National Bank of the Republic of Macedonia

MONETARY POLICY AND RESEARCH DEPARTMENT

Recent Macroeconomic Indicators
Review of the Current Situation

June 2017

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 (January- May 2017) and to make a comparison with the latest macroeconomic projections (April 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.

The analysis on the external environment assumptions show retention to the recent views for further recovery of the global economy, at a pace similar to the expected in the April projections. The assessments in terms of the major risks on global growth are also similar, and the same are related to the possibility for increased protectionism, uncertainty on possible effects from Brexit[1], increased instability on the financial markets, and potential faster monetary tightening by FED, in conditions of expecting fiscal stimuli by the new USA administration. In terms of the economic growth in the Euro area, as our most significant economic partner, the GDP projections for the first quarter of 2017 show an annual growth of 1.9% (growth of 0.6% on a quarterly basis), which is similar to the annual growth realized in the last quarter of 2016 (1.8%). The available data and research surveys on the economic sentiment of both companies and households in the second quarter are mainly favorable and point to further growth of the economy. Hence, in terms of positive performances, favorable conditions on financial markets and expectations for strengthening the global economy growth, in June, the ECB conducted an upward revision on the growth projections for the euro area for the current and the following two years[2], amid balanced risks assessment. At the same time, the labor market continues to register positive movements, whereby in April 2017 the unemployment rate decreased to 9.3% which is the lowest rate since March 2009. In term of consumer prices, the preliminary data show that inflation in May 2017 decelerated and reduced to 1.4% on an annual basis (1.9% in April), in conditions of smaller growth of the prices of energy and services. The core inflation also registers a deceleration and in May it amounted to 0.9% (1.2% in April). Thus, the June projections of the ECB show a downward revision in inflation[3] due to the lower expectations for oil price. Noting the positive effects of the monetary relaxation measures taken so far on the solid recovery of the European economy, at the meeting in June, the ECB made no changes in the monetary policy setup, although it showed readiness to adapt it through non-standard measures if slower than expected inflation adjustment occurred. Also, the market participants expect further adjustment of the monetary policy by the ECB and its gradual normalization in 2018, thereby the **interest rate EURIBOR** for 2017 and 2018 is expected to register a similar upward trend as in the April projections and continue to remain in the negative zone throughout the entire forecast horizon.

Observed from a viewpoint of the quantitative external environment indicators of the Macedonian economy, the forecasts regarding the foreign effective demand indicate minimal revisions in relation to the April projections. Namely, a minimally higher growth is expected in 2017, whereas a minimally lower growth compared to the previously projected is expected in 2018. In terms of the **foreign effective inflation**, the latest assessments for 2017 and 2018 are unchanged relative to the April projection. The latest assessments **for the primary commodities prices on the world markets for 2017 are revised downwards relative to the April projections, whereas for 2018 most prices register a small upward revision.** Thus, regarding the **world oil prices**, in 2017, a somewhat lower growth compared to the April projection

[1] On 29 March 2017, the UK officially started the EU exit procedure, and at the Summit held in 22 May, the EU Council adopted the start of the negotiation according to Article 50 of the Lisbon Agreement.
[2] Pursuant to the latest ECB's forecasts, the growth rate of real GDP for 2017, 2018 and 2019 is expected to amount to 1.9%, 1.8% and 1.7%, respectively. According to the previous (March) projections, the growth for these three years was forecasted to be 1.8%, 1.7% and 1.6%, respectively.
[3] The latest inflation forecasts are 1.5%, 1.3% and 1.6%, for 2017, 2018 and 2019 respectively, compared to the March forecasts for these years of 1.7%, 1.6% and 1.7%, respectively.

is expected, while in 2018, the same rate of decline is anticipated as before. **Metal prices** are generally corrected downwards in both years. Therefore, nickel prices are significantly corrected downwards, whereby in both years a small decline instead of the projected growth in April is expected, whereas the copper price in 2017 is expected to register a smaller than the projected growth in the April projection, and for 2018 a stabilization of the prices is expected, similar to the previous one. Regarding the **world prices of the primary food products**, pressures on the domestic inflation are still expected. Thus, in 2017 corn and wheat prices are expected to register a moderately lower growth compared to the April projections, whereas in 2018 the growth assessments are slightly revised upwards. However, one should bare in mind the exceptional variability of estimations for these primary commodities prices 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 projected dynamics within the April forecasting round indicates certain deviations in individual segments of the economy. Despite the downward revision of GDP in the last April projection, the published percentage data for **GDP for the first quarter** are below the expected for the economic growth, indicating a lower starting point and downward risks for the GDP projection for the entire 2017. Such downward deviation is mostly due to the higher than projected growth in import of goods and services and weaker than expected growth in private consumption, amid minimal growth of investments (instead of the projected decline). Given the small number of available high frequency indicators which indicate divergent movements, it is difficult to precisely assess the economy in the second quarter of the year. When it comes to **changes in consumer prices**, in May, as in the previous months of the year, a positive inflation rate is measured, which however represents a small downward deviation of the projected trajectory of the gradual inflation acceleration in the April projection for 2017. Thus, despite the downward revision of most of the external input assumptions in the inflation projection for the entire 2017, it is still currently estimated that risks on the inflation projection for 2017 are balanced. The uncertainty on the projected movement of the world primary commodities prices continues to remain the main risk on the inflation projection.

Recent available foreign reserves data (adjusted for the effects of price and exchange rate differentials and price changes of securities), as of May 2017, indicate their decline. Analyzing change factors, the decrease in reserves is mostly due to the transactions for the account of the government, NBRM's interventions, as well as the category others, which includes the decline of domestic banks' foreign currency deposits with the NBRM. In terms of available indicators of the external sector for the second quarter, the currency exchange market indicators as of May point to somewhat higher net inflows of the private transfers than the expected with the April projection. In addition, indicators of external trade for April indicate no significant deviation in the projected trade balance for the second quarter of the year, although the short-term period is a limiting factor for deriving reliable conclusions about the expectations for the entire quarter. The performances in the balance of payments in the first quarter of 2017 indicate higher current account deficit compared to the April projection, amid simultaneous higher net inflows in the financial account than expected. In current transactions, deviations are mostly driven by the balance of goods and services, where a higher than projected deficit is registered, whereas in primary income the performances are better than the expected. In terms of the financial account, the performance in direct foreign investments and portfolio investments is significantly better, whereas performances in other financial flows are weaker relative to the April projections for the first quarter, with the exception of the currency and deposits category. The analysis of foreign reserves adequacy indicators shows that they continue to hover in a safe zone.

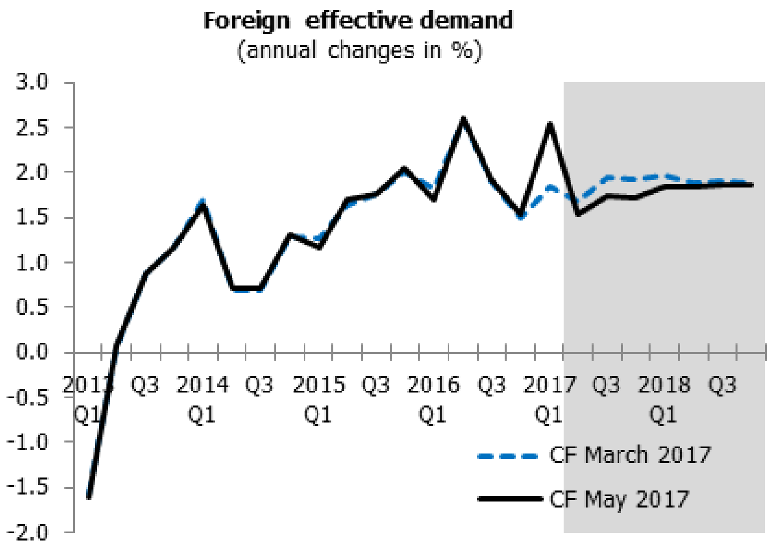
As for the monetary sector developments, final data as of April indicates further monthly decline of total deposits in banks (of 0.3%), but more moderate compared to the previous month (0.4%). Analyzed by sectors, the monthly decline of total deposits in April is equally driven by both sectors (corporate and household). In terms of the currency structure, both denar and foreign currency savings register a decline, whereby the decline in denar deposits is relatively higher. On an annual basis, total deposits in April grew by 6.3%, which is under the projected growth of 8.4% for the second quarter of 2017. Analyzing the credit market, in April, total loans registered a monthly growth of 0.6%, which was more moderate compared to the growth in the previous month (of 1.2%). The increase of total loans in April, similarly as in the previous month, is almost equally driven by the loans extended to both sectors (corporate and household). On an annual basis, total loans are higher by 0.6%, and if the effect of the regulatory changes is excluded, the annual growth of total loans in April amounted to 6.3% and is higher compared to the projected growth (of 4.5%).

In the first four months of the year, the Budget of the Republic of Macedonia registered a deficit of Denar 3,596 million, mostly financed through the a net issuance of government securities, and to a lesser extent through deposit withdrawal from the government account with the National Bank. The budget deficit constitutes 19.3% of the envisaged deficit in the Budget for 2017.

The latest macroeconomic indicators and assessments indicate certain deviations relative to the forecasted dynamics in individual segments in the economy, but the perceptions about the environment for conducting monetary policy and about the risks highlighted within the April forecasts are mainly unchanged. Foreign reserves (adjusted for price and exchange rate differentials and price changes of securities) decreased as of May 2017. Foreign reserves adequacy indicators continue to hover in the safe zone. In terms of the economic activity, the latest published data for first quarter GDP is lower than the expected, indicating a lower starting point for the future economic activity, which could result to lower performances in terms of the projected growth in the April projection cycle. In inflation, recent performances are relatively lower than the projected, while the expected development of the external assumptions suffered a downward correction, but however it is assessed that risks about inflation projection for 2017 are balanced. Within the monetary sector, data on total deposits in April indicate to lower deviations compared to the expected with the April projections, amid unfavorable downward shifts in both sectors, especially expressed in households. On the other hand, the growth pace of the credit activity currently is according to the expectations for the second quarter of the year, pursuant to the April projections, whereby the credit growth in April is almost equally driven by both sectors (corporate and household).

Selected economic indicators[1]					2016					2017					
	2012	2013	2014	2015	Q1	Q2	Q3	Q4	2016	Jan.	Feb.	Mar	Q1	Apr.	May
I. Real sector indicators															
Gross domestic product (real growth rate, y-o-y) [2]	**-0.5**	**2.9**	**3.6**	**3.8**	**2.4**	**2.9**	**2.0**	**2.4**	**2.4**				**0.0**		
Industrial production [3]															
y-o-y	-2.8	3.2	4.8	4.9	10.7	1.3	5.0	-1.8	3.4	-2.6	-1.3	-0.9	-1.5	-1.9	
cumulative average	-2.8	3.2	4.8	4.9	10.7	5.6	5.4	3.4	3.4	-2.6	-1.9	-1.5	-1.5	-1.6	
Inflation [4]															
CPI Inflation (y-o-y) [5]	4.7	1.4	-0.5	-0.3	-0.1	-0.7	-0.1	-0.1	-0.2	0.6	0.2	0.6	0.5	1.0	1.2
CPI Inflation (cumulative average)	3.3	2.8	-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
Core inflation (cumulative average)	2.1	3.0	0.6	0.5	1.7	1.6	1.5	1.4	1.4	1.4	1.4	1.6	1.6	1.7	1.8
Core inflation (y-o-y)	2.1	3.0	0.6	0.5	1.7	1.5	1.3	1.2	1.4	1.4	1.4	2.0	1.6	2.0	2.1
Labor force															
Unemployment rate	31.0	29.0	28.0	26.1	24.5	24.0	23.4	23.1	23.7				22.9		
II. Fiscal Indicators															
(Central Budget and Budgets of Funds)															
Total budget revenues	138,115	140,248	145,929	161,207	40,583	41,422	43,807	43,524	169,336	12,584	13,310	16,840	42,734	15,053	
Total budget expenditures	155,840	159,505	168,063	180,632	46,218	42,729	45,953	50,506	185,406	14,723	14,845	16,733	46,301	15,082	
Overall balance (cash)	-17,725	-19,257	-22,134	-19,425	-5,635	-1,307	-2,146	-6,982	-16,070	-2,139	-1,535	107	-3,567	183	
Overall balance (in % of GDP) [1]	-3.8	-3.8	-4.2	-3.5	-0.9	-0.2	-0.4	-1.1	-2.6	-0.3	-0.2	0.0	-0.6	-0.6	
III. Financial indicators [6]															
Broad money (M4), y-o-y growth rate	**4.4**	**5.3**	**10.5**	**6.8**	**6.2**	**2.5**	**4.0**	**6.1**	**6.1**	**6.7**	**5.1**	**4.2**	**4.2**	**5.9**	
Total credits, y-o-y growth rate	**5.4**	**6.4**	**10.0**	**9.5**	**8.4**	**3.5**	**2.5**	**0.9**	**0.9**	**0.6**	**-0.3**	**0.0**	**0.0**	**0.6**	
Total credits - households	6.5	10.2	11.8	12.9	13.0	8.8	7.3	7.0	7.0	7.1	6.7	6.6	6.6	6.5	
Total credits - enterprises	4.5	3.8	8.6	7.1	5.1	-0.5	-1.2	-3.8	-3.8	-4.4	-5.9	-5.2	-5.2	-4.2	
Total deposits (incl. demand deposits), y-o-y growth rate	**4.9**	**6.1**	**10.4**	**6.5**	**6.2**	**2.3**	**4.0**	**5.7**	**5.7**	**6.7**	**5.0**	**4.2**	**4.2**	**6.3**	
Total deposits - households	7.2	6.7	8.9	4.1	3.1	0.2	1.2	2.5	2.5	2.9	2.8	1.8	1.8	3.4	
Total deposits - enterprises	-1.6	3.1	15.7	13.0	16.0	5.6	11.3	13.4	13.4	15.9	9.0	8.8	8.8	12.0	
Interest rates [7]															
Interst rates of CBBills	3.73	3.25	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
Lending rates															
denar rates (aggregated, incl. denar and denar with f/x clause)	8.5	8.0	7.5	7.1	6.7	6.6	6.6	6.5	6.6	6.4	6.4	6.3	6.4	6.3	
f/x rates	7.0	6.5	6.3	5.9	5.6	5.5	5.4	5.2	5.4	5.1	5.1	5.0	5.1	5.0	
Deposit rates															
denar rates (aggregated, incl. denar and denar with f/x clause)	5.1	4.4	3.7	2.9	2.5	2.5	2.5	2.5	2.5	2.4	2.3	2.3	2.3	2.2	
f/x rates	2.2	1.8	1.4	1.3	1.1	1.1	1.0	1.0	1.0	1.0	0.9	0.9	0.9	0.9	
IV. External sector indicators															
Current account balance (millions of EUR)	**-240.0**	**-134.1**	**-43.2**	**-187.0**	**-58.7**	**-219.4**	**100.3**	**-125.6**	**-303.3**	**-7.2**	**-59.2**	**-59.1**	**-125.5**		
Current account balance (% of GDP)	*-1.6*	*-1.6*	-0.5	-2.1	-0.6	-2.2	1.0	-1.3	-3.1	-0.1	-0.6	-0.6	-1.2		
Trade balance (millions of EUR) [8]	**-1,946.7**	**-1,748.1**	**-1757.9**	**-1713.6**	**-373.2**	**-501.5**	**-391.4**	**-511.3**	**-1777.4**	**-117.4**	**-138.1**	**-169.8**	**-425.4**	**-152.7**	
Trade balance (% og GDP)	*-25.7*	*-21.4*	-20.5	-18.9	-3.8	-5.1	-4.0	-5.2	-18.0	-1.1	-1.3	-1.7	-4.1	-1.5	
import (millions of EUR)	-5,070.6	-4,983.3	-5504.5	-5801.1	-1356.6	-1557.7	-1540.0	-1652.4	-6106.7	-442.2	-517.7	-593.8	-1553.6	-540.8	
export (millions of EUR)	3,124.0	3,235.2	3746.6	4087.6	983.3	1056.2	1148.6	1141.1	4329.3	324.7	379.6	424.0	1128.3	388.1	
rate of growth of import (y-o-y)	0.3	-1.7	10.5	5.4	3.3	4.9	10.2	3.0	5.3	24.9	8.4	13.1	14.5	2.2	
rate of growth of export (y-o-y)	-2.8	3.6	15.8	9.1	5.3	1.4	10.5	6.4	5.9	12.6	9.7	21.4	14.7	5.3	
Foreign Direct Investment (millions of EUR)	**131.1**	**229.4**	**197.4**	**202.8**	**132.7**	**52.2**	**28.2**	**141.0**	**354.0**	**-7.8**	**52.2**	**63.9**	**108.2**		
External debt															
Gross external debt (in milllions of EUR)	5171.7	5219.7	5992.3	6290.5	6816.2	6886.6	7513.4	7253.2	7253.2						
public sector	2162.1	2172.4	2846.8	2933.7	3279.4	3283.1	3891.1	3445.5	3445.5						
public sector/GDP (in %)	28.5	26.7	33.2	32.4	33.2	33.3	39.5	34.9	34.9						
private sector	3009.5	3047.4	3145.5	3356.9	3536.8	3603.6	3622.3	3807.7	3807.7						
Gross external debt/GDP (in %)	68.2	64.0	70.0	69.4	69.1	69.8	76.2	73.5	73.5						
Gross official reserves (millions of EUR) [9]	**2,193.3**	**1,993.0**	**2,436.5**	**2,261.7**						**2,557.1**	**2,563.0**	**2,534.4**		**2,496.0**	**2,448.4**

/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.
/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.



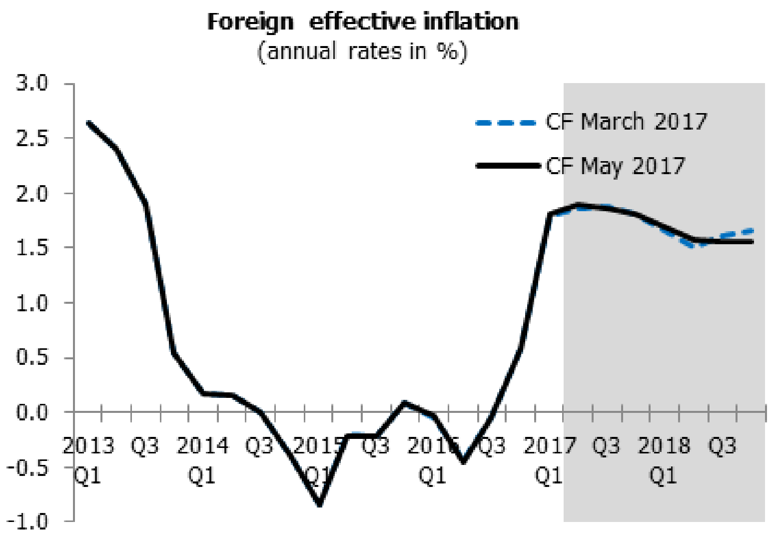
Source: "Consensus Forecast" and NBRM calculations.

In 2017, the foreign effective demand is expected to increase by 1.9%, which is a minimal upward revision of 0.1 p.p. in comparison with the April projection...

...due to the minimal upward corrections in many countries.

On the other hand, in 2018, the growth of foreign effective demand is expected to amount to 1.8% i.e. a minimal downward revision of 0.1 p.p. is conducted...

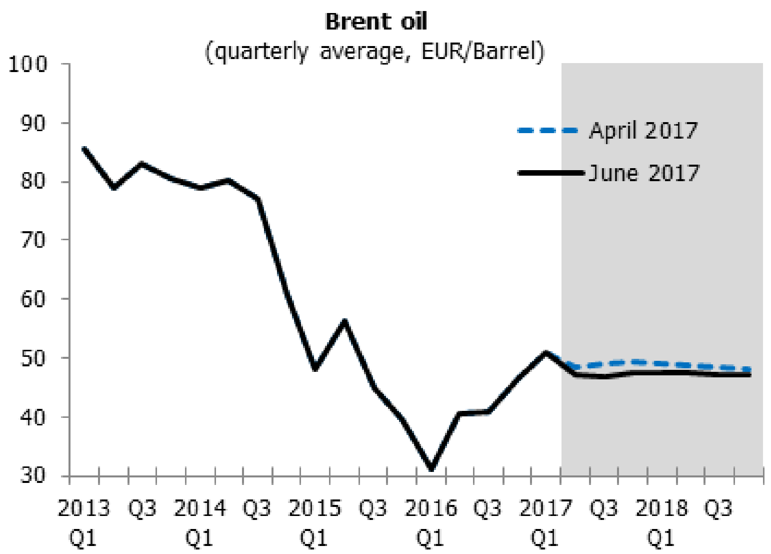
...which is mostly due to the expectations for a lower growth of the German economy.



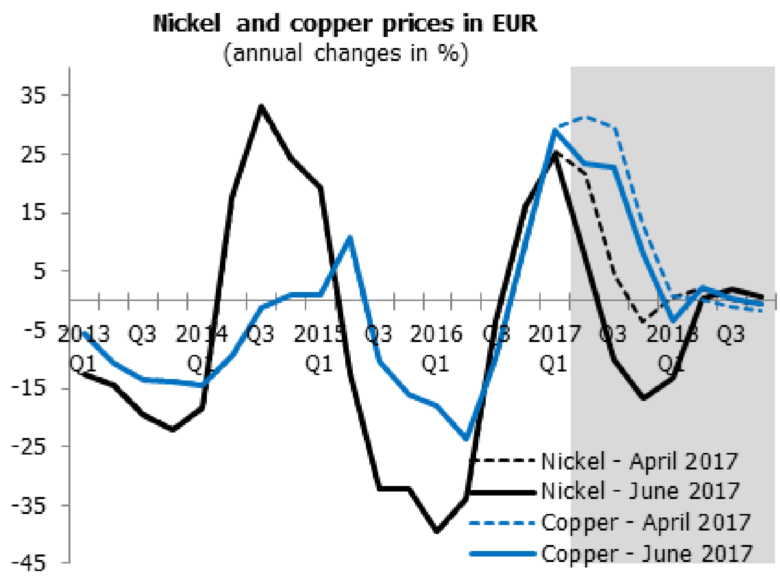
Source: "Consensus Forecast" and NBRM calculations.

The April forecasts for foreign effective inflation remained unchanged...

...i.e. the foreign effective inflation is expected to amount to 1.9% and 1.6% in 2017 and 2018, respectively.



Source: IMF and NBRM calculations.



Source: IMF and NBRM calculations.

In 2017, a downward revision of the oil price is conducted[4] expecting a slightly lower growth relative to the growth projected in April...

...mostly as a result of the higher production level of USA, despite continuing the agreement between the OPEC countries and some non-OPEC countries for reduction of the global oil production in order to influence the upward movement of prices[5].

On the other hand, the assessments for 2018 are the same as in the April projections...

...i.e. given the higher price level in 2017, a slight decline in oil price on world markets is projected.

In 2017, the copper price is revised downwards i.e. a slightly lower growth compared to the projected in April is expected...

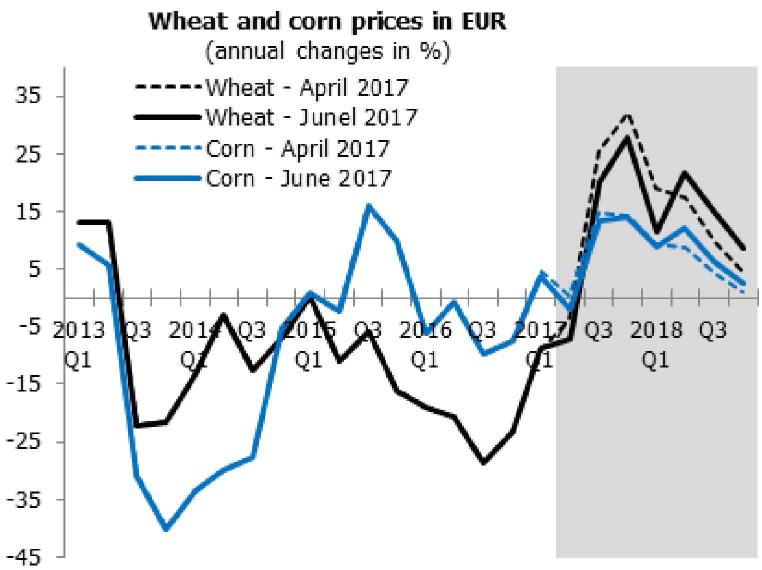
...mostly due to the expectations for a lower growth in the industrial output in China.

On the other hand, the price of nickel in 2017 is significantly revised downwards, expecting a minimal decline instead of the projected growth in April...

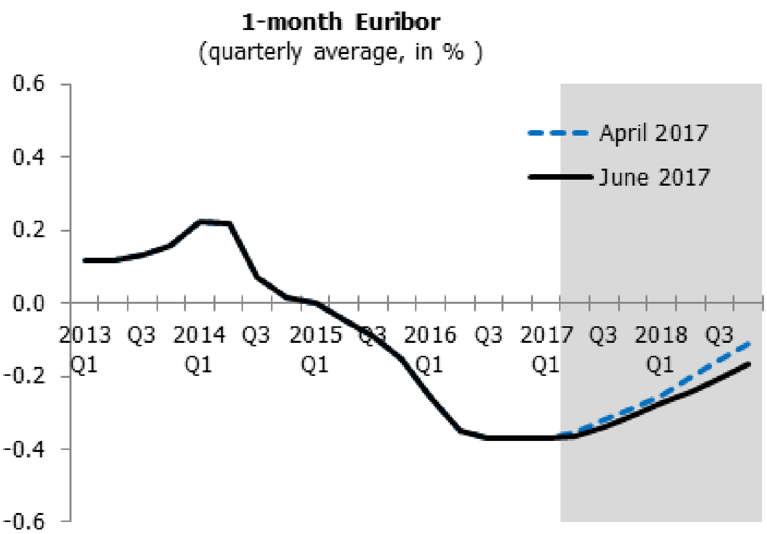
...largely due to the expectations for larger supply on the market, primarily due to the abolition of part of the export restrictions on the nickel producers in the Philippines[6] and Indonesia.

In 2018, changes in the forecasts of copper prices are insignificant, whereby their stabilization is further expected. On the other hand, nickel prices are revised downwards,

[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 25 May 2017, a Decision by OPEC countries was adopted for continuing the agreement for reducing oil production for an additional nine months (March 2018), whose aim is reduce the stocks of this fuel globally. Additionally, 11 oil producing countries which are not OPEC members including Russia are expected to support the continuation of the agreement, producing 1.8 million barrels less per day until March 2018.
[6] In January 2016, the Government of the Philippines closed i.e. discontinued the production of 23 nickel mines, in the campaign to reduce the ravages of industry on the environment. These 23 mines represent about 50% of the total nickel production in the Philippines, which is the largest nickel producer in the world. However, during March 2017, the government allowed 8 mines to place their nickel stocks on the market, which equal around 5 million tons, according to calculations.



Source: IMF and NBRM calculations.



Source: "Consensus Forecast" and NBRM calculations.

expecting a slight decline instead of the projected minimal growth in April.

In 2017, the stock exchange prices of wheat have been revised downwards, compared to the April projections...

...mostly due to the higher production level in Australia, the global demand decline and record level of the global wheat stock.

On the other hand, corn prices denominated in US dollars have been revised upwards for 2017, while prices denominated in euros have been revised downwards relative to the April projections...

...largely due to the expectations for smaller appreciation of the US dollar against the euro.

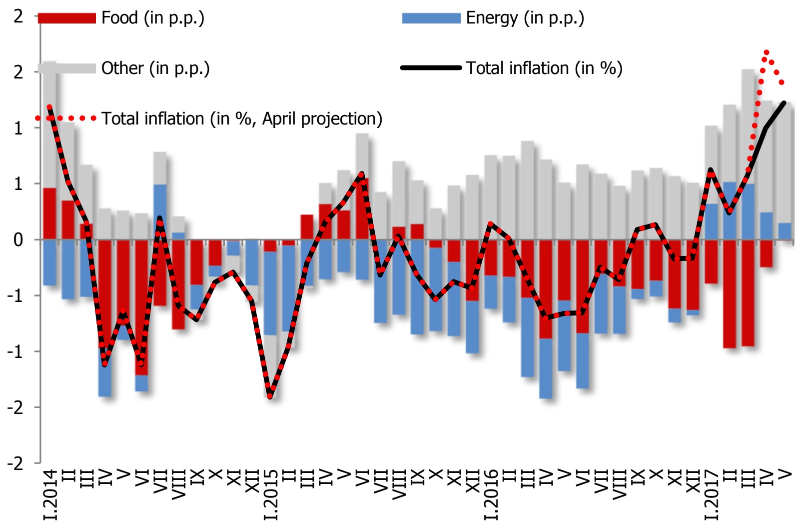
The expectations for wheat and corn prices in 2018 are slightly revised upwards compared to the projected in April.

In 2017 and 2018, insignificant revision of the expectations for the foreign interest rate have been conducted...

...whereby a monthly level of -0.35 (-0.33% in April) and -0.22% (-0.18% in April) for 2017 and 2018, respectively is envisaged...

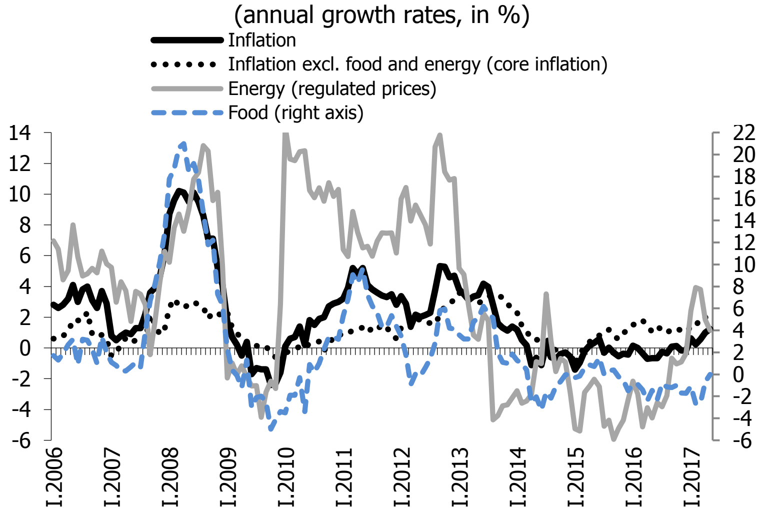
...amid expectations that part of the market participant will continue the Quantitative Easing Program of the ECB in the first half of 2018.

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



Source: SSO and NBRM.

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



Source: State statistical office and NBRM calculations.

In May 2017, the growth of domestic consumer prices accelerated and on a monthly basis amounted to 0.7%, compared to the monthly growth in April of 0.4%...

...whereby the acceleration was mostly a reflection of the shift in the dynamics of the food prices, as well as the energy component[7] and in core inflation.

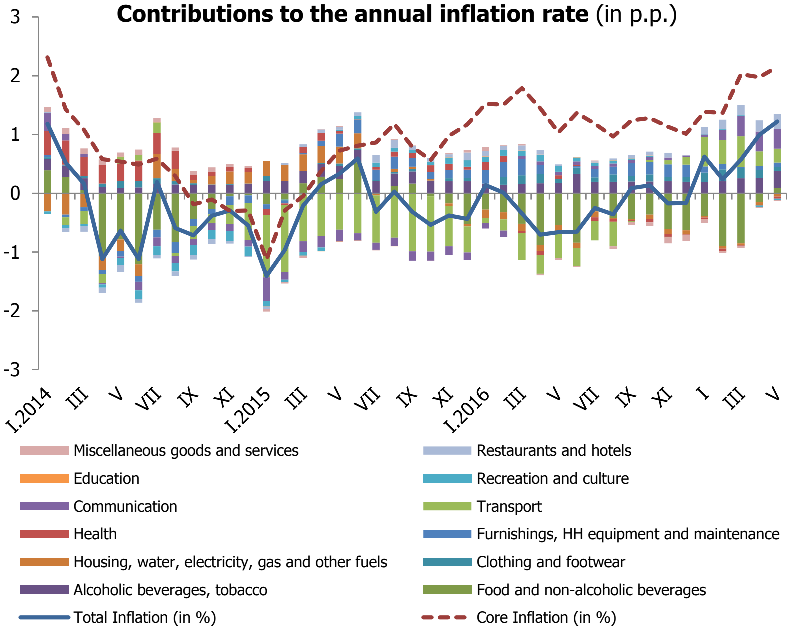
The monthly growth of consumer prices in May, mainly driven by the growth of food prices[8], and the core inflation has moderately positive contribution. On the other hand, energy prices, for the second consecutive month register a small negative contribution towards the monthly inflation.

The monthly growth affected the annual inflation rate which equaled 1.2 % in May (compared to 1% in April), which is still moderate downward deviation compared to the April projection.

Observed by price category, the downward deviation is mostly due to the lower performances in the energy component and core inflation...

...whereas food prices in May got out of the zone of "negative" changes and remained unchanged on an annual basis, compared to the projected decline, affecting in reverse.

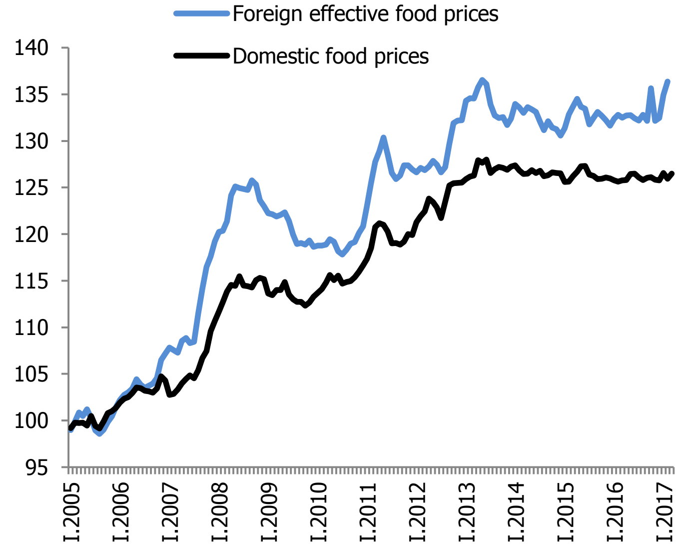
[7] Smaller negative contribution.
[8] Observed by group of products, fruits and vegetables registered the highest positive contribution in May.



Source: SSO and NBRM.

Foreign effective food prices* and domestic food prices

(indices, 2005 =100)



* Foreign effective food prices are calculated as weighted sum of food prices in countries that are major trade partners with Macedonia.
Source: State statistical office, Eurostat and NBRM calculations.

In May, core inflation equaled 0.2% on a monthly basis and 2.1% on an annual basis.

Regarding the structure of core inflation, the annual growth in May is due to the upward shift in the prices of most categories within core inflation, with the highest contribution of tobacco prices[9], the prices of "communications" category and prices of catering services.

The growth of the prices of external input assumptions in inflation projection for the entire 2017 has been revised downwards.

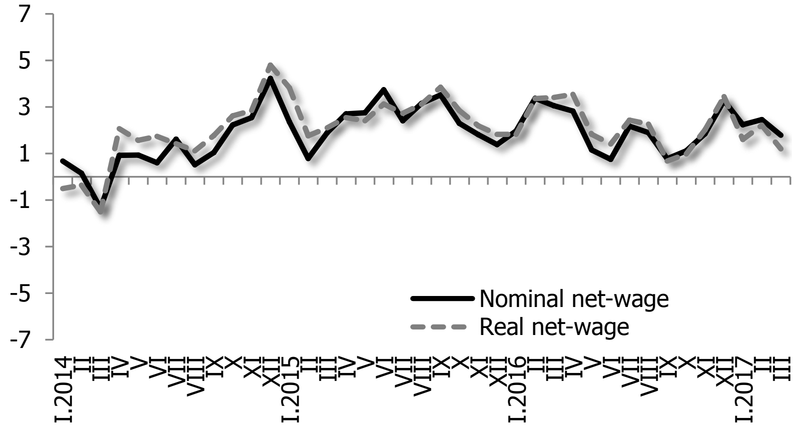
Thus, the latest oil and grain price estimates for 2017 indicate lower growth compared to the expectations of the April cycle projection.

Amid relatively small downward deviation of the actual projected inflation trajectory and simultaneously external assumptions revised downwards, it is currently assessed that the risks to inflation projection for 2017 are balanced. Namely, despite the downward revision of the external assumptions, the great uncertainty on the projected movement and changes in the primary commodities world prices, primarily in oil prices, impose the need for caution.

In March 2017, the average net wage registered a nominal annual growth of 1.8%, which is a moderate acceleration relative to the growth in the previous month, but does no significantly deviate in relation to the average nominal growth of wages in the previous two-year

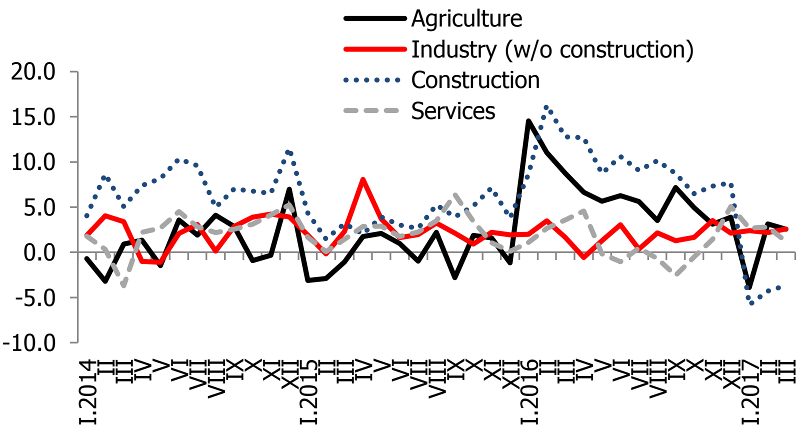
[9] The annual growth of tobacco prices in May is a combination of the increase in the price of a certain type of cigarettes in June 2016 and April 2017. In July 2016, the cigarette excise increased (from 1 July 2017 to 1 July 2023 the excise duty will increase by 0.20 denars each year) which did not 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.

period.

An upward shift of wages in March is registered in most activities, whereby the highest growth is registered in financial and insurance activities, art, entertainment and recreation, and higher growth of the wages is registered in mining. On the other hand, an annual reduction of wages in March is registered in construction, electricity supply, gas, heating and air conditioning and in several service activities[10].

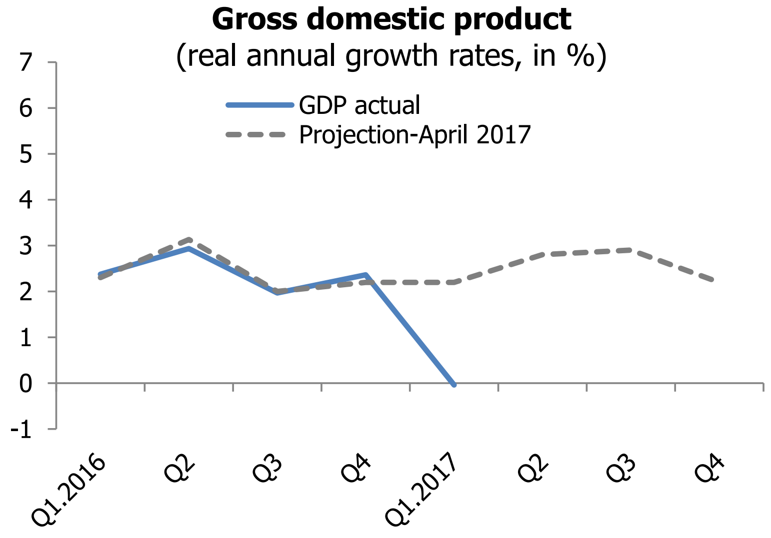
Amid small increase in the cost of living in March, **the real wages increased by 1.2%.**

The realizations in net income in the first quarter of the year are slightly lower than expected for the quarter within the April projection.

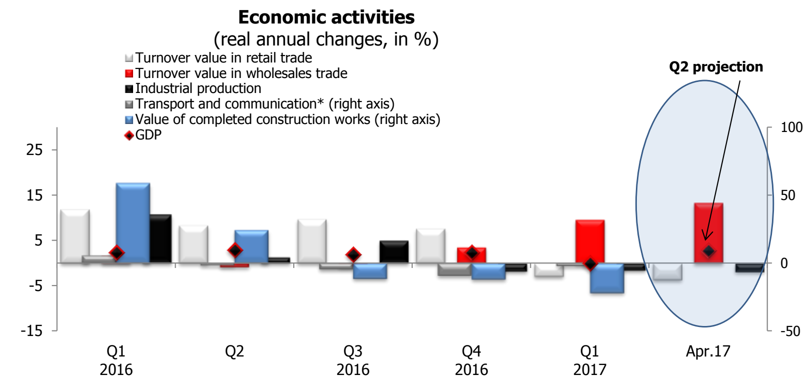
In the first quarter of 2017, the GDP growth rate amounted to 0.0% i.e. the GDP level remained unchanged compared to the same quarter in the previous year. These performances represent a downward deviation relative to the April projection for the first quarter.

In terms of the demand, in the first quarter the domestic demand had a positive contribution to the growth, compared to the net export whose contribution was negative. Observed by individual components, export has the largest individual positive contribution, and in relation to the domestic demand, private consumption has a solid positive contribution. Gross investments and public consumption have a small positive effect in the first quarter. However, these favorable shifts were mostly neutralized by

[10] Within the service sector, lower wages have been paid in the "administrative and auxiliary service activities", "professional, scientific and and technical activities" and "real estate activities".



Source: SSO and NBRM projections.



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

the stronger import pressures due to which the total economic activity stagnated on an annual basis.

The deceleration of the economic activity, in relation to the growth in the previews quarter is a reflection of the slower growth of private consumption and export and larger import pressures. In terms of the projection, the slower growth of personal consumption and stronger growth of import are key drivers of the downward deviation, whereas the deviation in investments is upwards.

Observing the production side, in the first quarter of 2017, higher added value was registered in many activities, which was mostly neutralized with the decline of the activities in construction and group activities of public administration, education and health[11].

It is difficult to give a precise assessment about the economy in the second quarter of the year, which is partially due to the limited volume of available high frequency data. Additionally, current data for April indicate divergent movements, and the instability connected with the political events in the country was also present in the second quarter, which was also a factor of the uncertainty of the assessments about the economic activity for the second quarter.

The growth of **total trade**, also continued during April and is due to the growth of wholesale trade, whereas retail trade and motor vehicle trade registered a decline.

Contrary to the positive movements in trade, **the industrial output** continued to hover in the zone of negative values at the beginning of the second quarter, which is mainly due to the weaker activity in the manufacturing industry, while the activity

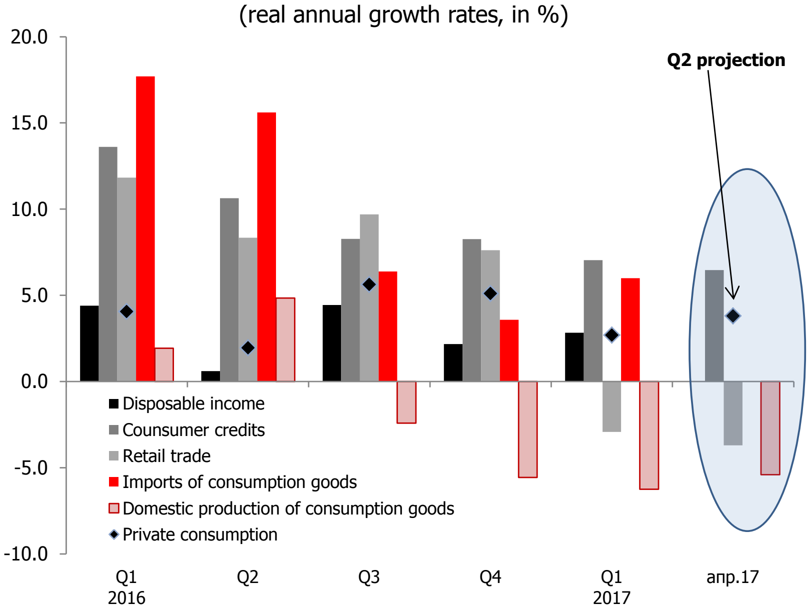
[11] In the first quarter, the added value has decreased in construction, "financial and insurance activities", cumulatively, in the activities "public administration and defense, "compulsory social security", "education", "health and social care", as well as in "arts, entertainment and recreation", "other services", "activities of households as employers" and "activities of households that produce commodities and provide services for own purposes".

in mining and energy sector register a small growth.

Considering the individual sectors within the manufacturing industry, decline in production was registered in most sectors, while the highest negative contribution accounts for clothing production and electric equipment production. The production decline was mitigated to a certain extent with the growth registered in the production of tobacco products, production of other non-metal products and production of motor vehicles, trailers and semi-trailers, as well as production of fabricated metal products.

The number of high frequency data for **private consumption** in the second quarter of 2017 is relatively small, and also the available data indicate divergent movements, making it difficult to give a precise conclusion for the shifts in the second quarter.

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



Source: SSO and NBRM calculations.

Thus, lending to the households continued to increase, as well as the increase of part of the components of the available income (pensions and social transfers of the government) continued.

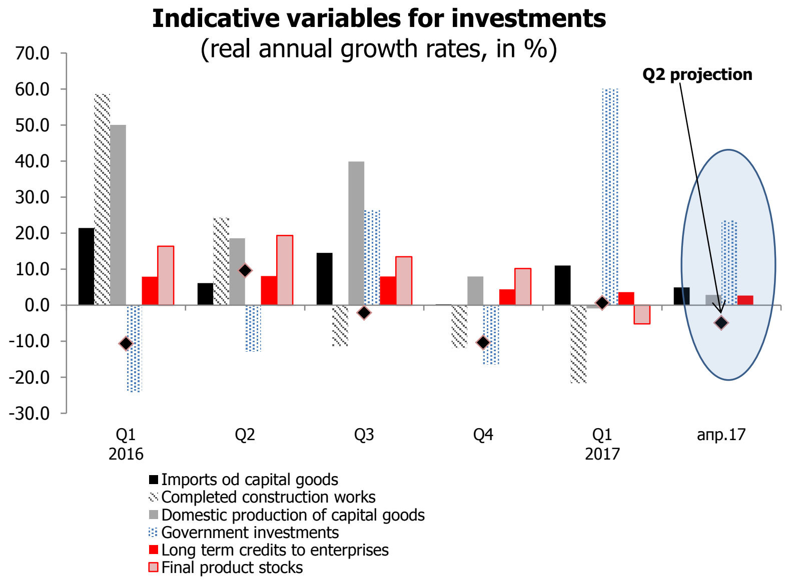
On the other hand, the turnover in retail trade continues to register a decrease, and the domestic production of consumer goods and import of consumer goods registers a decline.

The small number of available short-term indicators of **investment activity** points to investments growth in the second quarter of 2017...

....amid higher government capital investments and import of capital goods, as well as further growth of long-term lending to the corporate sector.

At the same time, in April, domestic production of capital goods register a growth on an annual basis.

In April 2017, the data on **foreign trade** show narrowing of the trade deficit...

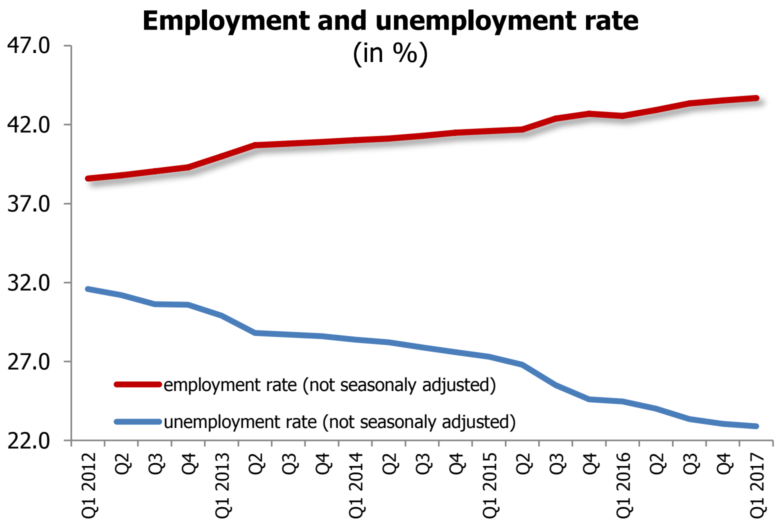


Source: SSO and NBRM calculations.

...amid higher nominal growth in exports compared to imports of goods and services.

Pursuant to the April budget financial data, **public consumption** registers growth, amid increase in expenditures for wages in the public sector...

...and higher expenditures for goods and services and health care transfers.



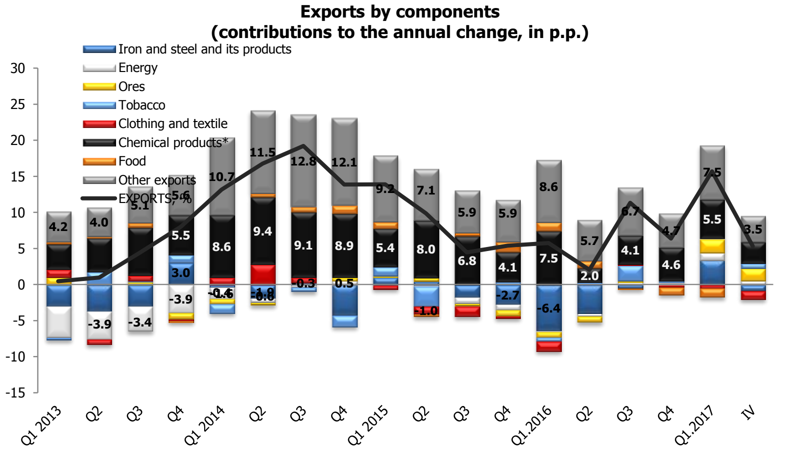
Source:SSO, LFS

The favorable labor market developments continued in the first quarter of 2017...

...given further decline in the unemployment rate, which in the first quarter it was reduced to 22.9% (23.1% in the fourth quarter of 2016)...

...and annual increase in the number of employed persons of 2.7%[12].

[12] Sectors trade and transport registered the highest increase.



Source: NBRM.

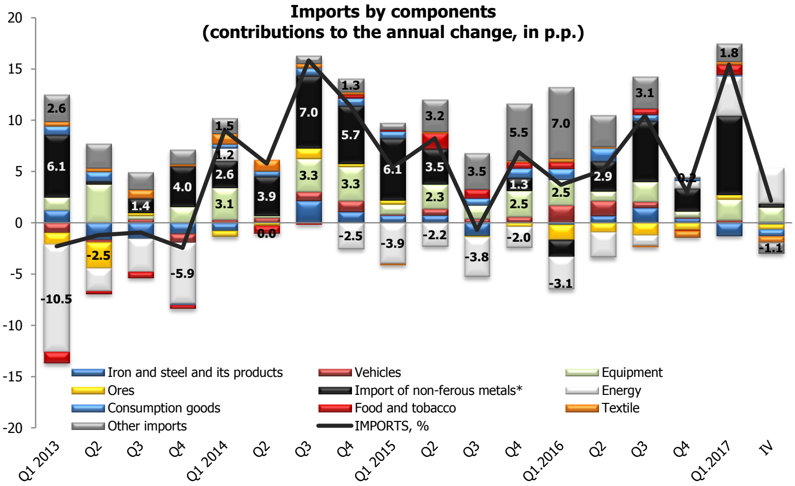
In April 2017, the foreign trade deficit registered a moderate narrowing on an annual basis, given higher increase in the import than the export component.

In April 2017, the **export** of goods registered an annual growth of 5.3%, largely due to the performance in the new export-oriented facilities in the economy, and less in the export of ore and other export...

...given simultaneous moderate fall in the export of clothing and textile and iron and steel.

In April 2017 the total export was within the expectations in the April projection. Positive deviations are registered in most of the export branches...

...amid downward deviations in export of iron and steel.



Source: NBRM.

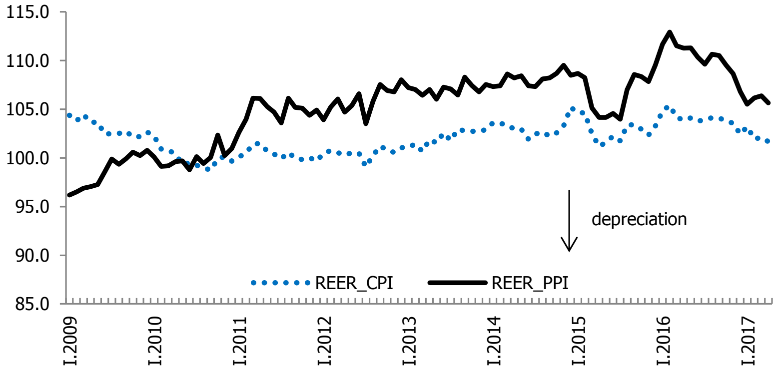
Import of goods in April 2017 registered a moderate annual growth, primarily due to the growth of import of energy, but also to the growth of the imports of equipment and machinery...

...amid moderate decline of the other import, import of clothes, consumer goods and ores.

Import of goods in April suggests lower than forecasted performances for the second quarter. Observed by categories, is mostly due to the downward deviations in part of the new export-oriented industrial facilities, which could be of a temporary character.

The exports and imports in April point to a performances in export within the projection for the first quarter according to the April projection and somewhat lower performances in the import component.
However, the evaluation period is too short and therefore reliable conclusions in this domain cannot be drawn.

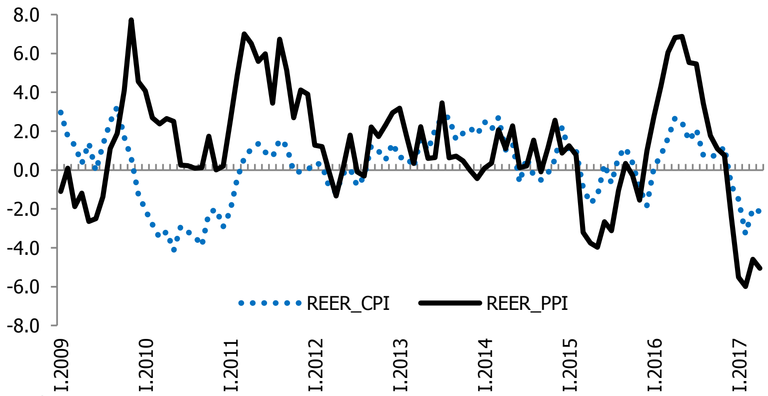
REER
(2010=100)



Source: NBRM.

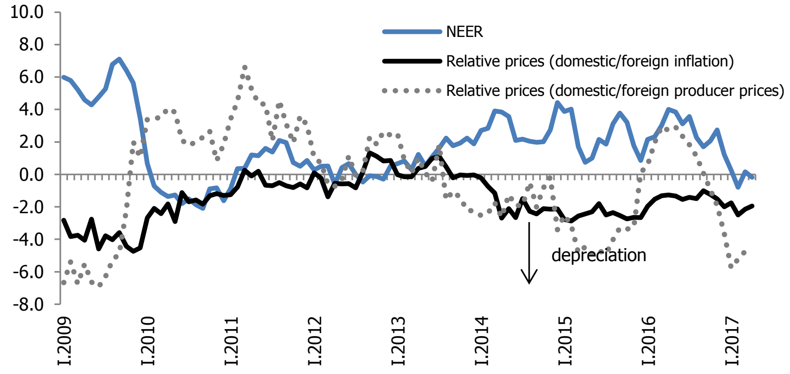
The favorable developments **in price competitiveness indicators of the domestic economy that started in December 2016, also continued in April 2017, analyzed on an annual basis.** The REER index deflated by consumer prices depreciated by 2.1% and the REER index deflated by producer prices registered larger depreciation of 5.1%.

REER
annual changes, in %



Source: NBRM.

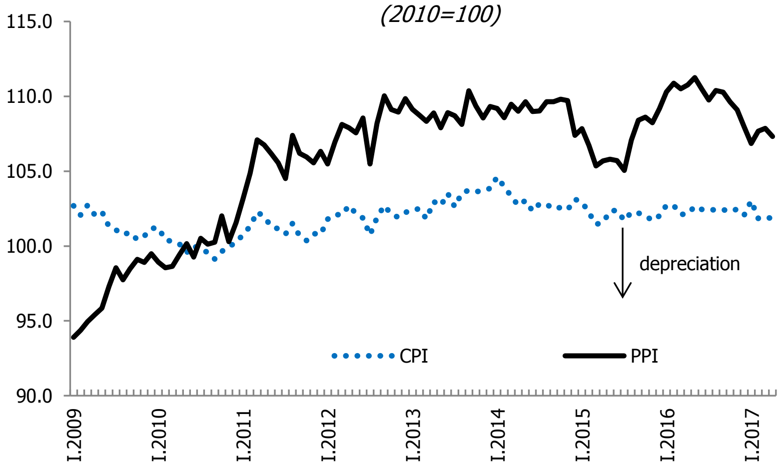
NEER and relative prices
annual growth rates, in %



Source: NBRM.

These developments are largely due to favorable movements in relative prices, and the relative prices of industrial products decreased by 4.9%, while the relative cost of living by 2.0%. The NEER acted in the same direction but more moderately, registering a slight depreciation of 0.2% annually, mostly as a result of the appreciation of the Russian ruble and the US dollar, given the depreciation of the Turkish lira and the British pound.

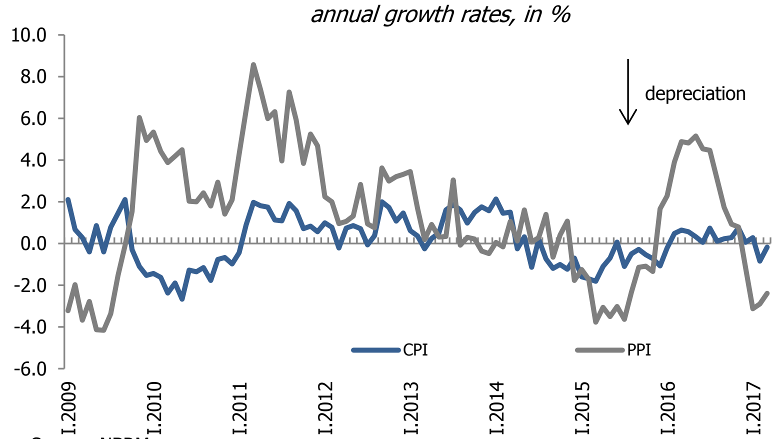
REER, excluding primary commodities
(2010=100)



Source: NBRM.

In April 2017, the analysis of **REER indices, as measured using weights based on the foreign trade without primary commodities**[13], also shows similar movements but at a more moderate intensity. The REER index deflated by consumer prices depreciated by 0.2%, while the REER deflated by producer prices depreciated by 2.4%.

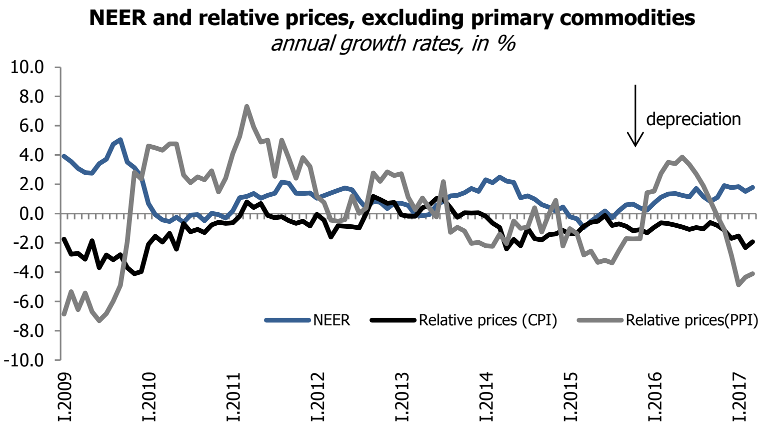
REER, excluding primary commodities
annual growth rates, in %



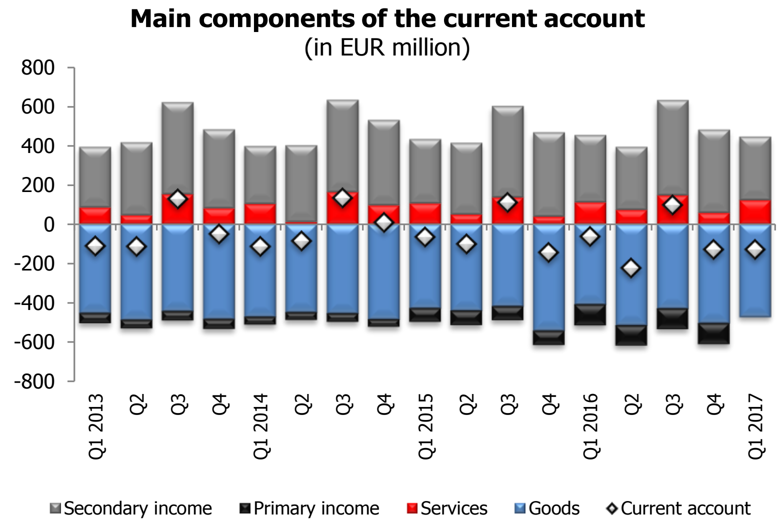
Source: NBRM.

On an annual basis, the relative consumer prices and the relative producer prices decreased by 1.9% and 4.1%, respectively. The NEER has appreciated by 1.8% on an annual basis.

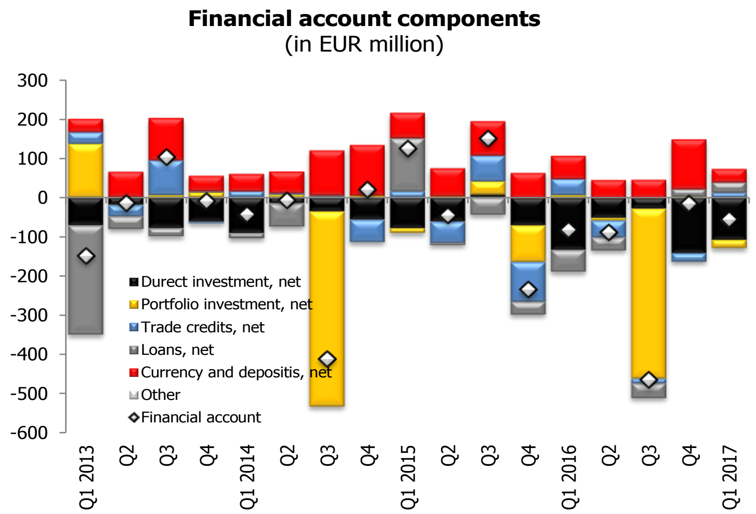
[13] Primary commodities not included in the calculation are: oil and oil derivatives, iron and steel, ores and imported raw materials for the new industrial facilities in the free economic zones.



Source: NBRM.



Source: NBRM.



Source: NBRM.

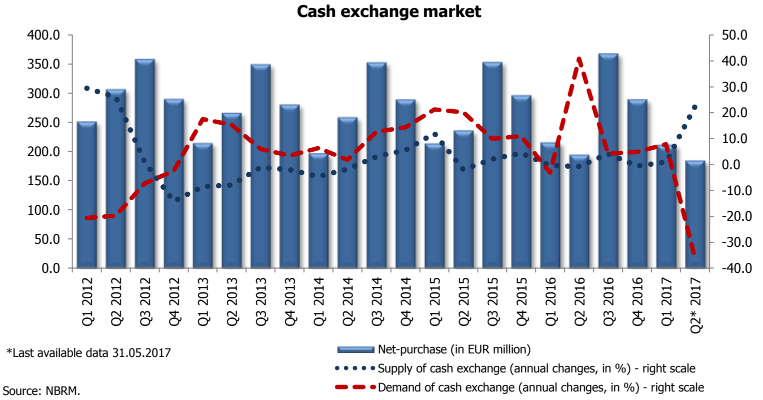
In the first quarter of 2017, the balance of payments' current account has registered a deficit of Euro 125.5 million (or 1.2% of GDP), which is higher than envisaged in April projection.

The deviation is mostly driven by the balance of goods and services, where a higher deficit than the projected is registered, while in primary income the performances are better than the expected.

In the financial account, during the first quarter of the year, net inflows of Euro 54.1 million (or 0.5% of GDP) have been registered, compared to the expectations for more moderate positive flows on net basis pursuant to the April projection[14].

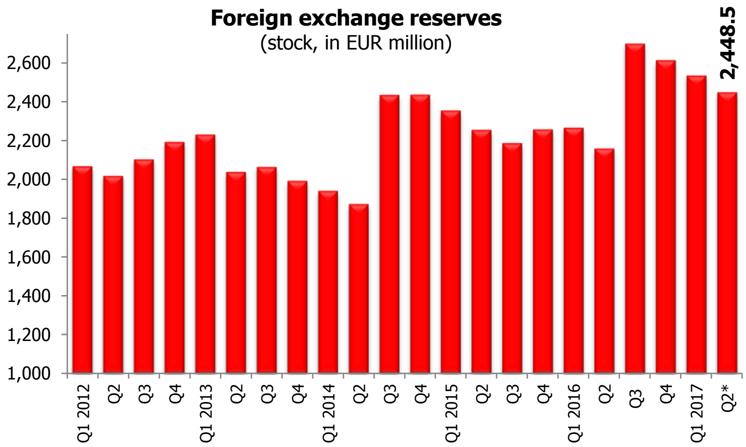
The positive deviations are especially evident in the foreign direct investments, where during the first quarter higher net inflows on net basis have been registered. Additionally, net inflows have been registered in portfolio investments, compared to the expectations for small net outflows. On the other hand, performances in other financial flows are weaker in relation to the April projections for the first quarter, with the exception of currency deposits, where the performed net outflows are on the projected level.

[14] According to the new methodology for compilation of the balance of payments BPM6, the terms net inflows and net outflows denote net incurrence of liabilities and net acquisition of financial assets, respectively.



*Last available data 31.05.2017

Source: NBRM.



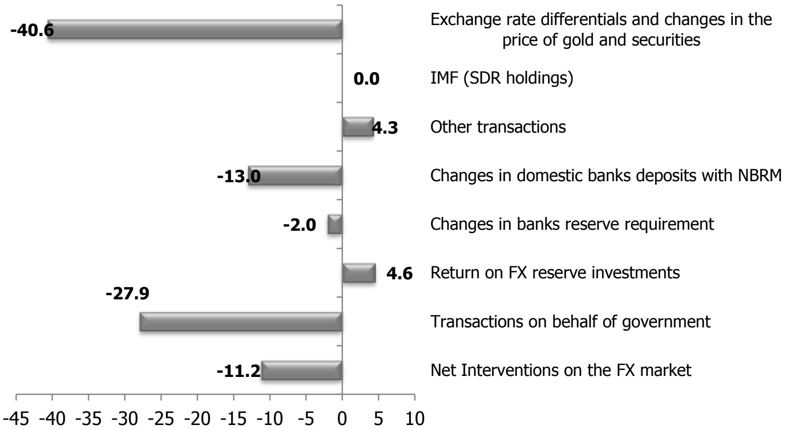
* last available data 31.05.2017
Source: NBRM.

Recent data on currency exchange operations as of May 2017 indicate a high annual increase in the supply and high decline in the demand for foreign currency.

The net purchase on the currency exchange market registered within April - May period equaled Euro 149 million, which is an annual increase of 80.1%. Such developments are due to the comparative base of the previous year, period when due to the political crisis there were pressures in the currency exchange market through decrease of the supply for foreign currencies and high growth of the demand for foreign currency.

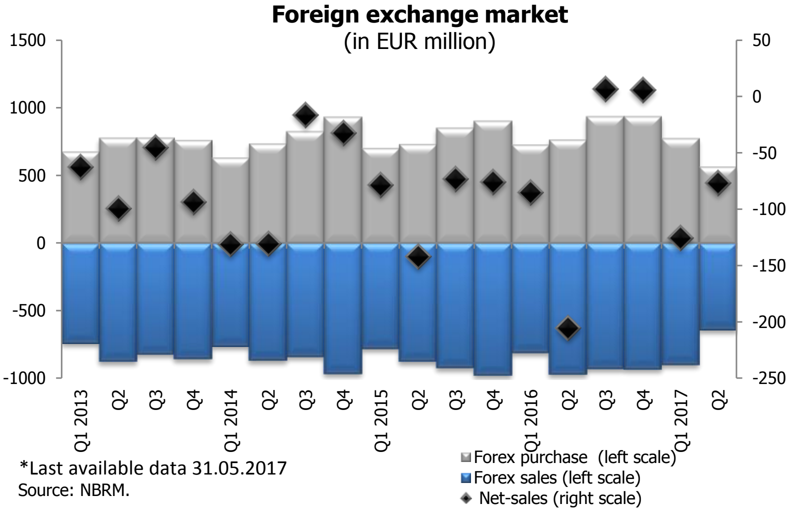
As of 30 May 2017, the gross foreign reserves stood at Euro 2448.4 million, which is a decrease by Euro 85.8 million compared to the end of the first quarter of 2017. The decrease in foreign reserves is primarily due to the changes in the category currency changes and change in the price of gold, as well as from the transactions for the account of the government. Additionally, the NBRM's interventions on the sales in the foreign exchange market as well as on the category others has a small negative impact, which also includes the decrease of foreign currency deposits of the domestic banks with the NBRM.

Factors of change of the foreign reserves in April - May 2017
(in EUR million)



Source: NBRM.

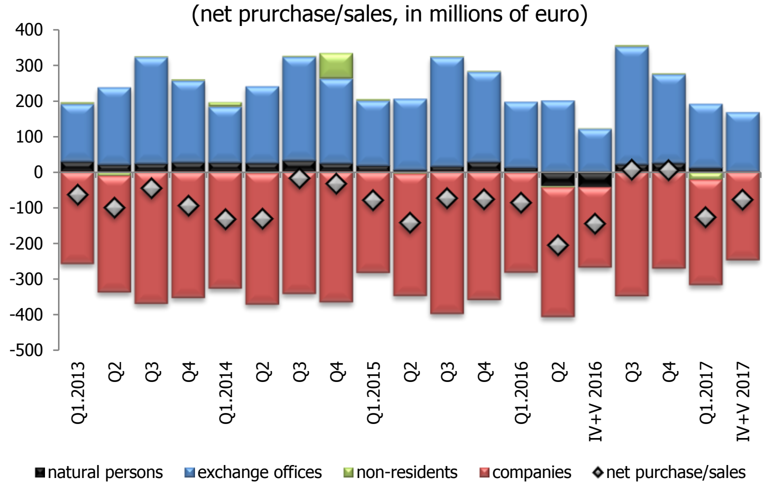
Foreign exchange market
(in EUR million)



*Last available data 31.05.2017
Source: NBRM.

In the period April - May 2017, the foreign exchange market of banks a net sale of Euro 76.2 million was registered, by Euro 68.3 million lower compared to the same period last year. Such annual change was due to the increased supply of foreign currency, given unchanged demand of foreign currency.

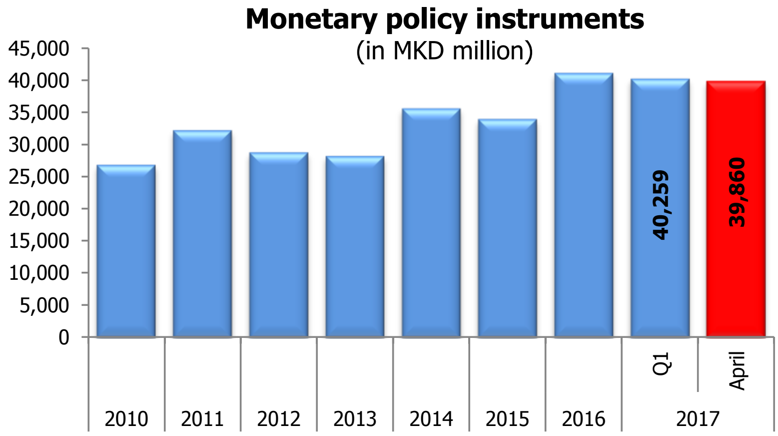
Structure of foreign exchange market,
(net prurchase/sales, in millions of euro)



Source: NBRM

Sector-by-sector analysis show that such changes are mostly due to the increased net purchase in exchange offices, as well as the registered low net purchase in natural persons (unlike the performed net sale in the same period of the previous year). Contrary to these shifts, net sale in companies registered a moderate increase.

The situation regarding monetary instruments[15] in April is moderately lower compared to the end of the first quarter. Such performances are in accordance with the expectations for creating liquidity through monetary instruments in the second quarter of 2017, pursuant to the April projection.

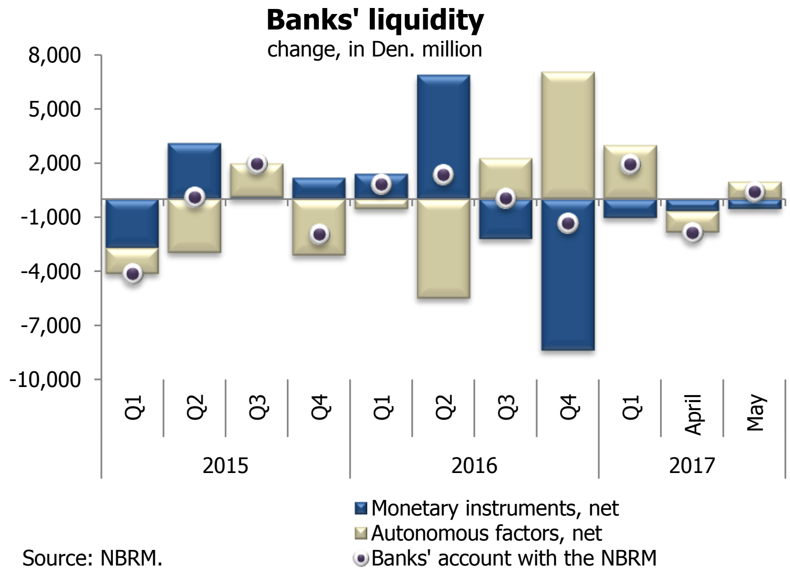


Source: NBRM.

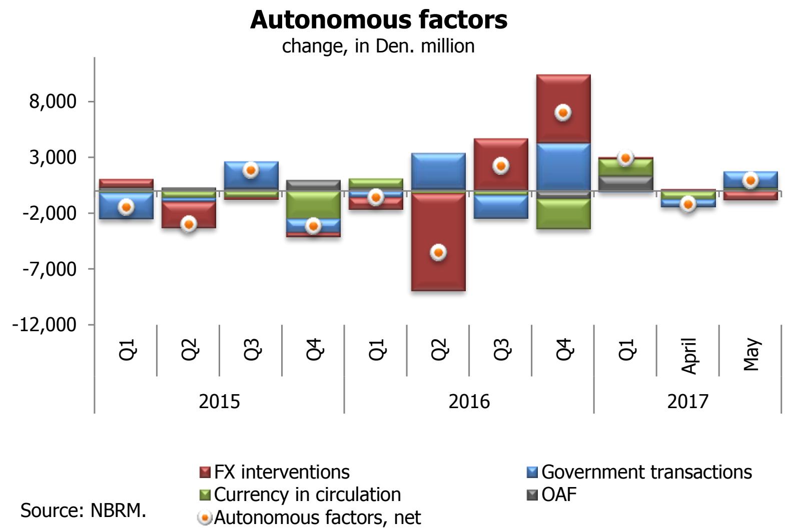
Viewed from the balance sheet perspective, in April net foreign assets of the NBRM decreased compared to the end of the first quarter, which is in accordance with the expectations for the second quarter, pursuant to the April projection. On the other hand, total deposits of the government at the end of April remained at a relatively stable level compared to the end of the first quarter of the year, whereas with the April projection this balance category is projected to register a decline in the second quarter.

In April, reserve money registered a decline on a monthly basis, entirely due to the lower banks' reserves with the NBRM, whereas currency in circulation registered a monthly increase. In terms of the projected changes for the second quarter, reserve money is expected to increase, amid simultaneous growth in both constituting categories.

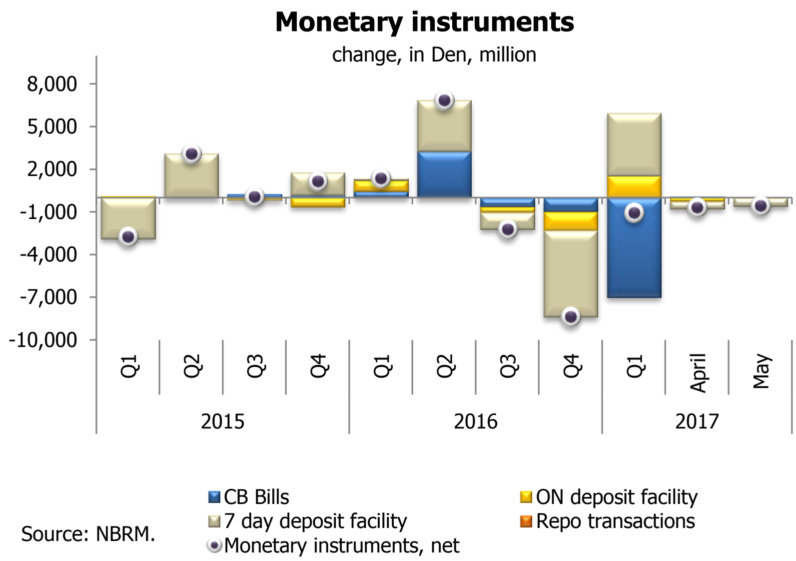
[15] It includes also the balance of the foreign currency deposits.



Source: NBRM

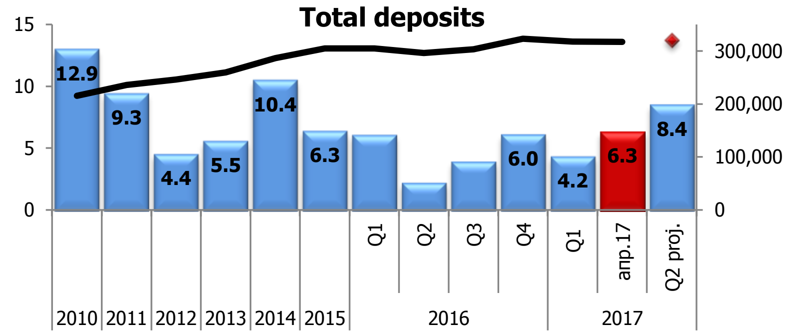


Source: NBRM



* Changes in monetary instruments in terms of liquidity creation / withdrawal.
Source: NBRM

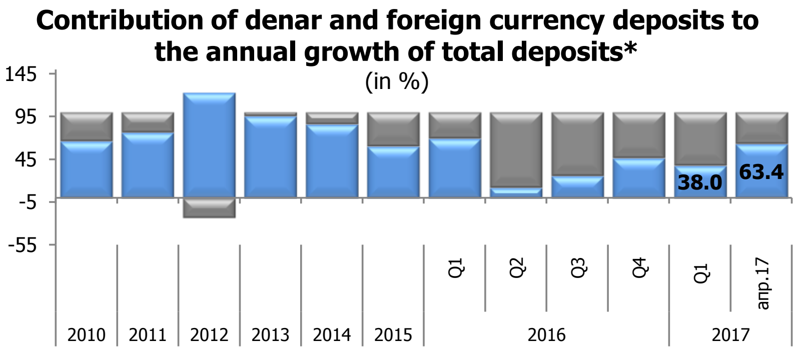
According to operational liquidity data, in May, the liquidity of the banking system registered a monthly increase. The increase in liquidity during this period was impacted by autonomous factors, primarily of the government transactions, which conditioned increased banks' interest to place part of excess liquid assets in short-term deposits with the NBRM. (7 days)



*Includes demand deposits
Source: NBRM.

In April, total deposits similar to the previous month registered a moderate monthly decline. Observed by sectors, the monthly decline (of 0.3%) in April, is almost equally is due to the decline in deposits of both sectors (corporate and household). In terms of currency structure, a decrease is registered in denar deposits and foreign currency deposits, whereby the decline in denar deposits is relatively high.

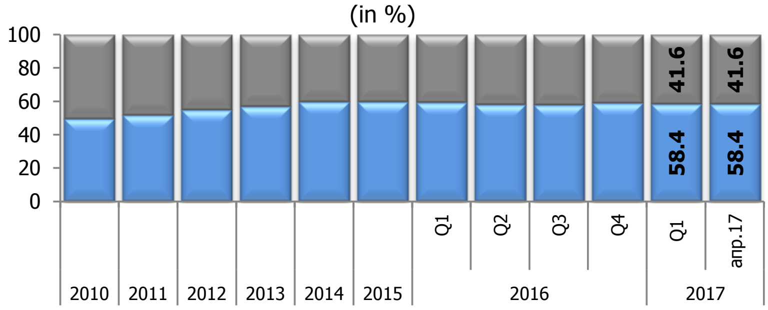
The annual growth rate of total deposits in April was 6.3% (4.2% in March) and is below the growth projected for the second quarter of 2017 (of 8.4%) with the April projection. Thus, the higher annual performance in April, compared to the previous month arises from the base effect, taking into account the significant decrease in the banks' deposit base at the end of April 2016 due to the political events in the country.



*includes demand deposits and denar deposits with F/X clause
Source: NBRM.

In terms of currency structure, the annual growth of total deposit results from denar deposits. Thus, the contribution of denar deposits in the annual growth amounts to 63.4%, which observed dynamically is a increase compare to the previous month.

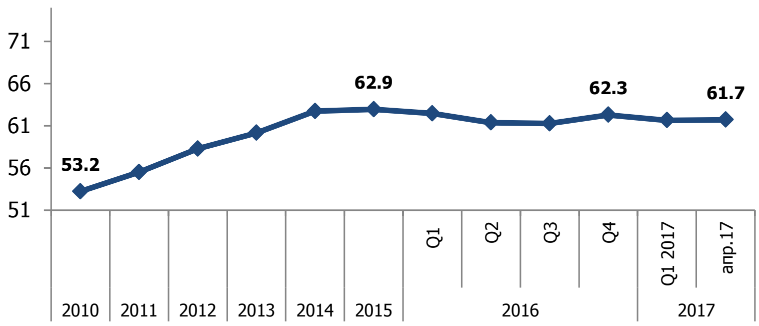
Share of denar and foreign currency deposits in total deposits
(in %)



*includes demand deposits and denar deposits with FX clause.
Source: NBRM.

The share of Denar deposits in total deposits in April remained relatively stable compared to the previous month, whereby Denar deposits continued to prevail in the banks' deposit base.

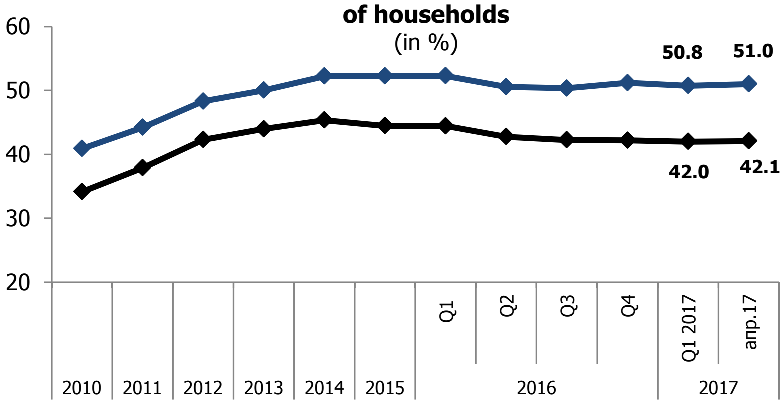
Share of Denar M4 in total M4
(in %)



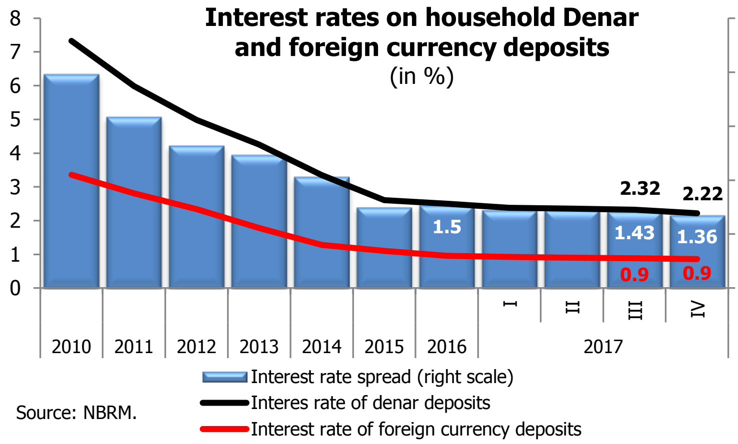
Source: NBRM.

Total household deposits in April, decreased, but to a lesser extend compared to the previous month. By currency, the decrease in household deposits is almost completely due to the lower foreign currency deposits, amid more significant growth in the denar deposits. As a result of such developments, the share of denar deposits in total household deposits increased in April.

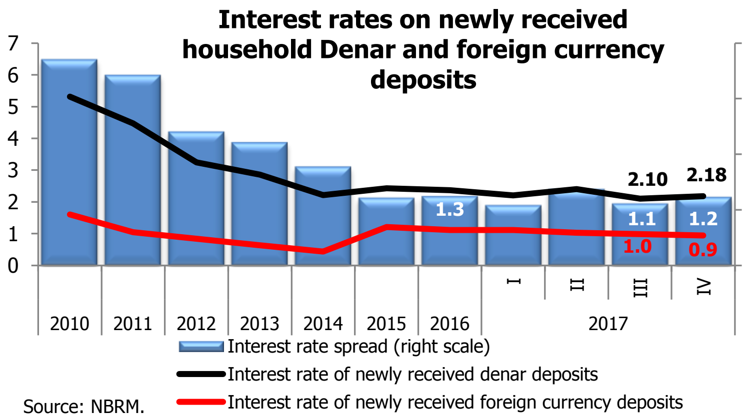
Share of Denar deposits of households in total deposits of households
(in %)



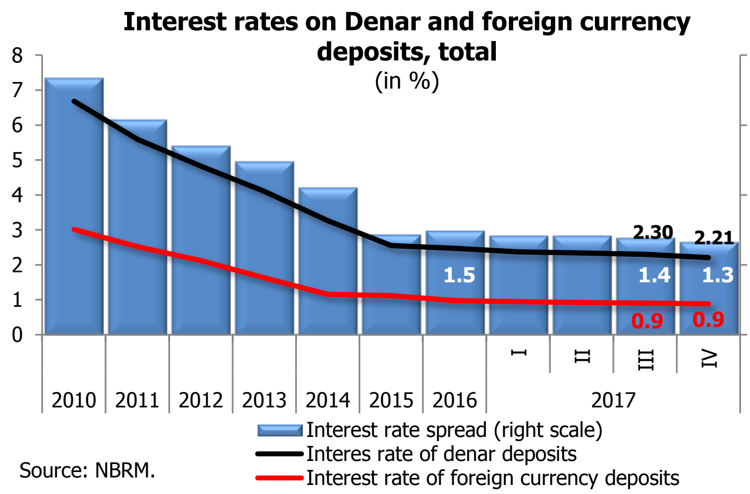
Source: NBRM.



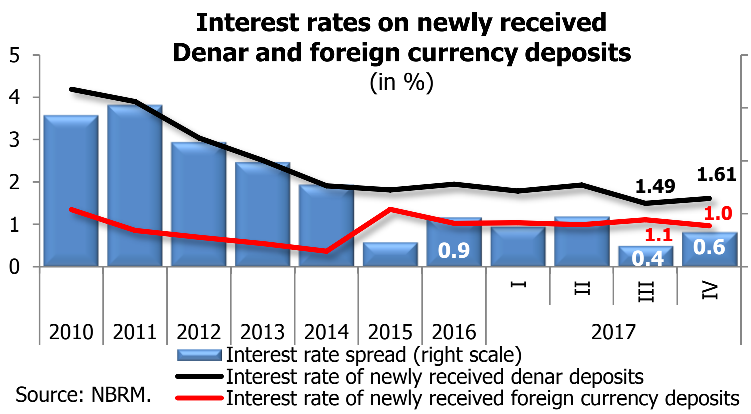
Source: NBRM.



Source: NBRM.



Source: NBRM.

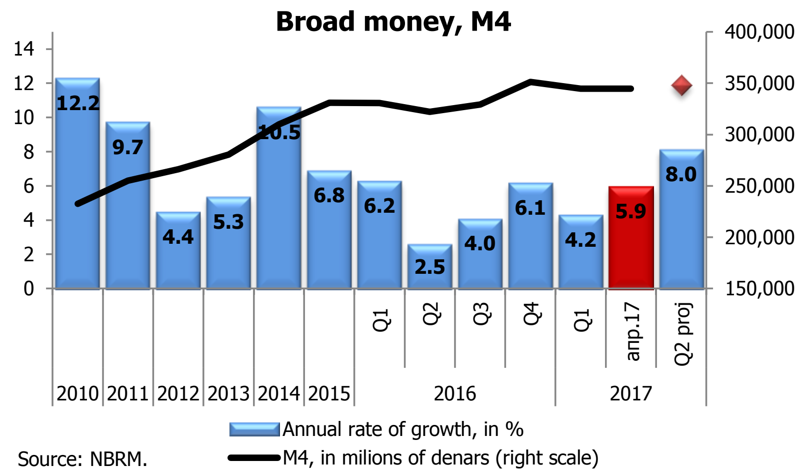


Source: NBRM.

The interest rates on household deposits in April registered a minimal decline of the interest rates on denar deposits compared to the previous month, which conditioned a moderate narrowing of the interest spread between denar and foreign currency interest rates. Interest spread of **new household deposits** has widened as a result of the increase in the interest rate on Denar deposits, amid simultaneous minimal decrease in the interest rate on foreign currency deposits.

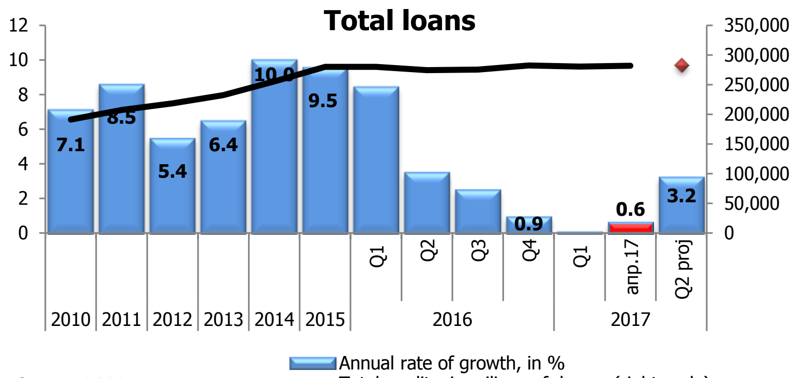
In April, **interest rates on total deposits** registered a moderate decline in the interest rate on denar deposits compared to the previous month, which amid relatively stable level of interest rates on foreign currency deposits conditioned narrowing of the interest spread between denar and foreign currency interest rates. **In newly accepted total deposits**, the interest spread between denar and foreign currency deposits, in April widened compared to the previous moth due to the higher interest rate on newly accepted denar deposits and reduced interest rate on newly accepted foreign currency deposits. However, regarding the interest rates on the newly accepted deposits, the characteristic variable movements should be kept in mind[16].

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



Source: NBRM.

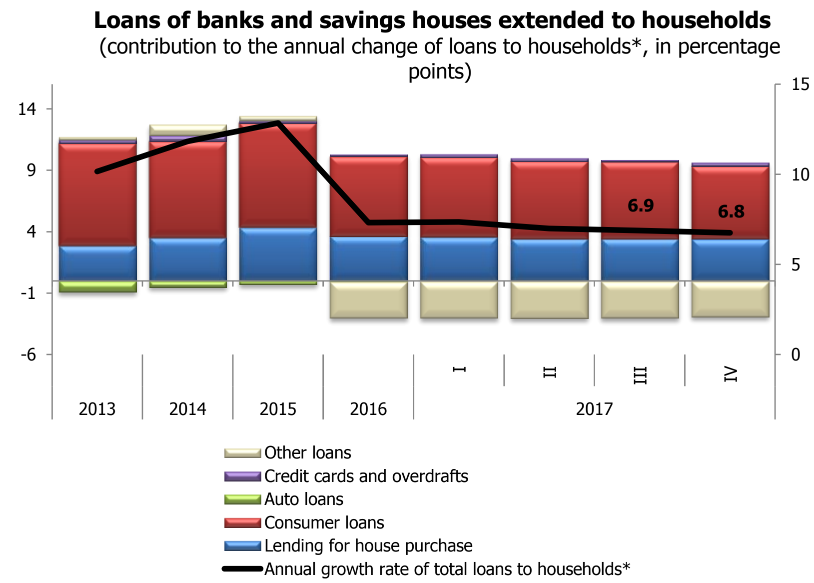
During April, the broadest money M4 remained at a relatively stable level. Amid relatively higher growth of currency in circulation from the total deposits decline, broad money in April registered a small growth. **On an annual basis, broad money is higher by 5.9%,** which reflects the lower base effect due to the political instability in the country in April last year. Thus, the registered annual growth is below the projected of 8.0% for the second quarter of 2017, pointing restraints in savings of the economic agents.



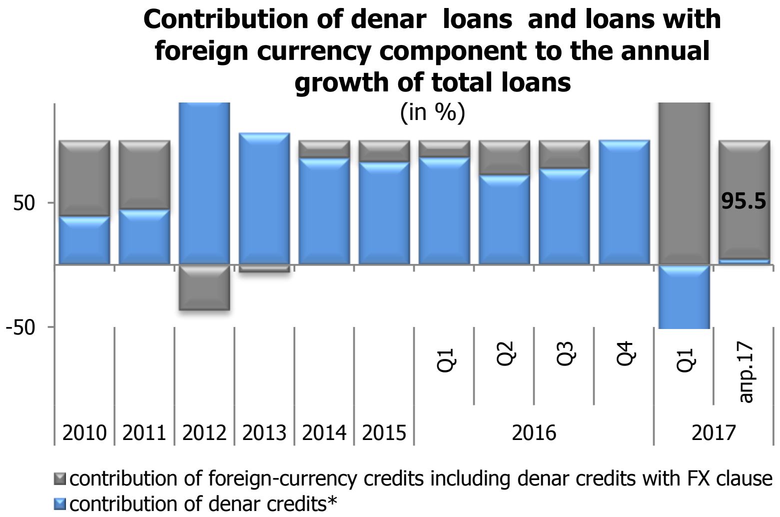
Source: NBRM.

In April, total loans to the private sector registered a monthly increase, but more moderate compared to the previous month. Analyzed by sectors, the monthly increase of the total credit activity (of 0.6%) arises from the higher performances in both sectors (corporate and household).

On an annual basis, total loans at the end of April increased by 0.6%, which is below the projected growth of 3.2% for the second quarter of 2017, according to the April projection. If we exclude the regulatory effect, the annual growth rate of total loans is 6.3% and is above the projected annual growth of 4.5% for the second quarter of 2017.

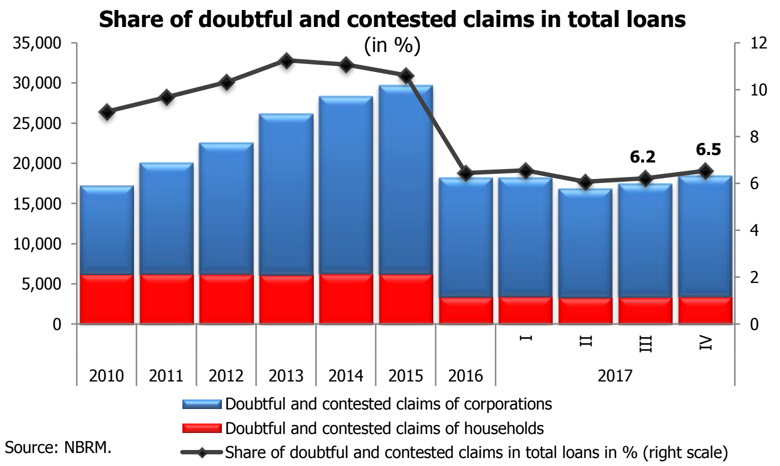


*Total loans to households do not include loans to self-employed individuals. Source: NBRM.



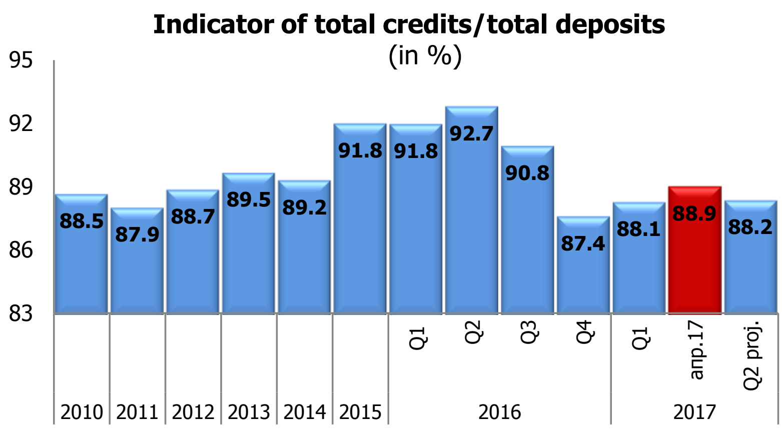
* does not include Denar credits with FX clause. Source:NBRM.

In terms of currency, the annual growth of total loans is entirely due to the growth of foreign currency loans including denar loans with FX clause, whereas denar loans[17] have a small positive contribution of 4.5% to the annual currency change.



Source: NBRM.

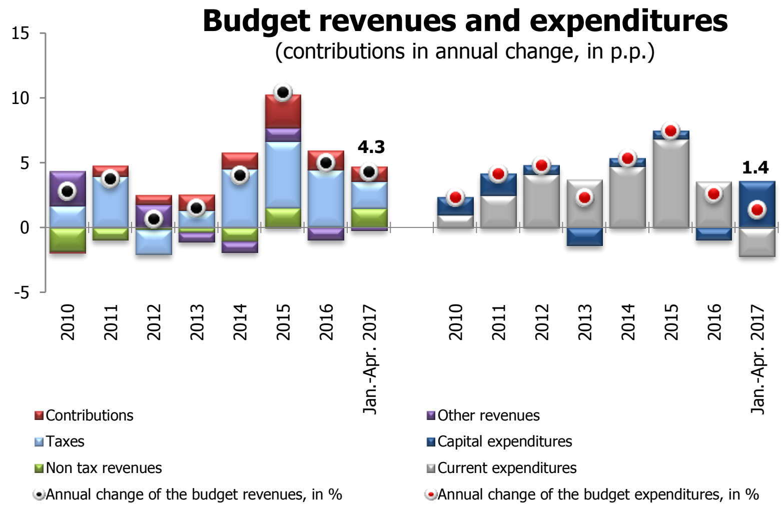
The share of doubtful and contested claims in total loans equaled 6.5% in April and increased by 0.3 p.p. compared to the previous month.

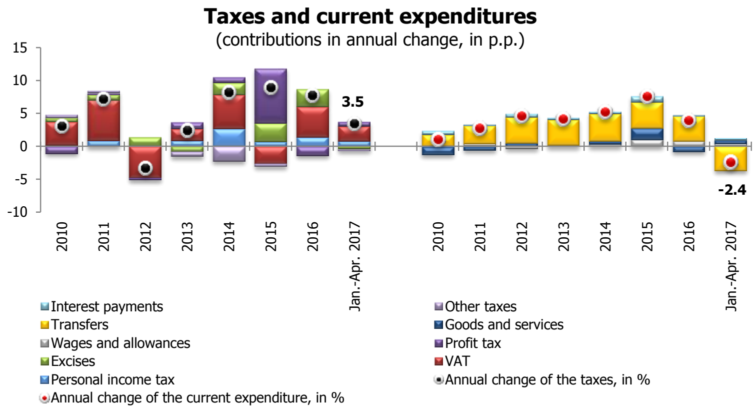


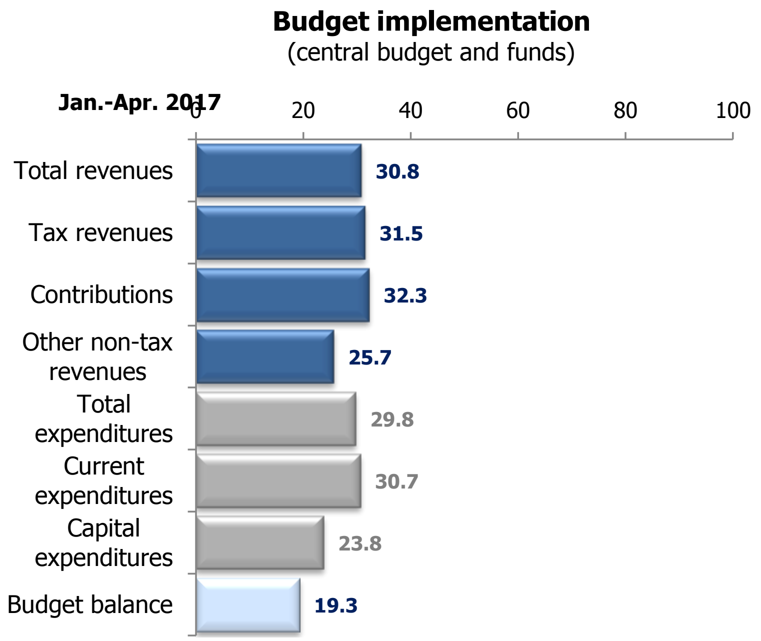
Source: NBRM.

Utilization of the deposit potential for lending to the private sector at the end of April amounted to 88.9% and is higher compared to the previous month (88.1%). April performance is higher compared to the expectations for the second quarter of 2017, according to the April projection. Excluding the effect of regulatory write-off, the ratio of loans and deposits at the end of April is 94.4%.

[17] Includes denar loans without FX clause, accrued interest and doubtful and contested claims.







Source: Ministry of Finance and NBRM's calculations.

In the period January-April 2017, the total revenues realized in the Budget of the Republic of Macedonia (central budget and budgets of funds) increased by 4.3% compared to the same period last year. The improved performances mostly arise from the positive contribution in taxes, non-tax revenues and contributions, while other revenues made a small negative contribution to the annual growth.

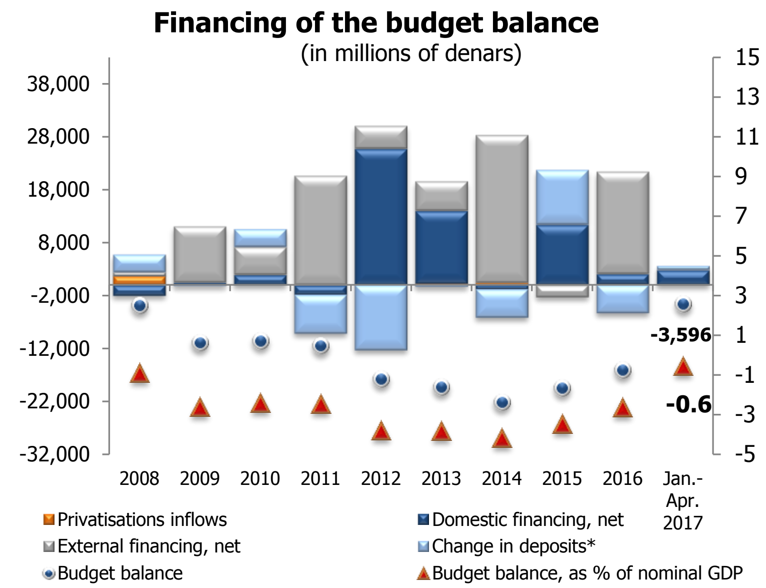
Tax revenues in January-April 2017 increased by 3.5% on an annual basis, largely due to higher performance of VAT, while moderate positive contribution was also made by the income from the profit tax and the personal income tax and import duties. On the other hand, revenues based on excise recorded an annual decrease.

In the period January-April 2017, the budget expenditures increased by 1.4% on an annual basis, which mostly arises from the higher capital expenses on an annual basis, while current expenditures are lower on an annual basis.

In January-April 2017, the realized budget revenues constitute 30.8% of the revenues projected for the entire year, according to the Budget for 2017. Analyzed by categories, higher performance was recorded in contributions and taxes (of 32.3% and 31.5% respectively), while the realization of other non-tax revenues accounted for 25.7%.

Analyzing budget expenditures, in the period January-April 2017, 29.8% of the planned expenditures for 2017 were realized, which is mostly due to the realization of the current costs (30.7% of the annual plan), while the realization of the capital expenditures is relatively lower (23.8% of the annual plan).

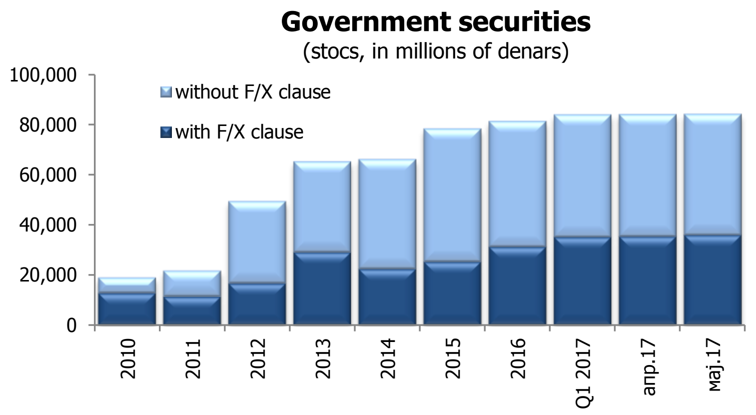
The budget deficit in January-April 2017 accounts for 19.3% of that planned deficit for 2017.



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

In the period January-April 2017, the Budget of the Republic of Macedonia registered **a deficit of Denar 3.596 million, which is 0.6% of the nominal GDP**[18]**.**

The deficit was mostly financed through the net issuance of government securities and to a lesser extent through deposit withdrawal from the account with the National Bank.

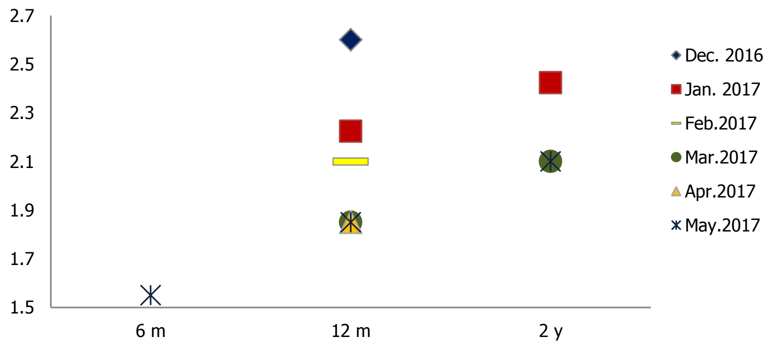


Source: NBRM.

The stock of issued government securities in the domestic market amounted to Denar 84,195 million in May 2017 and compared to the end of 2016 is higher by Denar 2,824 million.

[18] The analysis uses the NBRM April projections for the nominal GDP for 2017.

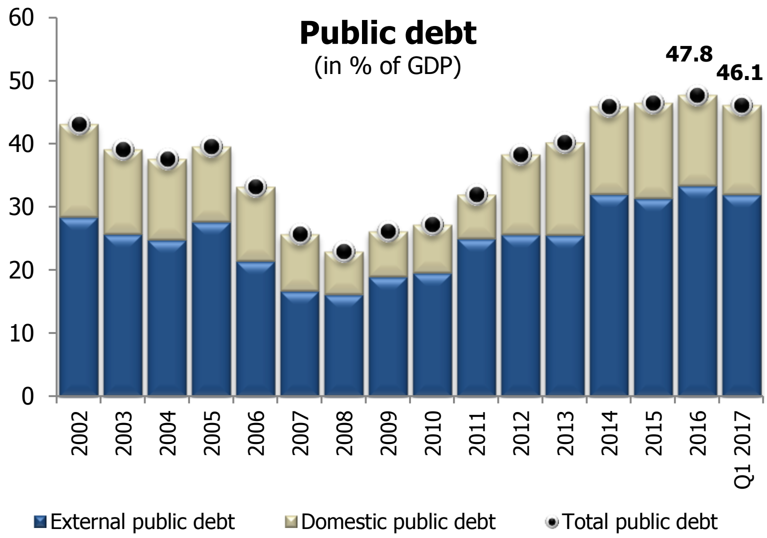
Interest rates of government securities in domestic currency (realized)



Source: Ministry of finance

In May 2017, the Ministry of Finance[19], kept the interest rates on government securities unchanged.

Compared to the end of the previous year, the interest rates on treasury bills with maturity of 6 and 12 months are lower by 0.75 percentage points in May. Also, the interest rates on government bonds with maturity of 2 years are lower by 0.3 percentage points in May compared to January 2017.



Source: NBRM's calculations based on data from the Ministry of Finance.

At the end of 2017, total public debt[20] equaled 46.1% of GDP[21], which is a quarterly decrease of 1.6 percentage points compared to the end of 2016. The change largely stems from the reduction in external debt (from 33.3% to 31.9% of GDP), amid moderate decline of the domestic debt (from 14.5% to 14.2% of GDP). Total government debt and public corporate debt are lower by 1.2 p.p and 0.4 p.p of GDP, respectively, compared to the end of 2016.

[19] At the auctions of government securities in May, there was an offer of 6- month and 12-month treasury bills without FX clause, 2-year bonds without FX clause and 12- month treasury bills with FX clause and 15-year government bonds with FX clause.

[20] The public debt is defined under the Law on Public Debt (Official Gazette of the Republic of Macedonia No. 165/14) according to which it is the sum of the government debt and the debt of public enterprises established by the state or municipalities, municipalities within the city of Skopje and the city of Skopje, and companies that are entirely or predominantly owned by the state or by the municipalities, the municipalities within the city of Skopje and the city of Skopje, for which the Government has issued a state guarantee.

[21] The analysis uses the NBRM April projections for the nominal GDP for 2017.

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 on reducing CB bill interest rate was adopted to cut the policy rate from 3.5% to 3.25%. At the same time, the interest rate on seven-day deposit facility was cut from 1.75% to 1.5%.

- A Decision amending the Decision on reserve requirement was adopted, which reduces the reserve requirement rate for banks' liabilities in domestic currency from 10% to 8% and increases the reserve requirement rate for liabilities in foreign currency from 13% 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[22], 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.

[22] For the method of determining the potential demand for CB bills see the Decision on CB bills, Official Gazette of the Republic of Macedonia No. 166/13).

September 2014

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

October 2014

– A Decision on reducing the interest rate on overnight deposit facility from 0.75% to 0.5% and on seven-day deposit facility from 1.25% to 1% was adopted.

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.

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, untill 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 current negative interest rates prevailing 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 Bazel 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 core and additional capital, **but the new Decision changes the structure of the core capital, which is divided into regular core capital and additional core capital.** The regular core 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 core capital, includes instruments which, among other things, contain a clause for their transformation into instruments of the regular core capital or for their write-off on temporary or permanent basis (reduction of 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 regular core capital, core capital and own funds,** i.e. 4.5% for the regular core capital, 6% for the core capital and 8% for the own funds of the risk-weighted assets. Thus, the greatest importance is given to the regular core capital positions (shares, reserves, retained undistributed profit), as capital positions with the highest quality.

January 2017

- At the regular meeting of the NBRM's Operational Monetary Policy Committee, held on 10 January 2017, the 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 the regular meeting of the NBRM's Operational Monetary Policy Committee, held on 14 February 2017, the 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. core 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 the regular meeting of the NBRM's Operational Monetary Policy Committee, held on 14 March 2017, the Committee decided to increase the supply of CB bills from Denar 25,000 million to Denar 30,000 million.