Introduction

The pandemic caused by the coronavirus and measures taken to protect public health had a strong negative impact on both the global and domestic economy. Given the deteriorating epidemiological situation and the outbreak of the second wave of the viral infection, which is likely to be present until at least the first half of the following year, it is certain that the negative effects from the pandemic will be stronger than initially expected, and the economic recovery to pre-crisis level will be slower. Although the new wave of health crisis is expected to be accompanied by targeted and less restrictive measures than those introduced in tackling the first wave of pandemic spread, however, the further presence of the virus and uncertainty will cause a partial restraint of economic entities for a longer period. **A positive risk to the economic outlook would be the vaccine development earlier than initially expected,** given the intensified global efforts in this field. Hence, the macroeconomic forecasts in this cycle are once again subject to extremely high uncertainty related to the assumptions about the spread of the coronavirus i.e. the prospects for its eradication. The rapid, timely and coordinated response of the monetary and fiscal policy in response to the crisis acted as a cushion for the initial impact to the real sector, with announcements of maintaining the accommodative character of the policies for a longer period than previously expected, until overcoming the crisis.

In conditions of a solid level of foreign reserves and absence of inflationary pressures, in the third quarter, the monetary setup maintained its accommodative character. The reduction of the interest rates on CB bills on three occasions during the first half of the year to the actual level of 1.5%, as well as the more significant reduction of the offered amount of CB bills conducted on two occasions during the second quarter contributed to an increased liquidity of the banking system and support of credit flows in the economy. The regulatory changes were also in this line which provided a greater flexibility for the banks and maintained the credit cycle. Given the prolonged effects from the Covid crisis and in accordance with the previously adopted regulatory changes, nearing the end of the third quarter, the banks provided some of their clients with a second favorable change in the credit terms for credit products. This support was entirely targeted at those clients most affected by the pandemic. Additionally, in August, the European Central Bank (ECB), announced that, at the request of the National Bank, for the first time it approved a repo line worth EUR 400 million, intended to provide foreign currency liquidity for the financial institutio0ns in the Republic of North Macedonia through the central bank. Such an instrument is especially important, because it provides a quick access to liquidity in euros, amid high uncertainty and possible major disruptions in the international markets due to the Covid-19 shock. The repo line will be available until the end of June 2021, with a possibility for extension if deemed necessary.

Certain changes occurred in the forecasts for the key indicators of the external economic environment in the period between the two forecasts. Thus, compared to April, the current perceptions of the foreign effective demand point to a deeper decline in 2020 (of 6.3%, compared to the estimates for a decline of 5% in April), and weaker growth in 2021 (of 6.4%, versus the expectations for growth of 4.9% in April). In terms of the foreign effective inflation, compared to the April forecasts, a minor downward revision for 2020 and minor upward correction for 2021 have been made, thus currently expecting a slowdown of the inflation in 2020 to 0.5% and moderate acceleration in 2021 to 1.4%. **The latest forecasts for the changes in prices of primary commodities in the world stock markets primarily indicate a fall in the prices for 2020 and a synchronized rise in 2021 with mainly upward revisions compared to the April forecasts.** However, the movements in prices of primary commodities are extremely volatile, and under strong influence of the pandemic developments, which creates greater uncertainty about their future dynamics.

The October perceptions for the decline of the Macedonian economy are less favorable compared to the April estimates. This mainly reflects the weaker performances in the first half of the year, as well as the estimates for a deeper decline in the second half, due to the second autumn wave of the virus spread and its presence in first half of the following year, as opposed to April estimates for a faster normalization. **Thus, a 4.9% drop in GDP is forecasted for 2020, followed by a partial recovery i.e. growth of 3.9% in 2021 (April: decline of 3.5% and growth of 4.7%, respectively).** Regarding the structure of the activity for 2020, a larger negative contribution compared to the April estimates is expected in the domestic demand, amid a slightly positive contribution of net exports. Within the domestic demand, the largest negative contribution is still expected from investments, which are strongly influenced by the weak demand and high level of uncertainty. A negative contribution is also expected from household consumption, reflecting the further presence of greater restraint, in conditions of uncertainty regarding jobs and income. Regarding the labor market, the expected negative effects from the crisis will be mitigated by the undertaken and announced fiscal measures, which will contribute to maintaining wage growth to a higher level and retaining employment in 2020. In conditions of declining foreign demand and temporary disruptions in the global production and logistic chains, exports will decline in 2020 but more moderately compared to April expectations. Reduced export activity, amid decline in domestic demand, will decrease import of goods and services, which would also decrease imports, whereby net exports would make positive contribution to growth. The partial recovery of the economy in 2021 would be supported by all sources of growth, with the domestic demand expected to have a positive, while net exports a negative contribution to the growth. In the medium term, further recovery of the economy is expected, with a slightly more moderate growth rate of 3.6% in 2022 (downward revision compared to the April estimates for a growth of 4%) and 4% in 2023. Pronounced downward risks to the forecasts taking into account that the recovery is largely conditioned on the pandemic duration, virus containment measures, and the speed of restoring confidence and stabilizing expectations.

Regarding the future path of price movements in the domestic economy, the latest forecast point to inflation of 1.1% in 2020, compared to the April expectations for an inflation rate of around 0%. Namely, the emergence of the pandemic caused shifts on both the supply side and the demand side for certain market segments, factors that probably contributed for a higher than expected inflation rate. **In addition, the increase of the electric prices, which was not incorporated in the forecasts had some contribution to the deviation. In 2021, the inflation rate is expected to moderately accelerate and reach 1.5%, and approach the level of around 2% in 2022-2023, which is in line with the April perceptions.** International markets marked by significant volatility of the prices of primary commodities, and thus uncertainty about the future movements in import prices, especially in the long run.

Credit activity of the banking system is still one of the important factors that support economic growth. The latest credit market assessments in the forecast horizon indicate faster than expected credit activity in 2020 and solid growth rates in the next three years. In order to encourage lending activity, the National Bank since the beginning of the crisis has adopted a series of measures, creating conditions to reduce financing costs through loans from banks, as well as to provide additional liquidity in the banking system. Given the increased credit support in the first three quarters of 2020 and the expectations for its continuation by the end of the year, for 2020, the credit growth would be 5.3%[1] (3% in the April forecast). With the gradual normalization of the situation and stabilization of expectations, gradual acceleration of the growth of the credit activity is expected in the next period. Thus credit growth for the period 2021-2022 would average 6.3% (6.5% in the April forecast) and would reach 7.6% in 2023. The estimates for the dynamics of the credit and deposits growth is based on the expectations for the stabilization of the situation in the domestic economy by the end of 2021. Regarding the sources of financing, given the solid growth of total deposits in the first three quarters of 2020, the growth for the whole 2020 is expected to amount to 4.4%[2] (2.3% with the April forecasts). Such changes in the deposit base are partially a reflection of the greater restraint from spending/investments in conditions of uncertainty, as well as the implemented economic measures of the government for dealing with the health crisis consequences, which provided additional assets to companies and households to improve their liquidity. In the next two years, amid assessment for faster economic growth and maintenance of high propensity to save in banks, an annual deposit growth is expected of about 6.9% on average (7.1% with the April forecast). In 2023, the deposits growth is expected to reach 8.2%.

[1] By including the balance of approved loans from the bank in bankruptcy, the credit growth in 2020 would amount to 7%.
[2] By including the data from the bank in bankruptcy, the deposits growth in 2020 would amount to 5%.

The outbreak of the pandemic has led to disruption in the global production chains and decline of the world trade. Such unfavorable external environment, as well as deteriorated expectations caused by the Covid-19 spread, moderately worsens the external position of the economy. The current account deficit of the balance of payments is expected to moderately deepen in 2020 to 3.7% of GDP (3.2% in the April forecasts). Such expectations are a reflection of the lower surplus in the secondary income, while a minor improvement is expected in other components compared to the previous year. The restrictive measures to contan virus spread significantly reduced the international movement of passengers, which caused a larger downward correction in foreign exchange inflows through non-formal remittances and appropriate downward adjustment of net purchased cash on the foreign exchange market. This effect is expected to be partially offset by higher foreign exchange inflows through formal channels (private transfers). In foreign trade, a downward adjustment in both components is expected, amid negative pressures on exports from the reduced foreign demand and temporary disrupted supply chains, as well as due to the corresponding reduction in import demand, supplemented by lower import pressures from lower domestic demand. The decline in imports will be further highlighted by the expected decline in stock prices of crude oil. In terms of the net effect, the forecasted movements of export and import of goods is expected to narrow the trade deficit. The estimates for a lower newly created value from the companies with foreign capital will contribute to a smaller deficit in primary income, and better performances are forecasted in the balance of services due to the more pronounced downward adjustment in import compared to the downward adjustment in the export of services (smaller outflows on net basis in other services and higher expected net export in the production services for further processing). The negative effects from the pandemic are expected to be partially present in 2021, with a more moderate reduction of the current account deficit to 2.6% of GDP (compared to the expected 1.8% in April), amid a forecasted slower growth of net inflows in the secondary income, but also a deterioration in the balance of goods and services, in conditions of a faster growth of import demand compared to the expected growth of the export activity. **For the period 2022-2023, the average current account deficit is expected to amount 1.6% of GDP, similar to the April expectations in the medium term. Analyzing the financial account, in the period 2020-2023 current transactions are expected to be largely financed through external government borrowings and foreign direct investment.** Foreign reserves adequacy ratios show that they were in the safe zone throughout the forecast horizon.

In general, compared to the April forecasts, the latest estimates for the period 2020-2023 point to prolonged pandemic effects on the global economy, and thus on the performances in the domestic economy from the pandemic. Contrary to the April estimates for the temporary nature of the health crisis, the current estimates poi8nt to a prolonged effect and the likelihood that economies will make up for the losses by 2022. Hence, the forecasts for the domestic economy indicate a deeper decline in 2020, more moderate pace of recovery in 2021 and stabilization in 2022. Observing risk sources, they are still assessed as markedly downward and almost entirely related to the COVID-19 pandemic. Currently, the main downward risk is related to the potential reintroduction of restrictive measures to contain virus spread, in response to the current second wave of the pandemic, as well as any slower virus management than currently expected. The possible materialization of these risks may lead to re-disruption of production and demand chains and to a significant slowdown of the expected dynamics of the economic recovery, and thus to difficulties in the survival of the companies and more pronounced deterioration in the labor market. On the other hand, faster progress in the coronavirus treatment and vaccine development are factors that instill optimism. If the coronavirus threat is overcome faster than expected, enhanced confidence could significantly boost global economy. Also, our country’s membership in the NATO alliance and potential start of the negotiations for full membership in the EU continue to pose a positive risk for the forecasts in the medium turn. According to the October macroeconomic scenario, inflation is expected to remain moderate. At the same time, no major imbalances in the balance of payments are expected, given the dominance of the trade of goods in its structure, as well as the partial change in the habits of our expatriates in sending remittances. In line with the forecasts for retaining favorable financial conditions globally, we expect normal access to capital markets. Consequently, foreign reserves will remain in the safe zone throughout the forecasting period. The National Bank constantly monitors the current developments, including the potential surrounding risks and stands ready to adjust policies and take timely measures, in accordance with its mandate.