National Bank of the Republic of Macedonia

MONETARY POLICY AND RESEARCH DEPARTMENT

Recent Macroeconomic Indicators
Review of the Current Situation

September 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 (April–August 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.

In the period since April, economic indicators continued to indicate a continuous increase in global economic activity, which led to increased optimism regarding the global growth forecasts. However, the main negative risks surrounding the global growth in the next period are still present, and they particularly refer to the possible increased protectionism worldwide, the uncertainty around the possible effects of Brexit, the effects of the possibly greater preferences of the central banks in the developed countries for monetary tightening, the possible financial market volatility, as well as the increased geopolitical risks. The strengthening of the activity in the euro area, among other things, also made a positive contribution to the growth of the global economy, whereby the achieved growth synchronization among all regional countries is particularly emphasized. According to the preliminary data, the annual growth of the real GDP of this our most significant partner accelerated to 2.3% in the second quarter of 2017 (from 2% in the first quarter), which is the highest performance since the beginning of 2011. Additionally, the high frequency data and the surveys on the economic sentiment of both economies and households indicate further solid growth in the third quarter, which increases the optimism about the economic prospects of the euro area. Hence, in September, the ECB made an upward revision of the forecasts regarding the growth of the euro area for 2017[1], whereby the risks are assessed as mainly balanced. Noting that the inflation situation continues to impose a need for a significant level of monetary accommodation, the ECB did not make changes in the monetary policy setup, although it repeated its willingness for its adjustment if the inflation prospects or the financial conditions change in the next period. However, it is a news that the ECB used the communication tool to announce that the decision on the setup of its instruments will be made at one of the meetings that will be held this autumn. The positive trends in the real economy are accompanied by further improvement of the labor market conditions. The unemployment rate continued to decline, and reduced to 9.2% in the second quarter, compared to 9.5% in the first quarter. In the first month of the third quarter, however, the unemployment rate was stable, at the level of June (9.1%). Inflation data show its acceleration in August, to a level of 1.5% on an annual basis, versus 1.3% in July. This performance is entirely due to the intensified growth of the energy prices (of 4%), while food and core inflation are unchanged, at the level of 1.4% and 1.2%, respectively. The ECB September forecasts show small downward revisions in inflation in 2018 and 2019, mainly as a result of the appreciation of the euro exchange rate, while the forecast for 2017 did not change[2]. Considering the latest macroeconomic developments and estimates, economic analysts expect that the ECB will begin to gradually reduce the quantitative monetary stimulus at the beginning of 2018, but that it will continue to keep the stimulating interest rate policy. Hence, in 2017 and 2018, **EURIBOR** is expected to follow a similar upward path as in the April forecasts, and will continue to be maintained in the negative zone throughout the entire forecast horizon.

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[1] According to the latest ECB's forecasts, the growth rate of real GDP for 2017 is projected at 2.2%, versus 1.9% in June, while the forecasts for 2018 and 2019 remain the same (1.8% and 1.7%, respectively).

[2] The latest inflation forecasts are 1.5%, 1.2% and 1.5%, for 2017, 2018 and 2019 respectively, compared to the June forecasts for these years of 1.5%, 1.3% and 1.6%, respectively.

Observed from a viewpoint of the individual quantitative external environment indicators of the Macedonian economy, the forecasts regarding the foreign effective demand in 2017 and 2018 have been revised upwards in comparison with the April expectations. In contrast, the **foreign effective inflation** has been corrected downwards throughout the entire projection period. According to the new estimates for the **euro / US dollar exchange rate**, the US dollar is expected to register significantly lower value compared to the April forecasts, especially in 2017. **Regarding the prices of primary commodities on the world markets, the comparison with April indicates lower growth rates of prices in 2017, in contrast to 2018, when the revisions are mostly upward.** More specifically, in 2017, the **world oil prices** are expected to register lower growth in comparison with the April estimate, while in 2018, oil price is now expected to remain mainly unchanged, in contrast to the April forecast for its decline. Regarding the **metal prices**, the latest estimations for 2017 indicate a lower growth rate of the nickel price, and the copper price has not been changed, and it is still expected to achieve double-digit growth this year. Furthermore, in 2018, considerably more favorable developments on the world metal market are expected, whereby both copper and nickel prices have been considerably corrected upwards. Observing the **world prices of the primary food products**, in 2017 and 2018, smaller import pressures on the domestic inflation are expected, taking into account the expectations for lower growth of wheat and corn prices on the world markets compared to April. 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 projected dynamics within the April forecasting round indicates certain deviations in the individual segments of the economy. According to the estimated **GDP** data, the economic activity registers a decline in the second quarter, dynamics which does not correspond to the shifts in the high-frequency indicators that indicated growth in the second quarter. Compared with the forecast, same as in the first quarter, the performance is lower than the expectations in the second quarter, mainly due to the high decrease in gross capital formation. Given the small number of available high frequency data, which indicate divergent movements, it is difficult to assess precisely the economy in the third quarter of the year. In summary, the performance in the first half of the year is significantly lower than in the April forecast, indicating a potentially downward deviation from the forecasted economic growth for the entire 2017. When it comes to changes in **consumer prices**, in August, positive inflation rate was measured, which is slightly higher than forecasted. However, seen cumulatively, the realized inflation rate in the first eight months is in line with the April forecast. In circumstances of performances within the forecast, the risks with regard to the inflation forecast for 2017 remain mainly associated with the uncertainty about the expected movement in prices of primary commodities.

Recent foreign reserves data as of August (adjusted for the effects of price and exchange rate differentials and price changes of securities) indicate decrease in the foreign reserves in the third quarter. According to the analysis of change factors, the fall in reserves is mostly due to the transactions for the account of the Government, due to the servicing of the regular liabilities to abroad[3], while the NBRM interventions on the foreign exchange market acted in the opposite direction. Analyzing the available data in the external sector for the third quarter of the year, the data on the currency exchange market as of August point to performances in private transfers close to forecasted in April. At the same time, the data on foreign trade as of July indicate trade deficit in line with the expectations for the third quarter of the year, amid lower export and import pressures. Regarding the balance of payments, the data for the second quarter indicate improved performances in the current and the financial transactions compared to the April forecast. The analysis of foreign reserves adequacy indicators shows that they continue to hover in a safe zone.

[3] In July, the regular repayment of part of the loan to Deutsche Bank was realized, as well as the annual interest on two Eurobonds.

As for the monetary sector developments, final data as of July show small decline in total deposits (of 0.1%) on a monthly basis, compared to the increase in the previous month (of 0.8%). Analyzed by sector, the decrease in July fully arises from the lower household deposits (despite their increase in the previous two months), which is partially associated with the withdrawal of part of the paid subsidies in the previous month[4], while corporate deposits register monthly growth. Analyzing the currency structure, the decrease in total deposits stems from the decrease in Denar savings, while foreign currency deposits are higher on a monthly basis. Regarding the forecast, in July total deposits registered a slight decline of Denar 244 million on a monthly basis, compared to the forecasted growth of Denar 5,946 million for the third quarter, according to the April forecast. Given the weaker performance of deposits, in July, total deposits increased by 7.3% on an annual basis, which is below the forecasted growth of 7.9% for the third quarter of 2017, according to the April forecast. Analyzing the credit market, in July, total loans registered monthly growth of 0.3%, which was more moderate compared to the growth in the previous month (of 0.9%). The monthly increase in the total lending fully arises from the higher performances in households, amid small decline in corporate loans. Regarding the forecast, in July, 16.4% of the forecasted growth of total loans (Denar 5,157 million) were realized in the third quarter, according to the April forecast. However, given exceeding the forecasted level of loans at the end of the second quarter, in July, total loans increased by 4.9% on an annual basis, which is within the forecasted growth for the third quarter (of 4.8%).

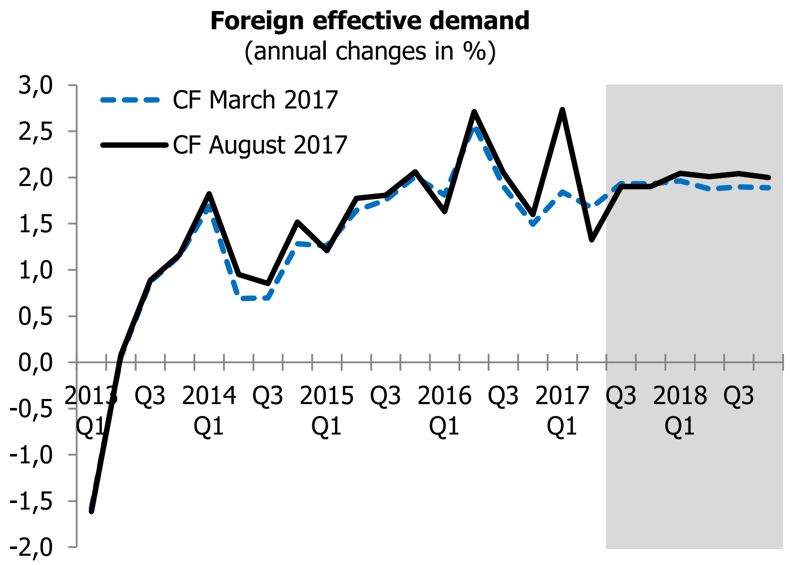
In the period January-July 2017, the Budget of the Republic of Macedonia registered a deficit of Denar 10,701 million, financed from domestic sources through withdrawal of deposits from the government account with the National Bank and with net issue of new government securities. The budget deficit constitutes 57.6% of the envisaged deficit in the Budget Revision 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. Concerning the foreign reserves, the indicators of their adequacy remain within the safe zone. In terms of economic activity, the lower starting point, as a result of the downward deviation in the first half of the year, indicates a potentially lower rate of economic growth for the entire 2017 compared to the April forecast. Regarding inflation, recent performances are in line with the forecast, but the uncertainty associated with the expected movement of the prices of primary commodities remains a risk to the forecast for 2017. Within the monetary sector, data on total deposits in July indicate weaker performance compared to the April forecasts, while the growth pace of credit activity corresponds to the forecasted growth path for the third quarter, amid further stronger credit support to the households sector.

[4] It reflects the preferences of this group of economic agents to hold cash assets.

Selected economic indicators/1		2015	2016								2017									
	2014	2015	Jan.	Feb.	Mar.	Q1	Q2	Q3	Q4	2016	Jan.	Feb.	Mar	Q1	Apr.	May	Jun.	Q2	Jul.	Aug
I. Real sector indicators																				
Gross domestic product (real growth rate, y-o-y) /2	3,6					2,4	2,9	2,0	2,4	2,4				0,0				-1,8		
Industrial production /3																				
y-o-y	4,8	4,9	8,0	15,2	8,9	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	
cumulative average	4,8	4,9	8,0	11,7	10,7	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	
Inflation /4																				
CPI Inflation (y-o-y) /5	-0,5	-0,4	0,1	0,0	-0,3	-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
CPI Inflation (cumulative average)	-0,3	-0,3	0,1	0,1	-0,1	-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
Core inflation (cumulative average)	0,5	0,5	1,5	1,5	1,6	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
Core inflation (y-o-y)	0,5	0,5	1,5	1,5	1,8	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
Labor force																				
Unemployment rate	28,0	26,1				24,5	24,0	23,4	23,1	23,7				22,9				22,6		
II. Fiscal Indicators																				
(Central Budget and Budgets of Funds)																				
Total budget revenues	145.929	161.207	12.918	12.926	14.739	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	15.174	
Total budget expenditures	168.063	180.632	14.606	15.695	15.917	46.218	42.729	45.953	50.506	185.406	14.723	14.845	16.733	46.301	15.082	17.089	16.202	48.373	17.569	
Overall balance (cash)	-22.134	-19.425	-1.688	-2.769	-1.178	-5.635	-1.307	-2.146	-6.982	-16.070	-2.139	-1.535	107	-3.567	-29	-1.733	-2.977	-4.739	-2.395	
Overall balance (in % of GDP)/1	-4,2	-3,5	-0,3	-0,5	-0,2	-0,9	-0,2	-0,4	-1,1	-2,6	-0,3	-0,2	0,0	-0,6	0,0	-0,3	-0,5	-0,7	-0,4	
III. Financial indicators /6																				
Broad money (M4), y-o-y growth rate	10,5	6,8	4,5	5,4	6,2	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	
Total credits, y-o-y growth rate	10,0	9,5	8,6	8,7	8,4	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	
Total credits - households	11,8	12,9	12,6	12,8	13,0	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	
Total credits - enterprises	8,6	7,1	5,5	5,8	5,1	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	
Total deposits (incl. demand deposits), y-o-y growth rate	10,4	6,5	4,3	5,3	6,2	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	
Total deposits - households	8,9	4,1	3,6	3,5	3,1	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	
Total deposits - enterprises	15,7	13,0	6,4	11,8	16,0	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	
Interest rates /7																				
Interst rates of CBBills	3,25	3,25	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	3,25	3,25	3,25	
Lending rates																				
denar rates (aggregated, incl. denar and denar with f/x clause)	7,5	7,1	6,8	6,7	6,7	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	
f/x rates	6,3	5,9	5,7	5,7	5,6	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	
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	2,5	2,5	2,5	2,4	2,3	2,3	2,3	2,2	2,2	2,2	2,2	2,1	
f/x rates	1,4	1,3	1,1	1,1	1,1	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	
IV. External sector indicators																				
Current account balance (millions of EUR)	-43,2	-187,0	13,1	-21,7	-50,1	-58,7	-219,4	100,3	-125,6	-303,3	-7,6	-58,3	-59,8	-125,7	-30,3	-48,3	-14,0	-92,6		
Current account balance (% of GDP)	-0,5	-2,1	0,1	-0,2	-0,5	-0,6	-2,2	1,0	-1,3	-3,1	-0,1	-0,6	-0,6	-1,2	-0,3	-0,5	-0,1	-0,9		
Trade balance (millions of EUR)/8	-1757,9	-1713,6	-65,8	-131,6	-175,8	-373,2	-501,5	-391,4	-511,3	-1777,4	-117,4	-138,4	-166,1	-421,8	-152,9	-178,1	-101,1	-432,2	-147,6	
Trade balance (% og GDP)	-20,5	-18,9	-0,7	-1,3	-1,8	-3,8	-5,1	-4,0	-5,2	-18,0	-1,1	-1,3	-1,6	-4,1	-1,5	-1,7	-1,0	-4,2	-1,4	
import (millions of EUR)	-5504,5	-5801,1	-354,1	-477,5	-525,0	-1356,6	-1557,7	-1540,0	-1652,4	-6106,7	-442,2	-517,9	-599,6	-1559,7	-550,9	-609,1	-534,1	-1694,1	-528,9	
export (millions of EUR)	3746,6	4087,6	288,3	345,9	349,2	983,3	1056,2	1148,6	1141,1	4329,3	324,8	379,6	433,4	1137,9	398,0	430,9	433,0	1261,9	381,4	
rate of growth of import (y-o-y)	10,5	5,4	-4,2	16,6	-1,7	3,3	4,9	10,2	3,0	5,3	24,9	8,5	14,2	15,0	4,1	14,7	7,4	8,8	**2,4**	
rate of growth of export (y-o-y)	15,8	9,1	-1,7	15,2	2,6	5,3	1,4	10,5	6,4	5,9	12,7	9,7	24,1	15,7	8,0	21,2	30,3	19,5	-5,6	
Foreign Direct Investment (millions of EUR)	197,4	202,8	29,9	54,9	47,8	132,7	52,2	28,2	141,0	354,0	-6,6	53,0	65,1	111,5	31,6	16,1	-62,5	-14,8		
External debt																				
Gross external debt (in milllions of EUR)	5992,3	6290,5				6816,2	6886,6	7513,4	7253,2	7253,2				7780,8						
public sector	2846,8	2933,7				3279,4	3283,1	3891,1	3445,5	3445,5				3819,8						
public sector/GDP (in %)	33,2	32,4				33,2	33,3	39,5	34,9	34,9				37,2						
private sector	3145,5	3356,9				3536,8	3603,6	3622,3	3807,7	3807,7				3961,0						
Gross external debt/GDP (in %)	70,0	69,4				69,1	69,8	76,2	73,5	73,5				75,7						
Gross official reserves (millions of EUR)/9	2.436,5		2.246,9	2.253,4	2.266,3						2.557,1	2.563,0	2.534,4		2.496,0	2.448,5	2.399,9		2.273,3	2.258

/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.



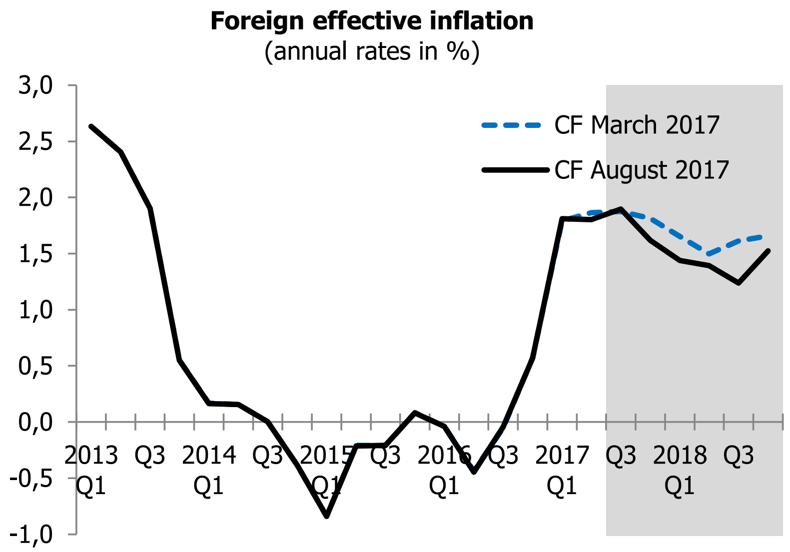
Source: "Consensus Forecast" and NBRM calculations.

According to the latest estimates, the foreign effective demand was revised upwards compared with the April forecasts.

Thus, in 2017, growth of 2% is expected, which is an upward revision of 0.2 percentage points in comparison with the April forecasts...

...largely due to the expectations for higher economic growth of Germany.

Foreign demand has been minimally revised upwards for 2018, whereby the growth is expected to amount to 2% (1.9% in April).



Source: "Consensus Forecast" and NBRM calculations.

The expectations about the foreign effective inflation for 2017 have been revised downwards...

...so that an inflation rate of 1.8%, versus 1.9% in April is expected...

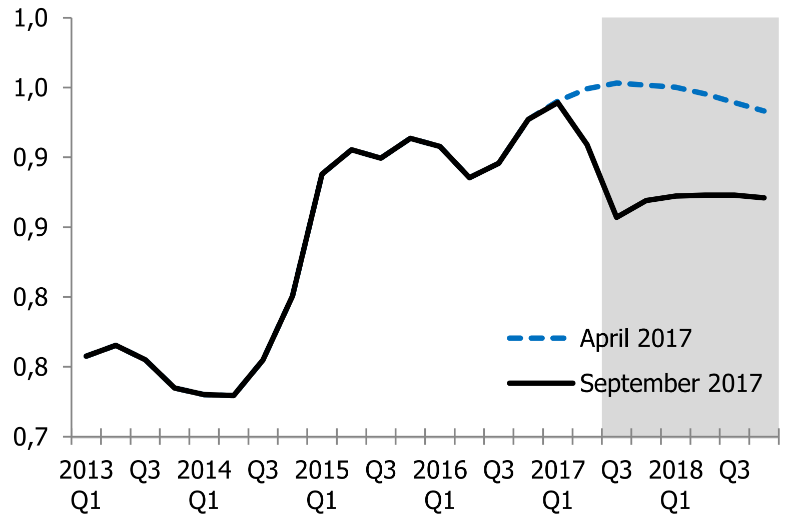
...amid expectations for slower price growth in Germany, Croatia[5] and France.

Downward revision was made in 2018 as well, when it is expected that the foreign inflation will equal 1.4% (1.6% in April)...

...largely as a result of the expectations for lower price growth in Serbia[6].

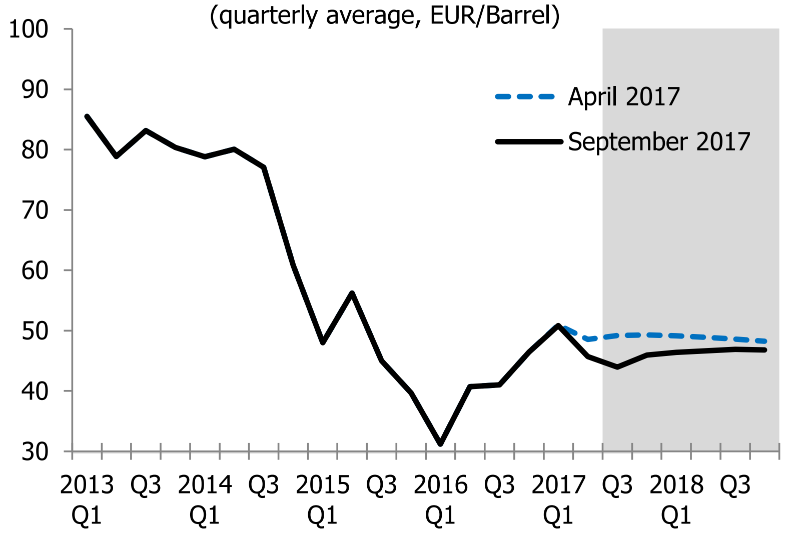
[5] Inflation in Croatia has been adjusted for the changes in the exchange rate.
[6] Inflation in Serbia has been adjusted for the changes in the exchange rate.

EUR/USD exchange rate



Source: "Consensus Forecast" and NBRM calculations.

Brent oil
(quarterly average, EUR/Barrel)



Source: IMF and NBRM calculations.

The latest expectations for the euro / US dollar exchange rate indicate lower values of the US dollar against the euro than those in the April forecasts...

...whereby depreciation of the value of the US dollar against the euro is expected for 2017, despite previous expectations for its significant appreciation, while for 2018, a greater depreciation of the US dollar against the euro is expected compared to the April forecasts...

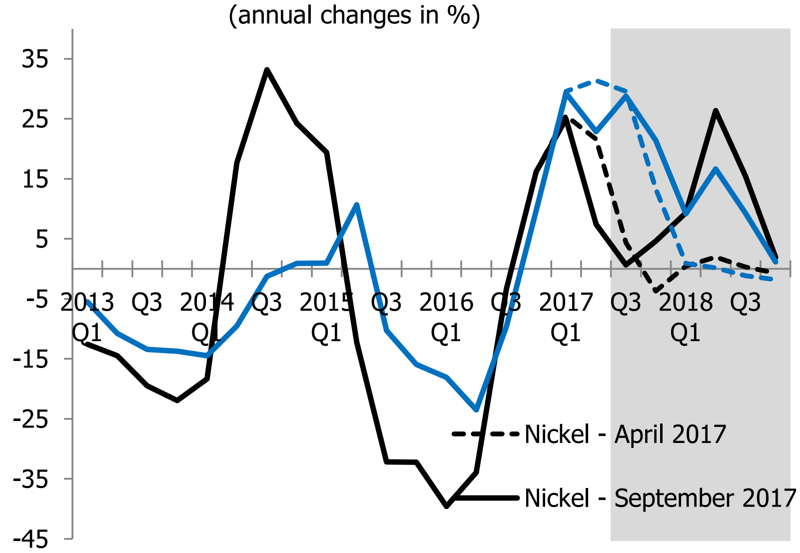
...which is largely due to the reduced political risks and more favorable economic performance than expected in the euro area, contrary to the further internal political uncertainty and external political tensions of the United States[7]. Despite the measures taken to limit global production[8], **the latest estimates for oil price[9] indicate slower growth for 2017 in comparison with the forecast in April...**

...which is largely a reflection of the expectations for increase in the production in the United States and reduced demand in China.

On the other hand, an upward revision was made for 2018, whereby a similar price level is now expected with 2017, unlike the previously forecasted slight decline in April.

[7] Tense political relations between the United States and North Korea.
[8] On 25 May 2017, the OPEC Member States made a decision to extend the agreement for reduction of oil production for nine more months (March 2018), which aims to reduce the inventories of this fuel globally. Also, 11 oil producing countries that are not OPEC Member States, including Russia, are expected to support the extension of the agreement, whereby 1.8 million barrels less per day should be produced until March 2018.
[9] 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.

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



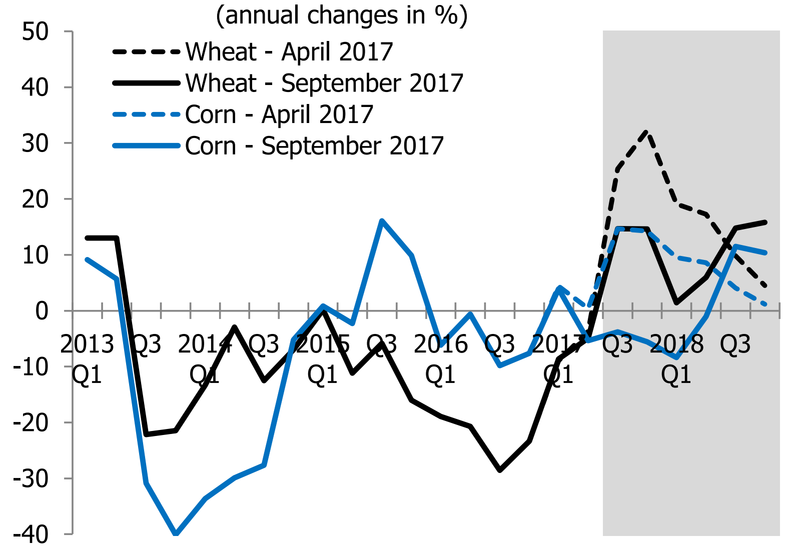
Source: IMF and NBRM calculations.

In 2017, metal prices denominated in US dollars have been revised upwards...

...while the expectations for prices denominated in euros indicate unchanged estimates for growth of the copper price and downward correction in the nickel price compared to the April forecasts.

In 2018, the forecasts of metal prices have been considerably revised upwards, now expecting their solid growth, contrary to expectations for price stabilization in the April forecasts.

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



Source: IMF and NBRM calculations.

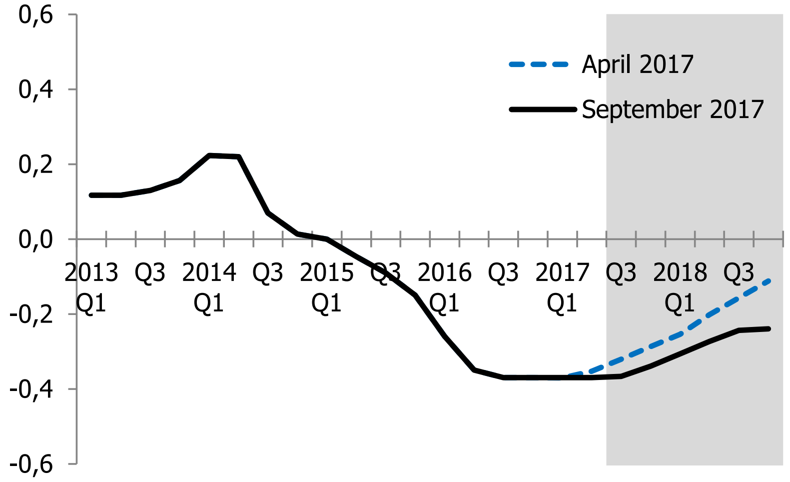
Stock exchange prices of corn and wheat have been revised downwards, compared to the April forecasts.

Thus, in 2017, there are expectations for slower growth of the wheat price and slight decline in the corn price contrary to the growth forecasted in April...

....which is mostly due to the expectations for an increase in the world wheat production and the increased corn production in Russia and Brazil.

Estimates for wheat and corn prices in 2018 indicate slower growth than expected in April.

1-month Euribor
(quarterly average, in %)



Source: "Consensus Forecast" and NBRM calculations.

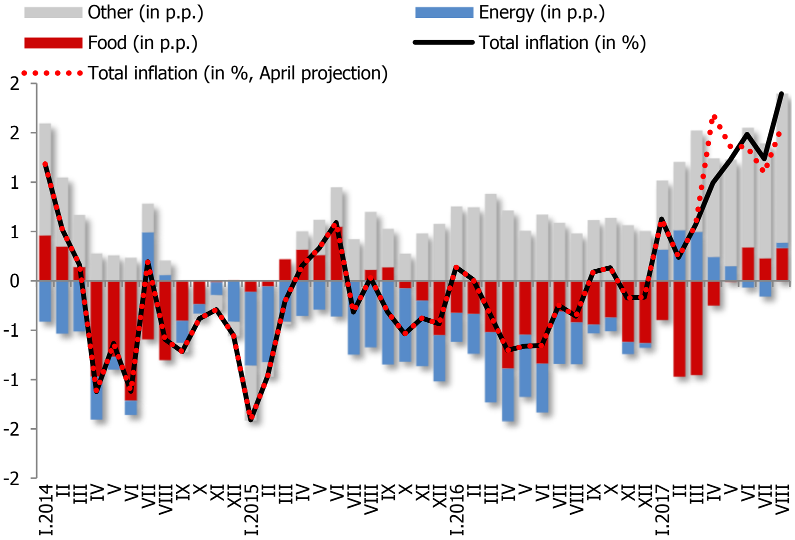
In 2017, there were no major changes in the expectations about the movement of the foreign interest rate...

...whereby similar average level of -0.36% (-0.33% in April) is forecasted, amid a continuation of the Quantitative Easing Program of the ECB by the end of the year.

For 2018, downward revision of the average one-month Euribor to -0.27%, versus the forecasted -0.18% in April was made...

...amid expectations for gradual reduction in the volume of quantitative easing by the ECB after December 2017, but maintaining the current stimulating interest rate policy.

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

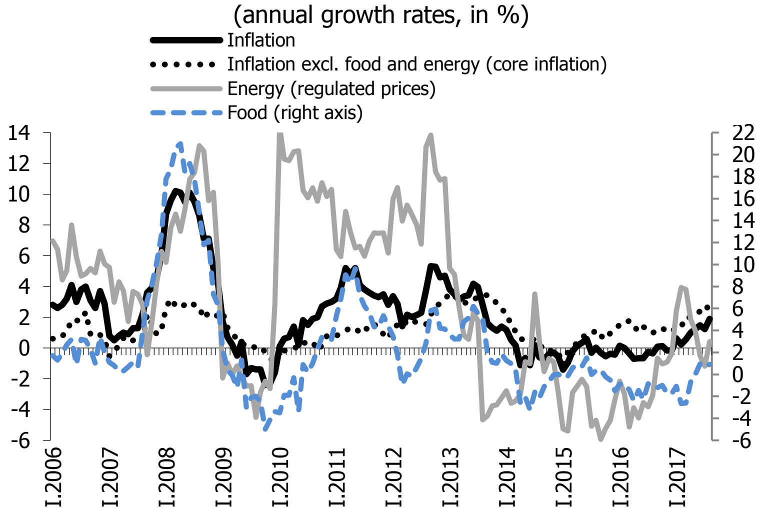


Source: SSO and NBRM.

In August 2017, domestic consumer prices registered a monthly increase of 0.4%[10] (versus the monthly decrease of 0.6% in July)**...**

...amid growth of food and energy prices, as well as acceleration in the core inflation rate.

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



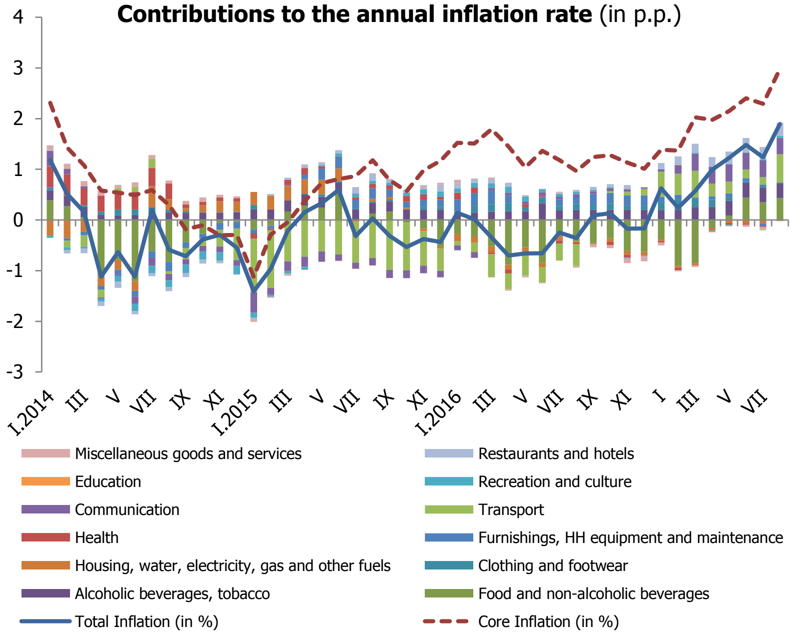
Source: State statistical office and NBRM calculations.

The annual inflation rate in August amounted to 1.9% (versus 1.2% in July), which is slightly higher than the expected movement for August, compared to the April cycle projections.

Observed by price category, the upward deviation is present in food prices and core inflation, while in energy, the deviation is downward.

Analyzed cumulatively, the realized inflation rate in the first eight months is in line with the April forecast.

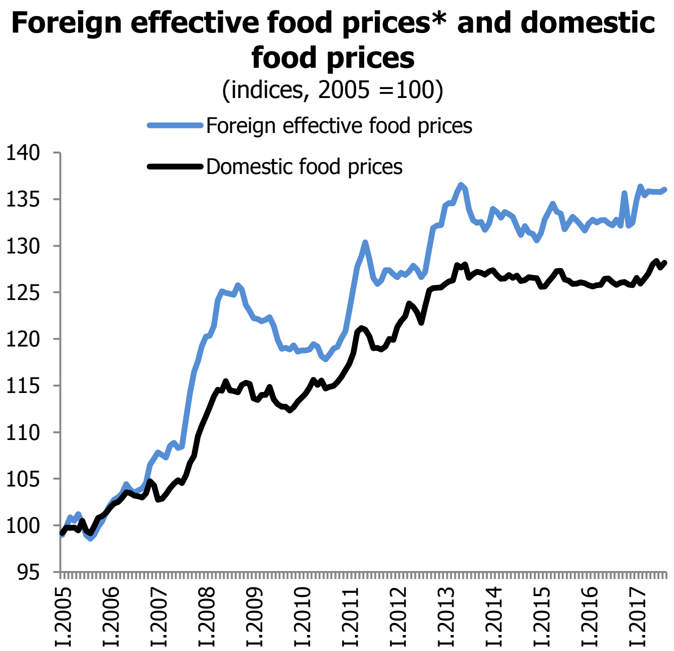
[10] Observed by group of products, the transport registered the highest positive contribution to the monthly growth in August (increase in prices of liquid fuels and lubricants and prices of air transport).



Source: SSO and NBRM.

In August, core inflation accelerated and equaled 0.6% on a monthly basis (0.1% in July) and 3% on an annual basis (2.3% in July).

This acceleration in the pace of growth is almost entirely due to the significant acceleration in the price growth of air transport. Also, in August, the annual price growth of most categories within the core inflation continued, and higher positive contribution, apart from the air transport prices, was also made by the prices of communications and tobacco[11].



* 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.

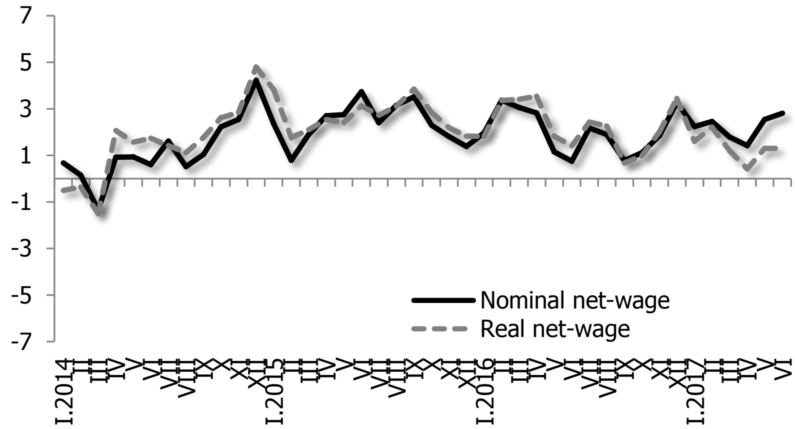
The expected price movements of external input assumptions in the inflation forecast for the whole of 2017 have been revised downwards.

Thus, the latest estimates for 2017, compared to the expectations in the April cycle projections, indicate lower growth in the oil and wheat prices, i.e. fall rather than rise in the corn price.

Given that the performances in domestic prices as of August are generally in line with the forecast, **the risks with regard to the inflation forecast for 2017 remain mainly associated with the uncertainty about the expected movement in prices of primary commodities.**

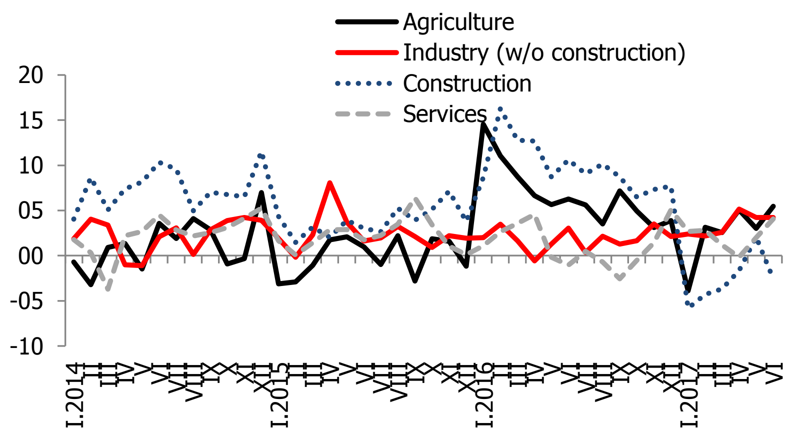
[11] The annual growth of tobacco prices in August is a combination of the increase in the price of a certain type of cigarettes in April and June 2017. In July 2017, the cigarette excise increased (from 1 July 2017 to 1 July 2023 the excise duty will increase by 0.20 denars/piece each year) which did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

Average net-wage
(annual changes, in %)



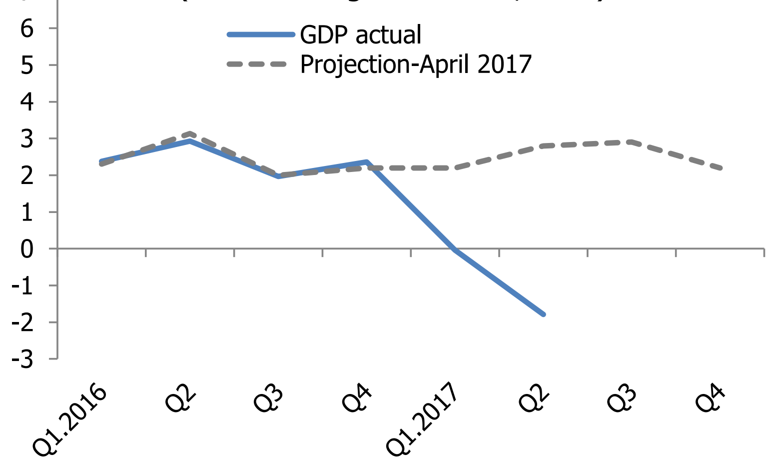
Source: SSO.

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



Source: SSO.

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



Source: SSO and NBRM projections.

In June 2017, the average net wage registered a nominal annual growth of 2.8%, which is a slight growth acceleration of 0.3 percentage points, compared to the growth last month.

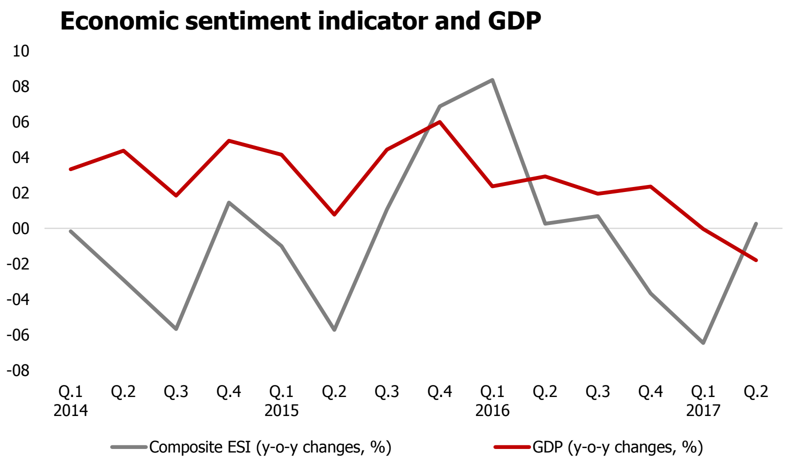
Upward movement in wages has been registered in most of the activities, with the highest growth recorded in arts, entertainment and recreation, and professional, scientific, and technical activities. On the other hand, in June, lower wages were paid only in construction.

Amid increase in the consumer prices, in June, the **real wages increased by 1.3%.**

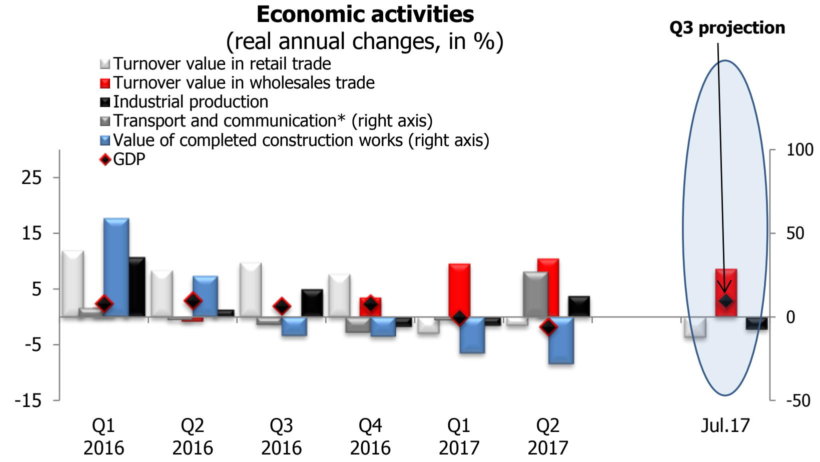
The performance in the net wages in the second quarter of the year is lower than the April forecast.

In the second quarter of 2017, GDP decreased by 1.8%, which is a significant downward deviation compared to the April forecast (growth of 2.8% in the second quarter). Such dynamics of GDP does not coincide with the movements of the key high frequency macroeconomic indicators in the second quarter.

Observing the demand, the decline in GDP is explained by the lower domestic demand in conditions of large reduction in gross capital formation, while private and public consumption grew. In the second quarter, net exports also made a positive contribution, amid significantly higher export growth compared to imports. Compared to the April forecast, the downward deviation completely derives



Source: State statistical office and European commission.



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

from gross capital formation (significantly sharper decline versus expected), while other components are generally in line with the forecast.

Analyzing the production, construction registered a large reduction in the value added, and decline was registered also in industry and part of the services sector[12]. On the other hand, the agricultural sector and trade continued to register growth of activity.

Most of the high frequency data on the shifts on the supply and demand side are available only for the first month of the quarter, which increases the uncertainty about the assessment for the third quarter based on this information. However, the results obtained from the surveys that measure the perceptions of economic agents[13], conducted in July and August, show a significant strengthening of the economic agents' confidence indicating an improvement of the situation in the economy during the third quarter.

Observed by economic sectors, the growth in the **total trade** continued during July, mainly driven by the growth in wholesale trade, while retail trade declined.

In the **industry**, after the growth in the second quarter, at the beginning of the third quarter, production declined, amid weaker activity in the processing industry and mining, while in the energy sector the production growth continued (although slower).

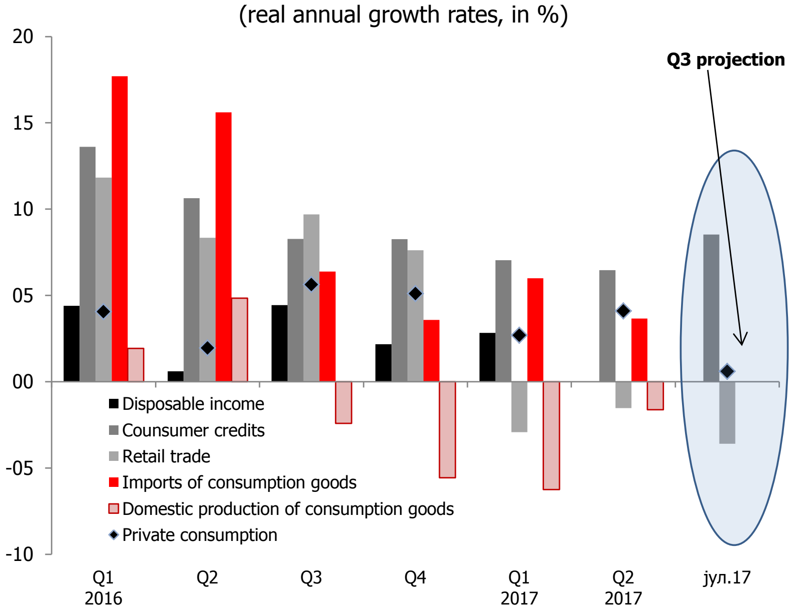
Within the processing industry, the lower production is mostly explained by the movements in two traditional sectors (clothing production and metal production), where in July, a significant decrease in production was registered. In

[12] Within the services sector, in the second quarter, lower value added was registered in the activities related to real estate, professional, scientific and technical activities and administrative and auxiliary services, the activities in the field of public administration and defense, social security, education and health, and social work and the activities in the field of arts, entertainment and recreation.

[13] 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).

most of other activities, there was an increase in production.

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



Source: SSO and NBRM calculations.

The number of high frequency data on the **aggregate demand** side is also limited, and the indicators indicate divergent movements.

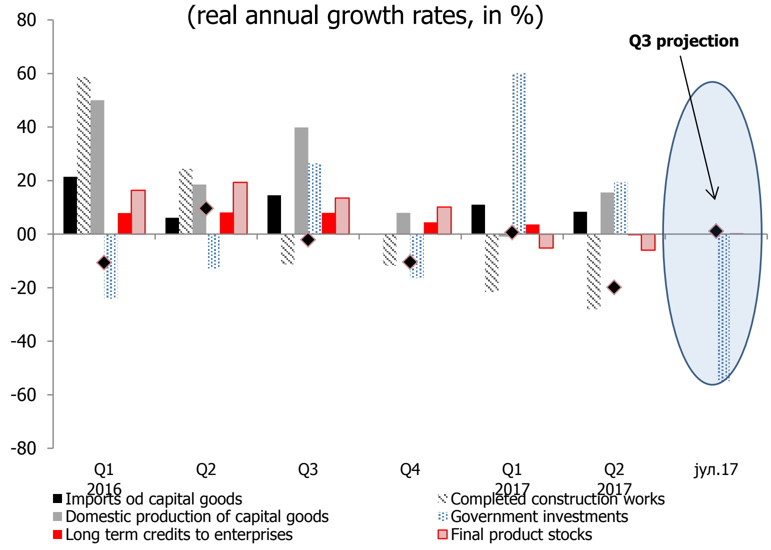
From the indicators of the movements in **private consumption**, household lending continues to grow, and at the same time the growth of part of the disposable income components (pensions and social government transfers) continued.

On the other hand, the turnover value in retail trade declined in July, while domestic production of consumer goods and the import of consumer goods also registered a decline.

Available short-term indicators of **investment activity** currently point to investments fall in the third quarter of 2017...

...amid lower government capital investments, domestic production of capital goods and the import of investment products.

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



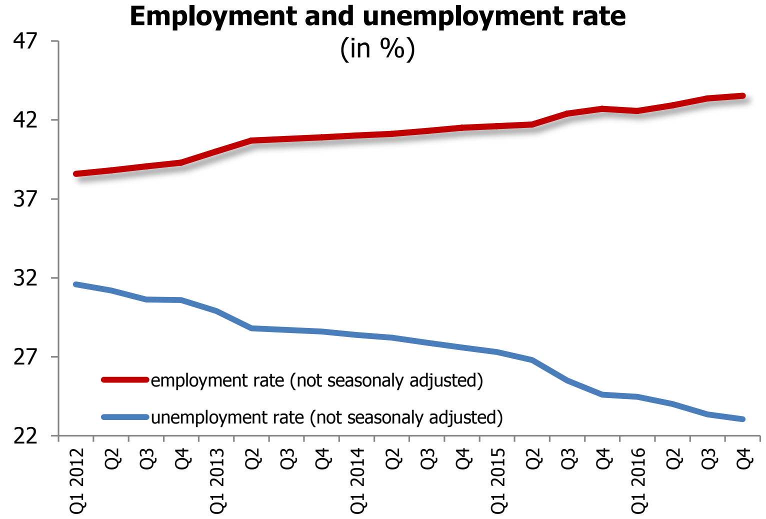
Source: SSO and NBRM calculations.

On the other hand, the growth of long-term lending to the corporate sector continued in July (although at a slower growth pace).

According to the data on **foreign trade,** the trade deficit in July 2017 increased, amid nominal decline in the export and growth of the import of goods and services.

According to the July fiscal budget data, **public consumption** registers a decline, amid a decrease in the expenditures on salaries in the public sector, lower expenditures on goods and services and health care transfers[14].

[14] Most of these assets relate to expenditures on goods and services.



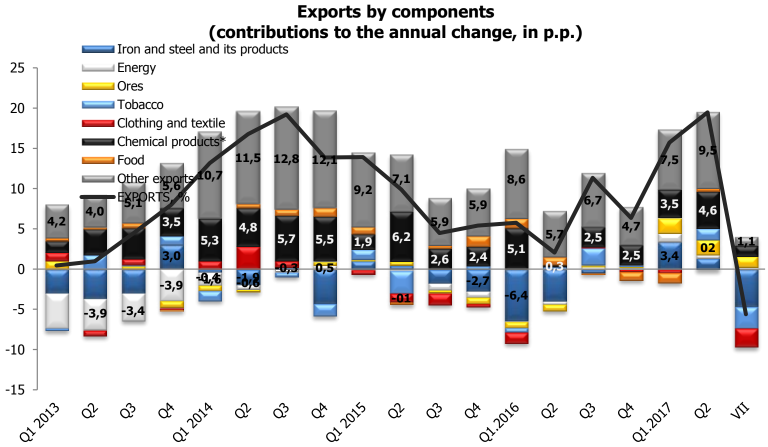
Source:SSO, LFS

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

...given further decline in the unemployment rate, which reduced to 22.6% in the second quarter (22.9% in the first quarter of 2017)...

...and annual increase in the number of employed persons of 2.7%[15].

[15] Processing industry, trade, transport and catering services made the largest contribution to the employment growth.

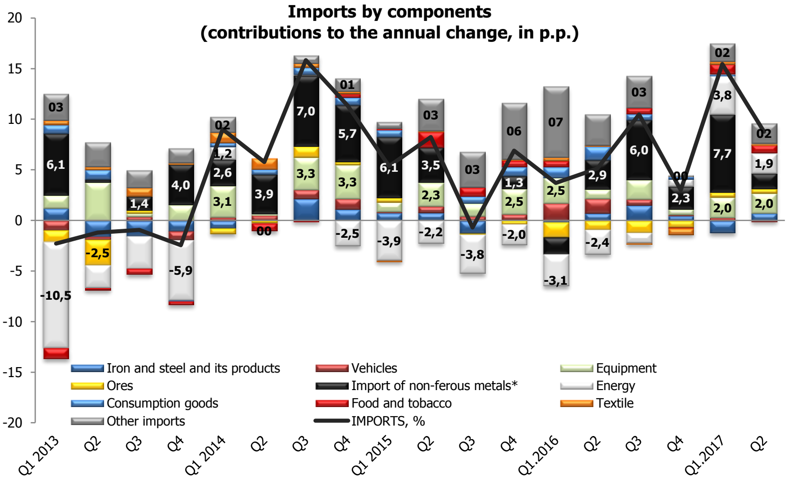


Source: NBRM.

In July 2017, the foreign trade deficit increased by 31% on an annual basis, amid a decrease in the export component and simultaneous increase in the import.

In July, the **export** of goods registered a moderate decrease of 5.6%, primarily as a result of the decrease in the export by part of the traditional sectors (metal processing industry, clothing and textile and tobacco). At the same time, the export from the new export-oriented industrial facilities, as well as the export of ores, recorded moderate growth.

Compared with the April forecast, the realized export in July was lower than the expectations for the third quarter, amid moderate downward deviations in most components.



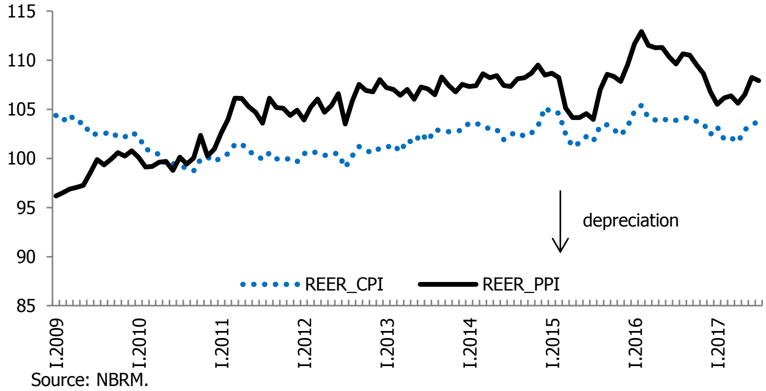
Source: NBRM.

Import of goods in July 2017 increased by 2.4% on an annual basis, reflecting the increase in the import in most components, except the import of iron and steel and food, where a decrease was registered.

Imports of goods in July 2017 were lower than expected for the second quarter with the April forecast, amid downward deviations in most import components.

The performances of the foreign trade components indicate a likelihood the trade deficit to be as forecasted for the third quarter of 2017, according to the April forecast. However, the period of one month is too short to draw more reliable conclusions.

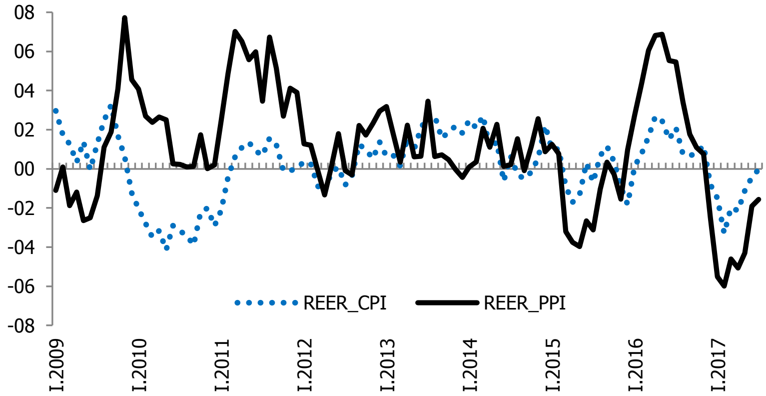
REER
(2010=100)



Source: NBRM.

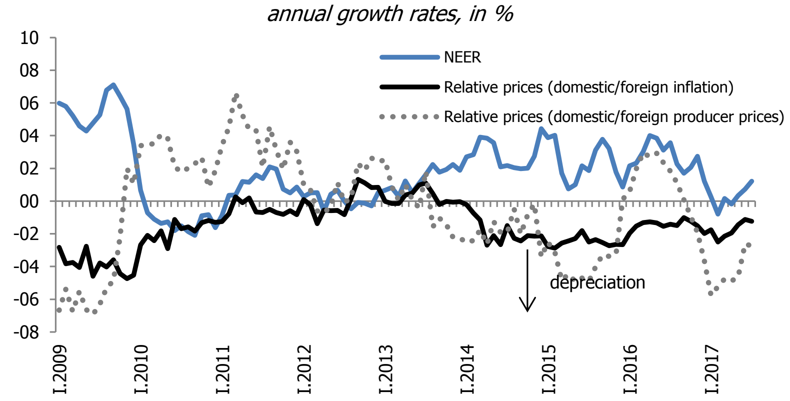
In July 2017, **price competitiveness indicators of the domestic economy registered divergent movements. Namely,** the REER index deflated by consumer prices registered no changes, while the REER index deflated by producer prices depreciated by 1.6%.

REER
annual changes, in %



Source: NBRM.

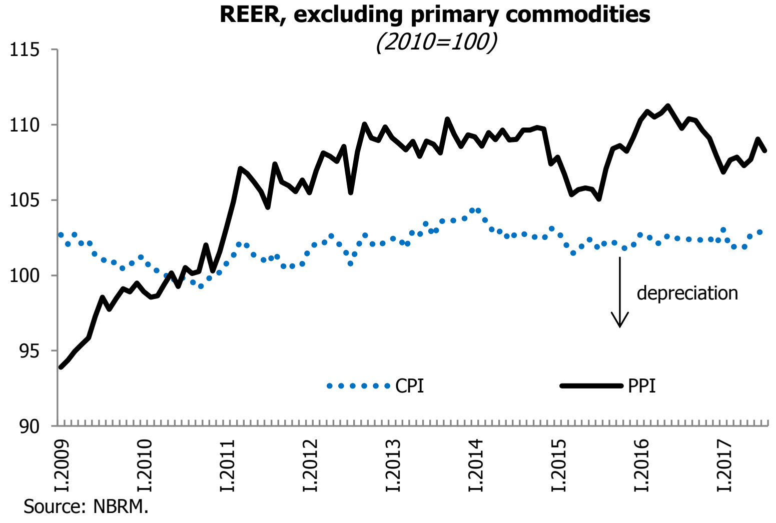
NEER and relative prices
annual growth rates, in %



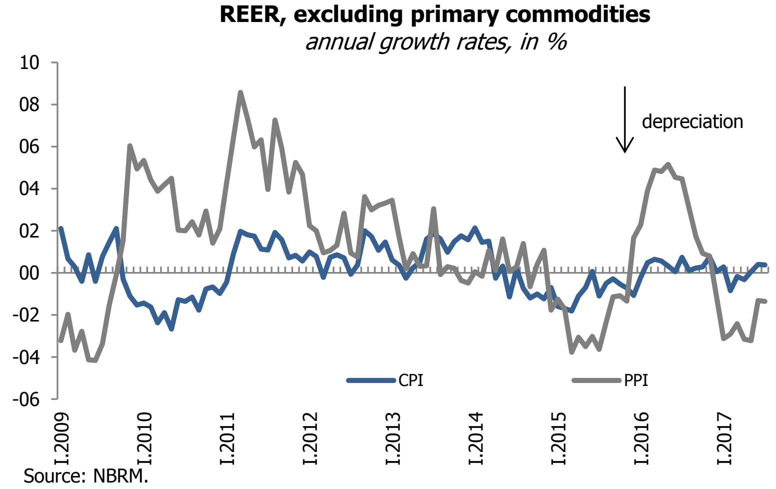
Source: NBRM.

These developments are due to favorable movements in relative prices, and the relative prices of industrial products decreased by 2.8%, while the relative cost of living by 1.6%. At the same time, the NEER acted in the opposite direction, recording a moderate appreciation of 1.2% on an annual basis, mostly as a result of the depreciation of the Turkish lira and the British pound.

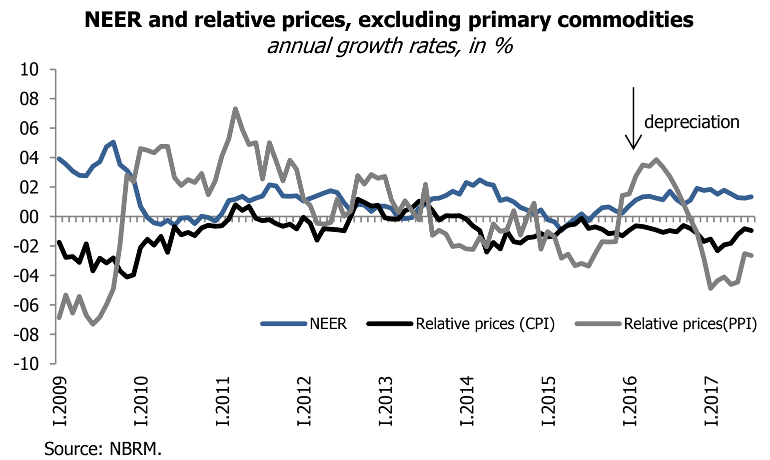
In July 2017, the analysis of **REER indices, as measured using weights**



based on the foreign trade without primary commodities[16], also shows similar movements. The REER deflated by consumer prices registered slight appreciation of 0.4%, while the REER deflated by industrial producer prices depreciated by 1.3%.

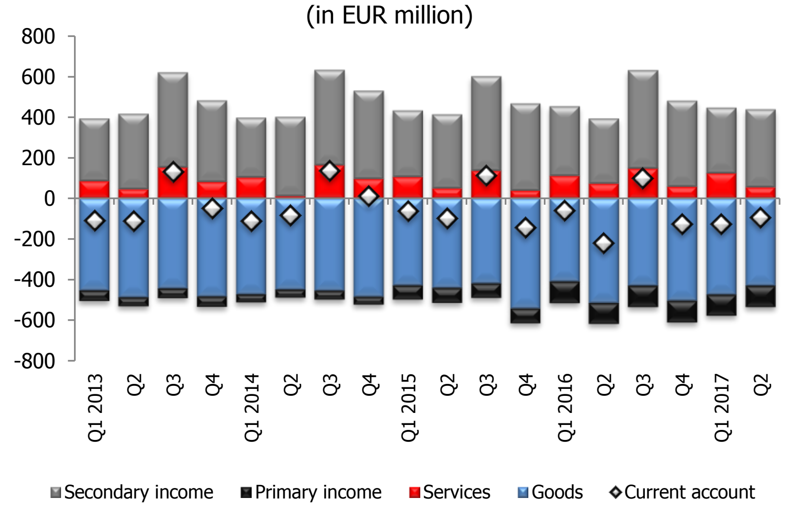


On an annual basis, the relative consumer prices and the relative producer prices decreased by 0.9% and 2.6%, respectively. The NEER has appreciated by 1.3% on an annual basis.



[16] 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.

Main components of the current account
(in EUR million)

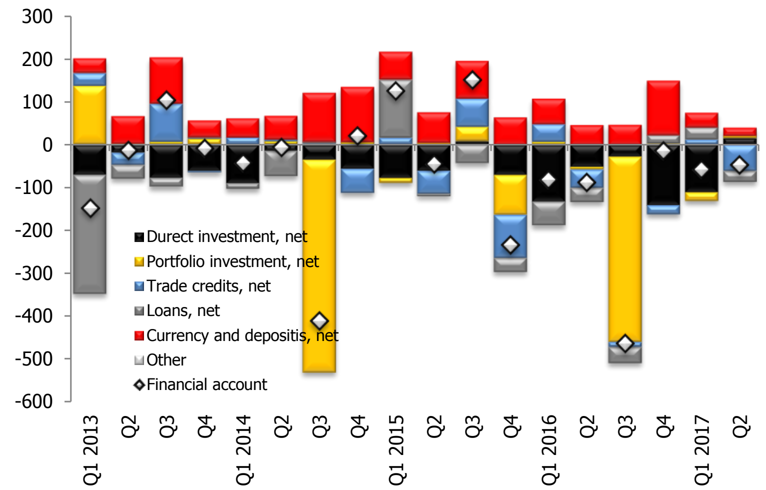


Source: NBRM.

In the second quarter of 2017, the balance of payments' current account registered a deficit of Euro 92.6 million (0.9% of GDP), i.e. a deficit lower than the expectations with the April forecast.

Analyzing individual categories, positive deviations are registered in the balance of goods, primary and secondary income, while the surplus in services is lower than expected with the April forecast.

Financial account components
(in EUR million)



Source: NBRM.

During the second quarter of 2017, the financial account registered net inflows of Euro 46.6 million (or 0.5% of GDP), which is higher than the expectations for the second quarter according to the April forecast[17].

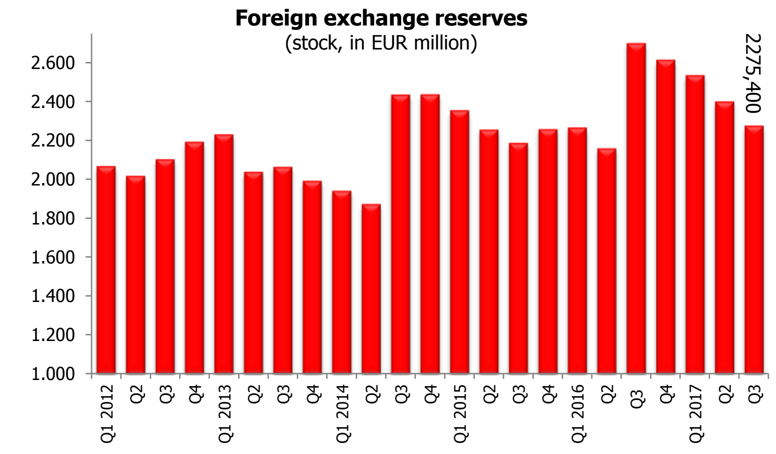
In the second quarter of 2017, significant positive deviations relative to the April forecast are registered in currency and deposits (realized net outflows that are lower than expected) and trade credits. The performances in portfolio investments are within the expectations with the forecast, while the performances in foreign direct investments and long-term loans are weaker in the second quarter. Foreign direct investments registered net outflows instead of the expected net inflows. Lower net inflows have also been registered in long-term loans, as a result of the lower withdrawals by other sectors.

As of August 2017, the supply of and the demand for foreign currency on the currency exchange market registered moderate growth.

In the period July – August 2017, the net purchase in the currency exchange market totaled Euro 275.5 million, which is a

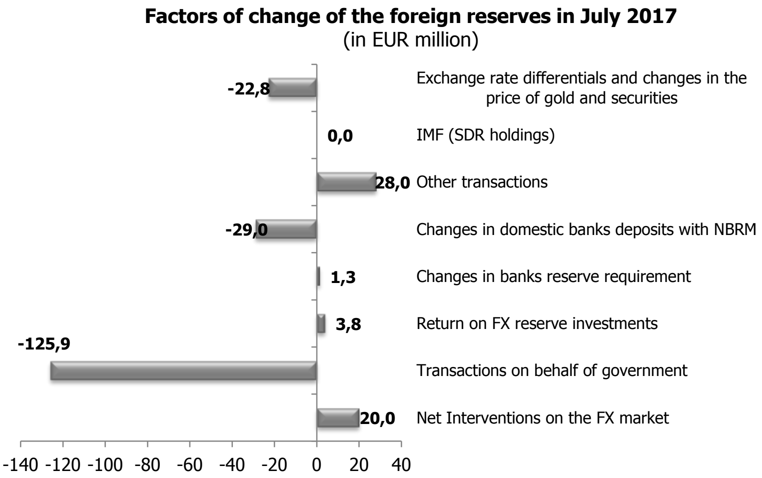
[17] According to the new methodology for compilation of the balance of payments BPM6, the terms net inflows and net outflows denote net incurrence of liabilities and net acquisition of financial assets, respectively.

moderate annual increase of 3.6%. These developments are the result of increasing supply of foreign currency of 3.3%, given the lower increase in the demand for foreign currency of 2.2%.



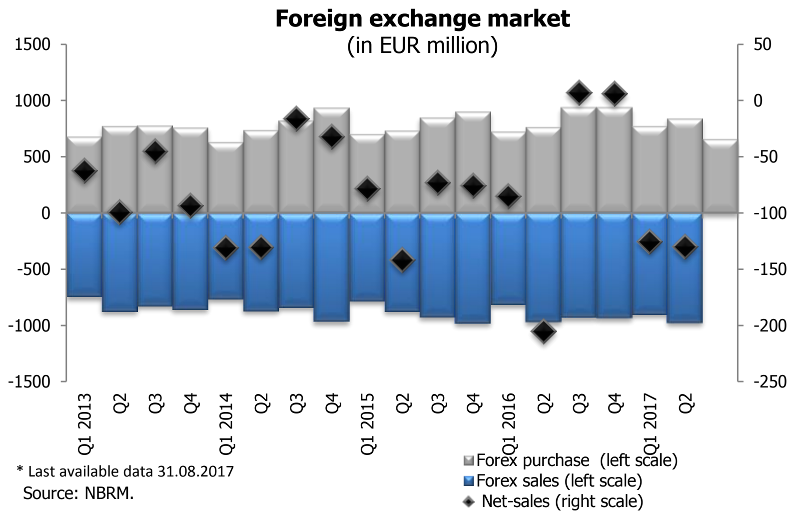
Source: NBRM.

As of 31 August 2017, the gross foreign reserves stood at Euro 2,275.4 million, which is a decrease of Euro 124.5 million compared to the end of the second quarter of 2017. The decrease in foreign reserves is mostly due to the transactions for the account of the Government, as a result of the regular servicing of the due external debt. Additionally, the category of currency changes and the change in the price of gold also had a negative impact.

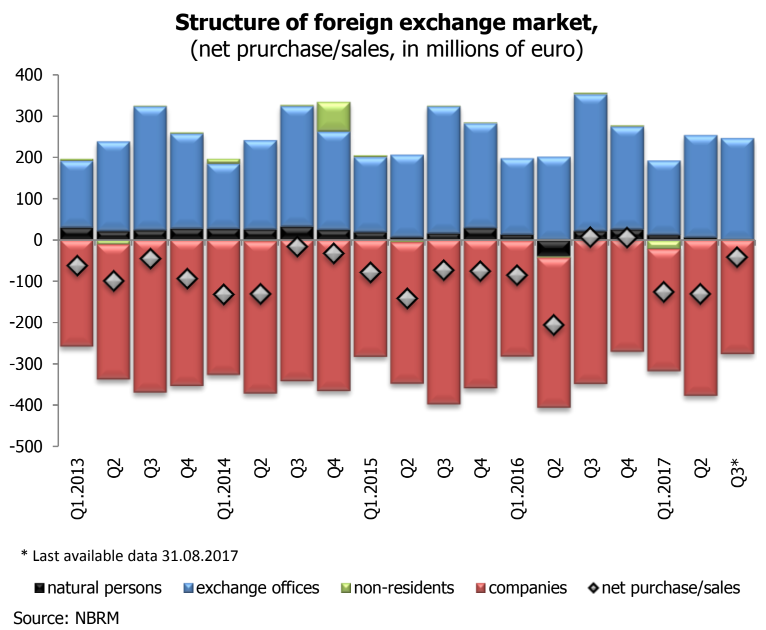


Source: NBRM.

In the period July-August 2017, the foreign exchange market of banks reported a net sale of foreign exchange of Euro 41 million, which is by Euro 82.9 million lower compared to the same



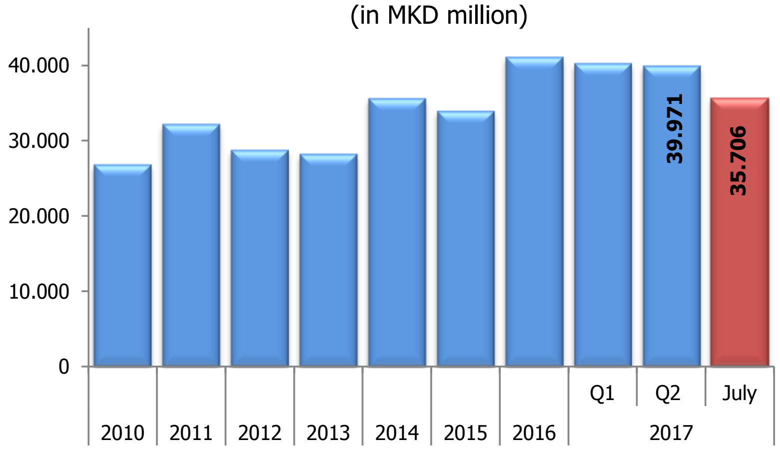
month of the previous year, when a net purchase of Euro 41.9 million was realized. This annual change is due to the higher increase in the demand for foreign currency than the supply.



Sector-by-sector analysis shows that these changes mainly arise from the higher net sales of companies, as well as the realized net sales of non-residents (in the period July-August 2016, non-residents realized net purchase). The realized net purchase from natural persons and exchange offices registered no significant change.

The situation regarding the monetary instruments at the end of July is lower compared to the end of the second quarter, which is contrary to the expectations for withdrawing liquidity through the monetary instruments in the third quarter of 2017, according to the April forecast.

Monetary policy instruments
(in MKD million)

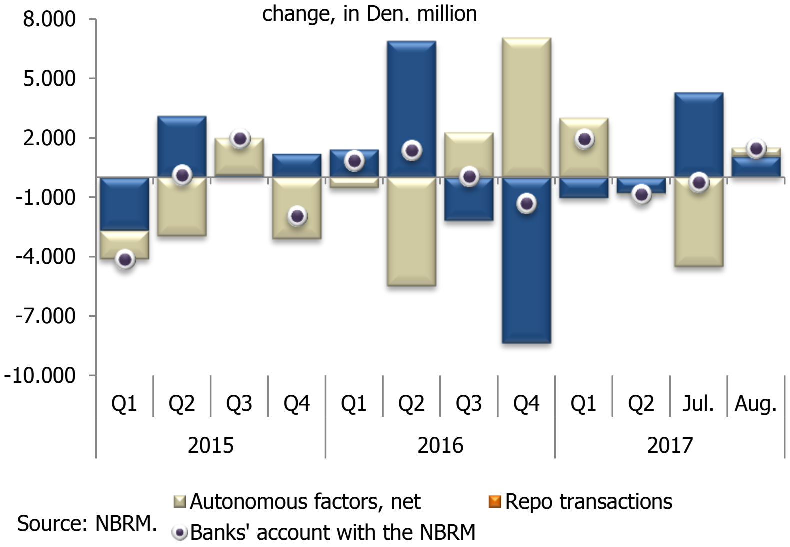


Source: NBRM.

The net foreign assets of the NBRM in July registers a decline compared to the end of June, which is sharper compared to forecasted for the third quarter. Total government deposits also recorded a decrease in the analyzed period, in smaller amount compared to the expectations for the third quarter, according to the April forecast.

In July, the reserve money registered an increase compared to the end of the second quarter, but moderately weaker compared to forecasted for the third quarter. The increase completely derives from the higher currency in circulation, while total liquid assets of banks registered a moderate decrease, contrary to the expectations for an increase in both categories according to the April forecast.

Banks' liquidity
change, in Den. million



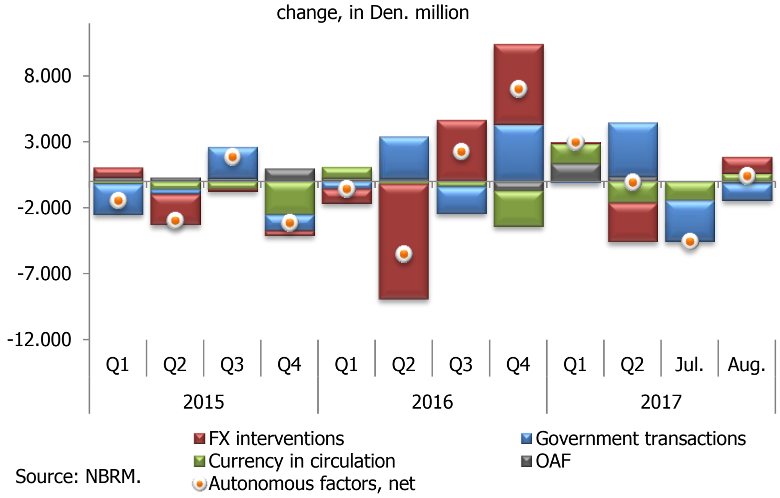
Source: NBRM.

According to operational liquidity data, in August, the liquidity of the banking system increased on a monthly basis. The increase in liquidity in this period is affected by autonomous factors (NBRM's foreign currency interventions with market makers by purchasing foreign currency and currency in circulation), as well as due to the reduction in the supply of CB bills[18] by the NBRM. Banks' interest in placing part of the excess liquid assets in short-term deposits with the NBRM (overnight and seven day deposits) was higher.

[18] 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.

Autonomous factors

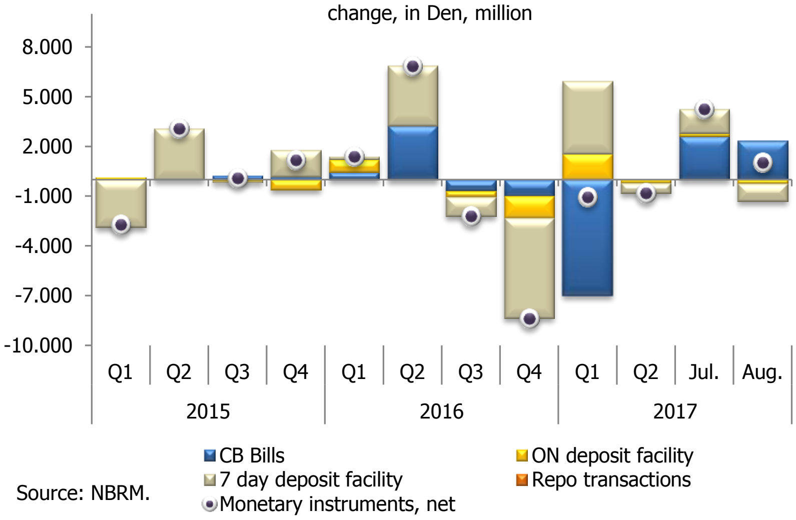
change, in Den. million



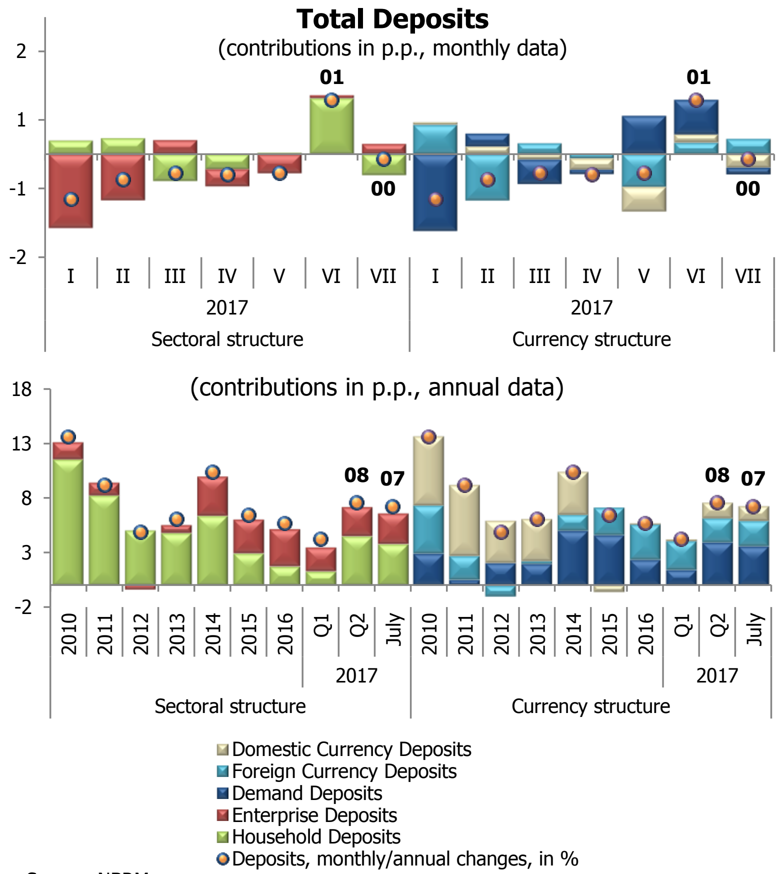
Source: NBRM.

Monetary instruments

change, in Den, million



Source: NBRM.

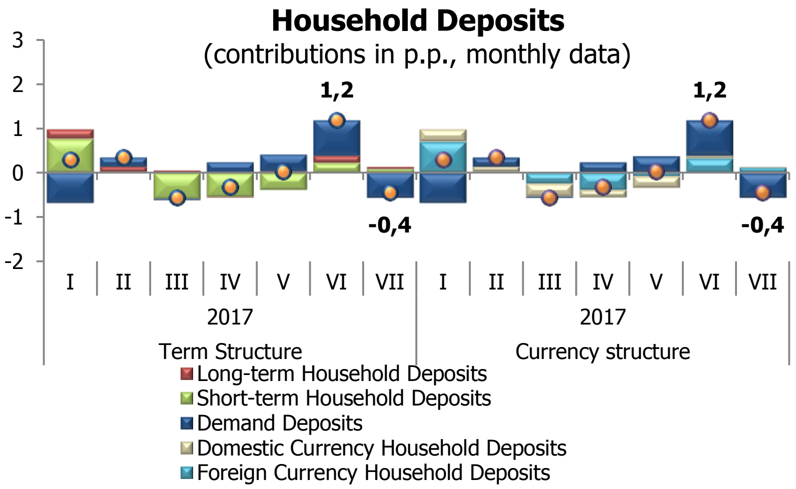


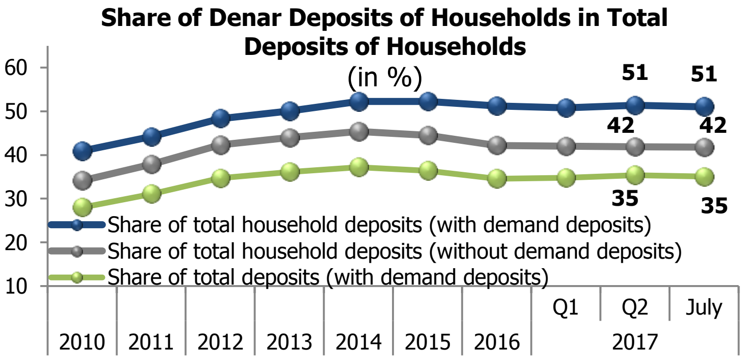
Source: NBRM.

In July 2017, total deposits in the banking sector registered a slight decline on a monthly basis, despite the increase in the previous month. Analyzed by sectors, the monthly decrease (of 0.1%) in July was entirely due to household deposits, while corporate deposits registered growth, which was moderately faster compared to the previous month. In July, the decrease in household deposits is partly associated with the withdrawal of part of the paid subsidies in the previous month as a result of the preferences of this group of economic agents to hold cash assets. In terms of currency structure, in July, Denar deposits registered a decline, while foreign currency deposits continued to grow, at a faster pace compared to the previous month.

As of July, total deposit performance is weaker than projected. However, it should be borne in mind that the data of one month are insufficient to draw a conclusion about the movements in the next two months of the quarter, and about performance of the forecasted growth.

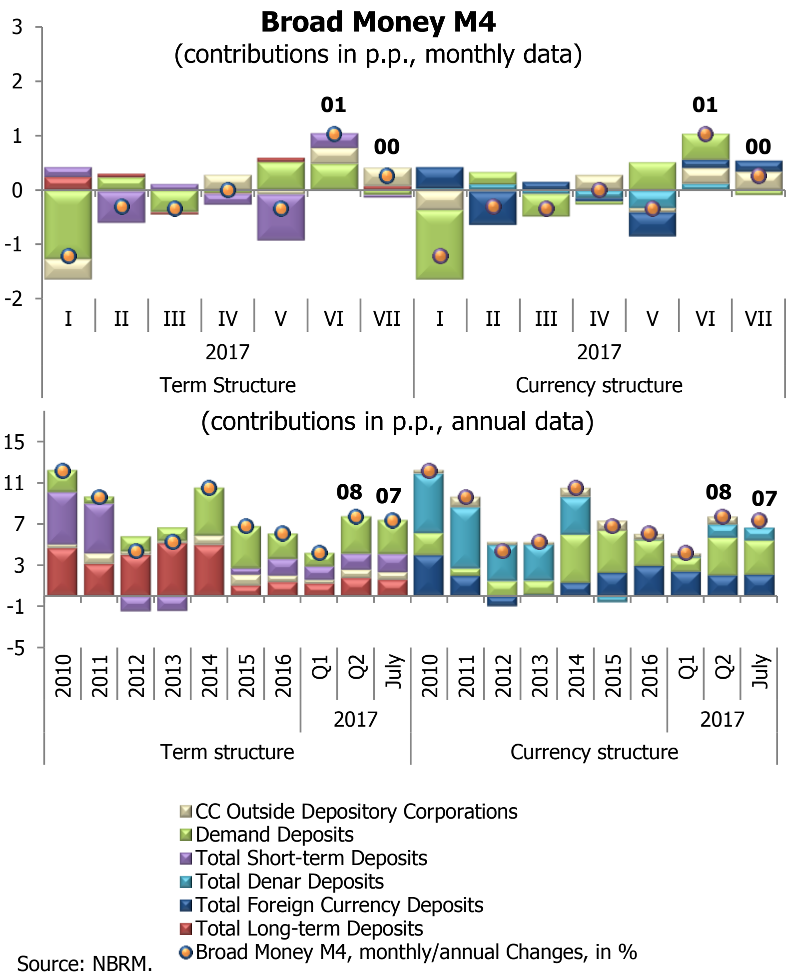
In July, the annual growth rate of total deposits equaled 7.3% (7.6% in June), which is below the growth for the third quarter of 2017 (of 7.9%) as forecasted in April. The performances in July contributed to slight decrease in the share of denar deposits in total deposits (from 58.9% to 58.6%).





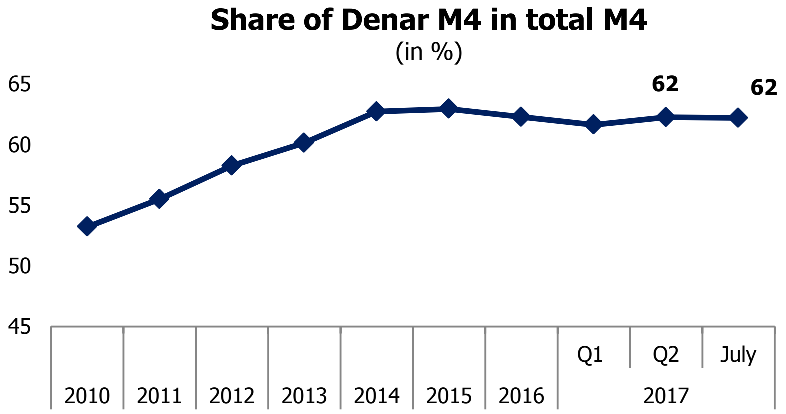
Source: NBRM.

In July, household deposits decreased on a monthly basis, despite the significant growth in the previous month. Analyzing by currency, the monthly decrease in household deposits (of 0.4%) arises from the decline in denar deposits, i.e. the demand deposits (largely due to withdrawal of the paid funds based on subsidies), despite their significant growth in the previous month. Foreign currency deposits continued to increase, but at a slower pace compared to the previous month. As a result of these developments, in July, the share of denar deposits (with demand deposits) in total household deposits decreased.

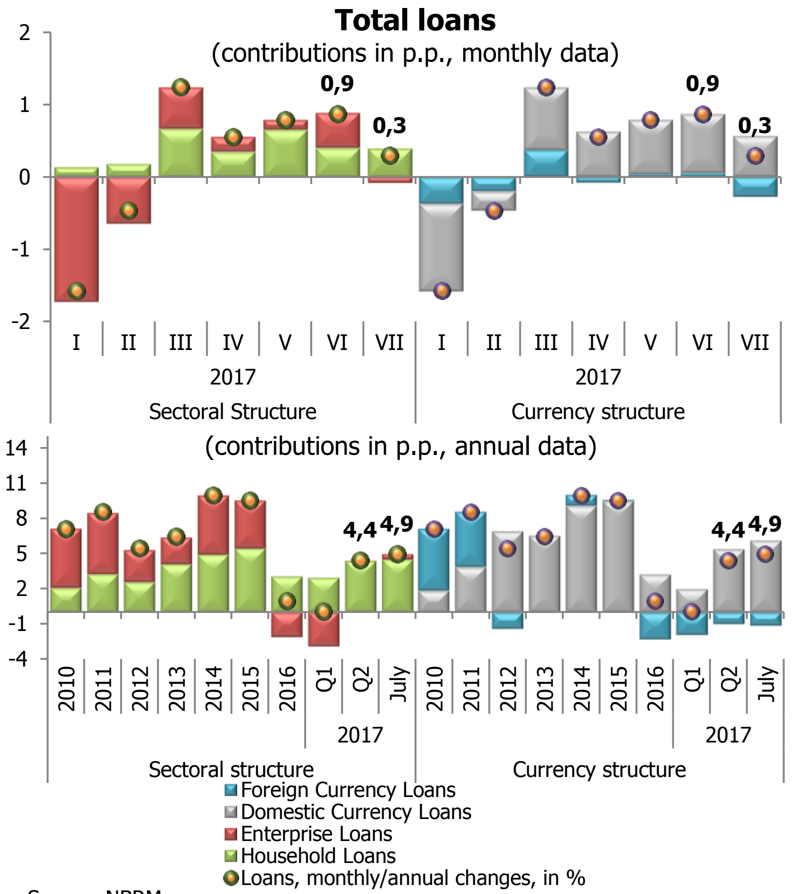


Source: NBRM.

During July, broad money M4 continued to increase, but at a slower pace compared to the previous month. The monthly growth of the broadest money supply of 0.3% is primarily due to the growth of currency in circulation and foreign currency deposits, amid negative contribution of denar deposits. **On annual basis, the broad money has increased by 7.4% (7.8% in June), which is below the forecasted growth of 7.9% for the third quarter of 2017.** The performance in July contributed to a minimal decline in the share of the denar share in the total money supply from 62.3% to 62.2% compared to the previous month.



Source: NBRM.

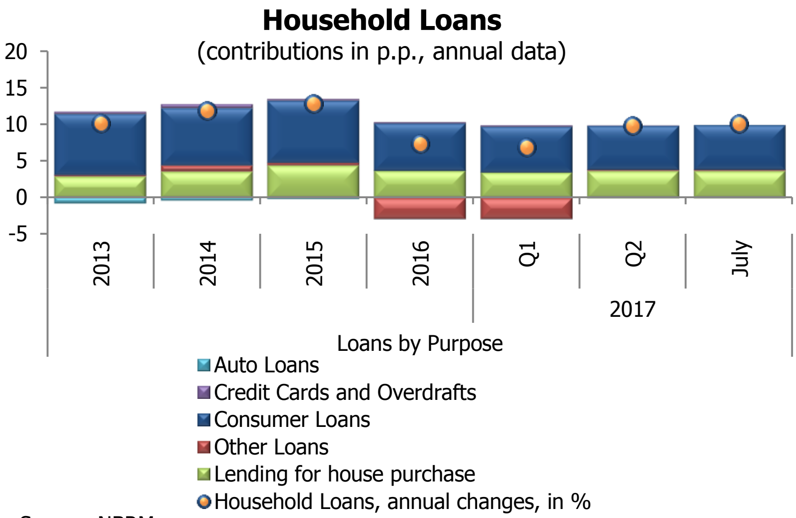


Source: NBRM.

In July, total loans to the private sector registered a monthly growth, which was slower compared to the previous month. Analyzed by sector, the monthly increase in the total lending (of 0.3%) fully arises from the higher performances in households, amid small decline in corporate loans.

As of July, total loan performance is weaker than projected. However, it should be borne in mind that the data of one month are insufficient to draw a conclusion about the movements in the next two months of the quarter, and about performance of the forecasted growth.

Despite the weaker credit flows, on an annual basis, the total loans in July grew by 4.9%, which is similar to the forecasted growth of 4.8% for the third quarter of 2017, reflecting the more favorable performance at the end of the second quarter. Observing the currency, the annual growth of total loans also in July 2017 stems from the growth of denar loans granted to households[19].

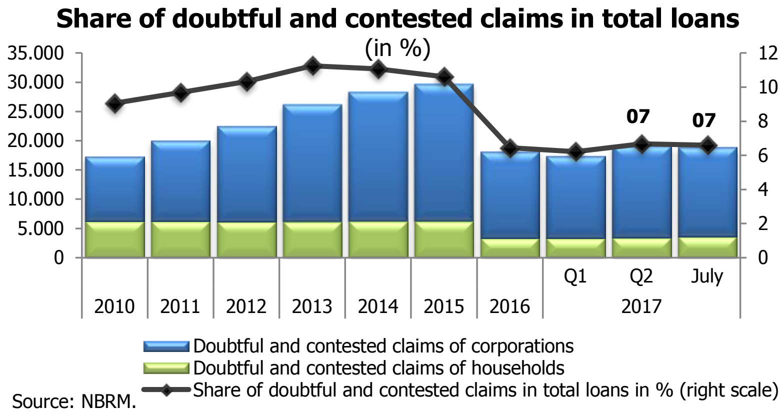


Source: NBRM.

In July, loans to households grew on an annual basis. On an annual basis, the growth of loans granted to households continued to accelerate (from 9.8% in June to 10.1% in July).

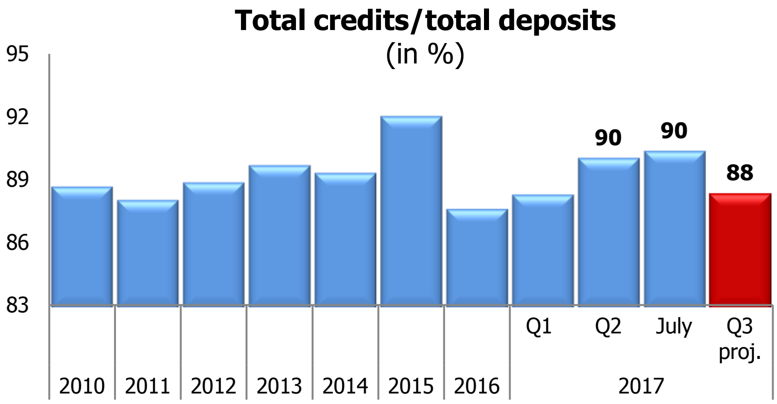
The share of doubtful and contested

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



Source: NBRM.

claims in total loans, after the growth in the previous months, in July registered minimal decline from 6.7% to 6.6%, on a monthly basis.



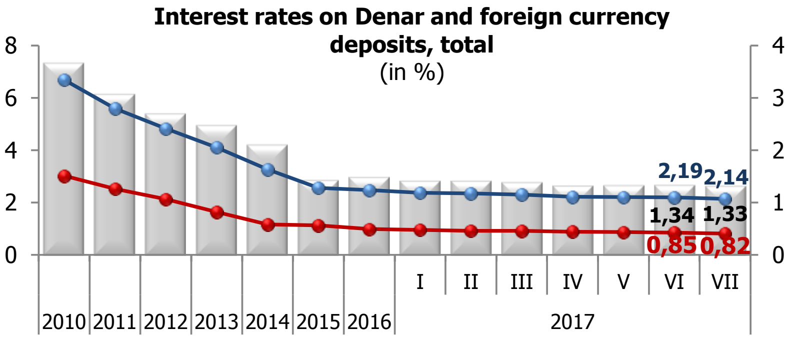
Source: NBRM.

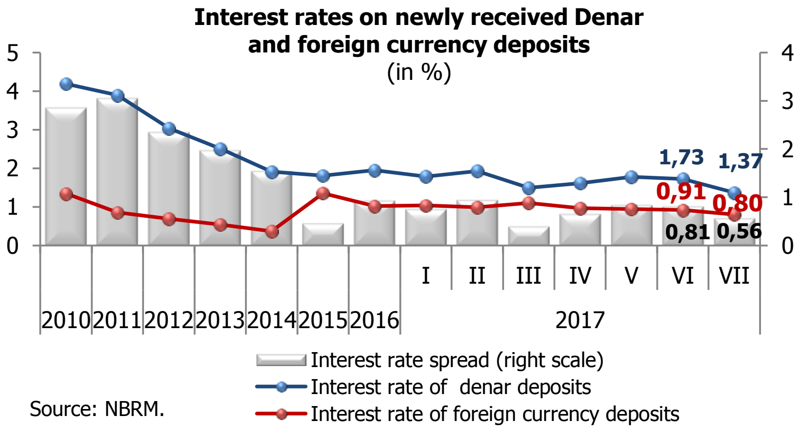
Utilization of the deposit potential for lending to the private sector in July increased on a monthly basis, from 89.9% to 90.2%. July performance is higher compared to the expectations for the third quarter of 2017, according to the April forecast.

In July, the interest rates on total deposits registered a slight downward movement in denar and foreign currency deposits compared to the previous month. In such conditions, the interest rate spread between the interest rates on denar and foreign currency deposits remained relatively stable (1.3 percentage points). For **newly accepted total deposits,** the interest spread between denar and foreign currency deposits in July narrowed compared to the previous month as a result of the relatively larger decrease in the interest rate on newly accepted denar deposits, relative to the minimal downward movement in the interest rate on newly accepted foreign currency deposits. However, regarding the interest rates on the newly accepted deposits, it should have in mind that they characterize with variable movements[20].

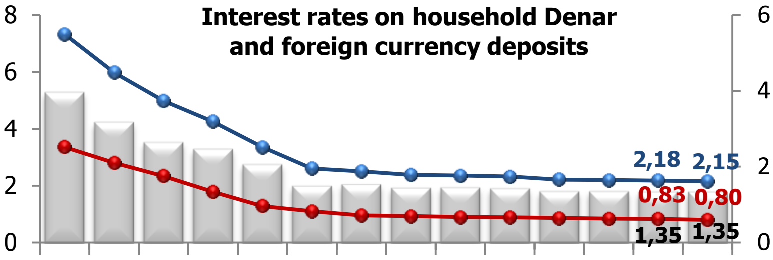
Interest rates on household deposits

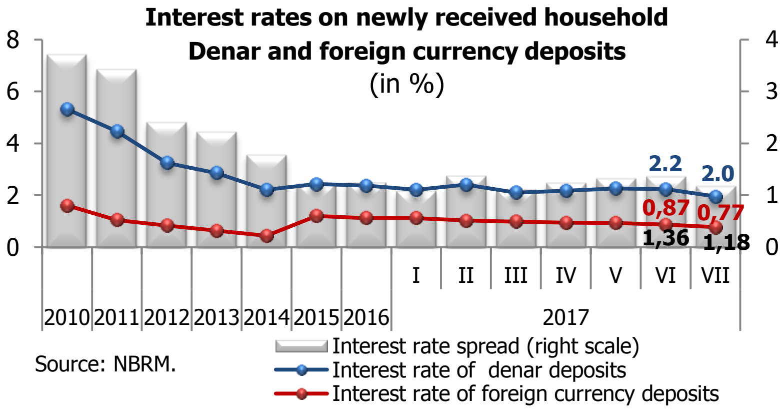
[20] Volatility of interest rate on newly accepted deposits results from the fact that they have been driven by the volume of newly accepted deposits (which can vary from month to month) and their interest rate.





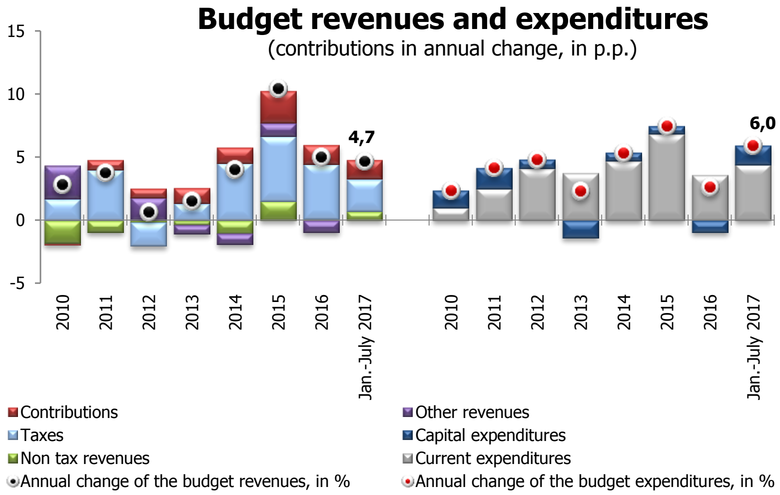
Source: NBRM.

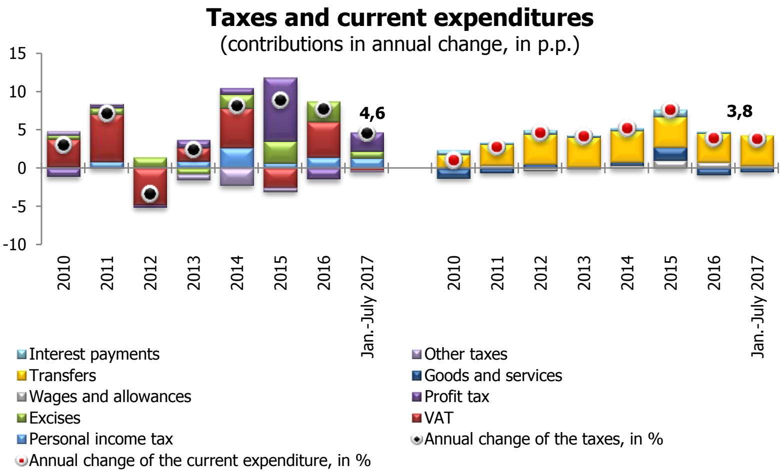


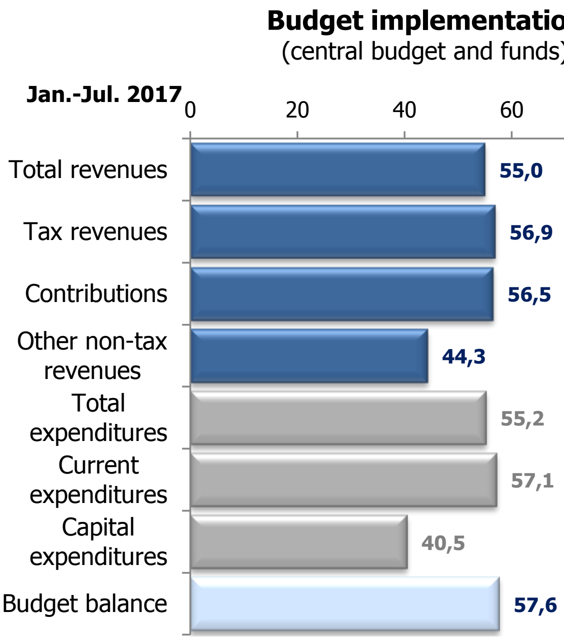


Source: NBRM.

in July moved downwards, whereby the interest rate spread between denar and foreign currency interest rates registered no changes (1.3 percentage points). Interest spread of **new household deposits** has narrowed as a result of the relatively lower interest rate on newly accepted denar deposits, relative to the minimal downward movement in the interest rate on newly accepted foreign currency deposits.







Source: Ministry of Finance and NBRM's calculations.

The total budget revenues realized in the Budget of the Republic of Macedonia (central budget and budget of funds) in the period January-July 2017, grew by 4.7% compared to the same period last year. The improved performance mostly arises from the higher realization in taxes and contributions, and to a lesser extent, from non-tax revenues.

In the period January-July, the total tax revenues in the Budget of the RM grew by 4.3% on an annual basis, whereby analyzed by individual tax categories, the largest contribution to the annual growth was made by the income from the profit tax, inflows of personal income tax and inflows of excise duties. The inflows based on VAT made a moderate positive contribution to the growth of the total tax revenues.

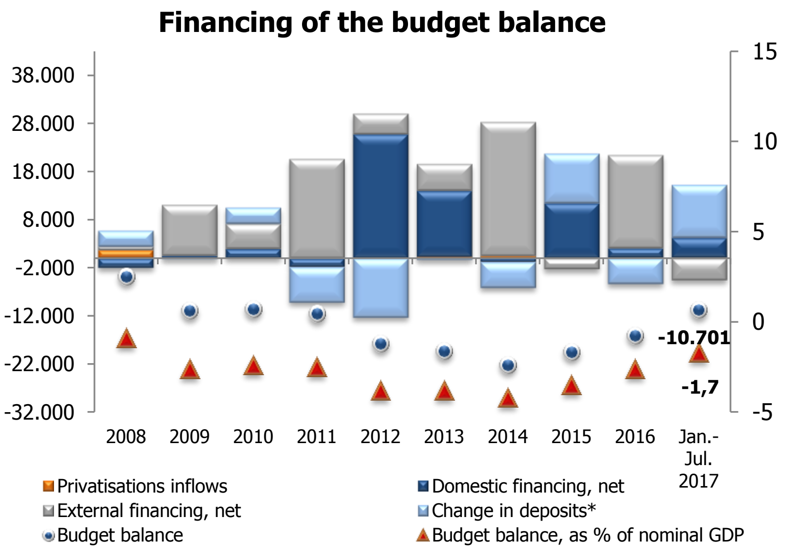
In the period January-July 2017, the budget expenditures increased by 6% on an annual basis, which is mostly due to the higher current expenditures, and to a lesser extent, from capital expenditures.

In January-July 2017, the realized budget revenues constituted 55% of the revenues projected for 2017, respectively, under the Budget Revision[21]. Analyzed by individual categories of budget revenues, higher performance was registered in taxes and contributions (realization of 56.9% and 56.5%, respectively), while the realization of the category of other non-tax revenues was lower and accounted for 44.3%.

Analyzing budget expenditures, in the period January-July 2017, 55.2% of the planned expenditures for 2017 were realized, which is mostly due to the realization of the current expenditures (57.1% of the annual plan), while the realization of the capital expenditures amounted to 40.5% of the annual plan.

In January-June 2017, the realized budget deficit constituted 57.6% of the deficit projected for 2017, respectively, under the Budget Revision.

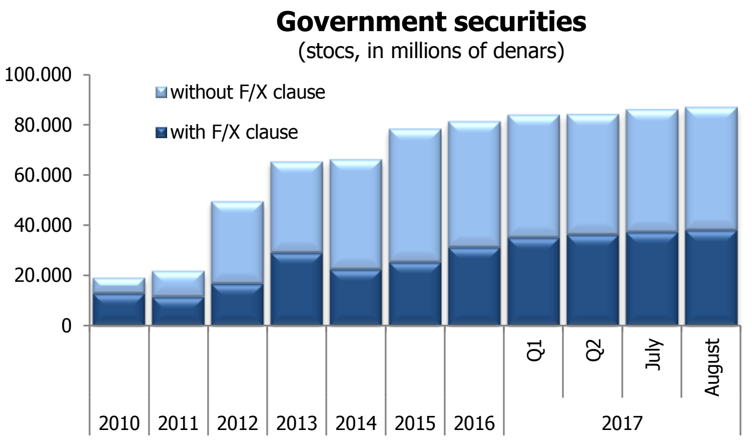
[21] The comparison is made with the Budget Revision for 2017 of August 2017.



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

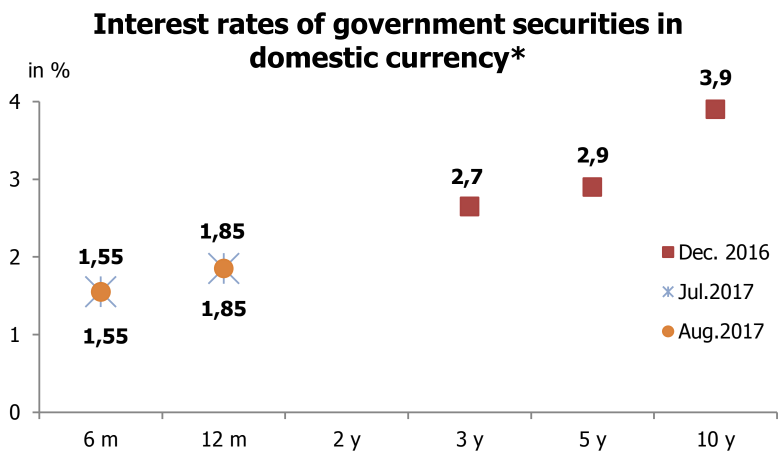
In the period January-July 2017, the Budget of the Republic of Macedonia registered a deficit of Denar 10,701 million, which is 1.7% of the nominal GDP[22].

The deficit was financed by domestic sources, by withdrawing deposits from the government account with the National Bank and net issue of government securities.



Source: NBRM.

At the end of August 2017, the stock of issued government securities on the domestic market was Denar 86,983 million, which is higher by Denar 2,743 million, compared to the end of the second quarter. On cumulative basis, for the period January-August 2017, government securities increased by Denar 5,613 million, amid growth of securities with an FX clause of Denar 6,892 million and decrease in denar securities of Denar 1,280 million.



* 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 issued government securities without FX clause in August[23] 2017 remained unchanged compared to the previous month.
Compared with the last auction of 2016, in August, the interest rates on the 6-month and 12-month treasury bills were lower by 0.75 percentage points, respectively.

[22] The analysis uses the NBRM April forecasts for the nominal GDP for 2017.
[23] At the auctions of government securities in August, there was an offer of 6-month treasury bills without FX clause, 12-month treasury bills without FX clause, 2-year government bonds with 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 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[24], 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 0.75% 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.

[24] 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, 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 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 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.

July 2017

- At the regular meeting of the NBRM's Operational Monetary Policy Committee, held on 11 July 2017, the 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.