirement rate for banks' liabilities in domestic currency from 10% to 8% and increases the reserve requirement rate for liabilities in foreign currency from 13% to 15%. In addition, the amendments stipulate a reserve requirement rate of 0% for banks' liabilities to nonresident financial companies with contractual maturity of over one year, as well as for all liabilities to nonresidents with contractual maturity of over two years. A rate of 13% still applies to short-term liabilities to nonresident financial companies in foreign currency with contractual maturity of up to one year. To maintain the reserve requirement in denars and in euros relatively stable, the amendments increase the reserve requirement in euros that is fulfilled in denars from 23% to 30%.

### **October 2013**

- A Decision amending the Decision on banks' liquidity risk was adopted. This decision reduces the proportion of time deposits assumed to outflow from banks, from 80% to 60%, and applies from 1 December 2013. This amendment makes more room for long-term bank lending to the real sector.

### **November 2013**

- A Decision amending the Decision on reserve requirement was adopted, which exempts the NBRM from paying reserve requirement remuneration (previously, this remuneration equaled 1%



for denar reserve requirement and 0.1% for euro reserve requirement). The Decision is being applied since 1 January 2014.

- A Decision on CB bills was adopted, which introduces a methodology for determining the potential demand for CB bills. In accordance with the established mechanism, if there is a higher demand than the potential across the overall banking system, banks that bid higher amounts of their own liquidity potential will be required to place this difference in seven-day deposits.

## **February 2014**

- A Decision on reducing interest rate on seven-day deposit facility from 1.5% to 1.25% was adopted.

## **April 2014**

- A Decision amending the Decision on the methodology for determining capital adequacy was adopted, introducing two amendments in the current decision that are expected to contribute positively to the credit support of the commercial banks to the corporate sector. Namely, with this Decision (and in accordance with the amendments to the new EU Regulation no. 575/2013 on prudential requirements for credit institutions and investment companies), performance guarantees or warranties that guarantee completion of works, stand out as items with low-intermediate risk, and therefore take lower conversion factor (20%), instead of 50% as it has been so far. That would mean that in the calculation of capital adequacy, smaller part of these off-balance sheet items would be treated as a balance sheet items, which could affect the improvement of capital adequacy and encourage lending to the corporate sector. There is another innovation motivated by the international practice of establishing funds by low-risk entities (central governments or multilateral development banks) whose main goal is funding development projects. These projects are mostly funded through one or more commercial banks, which also contribute funds by dividing the exposure into a defined ratio between the bank and the fund or by providing guarantees or other similar instruments used by the fund (warranty provider) to guarantee coverage of part of the credit risk in the event of default by the debtor. In order to cover these cases, this decision also introduces a more favorable regulatory treatment of the funds established by one or several central governments, multilateral development banks or public institutions. These funds will take 0% risk weight, and the requirement will be that the funding is executed by payment in stakes, i.e. on-balance sheet and off-balance sheet activities to be covered by the fund's equity.

## **September 2014**

- In order to further channel banks' excess liquidity to the non-financial sector, in September the NBRM revised the mechanism for transfer of the demand for CB bills, which is above the banks' potential into another instrument, i.e. seven-day standing deposit facility. According to these changes, for the seven-day standing deposit facility that banks are obliged to allocate if on the CB bills auctions they demand an amount higher than the potential<sup>15</sup>, an interest rate of 0% is determined. For the other assets that banks will voluntarily place into a seven-day standing deposit facility the regular interest rate will apply.

---

<sup>15</sup>For the method of determining the potential demand for CB bills see the Decision on CB bills, "Official Gazette of the Republic of Macedonia" no. 166/13).

## **September 2014**

- The National Bank of the Republic of Macedonia Council adopted the Decision amending the Decision on the reserve requirement, which extends the application of the non-standard measure for reduction of the base for the reserve requirement of commercial banks for the amount of new loans extended to net exporters and domestic producers of electricity. The main objective of the Decision is to provide further support to the two systemically important sectors of the economy. The current implementation of this measure has generated positive effects on the dynamics of lending and thus the overall economic growth, contributing to a reduction of the cost of funding of companies from both sectors, although with lower intensity than the potential. In such circumstances, and given the data that indicate some uncertainty about the pace of lending to the corporate sector in the next period, this Decision envisages continued application of this non-standard measure until 31 December 2015.

## **October 2014**

- A Decision on reducing the interest rate on overnight deposit facility from 0,75% to 0,5% and on seven-day deposit facility from 1.25% to 1% was adopted.

## **February 2015**

- The Council adopted the Decision amending the Decision on reserve requirement and the Decision amending the Decision on CB bills. In case of applying limited amount tender at CB bill auctions, in the last quarter of 2014 and early 2015, it is noticeable that commercial banks regularly begin the period with low fulfillment of the reserve requirement, while participating in the auction with high amounts over their liquidity potential. The amendments to the decisions require that the commercial banks start the reserve requirement period with amounts on their accounts in the National Bank of at least the reserve requirement amount. Additionally, a second measure is proposed that provides restricting the use of the reserve requirement during the entire maintenance period, thus, the banks will be required to maintain daily liquidity of at least 50% of the reserve requirement. These measures do not reduce banks' flexibility in liquidity management; they are expected to contribute to lower reliance on reserve requirement when establishing the demand for CB bills<sup>16</sup>.

## **March 2015**

- A Decision on reducing the interest rate on overnight deposit facility from 0,5% to 0,25% and on seven-day deposit facility from 1% to 0.5% was adopted.
- The National Bank Council adopted the Decision amending the Decision on CB bills, which introduces a new manner of establishing the bids of banks at the auctions of CB bills. According to the Decision, the amount of supply of individual bank is calculated by applying its appropriate percentage share in the total supply of treasury bills, reduced by the amount of past due CB bills of the Macedonian Bank for Development Promotion AD Skopje. In order to ensure operational efficiency in conducting auctions of this type and greater transparency toward banks, before the auction the NBRM shall inform the banks on the maximum offer that can be submitted by each bank. This opportunity for setting the supply of banks is expected to stabilize the demand at the level of the amount offered, which eliminates the need for calculation of potential demand and subsequently it repeals the obligation for mandatory seven-day deposits for banks when demand at the auction exceeds the potential demand.

---

<sup>16</sup> Decision amending the Decision on the reserve requirement was abandoned in March.