National Bank of the Republic of Macedonia

MONETARY POLICY AND RESEARCH DEPARTMENT

Recent Macroeconomic Indicators
Review of the Current Situation

January 2018

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 (September- December 2017) and to make a comparison with the latest macroeconomic forecasts (October 2017). 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 forecasts. The review focuses on the changes in external assumptions and performance with domestic variables and the effect of these changes on the environment for monetary policy conduct.

No major changes were registered in the global environment in the period from the October forecasts onwards. Thus, further strengthening of the economic activity is expected, amid favorable expectations for the euro area as our most important trade partner. Risks regarding global growth forecasts, as before, are mainly related to the possibility of increased global protectionism, uncertainty regarding the Brexit effects, effects from the normalization pace of central banks' monetary policy in the developed countries, possible increased volatility in financial markets, as well as increased geopolitical risks. The euro area economy, as our main trade partner, continued to increase at an accelerated pace in the third quarter also, reaching an annual growth of 2.6% (2.4% in the second quarter), mainly driven by the consumption of households and investments. Additionally, the available high-frequency data and surveys of households and economies also indicate a solid economic growth in the last quarter of the year. Favorable movements also continued in the labor market, whereby the number of employees in the third quarter increased by 1.7% (1.6% in the second quarter), and the unemployment rate registers further decrease reaching 8.8% in October, which is the lowest rate since January 2009. In accordance to such developments, in December 2017, ECB revised the GDP[1]forecasts upwards, assessing the growth risks as mainly balanced, whereas inflation forecasts are mainly unchanged compared to September, except for 2018[2]. In terms of the EURIBOR interest rate, a similar rate as in October is expected during the whole forecasts period, whereby economic agents' expectations aim to maintain the existing ECB interest policy during 2019 also, despite the announced completion of the programme for quantitative easing in September 2018.

Observed from a viewpoint of the individual quantitative external environment indicators for the Macedonian economy, the forecasts regarding the foreign effective demand were revised upwards for 2017 and 2018, while for 2018 the estimation remains unchanged. A minor upward revision in the entire forecasts period was also conducted in **foreign effective inflation**. In terms of the **euro/US dollar exchange rate**, the US dollar is expected to register a greater depreciation in the two following years compared to the October forecasts. **The changes of primary commodities prices in the global markets are mainly upward in the 2017-2018 period, whereas for 2019 are generally revised downwards compared to the October forecasts.** Observed by individual products, the latest assessments of **world oil prices** point to a higher price growth in 2017 and especially in 2018 and greater decline in 2019 compared to October. In 2017 and 2018, a higher growth is also expected in **metal prices**, whereas the expectations for 2019 are less favorable compared to October, amid estimations for lower growth of nickel prices and slight decline of the copper prices, rather than the previously estimated growth. In terms of **global prices of primary food products**, their revisions are in different directions relative to the October estimations. Thus, a lower growth of wheat prices is expected in 2017 and 2018 and higher growth in 2019 compared to October. On the other hand, a smaller decline of corn prices is

[1] Pursuant to the latest ECB forecasts, the real GDP growth rate is envisaged to amount to 2.4% for 2017, 2.3% for 2018 and 1.9% for 2020, compared to the growth rate of 2.2%, 1.8% and 1.7% for 2017, 2018 and 2019 in the September forecasts, respectively.

[2] The latest forecasts on inflation are 1.5%, 1.4%, 1.5% and 1.7% for 2017, 2018, 2019 and 2020, respectively, with an upward revision for 2018 only (1.2% in September).

expected in 2017 and higher decline in 2018 relative to October estimations, whereas the expected growth for 2019 is unchanged. However, it should have in mind that the estimations for the prices of these commodities are extremely volatile, which creates uncertainty about the assessment of their future dynamics and effects on the domestic economy, especially in the long-term.

The comparison of the latest macroeconomic indicators with their forecast dynamics within the October forecast round does not indicate major deviations in the individual segments of the economy. Regarding the economic activity, currently available high-frequency data for the first two months of the fourth quarter point to more favorable shifts in the economy, in line with the survey results which show retention of economic agents' confidence. This, in addition to published GDP percentage data, according to which the economic activity registers a slight growth in the third quarter, corresponds with the forecasted movement for improving the situation in the second quarter of the year. Regarding changes in consumer prices, the inflation ratio in December was 2.4% which is in line with the forecasted. Observed for the whole year 2017, the inflation ratio amounts to 1.4%, slightly under the forecasted in the October forecasts. In conditions when inflation generally follows the forecasted trajectory, the risks regarding the inflation forecast for 2018 remain associated to the uncertainty about the expected movement of primary commodities prices.

At the end of the fourth quarter of 2016, foreign reserves data indicate an increase in foreign reserves (adjusted for the price and exchange rate differentials and price changes of securities). Observing the factors of change, the upward changes in the reserves are mostly due to the NBRM interventions on the currency market with net purchase. Transaction on behalf of the government are in the opposite direction. Regarding external sector indicators, data on external trade as of November point to possibilities for a better trade balance compared to the expected. The latest available data for net purchase from exchange operations, as of the second decade of December, point to net inflows from private transfers that are within the expected with the October forecast. Data on balance of payments as of October suggest a better current account balance due to a better balance in goods and services and in primary income, as well as the possibility of achieving lower net inflows in the financial account compared to the expectations for the fourth quarter. However, data are available for a very short period and are not sufficient to reach reliable conclusions. The analysis of foreign reserves adequacy indicators shows that they continue to hover in a safe zone.

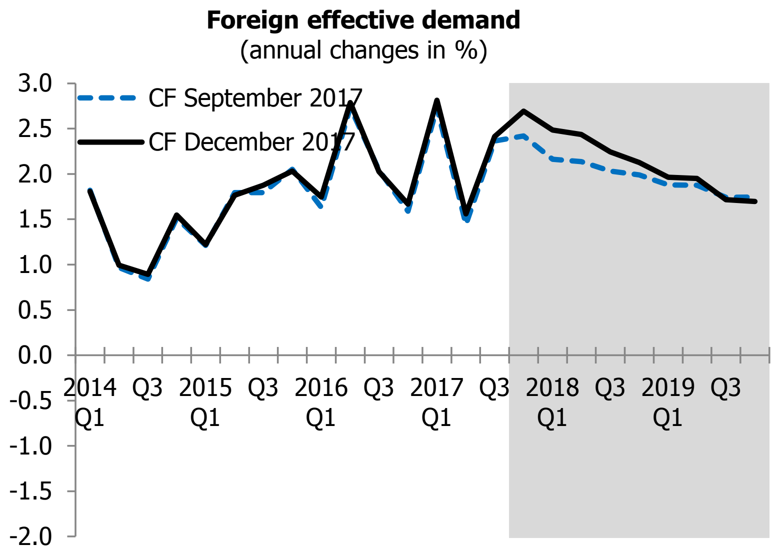
As for the monetary sector developments, final data as of November show further growth of total deposits with the banks (of 0.9%) on a monthly basis, with a similar pace as in the previous month (of 1.0%). Analyzed by sector, the growth of deposits in November was mostly due to increased household deposits, and growth but relatively lower was registered in corporate deposits. In terms of currency structure, the growth of total deposits is almost entirely due to denar deposits i.e. demand deposits, and foreign currency deposits also had a positive contribution in the monthly growth of total deposits. **On an annual basis**, total deposits grew by 5.8% in November, which is above the forecasted growth of 3.6% for the fourth quarter of 2017, according to the October forecast. Regarding the credit market, in November total loans registered a significant growth acceleration (0.9%) compared to the previous month (growth of 0.1%) mostly driven by performances in the corporate sector, compared to their negative contribution in the growth of the previous four-month period. On an annual basis, total loans in November grew by 5.6%, which is higher compared to the forecasted for the fourth quarter (4.6%). Given the performances in October-November and usual seasonal growth in deposits and loans in the last month of the year, performances in both categories are expected to be within the forecasted trajectories, pursuant to the October forecast.

In the period January-November 2017, the Budget of the Republic of Macedonia registered a deficit of Denar 13,184 million, financed from domestic sources i.e. through deposits withdrawal from the government account with the National Bank and with net issue of new government securities on the domestic market. The budget deficit constitutes 71% of the forecasted deficit in the Budget Revision for 2017.

The latest macroeconomic indicators and assessments indicate significant deviations in terms of the forecasted dynamics and the perceptions about the environment for conducting monetary policy and about the risks highlighted in the October forecasts are mainly unchanged. Foreign reserves (adjusted for price and exchange rate differentials and price changes of securities) registered a growth compared to the third quarter. Also, foreign reserves adequacy indicators continue to hover in the safe zone. In terms of economic activity, the growth in the third quarter and generally favorable signs from high-frequency indicators and surveys for the last quarter are in line with the expectations within the October round of forecasts for improved economic situation in the second half of 2017. Regarding inflation, recent performances are in line with the forecast, but the uncertainty associated with the expected movement of primary commodity prices remains a risk to the forecast for 2018. Within the monetary sector, the dynamics of deposits and loans is within the forecasted.

Selected economic indicators /1		**2015**	**2016**					**2017**																
	2014	2015	Q1	Q2	Q3	Q4	2016	Jan.	Feb.	Mar	Q1	Apr.	May	Jun.	Q2	Jul.	Aug	Sep	Q3	Oct.	Nov.	Dec	Q4	2017
I. Real sector indicators																								
Gross domestic product (real growth rate, y-o-y) /2	**3.6**		**3.6**	**2.3**	**2.4**	**3.3**	**2.9**				**0.0**				**-1.3**				**0.2**					
Industrial production /3																								
y-o-y	4.8	4.9	10.7	1.3	5.0	-1.8	3.4	-2.6	-1.3	-0.9	-1.5	-1.9	9.2		3.7	-2.2	-5.3	0.3	-2.4	1.3	4.1			
cumulative average	4.8	4.9	10.7	5.6	5.4	3.4	3.4	-2.6	-1.9	-1.5	-1.5	-1.6	0.6		1.2	0.7	-0.1	-0.1	-0.1	0.1	0.5			
Inflation /4																								
CPI Inflation (y-o-y) /5	-0.5	-0.4	-0.1	-0.7	-0.2	-0.1	-0.2	0.6	0.2	0.6	0.5	1.0	1.2	1.5	1.2	1.2	1.9	1.7	1.6	1.9	2.2	2.4	2.2	2.4
CPI Inflation (cumulative average)	-0.3	-0.3	-0.1	-0.4	-0.3	-0.2	-0.2	0.6	0.4	0.5	0.5	0.6	0.7	0.9	0.9	0.9	1.0	1.1	1.1	1.2	1.3	1.4	1.4	1.4
Core inflation (cumulative average)	0.5	0.5	1.6	1.4	1.3	1.3	1.3	1.4	1.4	1.6	1.6	1.7	1.8	1.9	1.9	1.9	2.1	2.1	2.1	2.2	2.3	2.3	2.3	2.3
Core inflation (y-o-y)	0.5	0.5	1.6	1.3	1.1	1.1	1.3	1.4	1.4	2.0	1.6	2.0	2.1	2.4	2.2	2.3	3.0	2.7	2.7	2.9	2.9	2.9	2.9	2.3
Labor force																								
Unemployment rate	28.0	26.1	24.5	24.0	23.4	23.1	23.7				22.9				22.6				22.1					
II. Fiscal Indicators																								
(Central Budget and Budgets of Funds)																								
Total budget revenues	145,929	161,207	40,583	41,422	43,807	43,524	169,336	12,584	13,310	16,840	42,734	15,053	15,356	13,225	43,634	15,173	14,482	14,949	44,604	15,390	14,352			
Total budget expenditures	168,063	180,632	46,218	42,729	45,953	50,506	185,406	14,723	14,845	16,733	46,301	15,082	17,089	16,206	48,377	17,567	14,564	15,218	47,349	15,657	16,214			
Overall balance (cash)	-22,134	-19,425	-5,635	-1,307	-2,146	-6,982	-16,070	-2,139	-1,535	107	-3,567	-29	-1,733	-2,981	-4,743	-2,394	-82	-269	-2,745	-267	-1,862			
Overall balance (in % of GDP) /1	-4.2	-3.5	-0.9	-0.2	-0.4	-1.2	-2.7	-0.3	-0.2	0.0	-0.6	0.0	-0.3	-0.5	-0.8	-0.4	0.0	0.0	-0.4	0.0	-0.3			
III. Financial indicators /6																								
Broad money (M4), y-o-y growth rate	**10.5**	**6.8**	**6.2**	**2.5**	**4.0**	**6.1**	**6.1**	**6.7**	**5.1**	**4.2**	**4.2**	**5.9**	**6.4**	**7.8**	**7.8**	**7.4**	**6.5**	**6.4**	**6.4**	**6.2**	**5.9**			
Total credits, y-o-y growth rate	**10.0**	**9.5**	**8.4**	**3.5**	**2.5**	**0.9**	**0.9**	**0.6**	**-0.3**	**0.0**	**0.0**	**0.6**	**1.5**	**4.4**	**4.4**	**4.9**	**5.1**	**4.3**	**4.3**	**4.8**	**5.6**			
Total credits - households	11.8	12.9	13.0	8.8	7.3	7.0	7.0	7.1	6.7	6.6	6.6	6.5	6.7	9.5	9.5	9.8	10.0	9.8	9.8	9.3	9.7			
Total credits - enterprises	8.6	7.1	5.1	-0.5	-1.2	-3.8	-3.8	-4.4	-5.9	-5.2	-5.2	-4.2	-2.8	0.0	0.0	0.8	1.0	-0.5	-0.5	0.9	1.9			
Total deposits (incl. demand deposits), y-o-y growth rate	**10.4**	**6.5**	**6.2**	**2.3**	**4.0**	**5.7**	**5.7**	**6.7**	**5.0**	**4.2**	**4.2**	**6.3**	**6.4**	**7.6**	**7.6**	**7.3**	**6.1**	**6.0**	**6.0**	**6.1**	**5.7**			
Total deposits - households	8.9	4.1	3.1	0.2	1.2	2.5	2.5	2.9	2.8	1.8	1.8	3.4	5.5	6.5	6.5	5.4	5.7	5.6	5.6	5.3	5.4			
Total deposits - enterprises	15.7	13.0	16.0	5.6	11.3	13.4	13.4	15.9	9.0	8.8	8.8	12.0	7.9	10.8	10.8	11.4	6.2	5.6	5.6	7.2	5.0			
Interest rates /7																								
Interst rates of CBBills	3.25	3.25	3.25	4.00	4.00	3.75	3.75	3.50	3.25	3.25	3.25	3.25	3.25	3.25	3.25	3.25	3.25	3.25	3.25	3.25	3.25			
Lending rates																								
denar rates (aggregated, incl. denar and denar with f/x clause)	7.5	7.1	6.7	6.6	6.6	6.5	6.6	6.4	6.4	6.3	6.4	6.3	6.3	6.2	6.3	6.2	6.2	6.1	6.2	6.1	6.0			
f/x rates	6.3	5.9	5.6	5.5	5.4	5.2	5.4	5.1	5.1	5.0	5.1	5.0	5.0	5.0	5.0	4.9	4.9	4.8	4.9	4.8	4.8			
Deposit rates																								
denar rates (aggregated, incl. denar and denar with f/x clause)	3.7	2.9	2.5	2.5	2.5	2.5	2.5	2.4	2.3	2.3	2.3	2.2	2.2	2.2	2.2	2.1	2.1	2.1	2.1	2.2	2.2			
f/x rates	1.4	1.3	1.1	1.1	1.0	1.0	1.0	1.0	0.9	0.9	0.9	0.9	0.9	0.8	0.9	0.8	0.8	0.8	0.8	0.8	0.8			
IV. External sector indicators																								
Current account balance (millions of EUR)	**-43.2**	**-177.1**	**-48.2**	**-209.4**	**108.1**	**-115.5**	**-265.0**	**-13.0**	**-58.2**	**-68.9**	**-140.1**	**-42.7**	**-53.0**	**0.2**	**-95.5**	**60.4**	**66.4**	**48.2**	**174.9**					
Current account balance (% of GDP)	-0.5	-2.0	-0.5	-2.2	1.1	-1.2	-2.7	-0.1	-0.6	-0.7	-1.4	-0.4	-0.5	0.0	-0.9	0.6	0.7	0.5	1.7					
Trade balance (millions of EUR) /8	**-1757.9**	**-1713.6**	**-373.2**	**-501.5**	**-391.4**	**-511.3**	**-1777.4**	**-122.1**	**-138.1**	**-174.9**	**-435.1**	**-164.6**	**-182.1**	**-104.2**	**-450.8**	**-134.1**	**-152.6**	**-99.2**	**-385.9**	**-152.6**	**-184.6**			
Trade balance (% og GDP)	-20.5	-18.9	-3.8	-5.1	-4.0	-5.2	-18.0	-1.2	-1.4	-1.7	-4.3	-1.6	-1.8	-1.0	-4.4	-1.3	-1.5	-1.0	-3.8	-1.5	-1.8			
import (millions of EUR)	-5504.5	-5801.1	-1356.6	-1557.7	-1540.0	-1652.4	-6106.7	-450.9	-521.8	-611.0	-1583.8	-565.3	-616.9	-539.6	-1721.8	-550.0	-537.5	-561.3	-1648.9	-622.9	-619.9			
export (millions of EUR)	3746.6	4087.6	983.3	1056.2	1148.6	1141.1	4329.3	328.8	383.7	436.1	1148.6	400.7	434.8	435.4	1270.9	415.8	385.0	462.2	1263.0	470.3	435.3			
rate of growth of import (y-o-y)	10.5	5.4	3.3	4.9	10.2	3.0	5.3	27.3	9.3	16.4	16.7	6.8	16.1	8.5	10.5	6.5	5.5	9.2	7.1	16.7	17.8			
rate of growth of export (y-o-y)	15.8	9.1	5.3	1.4	10.5	6.4	5.9	14.0	10.9	24.9	16.8	8.7	22.3	31.0	20.3	2.9	8.9	18.2	10.0	21.3	23.6			
Foreign Direct Investment (millions of EUR)	**197.4**	**202.8**	**129.3**	**41.4**	**20.1**	**126.1**	**316.9**	**-6.5**	**53.0**	**65.1**	**111.6**	**33.0**	**17.3**	**-61.2**	**-10.8**	**4.7**	**-8.3**	**-46.6**	**-50.2**					
External debt																								
Gross external debt (in milllions of EUR)	5992.3	6290.5	6813.1	6861.2	7488.7	7216.6	7216.6				7786.8				7786.8				7710.2					
public sector	2846.8	2933.7	3279.1	3282.8	3890.9	3445.3	3445.3				3819.9				3741.0				3710.6					
public sector/GDP (in %)	33.2	32.4	33.7	33.8	40.0	35.4	35.4				37.4				36.6				36.3					
private sector	3145.5	3356.9	3534.0	3578.4	3597.8	3771.2	3771.2				3967.0				4045.8				3999.7					
Gross external debt/GDP (in %)	70.0	69.4	70.1	70.6	77.0	74.2	74.2				76.2				76.2				75.5					
Gross official reserves (millions of EUR) /9	**2,436.5**							**2,557.1**	**2,563.0**	**2,534.4**		**2,496.0**	**2,448.5**	**2,399.9**		**2,273.3**	**2,275**	**2,271**		**2301.0**	**2273.6**	**2335.3**		

/1 While calculating the relative indicators, the annual GDP from the official announcement of SSO is used. For 2017, the projected level from the NBRM projections from October 2016 is used.
/2 Preliminary data for 2015. Estimated data for 2016.
/3 The changes of Index of industrial production are according to base year 2010=100.
/4 CPI calculated according to COICOP 2016=100.
/5 Inflation on annual basis corresponds to end-year inflation (December current year/December previous year)
/6 The calculations are based on the New Methodology for compiling standard forms of the monetary balance sheets and surveys and the new accounting plan (in force since 01.01.2009).
/7 As of January 2015 data for active and passive interest rates are compiled according to the new methodology of NBRM.
/8 Trade balance according to foreign trade statistics (on c.i.f. base).
/ 9The data from 2008 include accrued interest. The latest available data on gross official reserves are preliminary data.



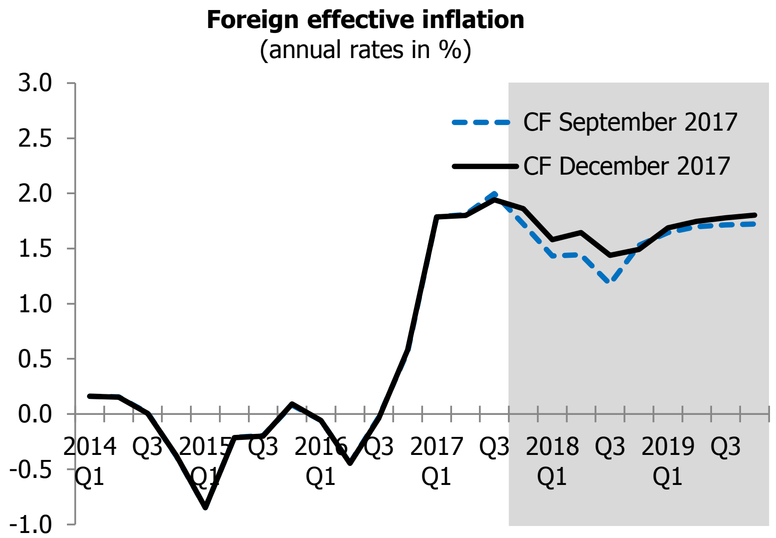
Source: "Consensus Forecast" and NBRM calculations.

The expectations for the foreign effective demand in 2017 and 2018 were revised upwards compared to the October forecasts...

...whereby a growth of 2.4% and 2.3%, respectively is expected in 2017 and 2018. The expected growth of foreign demand is higher by 0.2 percentage points compared to October...

...largely as a result of the expectations for a stronger economic growth in Germany.

In 2019, the October estimations for growth in foreign effective demand of 1.8% were retained.



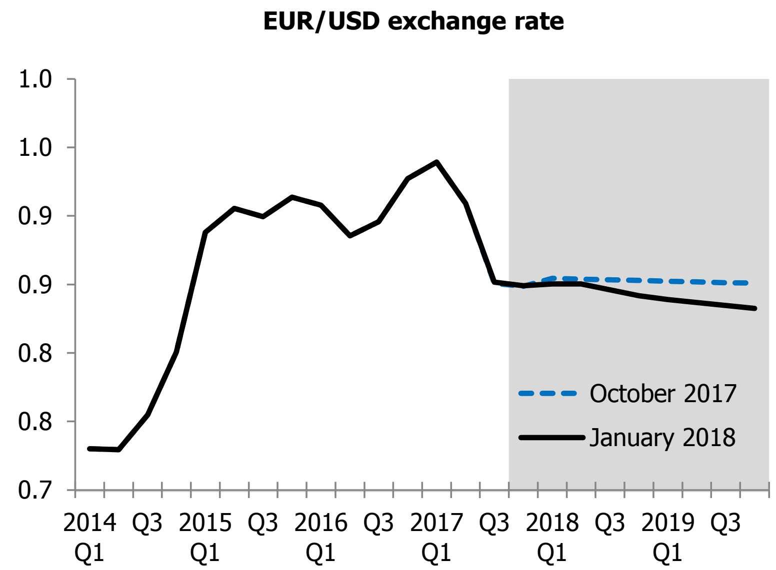
Source: "Consensus Forecast" and NBRM calculations.

Regarding foreign effective inflation, the estimations for the entire forecast period were revised upwards compared to the October forecast round...

...largely due to estimations for higher imported inflation from Serbia[3]...

...therefore the foreign effective inflation is expected to amount 1.9% in 2017, and afterwards decelerate to 1.6% and 1.8% in 2018 and 2019, respectively.

[3] Inflation in Serbia has been adjusted for the changes in the exchange rate.



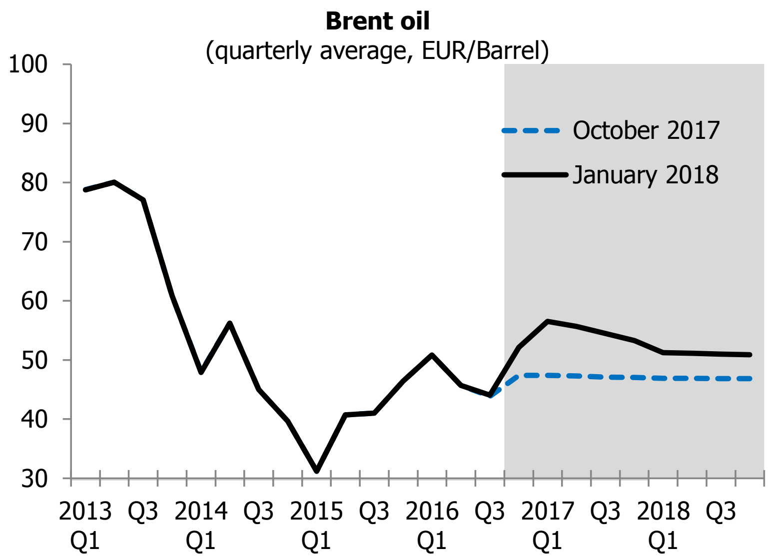
Source: "Consensus Forecast" and NBRM calculations.

Performances for euro/US dollar exchange rate for 2017 are in line with the October forecasts...

...i.e. the US dollar value decreased by 1.9% against the euro.

On the other hand, a higher depreciation of the US dollar against the euro is expected for 2018 and 2019 compared to the October forecasts...

...which is mostly due to the more favorable economic performances and forecasts for the euro area, amid gradual decrease of the volume of ECB's quantitative easing after December 2017.



Source: IMF, World Bank and NBRM calculations.

The latest oil price estimations[4] for 2017 and 2018 were revised upwards compared to the October forecasts...

...whereby a higher price increase is now expected, especially in 2018...

...mostly due to the agreement of the OPEC states and Russia to continue the agreement for the reduction of oil production[5] and interruption of supplying capacities[6].

On the other hand, a downward revision was made for 2019...

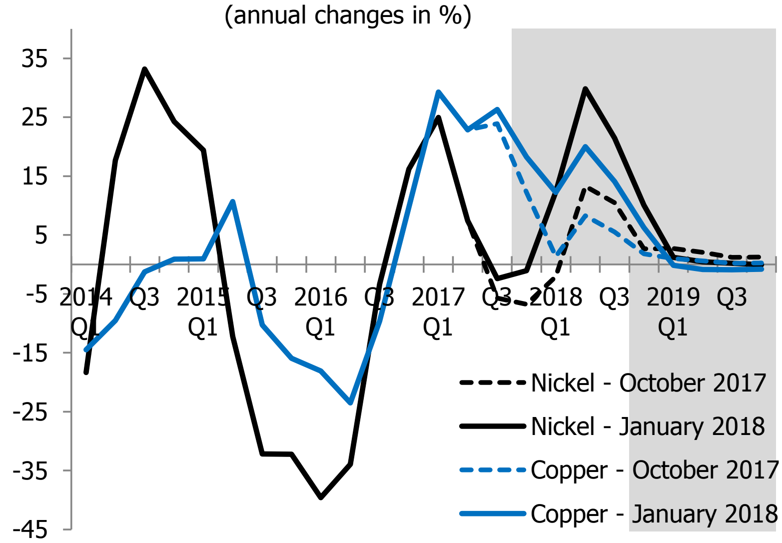
...expecting a greater oil price reduction than the one forecasted in October.

[4] For the analysis of prices of oil, metals and primary food products, various reports of the IMF, World Bank, FAO, OPEC, the ECB and the specialized international economic portals are used.

[5] On 30 November 2017, the OPEC Member States and Russia made a decision to extend the measure for reduction of oil production for nine additional months i.e. until the end of 2018, which aims to reduce the inventories of this fuel globally. Also, other oil producing countries that are not OPEC Member States, including Russia supported the extension of the agreement, decreasing oil production by 1.8 million barrels per day until December 2018. Additionally, Nigeria and Libya also joined in the measure, countries that previously were not part of the agreement.

[6] In the first half of December, due to the effect, a key oil pipeline in the North Sea was closed. It is expected that the reparation will last around three weeks, which will contribute to disrupt the supply of about 10 million barrels of oil for that period.

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



Source: IMF, World Bank and NBRM calculations.

In 2017 and 2018, metal prices were revised upwards...

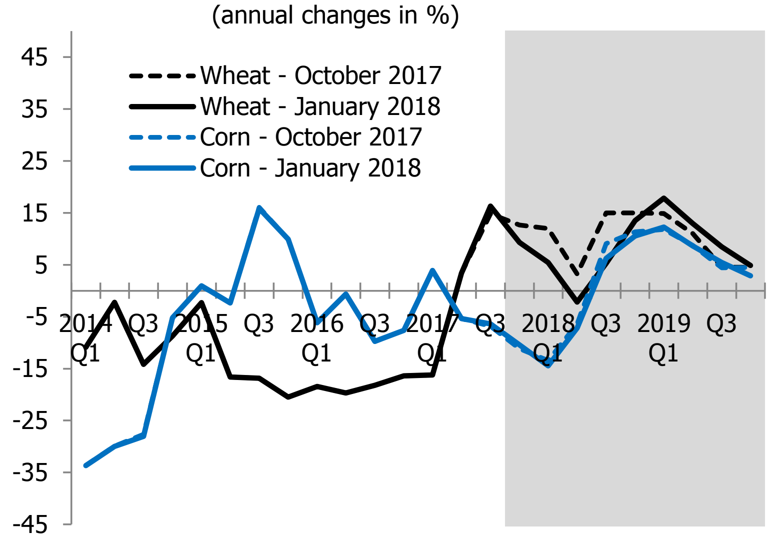
...expecting a higher growth of the nickel and copper prices, especially in 2018, compared to the October forecasts...

...which is mostly due to the expectations for increased demand of these metals by the automobile industry, as well as possible interruption in the supplying capacities.

On the other hand, metal price forecasts were slightly revised downwards for 2019...

...expecting smaller growth in the nickel price and minor decline of the copper price, instead of the previously expected minimum growth.

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



Source: IMF, World Bank and NBRM calculations.

Expectations for stock exchange prices of wheat[7] for 2017 and 2018 were revised downwards...

...amid expected lower growth of wheat prices, mostly due to the expectations for increased production level of wheat in the EU countries, as well as expectations for increased level of world inventories.

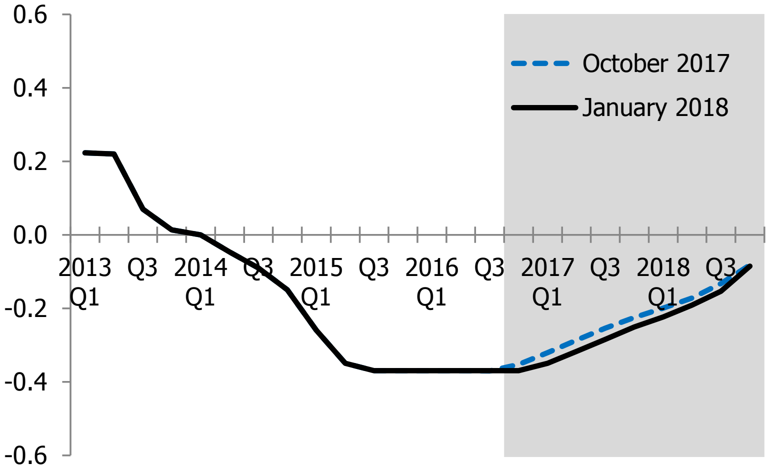
On the other hand, corn prices were revised in different directions.

...whereby a lower decline is now expected in 2017, amid increased demand of corn in USA and higher decline in 2017 as a result to the expectations for increased level of world inventories.

The wheat price is revised upwards for 2019 and its higher growth compared to October is now expected, whereas the expected growth of corn price remains unchanged.

[7] The October 2017 forecasts started to use a new series of data on wheat prices released by the World Bank, instead of the current IMF series. Due to the differences between the two series, in order to ensure consistency, series of data released by World Bank is used amid comparing both forecasts.

1-month Euribor
(quarterly average, in %)



Source: NBRM calculations.

The one-month EURIBOR rate for 2017 is the same with the October forecast...

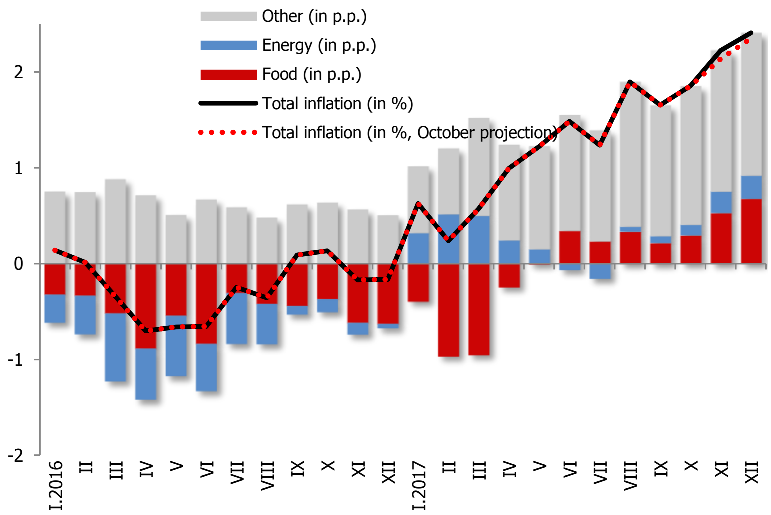
...whereby the interest rate averages -0.37%.

Foreign interest rate was slightly revised downwards to -0.30% and -0.16%, for 2018 and 2019 respectively, compared to the forecasted rates of -0.27 and -0.15% in October.

...amid continuing the ECB's quantitative easing program after December 2017, although at a reduced volume, and efforts to maintain the current stimulative interest rate policy for a longer period after the completion of the purchase of assets[8].

[8] At the ECB's regular meeting in December, the European Central Bank, decided to maintain the current interest rate, amid continuing the ECB's quantitative easing program until September 2018 with a reduced volume (Euro 30 billion monthly).

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

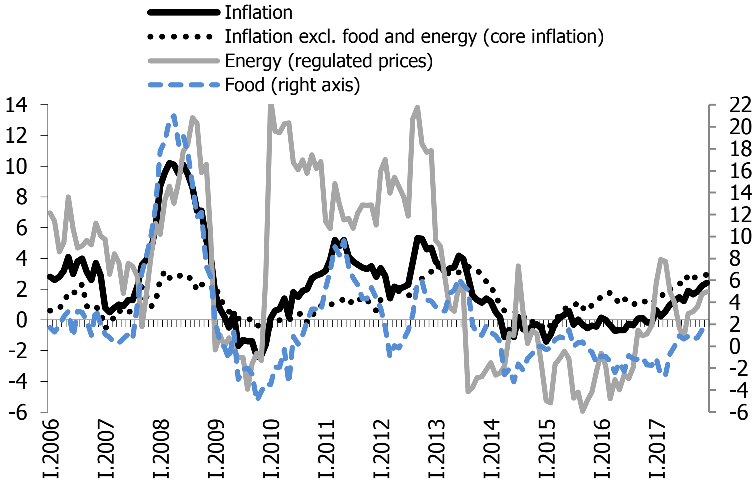


Source: SSO and NBRM.

In December 2017, domestic consumer prices registered a monthly increase of 0.1%[9] (monthly increase of 0.2% in November)...

...amid growth of energy prices and core inflation and simultaneously unchanged food prices.

Inflation and volatility of food and energy
(annual growth rates, in %)



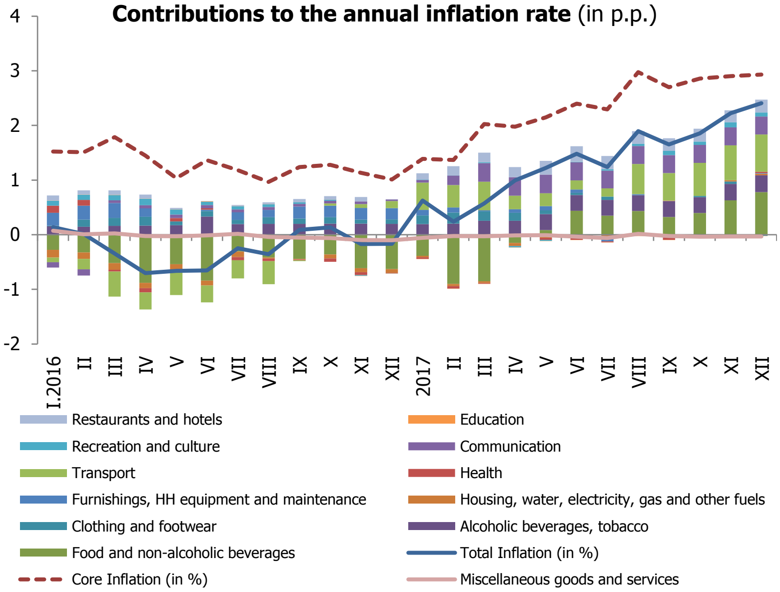
Source: State statistical office and NBRM calculations.

In December, the annual inflation rate amounts to 2.4% (compared to 2.2% in November) and compared to the October forecast round, the performance in December is in line with the expectations.

Observed by individual price categories, core inflation is in line with the expectation, the upward deviation is present in energy prices, while in food the deviation is downward.

Analyzed cumulatively, for the entire 2017, the inflation rate of 1.3% is generally in line with the forecasted in the October round of forecasts.

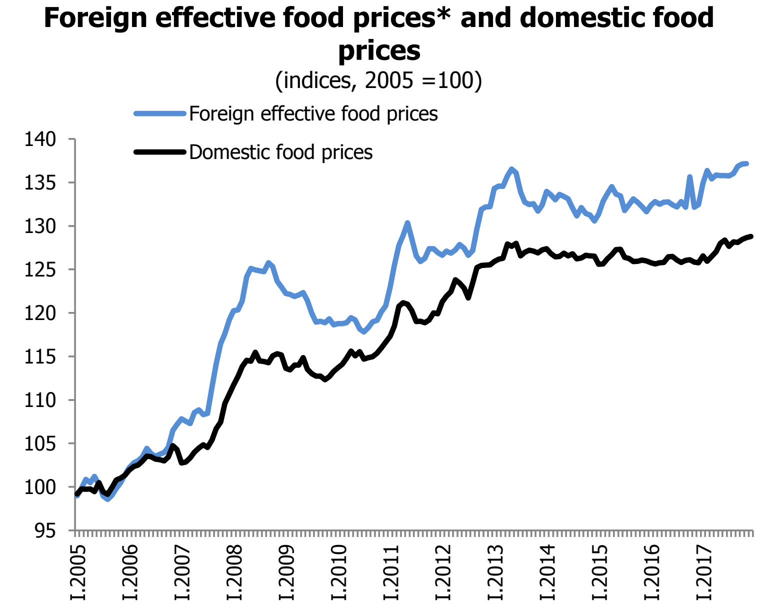
[9] Observed by group products, hospital services and liquid fuels have the highest positive contribution to the monthly growth.



Source: SSO and NBRM.

Core inflation rate in December amounted to 0.1% on a monthly basis, whereas on an annual basis the increase amounted to 2.9% (same as in November).

Core inflation structure in December is similar to the previous month. The annual growth is related to the price growth in most categories within the core inflation, from which prices of transport services i.e. air transport, communications and tobacco[10] and hotel and restaurant prices have the highest positive contribution.



* 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.

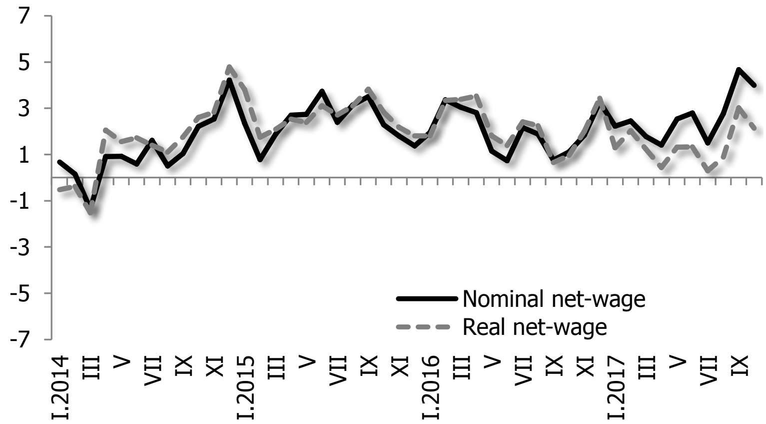
Regarding the expected price movements of external input assumptions, the inflation forecast has been revised in different directions.

The latest oil prices estimations for 2018 indicate a higher growth compared to the expectations of the October round of forecasts. On the other hand, expectations in grain prices are somewhat more favorable i.e. it is expected that wheat prices will grow slowly, while corn prices are expected to register a greater decline compared to the expected in October.

Amid performances generally in line with the forecast and external assumptions revised in divergent directions, it is assessed that the risks to inflation forecast for 2018 are currently balanced. The uncertainty around the forecasted movement of primary commodity world prices, especially oil prices, remains.

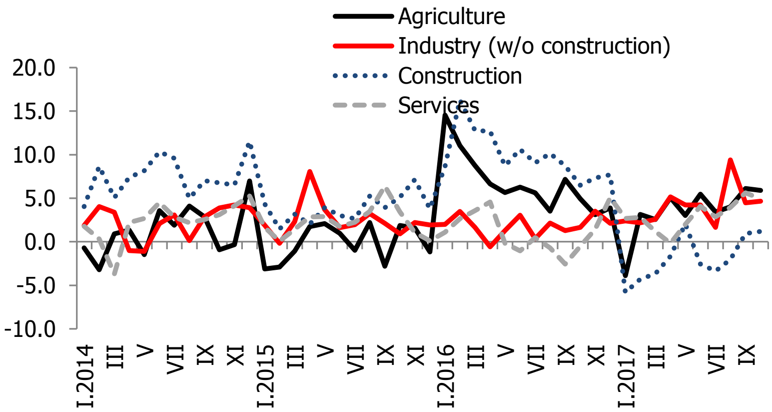
[10] The annual growth of tobacco prices in December is a combination of the increase in the price of a certain type of cigarettes in April and June 2017. In July 2017, the cigarette excise increased (from 1 July 2017 to 1 July 2023 the excise duty will increase by 0.20 denars/piece each year) which did not reflect on the monthly changes in tobacco prices.

Average net-wage
(annual changes, in %)



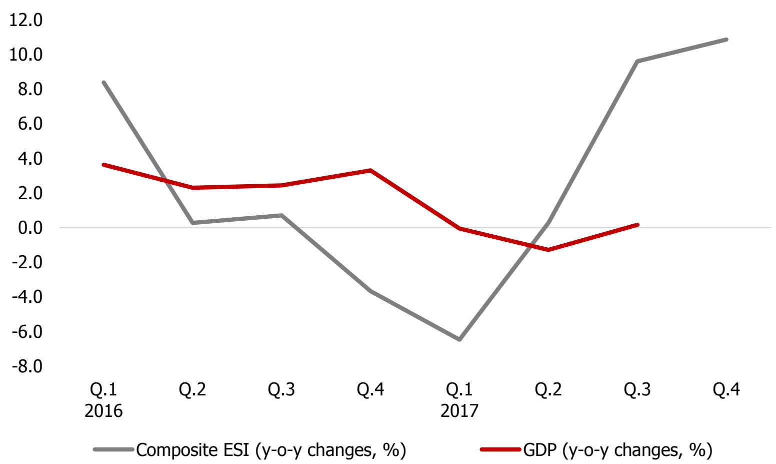
Source: SSO.

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



Source: SSO.

Economic sentiment indicator and GDP



Source: State statistical office and European

In October 2017, the average net wage registered a nominal annual growth of 4.0%, which is a slight growth acceleration of 0.7 percentage points, compared to the last month's growth. Wage growth in October is registered in all sectors, mostly expressed in the "art, entertainment, recreation", mining and manufacturing industry.

Amid a moderate increase in the costs of living in October, **the real wages increased by 2.1%.**

October movements in wages are higher than expected for the fourth quarter within the October forecast.

The available high-frequency data for the shifts on the supply and demand side point to a growth in the economy in the last quarter of the year. Results obtained from the surveys that monitor economic agents' perceptions for the situation in the economy[11] are more favorable and show additional strengthening of the economic agents' confidence in the fourth quarter.

The industrial output in the period October-December registers an annual growth, amid growth of the output in the manufacturing industry and energy sector, whereas the production in mining was reduced.

Observed by individual activities within the manufacturing industry, annual

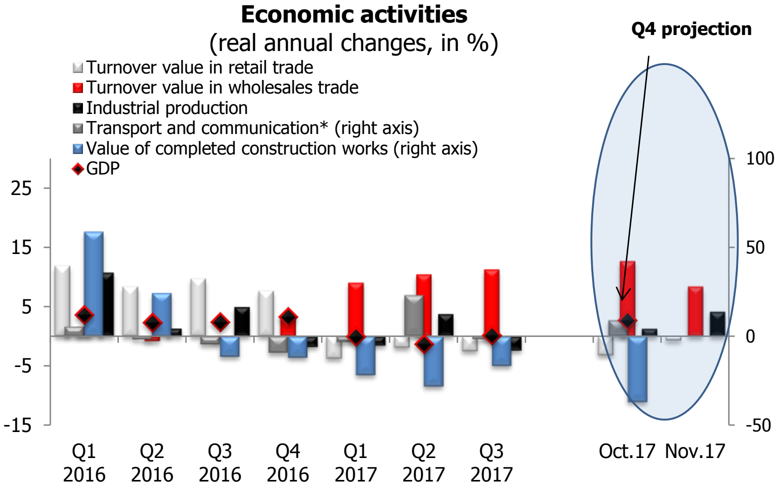
[11] It refers to the surveys conducted by the European Commission to measure the economic confidence of entities in an economy. The composite indicator of economic confidence is obtained as a weighted average from the confidence indicators for consumers and confidence indicators for individual economic sectors (construction, industry, retail trade and services).

growth of production is registered in most activities, with the largest contribution of activities where the largest export oriented facilities produce (machinery and devices, electronic equipment). On the other hand, production in most traditional activities registers a decline, with the highest negative contribution from metal production, clothes and beverages.

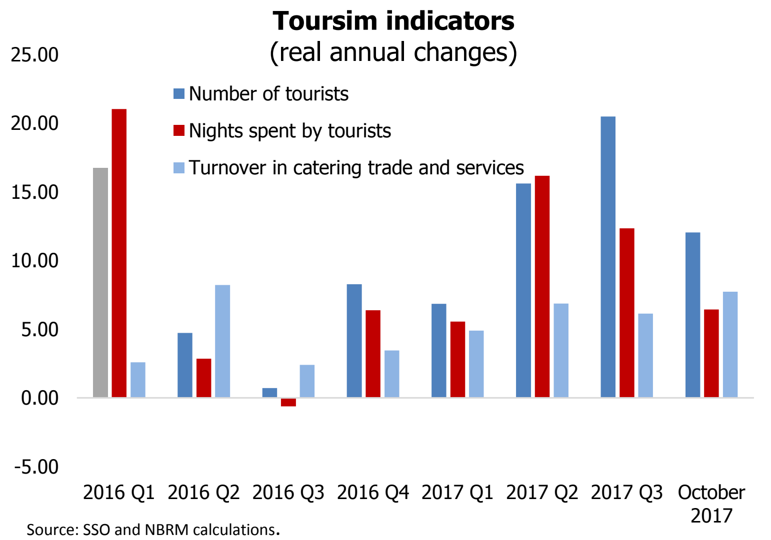
In October, **rail traffic registered an increase**, and favorable movements were also registered in **total trade**, which in continues to grow in October-November. The growth is mainly a reflection of the wholesale trade, while retail trade, on average, registers an annual decrease in the first two months of the quarter.

The increased number of tourists, overnight stays and turnover in the **catering services** in October indicates continuation of the favorable movements in this sector during the fourth quarter.

On the other hand, data on the performances in the construction sector for the first month of the quarter point to its unfavorable effect on the economic situation. At the beginning of the fourth quarter, **construction** registers a decline due to the decline in civil engineering and high-rise buildings.



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

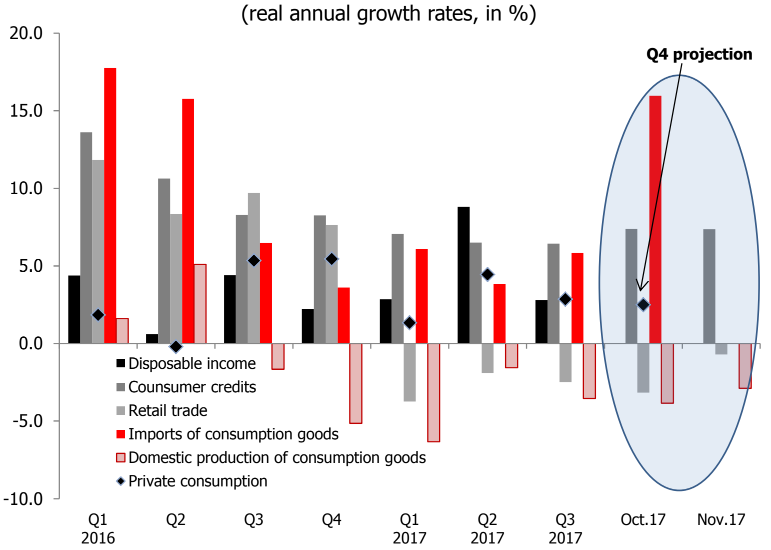


Source: SSO and NBRM calculations.

High frequency data on the **aggregate demand** side in October and November also indicate more favorable movements in the fourth quarter.

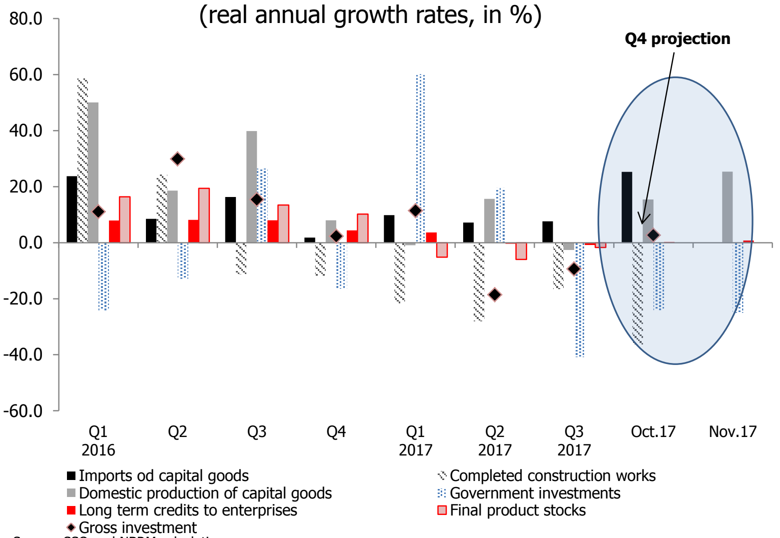
Indicators of shifts in **private**

Indicative variables for private consumption
(real annual growth rates, in %)



Source: SSO and NBRM calculations.

Indicative variables for investments
(real annual growth rates, in %)



Source: SSO and NBRM calculations.

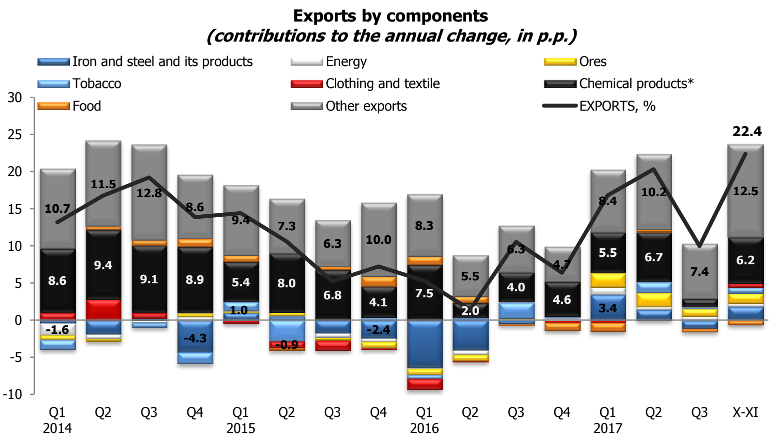
consumption are mainly favorable, in conditions of annual growth in household lending, favorable shifts in part of the disposable income components (average wage, pensions and private transfers) and higher export of consumer goods. On the other hand, cumulatively, in the first two months of the quarter, the turnover value in retail trade declined, while domestic production of consumer goods also registered a decline.

In the **investment consumption** domain, the available short-term indicators in the fourth quarter point to movements in different directions. Thus, a significant annual growth of the domestic production of capital goods (after the decline in the previous quarter) is registered), minor growth of long-term lending to the corporate sector[12] (after two quarters of decline), as well as the positive signs of the intensified growth of the export of investment products in October. On the other hand, an annual decline of the construction activity and government capital investments was registered during the quarter.

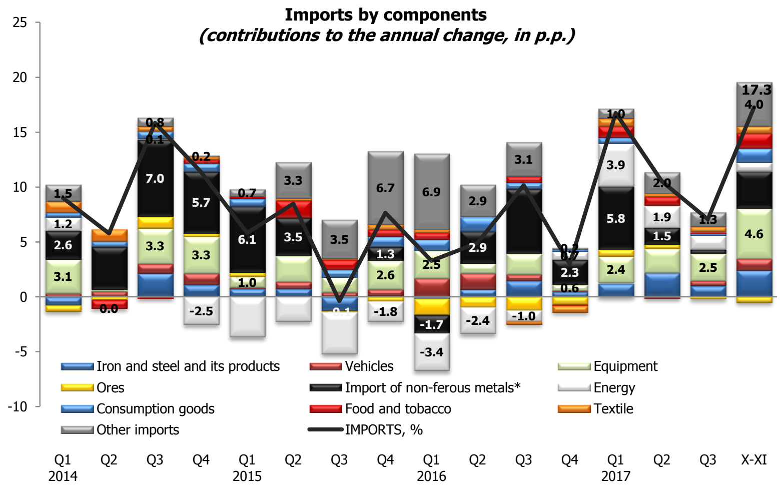
The data on **foreign trade** show widening of the trade deficit in the first two months of the last quarter of 2017, amid a simultaneous nominal growth of both export and import of goods.

In accordance to the fiscal budget data for October and November, **public consumption** registers a decline, mainly due to the lower expenditures of goods and services.

[12] It refers to the average performance for October and November.



Source: NBRM.



Source: NBRM.

In the period October-November 2017, the foreign trade deficit registered a moderate widening (of 5.4%) on an annual basis which is due to the higher growth of total export compared to the growth of the import component.

Export of goods in October and November is higher by 22.4% compared to the same period in the previous year, which is mostly due to the favorable performances in the new export oriented facilities, and almost all other export segments (except export of food where a moderate decline is registered) had a positive contribution to the growth.

Compared to the October forecast, **the export in October and November was higher than expected for the last quarter.** Thus, upward deviations were registered in several components, amid more significant individual contribution of export in part of new export oriented facilities in the economy. On the other hand, export of food and ores is weaker compared to the expected according to the October forecast.

Import of goods in the period October-November 2017 is higher by 17.3% on an annual basis. The growth of import is relatively dispersed. Decrease was registered in the import of ores only, which is associated with the non-function of a larger capacity of the metal processing industry.

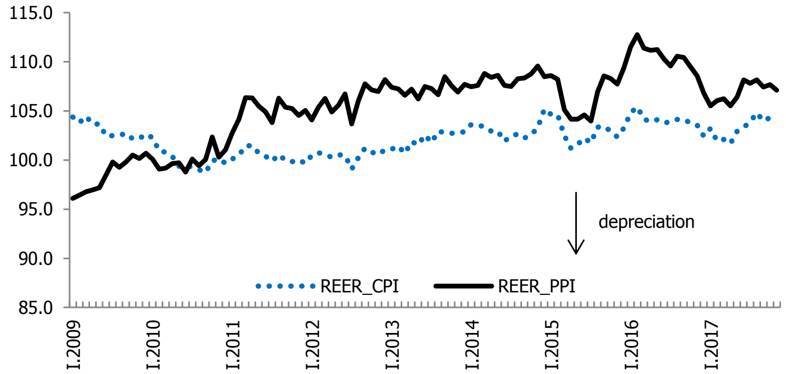
The import of goods in October and November 2017 is higher compared to the forecased for the fourth quarter, in accordance with the October forecast, as a result of the upward deviations in most import segments, amid more expressed individual contribution of a more significant industrial capacity.

Import of energy and ores is an exception where a moderate downward deviation is registered.

The performances of the foreign trade components indicate a trade deficit that is slightly lower than expected for the last quarter of 2017, according to the October forecast.

REER

(2010=100)

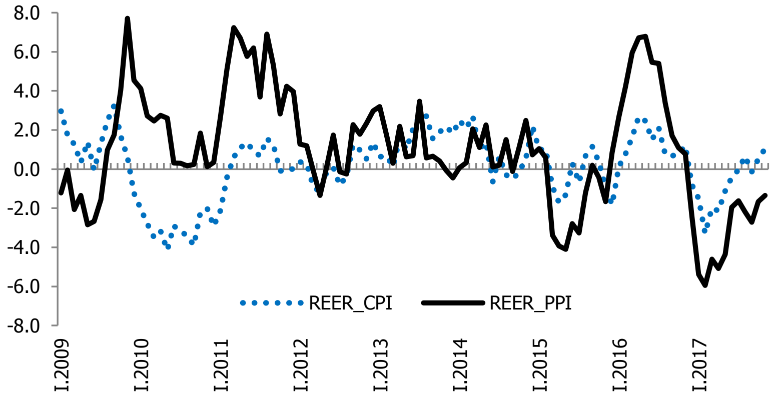


Source: NBRM.

In November 2017, **price competitiveness indicators of the domestic economy registered divergent movements. Namely,** the REER index deflated by consumer prices registered an appreciation of 1.1%, while the REER index deflated by producer prices depreciated by 1.3%.

REER

annual changes, in %

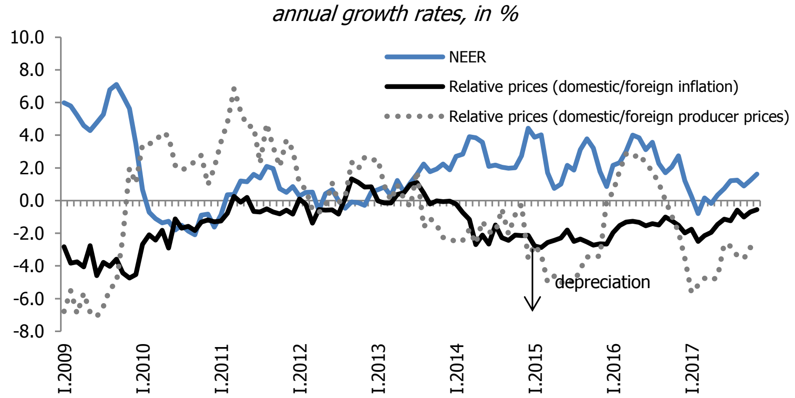


Source: NBRM.

These developments are due to favorable changes in relative prices, whereby relative prices of industrial products decreased by 2.9%, while the relative cost of living registered a moderate decrease of 0.6%. The NEER acted in the opposite direction, recording a moderate appreciation of 1.6% on an annual basis, mostly as a result of the depreciation of the Turkish lira.

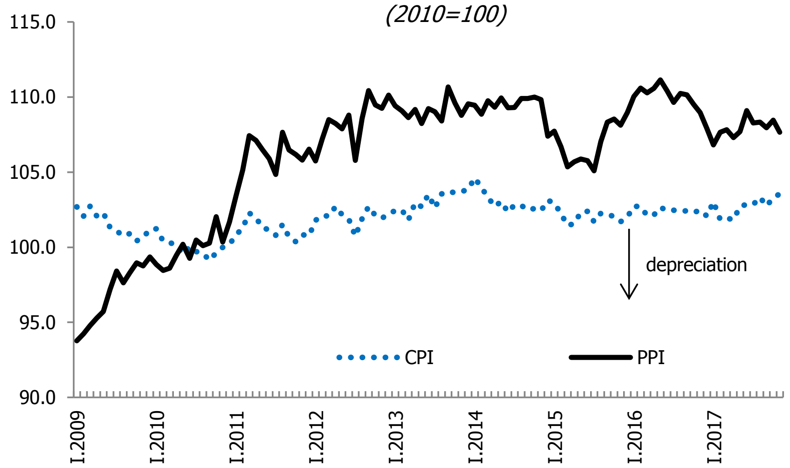
NEER and relative prices

annual growth rates, in %



Source: NBRM.

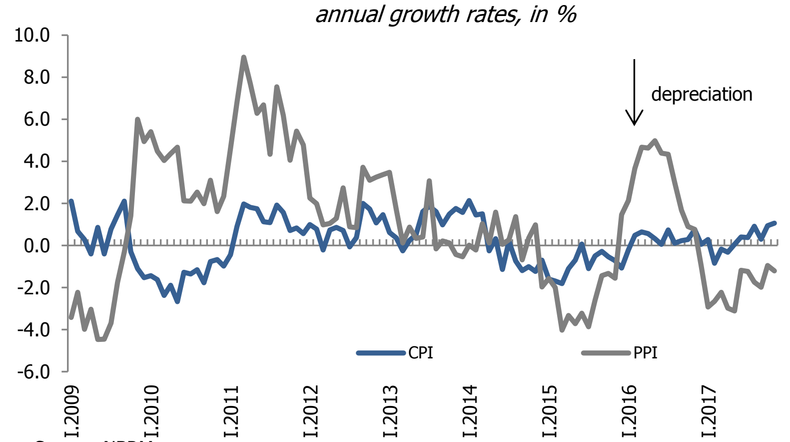
REER, excluding primary commodities
(2010=100)



Source: NBRM.

In November 2017, the analysis of REER indices, as measured using weights based on the foreign trade without primary commodities[13], also shows similar movements. Namely, the REER deflated by consumer prices registered an appreciation of 1.1%, while the REER deflated by producer prices depreciated by 1.2%.

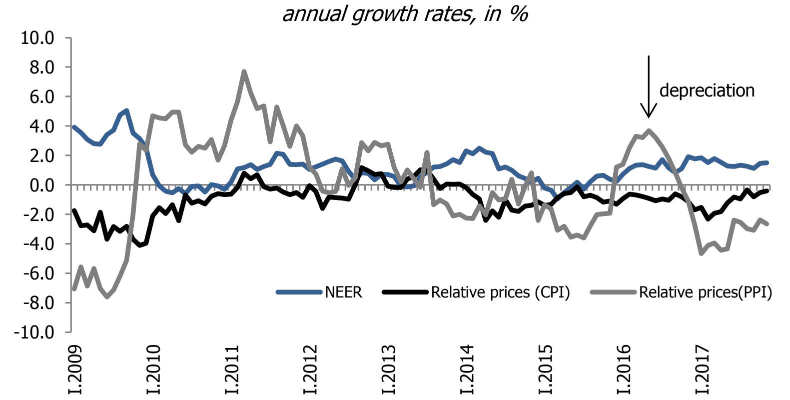
REER, excluding primary commodities
annual growth rates, in %



Source: NBRM.

On an annual basis, the relative consumer prices and the relative producer prices decreased by 0.4% and 2.6%, respectively. The NEER has appreciated by 1.5% on an annual basis.

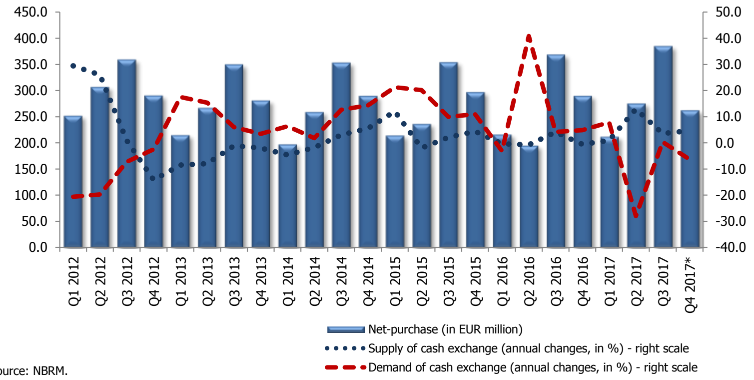
NEER and relative prices, excluding primary commodities
annual growth rates, in %



Source: NBRM.

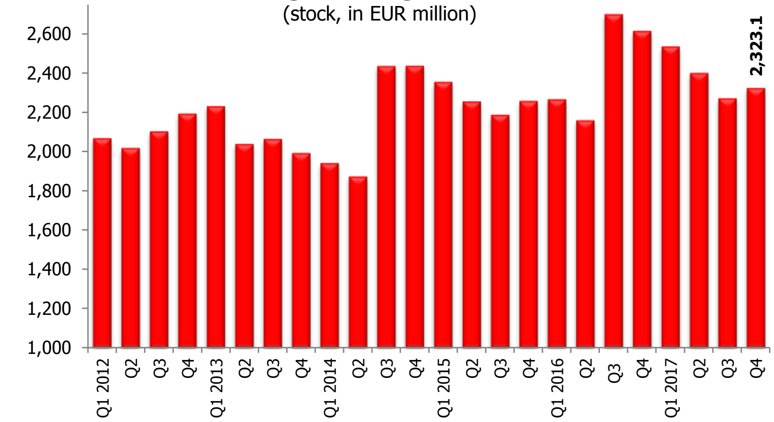
[13] Primary commodities not included in the calculation are: oil and oil derivatives, iron and steel, ores and imported raw materials for the new industrial facilities in the free economic zones.

Cash exchange market



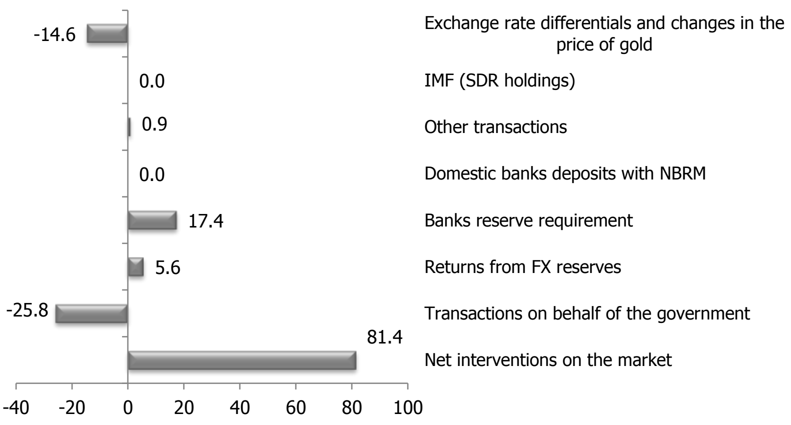
Source: NBRM.

Foreign exchange reserves
(stock, in EUR million)



Source: NBRM.

Factors of change of the foreign reserves in the fourth quarter of 2017 (in EUR million)

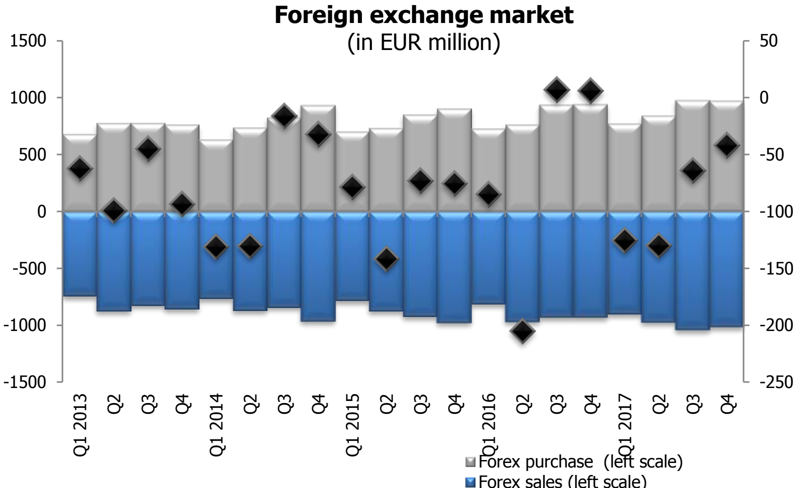


Source: NBRM.

Recent data on currency exchange operations as of 31 December 2017 indicate annual increase of the supply and decline of demand for foreign currency.

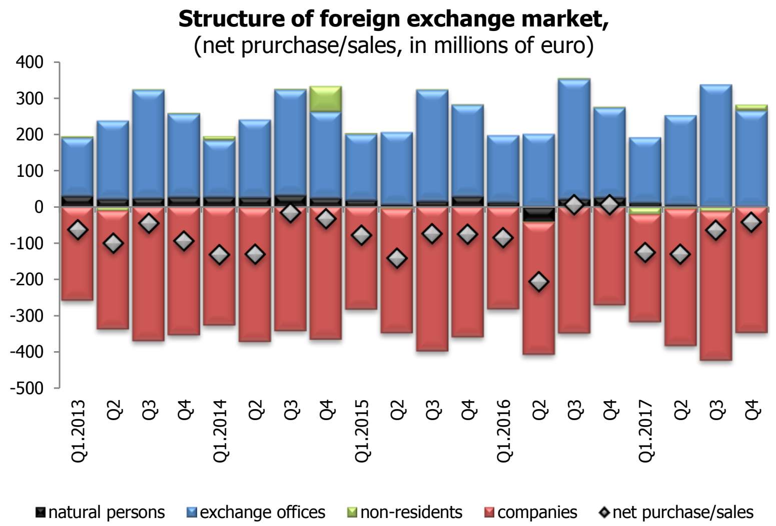
The net purchase on the currency exchange market in the fourth quarter amounted to Euro 312 million, which is an annual increase of 7.8%.

As of 31 December 2017, the gross foreign reserves stood at Euro 2,336 million, which is an increase of Euro 64.8 million compared to the end of the third quarter of 2017. The growth of foreign reserves are mostly due to NBRM's interventions on the currency market. On the other hand, transactions for the account of the government were reducing.



Source: NBRM.

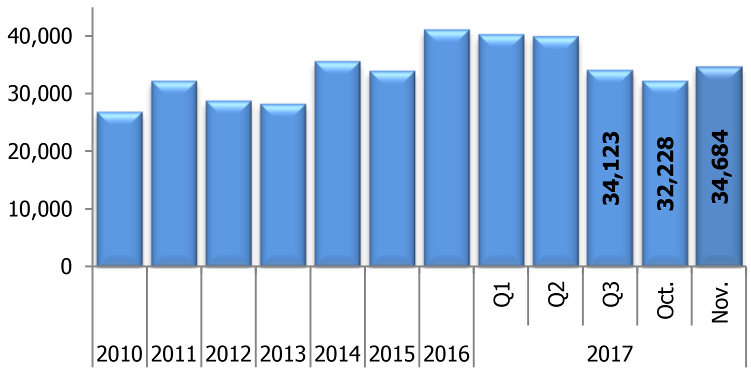
In the third quarter of 2017, the foreign exchange market of banks reported a net sale of foreign currency of Euro 41.5 million, contrary to the small net purchase registered in the same period last year. This annual change is a result of the faster growth in the demand for relative to the supply of foreign currency.



Source: NBRM

Sector-by-sector analysis shows that such changes are mostly due to the reduced net sales of companies.

Monetary policy instruments
(in MKD million)



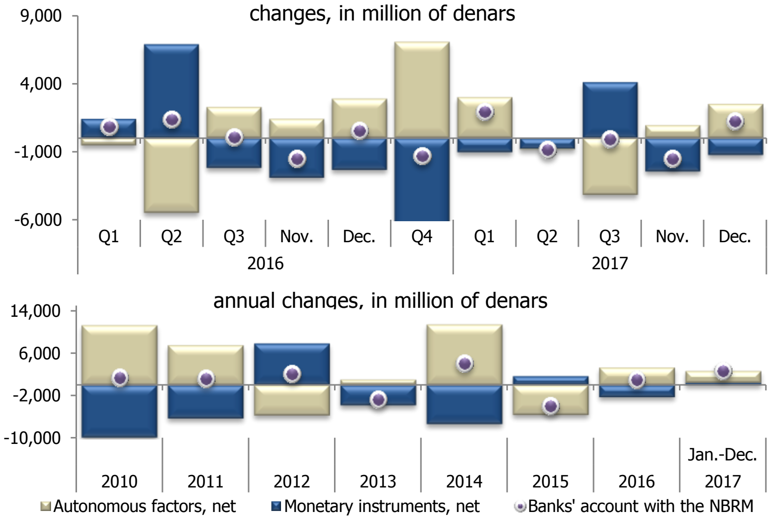
Source: NBRM.

The situation regarding monetary instruments increased in November compared to the previous month. Compared to the end of the third quarter, the situation regarding monetary instruments is moderately higher compared to the expectations for its decrease, and thus creating liquidity in the banking system, in the last quarter of 2017, in accordance with the October forecast.

NBRM's net foreign assets decreased in November. Government deposits also recorded a decrease in November. The situation of these balance sheet categories in November are higher compared to the end of the third quarter, compared to the expectations for their decline in the fourth quarter of the year, in accordance with the October forecast.

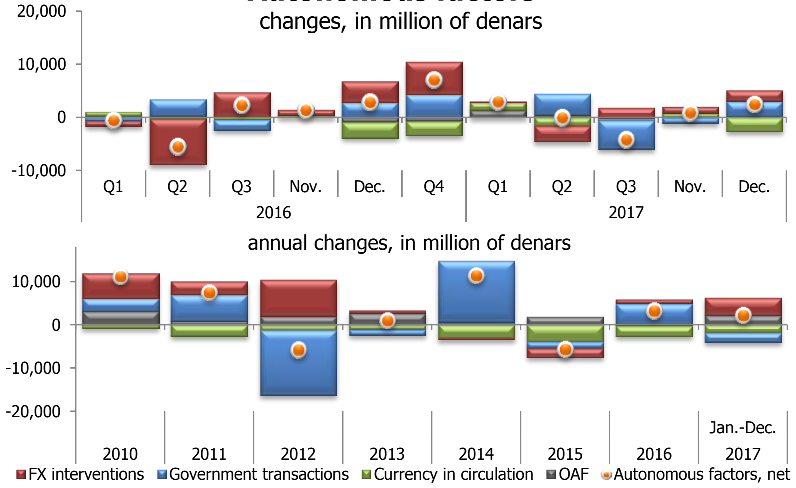
Reserve money in November registered a decline on a monthly basis. Compared to the end of the third quarter, reserve money are lower compared to the expectations for growth in the fourth quarter of the year, in accordance with the October forecasts.

Banks liquidity*



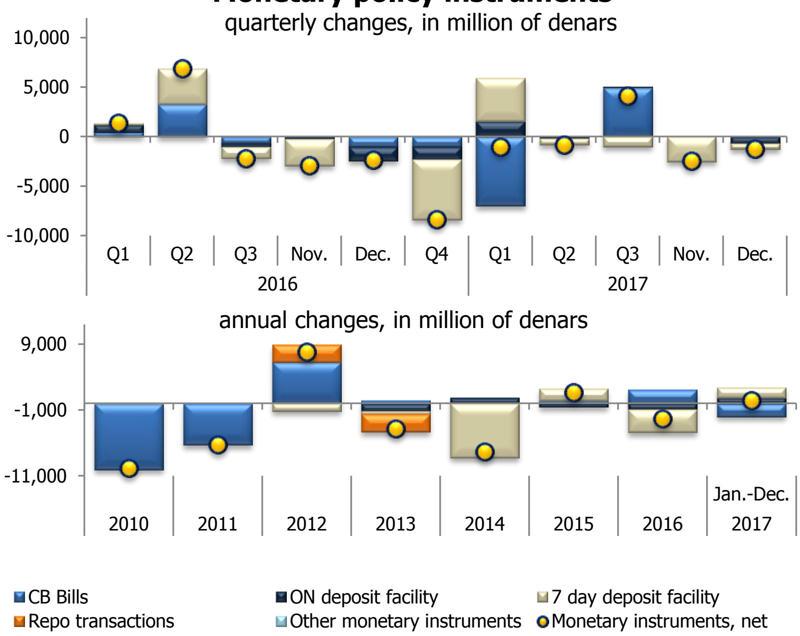
Source: NBRM. *
positive change: liquidity creation, negative change: liquidity withdrawal

Autonomous factors*



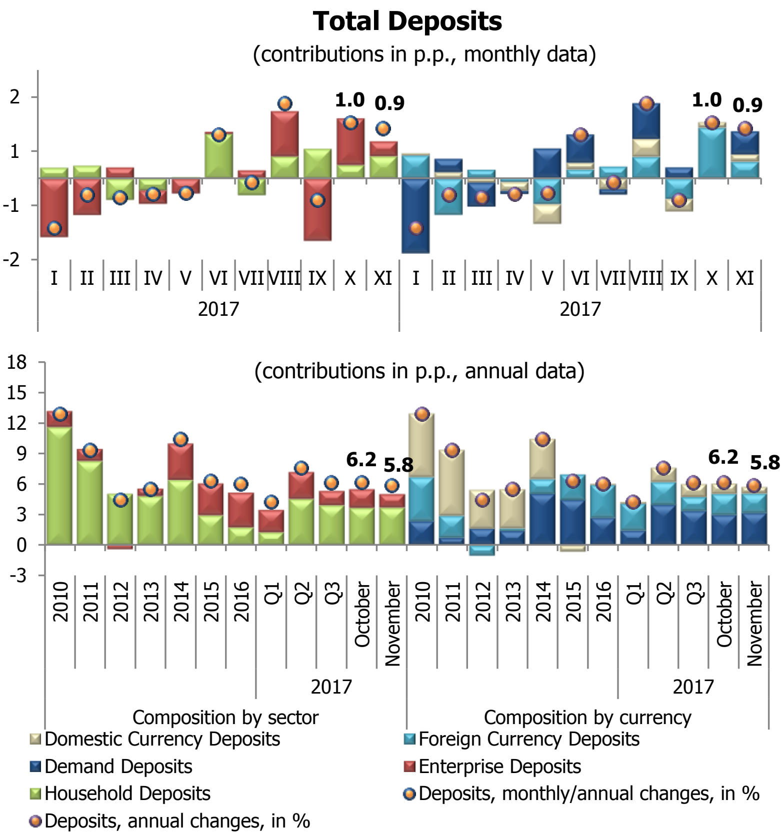
Source: NBRM .
* positive change: liquidity creation, negative change: liquidity withdrawal

Monetary policy instruments*



Source: NBRM .
* positive change: liquidity creation, negative change: liquidity withdrawal

According to operational liquidity data, in December, the liquidity of the banking system increased. The liquidity increase was dominantly influenced by autonomous factors (NBRM's currency interventions i.e. net purchase of foreign currency from the currency market and government transactions), whereas currency in circulation acted toward the decline of the liquidity of the banking system. Amid the growth of liquidity under the influence of autonomous factors and unchanged supply of CB bills, banks placed the excess liquidity assets in deposits with the NBRM.

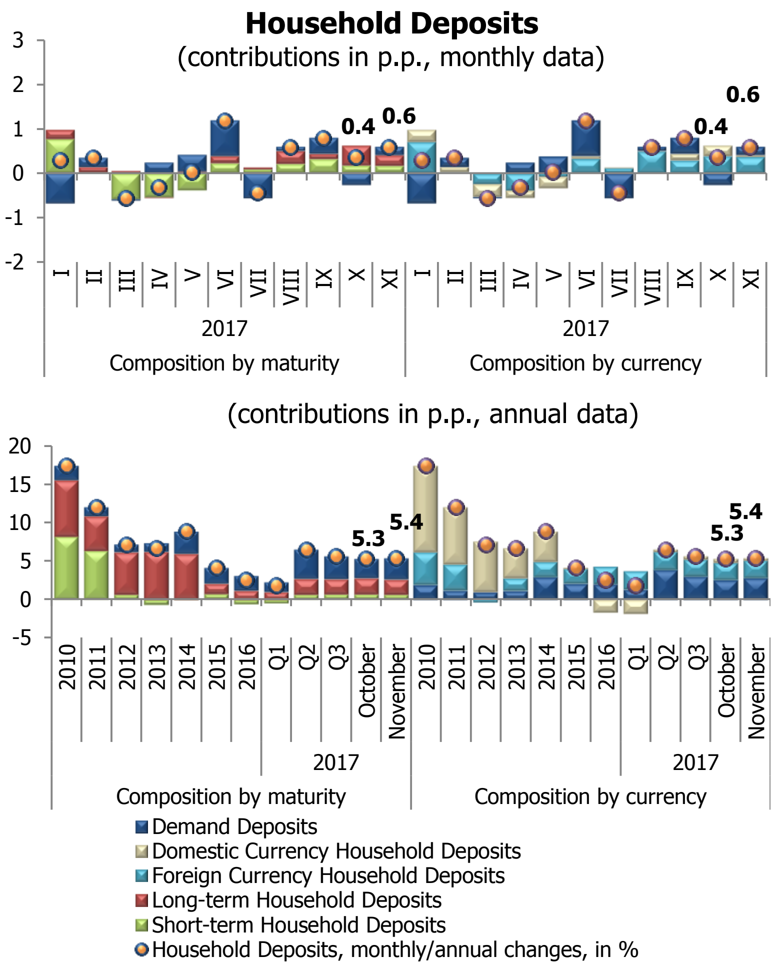


Source: NBRM.

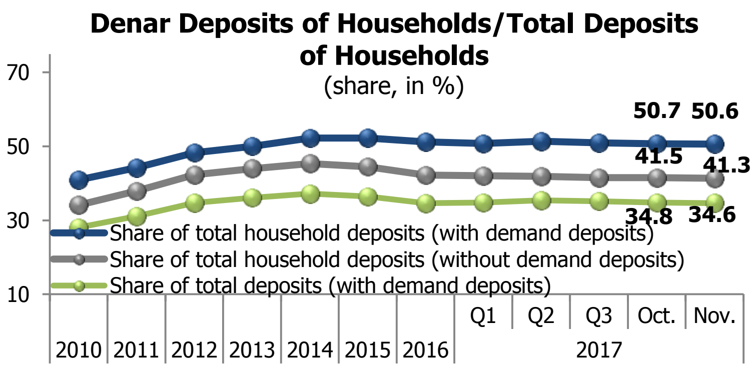
In November 2017, total deposits in the banking sector continued to increase on a monthly basis, at a similar pace as in the previous month. Analyzing by sector, the monthly increase (of 0.9%) in November is primarily due to the growth of household deposits amid moderate growth of corporate deposits. In terms of currency structure, the growth of deposits in November is dominantly driven by domestic currency deposits and foreign currency deposits also had a positive contribution on the monthly growth of total deposits.

The total deposits' increase in October and November is in line with the October forecast.

In November, the annual growth rate of total deposits was 5.8% (6.2% in October), which is above the forecasted growth for the fourth quarter of 2017 (of 3.6%) in the October forecast. On an annual basis, the growth of total deposits in November it terms of currency is mostly due to the growth of demand deposits and foreign currency deposits, amid moderate increase of denar deposits. Analyzed by sectors, the annual deposits growth is mostly due to the growth of household deposits, amid annual growth of corporate deposits.

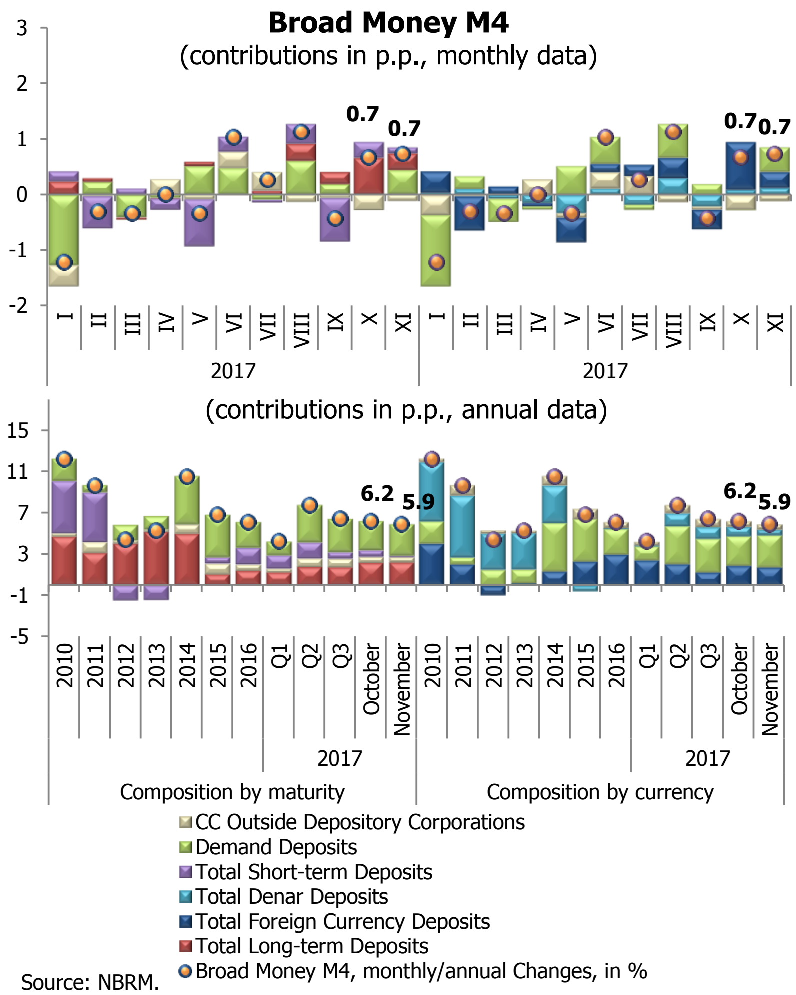


Source: NBRM.



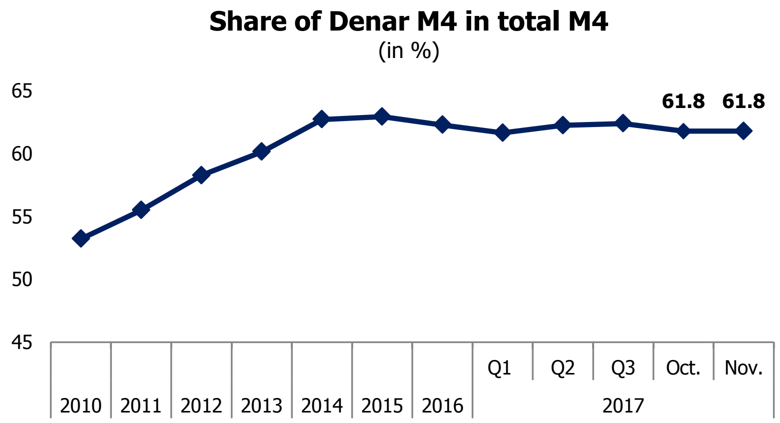
Source: NBRM.

The increase of household deposits moderately accelerated in November. The acceleration of the monthly growth pace of household deposits (from 0.4% to 0.6%) was primarily due to the increase of demand deposits, which in November had a negative contribution to the growth. In terms of currency, the monthly growth is still under a dominant influence of foreign currency deposits. Analyzing the maturity structure, the monthly growth of household deposits is primarily driven from the growth of long-term deposits, amid moderate growth of short-term deposits. With the performances in November, the share of denar deposits (with demand deposits) in total household deposits remained at a relatively stable level amounting to 50.6% in November (50.7% in October).

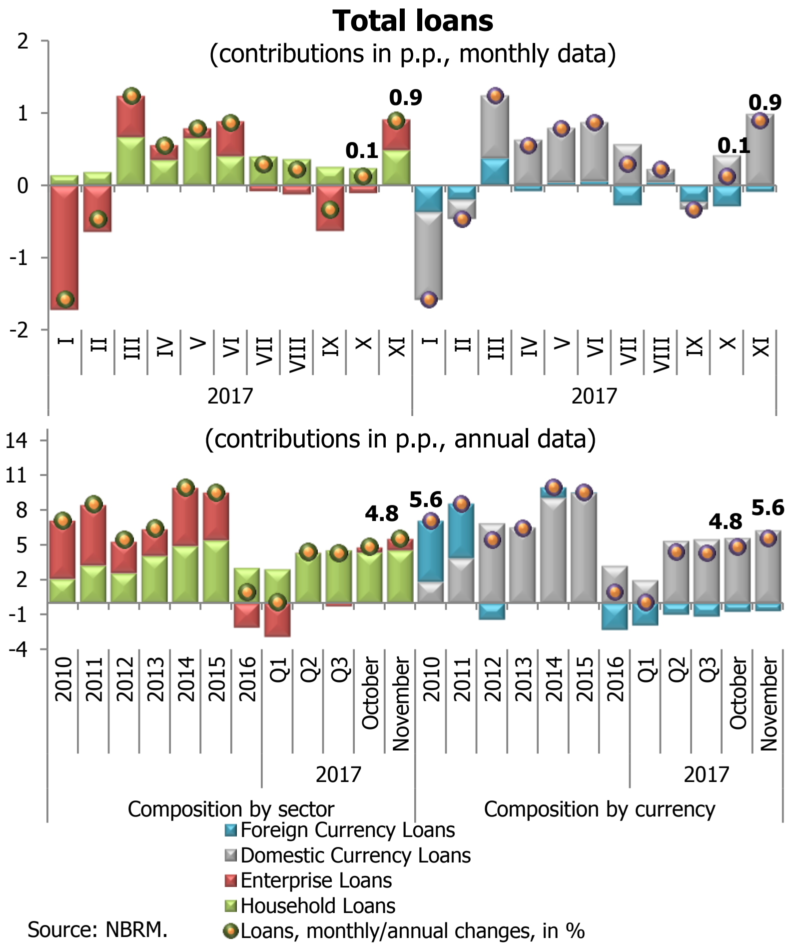


Source: NBRM.

In November, broad money M4 continued to increase on a monthly basis, at an almost similar pace as in the previous month. The monthly growth of the broadest money supply (of 0.7%) is entirely due to the increase in the total deposits, whereas currency in circulation had a negative contribution. **On annual basis, the broad money is higher by 5.9% (6.2% in October), which is above the forecasted growth of 4.1% for the fourth quarter of 2017.** With the performances in November, the share of the denar share in the total money supply remained at a stable level of 61.8%.



Source: NBRM.

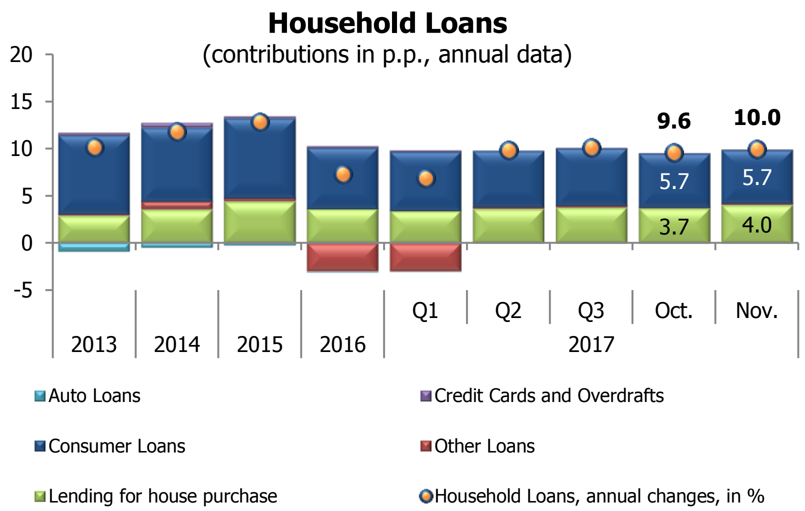


Source: NBRM.

In November, total loans to the private sector registered a significant increase acceleration compared to the previous month. Analyzed by sectors, the monthly increase of the overall credit activity (of 0.9%) is almost equally due to lending to both sectors, thus in November, after a four-month period, a positive contribution of loans approved to the corporate sector in the monthly growth of total loans was registered.

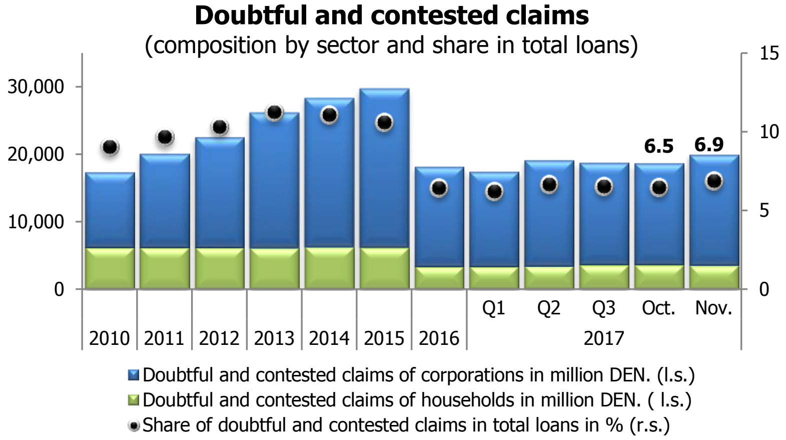
The growth of total loans in the period October-November is in line with the October forecast.

On an annual basis, total loans in November grew by 5.6%, which is above the forecasted (growth of 4.6%) for the fourth quarter of 2017. Observing the currency, the annual growth of total loans in November 2017 also stems from the growth of denar loans, amid continued annual decline in foreign currency loans.



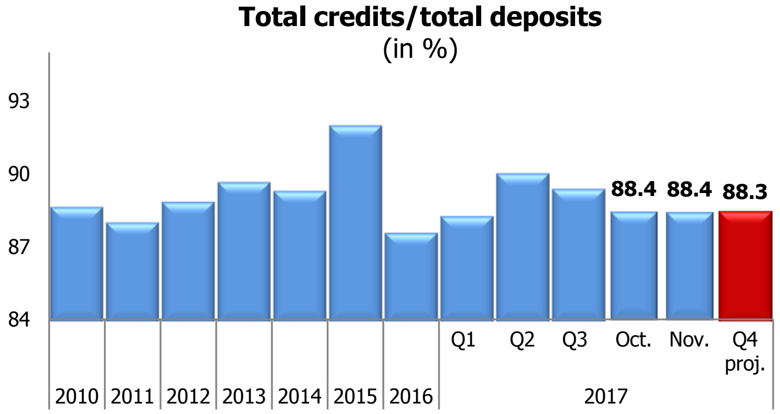
Source: NBRM.

The growth of household loans in November moderately accelerated on an annual basis, mainly influenced by the increased amount approved housing loans.



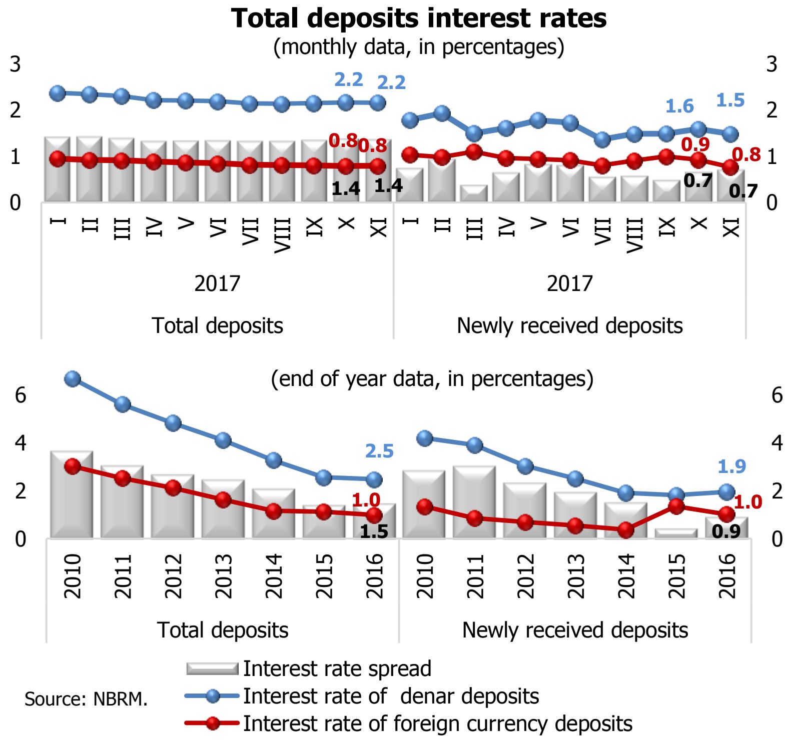
Source: NBRM.

The share of doubtful and contested claims in total loans in November increased to 6.9% (6.5% in October) which is entirely due to the increased doubtful and contested claims of enterprises.



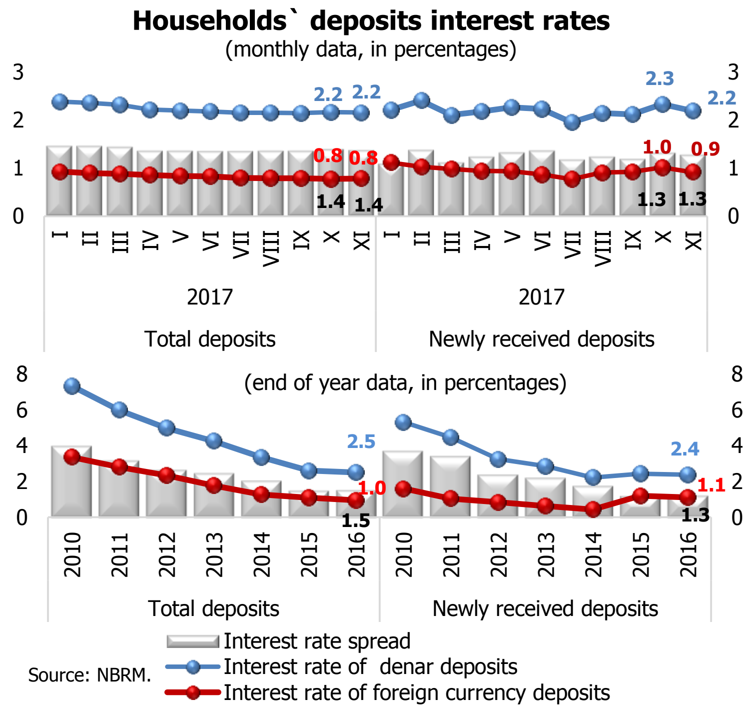
Source: NBRM.

The utilization of the deposits' landing potential of the private sector in November remained at a stable level of 88.4% as in the previous month. November performance is insignificantly higher compared to the expectations for the fourth quarter of 2017, according to the October forecast.



Source: NBRM.

In November, the interest rates on total deposits remained at the same level as in the previous month, maintaining a stable interest rate spread between the interest rates on denar and foreign currency deposits of 1.4 percentage points. Regarding **newly accepted total deposits**, the interest spread between denar and foreign currency deposits remained at a stable level of 0.7 percentage points, amid simultaneous decline of 0.1 percentage points in interest rates on newly accepted denar and foreign currency deposits. However, regarding the interest rates on the newly accepted deposits, it should be taken into account that they are characterized with variable movements[14].

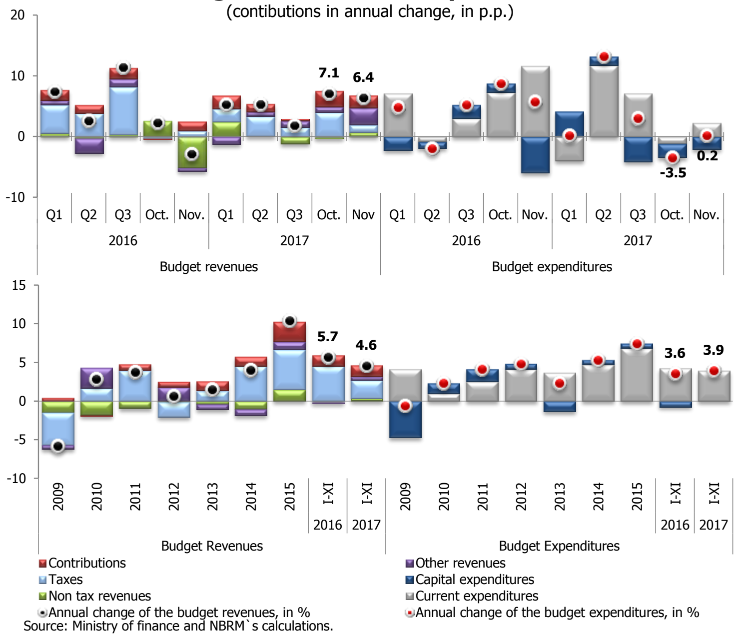


Source: NBRM.

In November, the **interest rates on household deposits** remained at the same level as in the previous month, whereby the interest rate spread between denar and foreign currency interest rates remained stable and amounted to 1.4 percentage points. Regarding **newly accepted household deposits**, interest rates of newly accepted denar and foreign currency deposits registered a minor decline of 0.1 percentage points, respectively, whereby the interest rate spread remained stable at 1.3 percentage points.

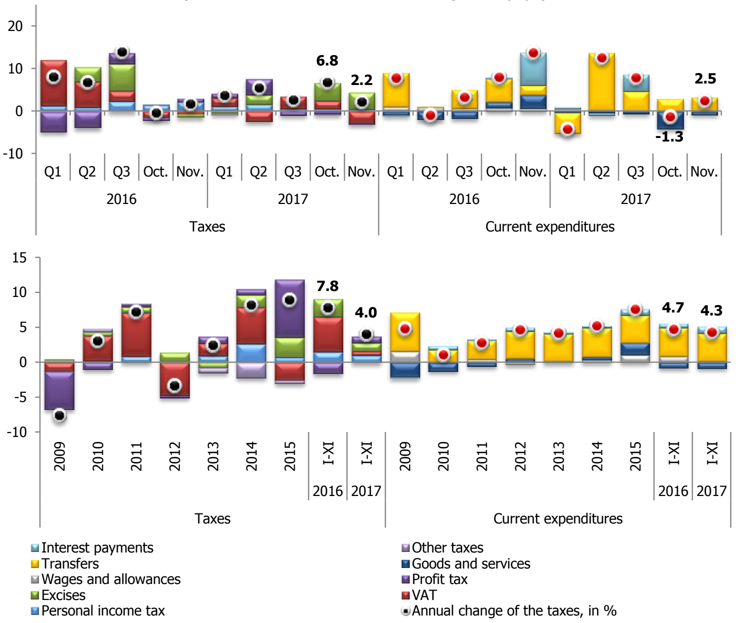
[14] Volatility of interest rate on newly accepted deposits results from the fact that the same have been driven by the volume of newly accepted deposits (which can vary from month to month) and their interest rate.

Budget revenues and expenditures
(contibutions in annual change, in p.p.)



Source: Ministry of finance and NBRM`s calculations.

Taxes and current expenditures
(contirbutions in annual change, in p.p.)



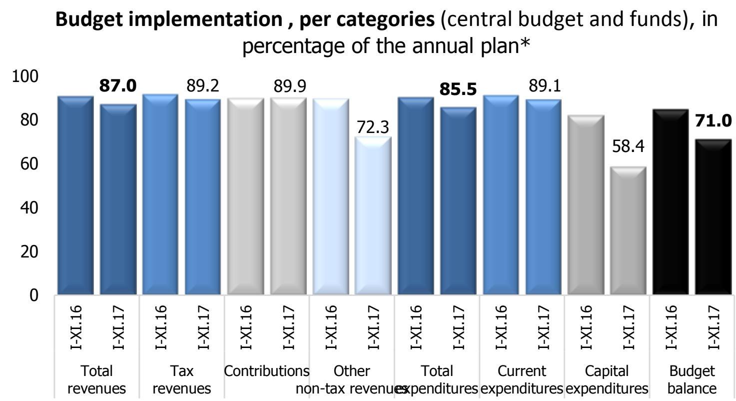
Source: Ministry of finance and NBRM`s calculations.

In November 2017, total budget revenues in the Budget of the Republic of Macedonia (central budget and budget of funds) are higher by 6.4% while the growth in total expenditures is lower and amounts to 0.2% on an annual basis. The higher budget revenues are mostly due to the improved performances in other revenues and contributions, whereas the performance of budget expenditures was a reflection of the higher performances in current expenditures.

Cumulatively, in the period January-November 2017, total budget revenues increased by 4.6% compared to the same period in the previous year, which is mostly due to the increased tax performances, while other budget revenue categories also had positive but minor contribution. In the period January-November 2017, the budget expenditures increased by 3.9% on an annual basis, which is mostly due to the higher current expenditures.

In November, total inflows of taxes in the Budget of the RM were higher by 2.2% on an annual basis, with a dominant contribution of the excise duties. On the other hand, current expenditures in November increased by 2.5% on an annual basis, which is mostly due to the higher performances in “transfers” category.

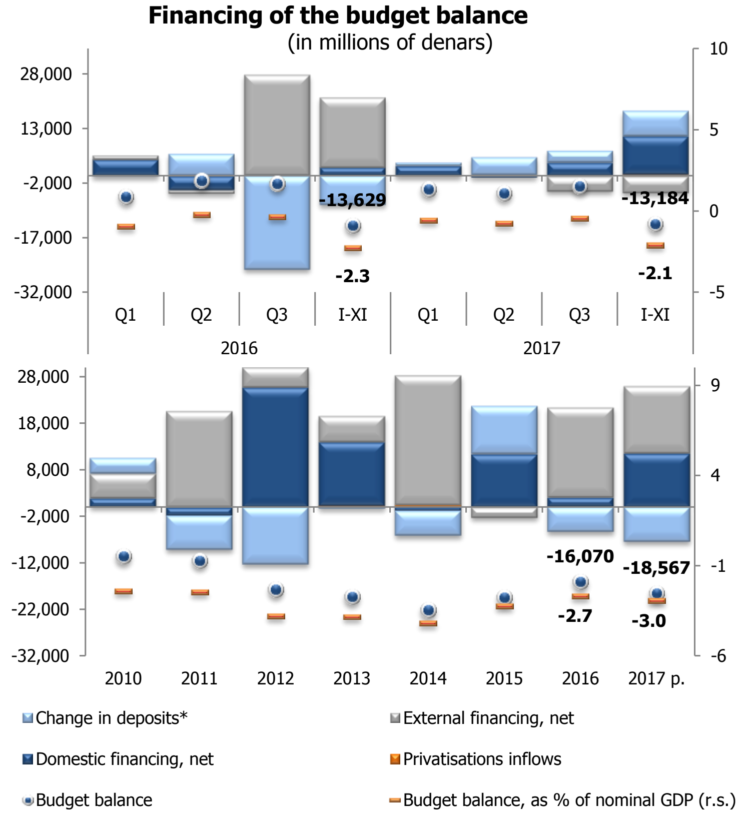
Cumulatively, in the period January-November, inflows from taxes increased by 4.0% on an annual basis which is mostly due to the higher performance in inflows from excise duties, profit tax and personal income tax. Regarding current expenditures, the growth rate in the analyzed period was 4.3% on an annual basis with a dominant contribution of transfers.



*for 2016, figures are calculated compared to realized Budget for 2016.
Source: Ministry of Finance and NBRM's calculations.

In the period January-November 2017, the budget revenues constituted 87.0% of revenues forecasted for 2017, in accordance with the Budget Revision[15]. Analyzed by individual categories of budget revenues, performances in taxes and contributions was 89.2% and 89.9%, respectively, while the performance in the category other non-tax revenues[16] was 72.3%.

Analyzing budget expenditures, in the period January-November 2017, 85.5% of the planned expenditures for 2017 were realized, where performance in current expenditures was 89.1%, while the performances in capital expenditures was lower and amounted to 58.4%.



* Positive change: deposits withdrawal; negative change:deposits accumulation.
Source: MoF.

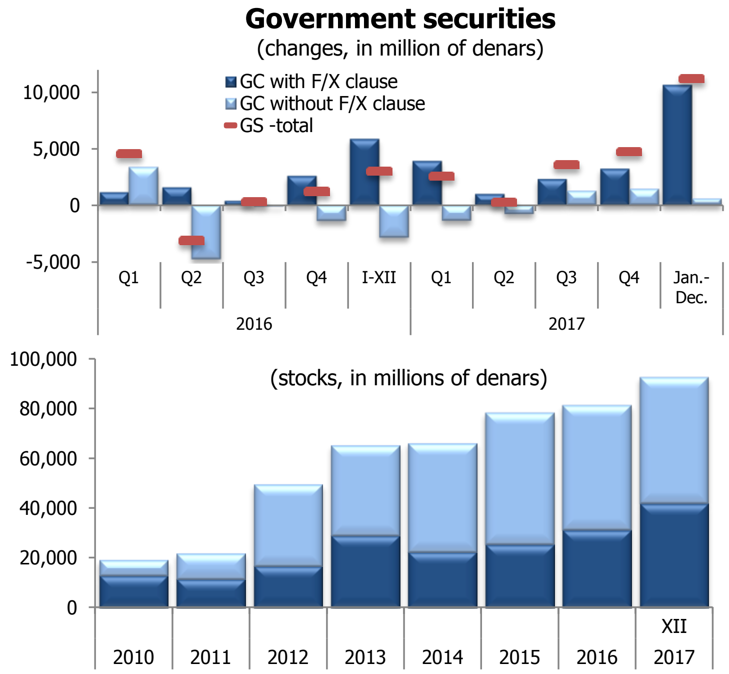
In the period January-November 2017, the Budget of the Republic of Macedonia registered a deficit of Denar 13,184 million, which is 2.1% of the nominal GDP[17]. In the period January-November 2017, the realized budget deficit constituted 71% of the deficit forecasted for 2017 pursuant to the Budget Revision.

The deficit in the period January-November 2017 was financed by domestic sources, through net issuance of new government securities and deposits withdrawal on the account of the government with the National Bank.

[15]The comparison is made with the Budget Revision from August 2017 and the reallocation of the budget assets among budget users from November 2017.

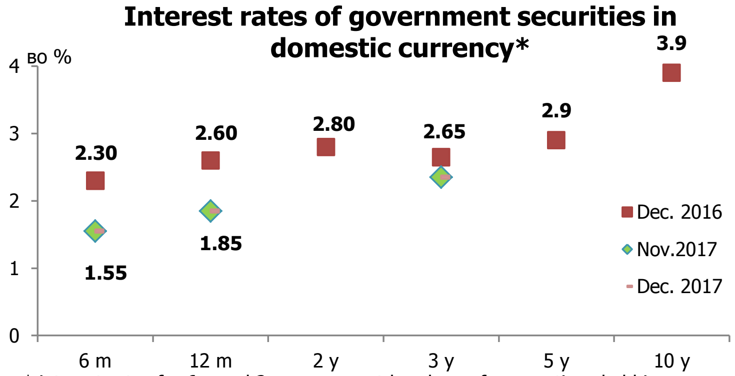
[16]Other non-tax revenues include non-tax revenues, capital revenues, donations from abroad and revenues of recovered loans.

[17]The analysis of nominal GDP for 2017 uses the NBRM October forecasts.



Source: MoF.

The stock of issued government securities in the domestic market amounted to Denar 92,584 million at the end of December 2017 and compared to the end of third quarter is higher by Denar 4,736 million. On a cumulative basis, for the entire 2017, government securities increased by Denar 11,214 million, constituting 97.5% of the forecasted amount for 2017[18].



* interest rates for 6m and 2y government bonds are from auctions held in November 2016, while interest rates for 3y and 5y government bonds are from auctions held in September 2015 and November 2014, respectively.

Source: Ministry of Finance.

The interest rates on government securities in December 2017 remained the same compared to the previous month[19], while the same are decreasing compared to the same month of the previous year by 6-month, 12-month and 3-year securities by 0.75, 0.75 and 0.3 percentage points, respectively.

[18] The comparison is made with the annual plan for domestic debt with the Budget Revision for 2017 from August 2017.

[19] At the auctions of government securities in November, there was an offer of 6-month treasury bills without FX clause, 12-month treasury bills without FX clause, 3-year government bonds without FX clause and 15-year government bonds with FX clause.

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 - 2017

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 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% of 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 the 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 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[20], 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.

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 0.5% to 0.5% and on seven-day deposit facility from 1.25% to 0.5% was adopted.

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.

April 2015

- A new Decision on the credit of last resort which, besides the current possibility of approving credit of last resort to banks against a collateral of debt securities, foreign currencies and banks' claims on the National Bank, introduces the possibility of extending this credit also against pledging banks' claims on customers. This modality of the credit of last resort is planned to be activated if the bank does not have debt securities and foreign currencies. The Decision specifies the types of claims that are acceptable for the National Bank as collateral for the credit of last resort.

[20] 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).

June 2015

- The National Bank Council adopted preventive measures for managing capital flows of the Republic of Macedonia to the Republic of Greece. Preventive measures pertain to restriction of capital outflows from residents of the Republic of Macedonia (natural persons and legal entities) to Greek entities based on newly concluded capital transactions, but not to a restriction of the outflows based on incoming payments for capital transactions already concluded. These measures limit capital outflows only to the Republic of Greece and to entities from the Republic of Greece (such as outflows for founding of a company, investing in securities, investing in documents for units in investment funds, investing in investment gold, financial credits, long-term loans, etc.) but not to block or in any way to impede current and future commercial operations with entities from the Republic of Greece. Current transactions remain free. Also, in order to maintain the security of foreign investors regarding the exercising of their rights to their property in the Republic of Macedonia, outflows based on realized dividends have not been restricted either. Furthermore, in order to secure the funds that domestic banks have in the banks in the Republic of Greece, Macedonian banks are required to withdraw all loans and deposits from banks based in the Republic of Greece and their branches and subsidiaries in the Republic of Greece or abroad, regardless of the agreed maturity. However, in order to allow smooth functioning of payment operations for the transactions that are not prohibited, an exception to this requirement has been made for the funds on the current (correspondent) accounts with those banks. Existing prudential and supervisory measures and limits for banks to investments in securities including Greek securities are supplemented by explicit ban on all residents to invest in Greek securities. Those are temporary protective measures, introduced to prevent the threat of any significant outflows of capital from the Republic of Macedonia to the Republic of Greece to cause significant disturbance to the equilibrium in the balance of payments and undermine the stability of the financial system.

August 2015

- The National Bank Council adopted the Decision on amending the Decision on reserve requirements that reduces the reserve requirement rate for the bank liabilities to natural persons in domestic currency with contractual maturity of over one year from 8% to 0%, with these liabilities obtaining the same treatment as the liabilities with maturity over two years, for which rate of 0% since 2012 has been applied. Having in mind that the amendment releases the banks from the reserve requirement for the natural persons' denar deposits with maturity exceeding one year, this measure is expected to have adequate influence toward larger supply of denar savings products with stimulative interest rates.

- The National Bank Council adopted the Decision on amending the Decision on CB bills that envisages adjustment of the mechanism of participation at the CB bills auction of the National Bank, where the main criterion will be the individual share of the banks in the total liabilities in domestic currency without currency clause of the banking system. With these amendments, the National Bank continues to support the natural persons' savings in domestic currency and on a longer run, which creates room for the banks for active credit support to the private sector.

December 2015

- The Council adopted the Decision amending the Decision on the methodology for determining the capital adequacy, introducing measures to slow the growth of long-term consumer loans. The measure increases capital requirements for banks on long-term consumer loans with maturity equal to or longer than eight years. Thus, the risk weight for claims on consumer loans with a contractual maturity equal to or longer than eight years, increases from 75% i.e.

100% to 150%. To avoid major shocks in the market of consumer lending, yet the growth rates to be reduced to a moderate level, this measure is aimed only at newly approved long-term consumer loans, i.e. loans with maturity equal or longer than 8 years approved after 1 January 2016. At the same time, this decision introduces higher capital requirement (risk weight of 75%) for the increase of overdrafts and credit cards in relation to 31 December 2015. The aim of this decision is to prevent the possibility of changeover to this type of borrowing as a result of the measure to decelerate consumer loans. Also, this Decision facilitates the access of legal entities. Namely, the capital requirement for guarantees issued by banks is reduced, which guarantees payment based on a certain business relationship of the client and banks' claims backed by commercial property that meets certain conditions. This way allows banks to allocate lower amount of capital for credit and guarantee operations with legal entities, including small and medium enterprises, which can cause reduction in the cost of banks and therewith, of clients for this type of operation.

- The National Bank Council adopted the Decision on amending the Decision on credit risk management, which requires starting from 1 January 2016, and by June 30 2016 to write-off all claims that have been fully booked for more than two years, and where the bank has identified and fully covered the credit risk of default at least two years before. According to the existing regulations, banks are required to fully reserve claims where the client defaulted at least 1 up to 5 years if there is a specific collateral, and the new measure requires from banks to write them off two years after their full provisioning. In addition, banks will still be allowed and required to take actions to collect these claims, although they are written off. The measure does not incur additional costs for banks since claims which are fully provisioned are written off, at least two years before.

- The National Bank Council decided to extend the application of the non-standard measure to reduce reserve requirement base in denars of commercial banks for the amount of newly approved loans to net exporters and domestic producers of electricity for two more years, until the end of 2017.

- On 29 December 2015, the Decision on introducing special protective measures adopted by the National Bank Council on 28 June 2015 due to the debt crisis in Greece at that time, ceased being valid. The measures were adopted to protect against any disruptions in the balance of payments or the stability of the financial system of the Republic of Macedonia due to any significant capital outflows from Macedonia to Greece. They were temporary for a period of up to six months, with a possible extension of their application. The protective measures served their purpose and prevented major capital outflows from the Republic of Macedonia, yet not disturbing the business of domestic companies with Greek companies. They delivered equilibrium in the balance of payments and stability of the domestic banking system. The situation in Greece has been stabilizing for quite some time. The lenders continued to financially support Greece, which, in turn, pledged to apply economic and social reforms, and austerity measures. Therefore, after the expiry of six-month validity period of the protective measures on 28 December 2015, since 29 December 2015, this decision is no longer in use.

May 2016

- At the regular meeting of the NBRM's Operational Monetary Policy Committee held on 3 May 2016, it was decided the interest rate on CB bills to be increased by 0.75 percentage points, from 3.25% to 4%. The decision to tighten the monetary policy is a reaction to the increased demand for foreign currency and pressures on banks' deposit base, which were entirely due to the deteriorating expectations of economic agents, caused by the unstable political situation in the country. Thus, the change in the interest rate is a response to the action of factors of non-economic nature.

- The National Bank Council adopted the Decision on reserve requirement, which increased the reserve requirement rate for banks' liabilities in domestic currency with FX clause. The measure has been aimed at further encouraging the process of denarization of deposits in the domestic banking system. Given the negligible market share of these liabilities in the banks' balance sheets, the changes are exclusively for further maintenance of low propensity of the economic agents for placing this type of deposits in domestic commercial banks.

- In order to maintain and increase deposits in the domestic banking system, the National Bank Council reviewed and improved the terms for placing foreign currency deposits of domestic banks at the National Bank and adopted the Decision on foreign currency deposit with the National Bank of the Republic of Macedonia. Accordingly, starting from 13 May 2016, the banks can place foreign currency deposits at the central bank at higher interest rates compared to the current negative interest rates that prevail in the international financial markets. It is expected that this measure will contribute to reduce the cost of domestic banks, which would accordingly contribute to higher interest rates on the deposits of their clients, domestic legal and natural persons.

October 2016

- In the regular meeting held on 25 October 2016, the NBRM's Operational Monetary Policy Committee decided not to offer additional foreign currency deposits that banks would place in the NBRM.

December 2016

- At the regular meeting of the NBRM's Operational Monetary Policy Committee, held on 13 December 2016, the Committee decided to cut CB bill interest rate by 0.25 percentage points, to 3.75%, and to increase the supply of CB bills at the 14 December auction from Denar 22,000 million to Denar 23,000 million.

- The National Bank Council adopted the Decision on amending the Decision on the methodology for determining the capital adequacy. This Decision is part of the compliance process of the domestic regulations with the reforms of the international capital standard Basel 3, as well as with the provisions of the European Regulation 575/2013 on prudential requirements for credit institutions and investment firms, in the part of the structure of the banks' own funds. The most significant amendments relate to the strengthening of the quality of own funds, both in terms of their structure and in terms of the criteria that should be met by certain positions in order to be a part of the banks' own funds. In this context, the own funds continue to be divided into Tier 1 and Tier 2 capital, **but the new Decision changes the structure of the Tier 1 capital, which is divided into Common Equity Tier 1 capital and Additional Tier 1 capital.** The Common Equity Tier 1 capital includes capital positions with the highest quality (equity capital and reserves) which are fully and readily available to cover risks and losses during the bank's operation. The new own funds component, the Additional Tier 1 capital, includes instruments which, among other things, contain a clause for their transformation into instruments of the Common Equity Tier 1 capital or for their write-off on temporary or permanent basis (reduction in the value of their principal), if the so-called critical event occurs. **The amendments to the Decision on the capital adequacy replace current restrictions in terms of size and ratio of individual elements of the own funds with the statutory prescribed minimal rates for the Common Equity Tier 1 capital, Tier 1 capital and own funds,** i.e. 4.5% for the Common Equity Tier 1 capital, 6% for the Tier 1 capital and 8% for the own funds of the risk-weighted assets. Thus, the greatest importance is given to the Common Equity Tier 1 capital positions (shares, reserves, retained undistributed profit), as capital positions with the highest quality.

January 2017

- At its regular meeting held on 10 January 2017, the NBRM's Operational Monetary Policy Committee decided to cut CB bill interest rate by 0.25 percentage points, to 3.5%, and to increase the supply of CB bills from Denar 23,000 million to Denar 25,000 million.

February 2017

- At its regular meeting held on 14 February 2017, the NBRM's Operational Monetary Policy Committee decided to cut CB bill interest rate by 0.25 percentage points, to 3.25%, and the supply of CB bills to be unchanged, at the level of Denar 25,000 million.

- At the regular meeting of the NBRM Council held on 27 February 2017, several decisions arising from the amendments to the Banking Law from October 2016 were adopted, for compliance with the Basel Capital Accord, the so-called Basel 3, as well as with the relevant European regulations. Pursuant to the amendments to the Banking Law made in October 2016, the banks are required to maintain adequate amount of capital to cover the so-called capital conservation buffers. The Law prescribes four capital buffers: (1) capital conservation buffer maintained at 2.5% of the risk weighted assets; (2) countercyclical capital buffer which can be up to 2.5% of the risk weighted assets, and more depending on other systemic factors/indicators, (3) capital buffer for systemically important banks which ranges from 1% to 3.5% of the risk weighted assets, and (4) systemic risk buffer which can range from 1% to 3% of the risk weighted assets. Pursuant to the provisions of the Banking Law on this basis, the Council adopted the following decisions:
- The Decision on the Methodology for Identifying Systemically Important Banks, which prescribes the manner of identifying the systemically important banks, i.e. the banks the operations of which are important for the stability of the entire banking system. In addition, the amount of the capital conservation buffer that the systemically important banks should meet depending on the level of system importance, has been set. Also, the Decision on the Methodology for Developing Recovery Plan for Systemically Important Banks, that requires systemically important banks to submit a Recovery Plan to the National Bank, was adopted at today's session.
- The Decision on the Methodology for Determining the Rate of Countercyclical Capital Buffer for Exposure in the Republic of Macedonia. This capital buffer aims to limit the risks arising from high credit growth, so it is introduced in case of high credit growth, on the basis of prescribed criteria.
- The Decision on the Methodology for Determining the Maximum Distributable Amount, envisaging restriction of the bank's earnings distribution, if it fails to maintain adequate amount of capital buffers. The capital buffers can be covered only by the highest quality capital positions, i.e. Common Equity Tier 1 capital.
- The Decision on the Methodology for Managing Leverage Risk, which is a standard of the Basel Capital Accord, Basel 3, and the European banking regulations, which introduces the leverage ratio, as a correlation between the capital and activities of the bank. Banks in RM register extremely low indebtedness, and the purpose of introduction of this standard at the international level was protection against possible excessive borrowing by banks, in terms of satisfactory level of capital adequacy.

March 2017

- At its regular meeting held on 14 March 2017, the NBRM's Operational Monetary Policy Committee decided to increase the supply of CB bills from Denar 25,000 million to Denar 30,000 million.

July 2017

- At its regular meeting held on 11 July 2017, the NBRM's Operational Monetary Policy Committee decided to reduce the supply of CB bills from Denar 30,000 million to Denar 27,500 million.

August 2017

- At its regular meeting held on 8 August 2017, the NBRM's Operational Monetary Policy Committee decided to reduce the supply of CB bills from Denar 27,500 million to Denar 25,000 million.

December 2017

- At its regular meeting held on 21 December 2017, the NBRM’s Council decided to continue the application of the non-standard measure for reducing the base of reserve requirement in denars of the commercial banks for the amount of newly approved loans of net exporters and domestic producers of electricity for two additional years.