Revision of macroeconomic forecasts
- May 2020 -

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The beginning of 2020 marked by a global crisis

- **The world has been facing one of the largest and most severe health crises** since the early 1990s, which, unlike the previous ones, is marked by an extremely fast transmission, thus inevitably requiring prompt and strong measures

- **The measures, besides being bold and prompt, have also been taken simultaneously** in all countries, which means that every economy will be affected not only by the domestic restrictive measures, but also by the unfavorable external environment (reduced foreign demand), which is especially important because of the high globalization

- **The measures imply restrictions on production factors and therefore result in reduced supply of goods and services, and lower demand.** Deteriorated expectations of economic agents, along with declining income, and especially tight financial markets conditions will delay private spending and investment. Hence, this is a specific combined shock to supply and demand

- **It is therefore generally expected that the health shock will have greater economic effects, at least in the short term, and the severity of the effects by country** will depend on the success of health measures and the speed of restarting the capacities, on private sector balance sheets capability to absorb shock, as well as on the response of fiscal, monetary and financial policies to mitigate the effects

IMF forecasts for the global economy

- **According to the IMF, after the global growth of about 3% last year, it is expected to fall by 3% this year,** which is the largest fall after the Great Depression (the fall in 2008 was 0.1%)

- **There are forecasts for synchronized recession** in almost all economies, more pronounced in developed economies (decline of 6.1%), and less in developing economies (decline of 1%).

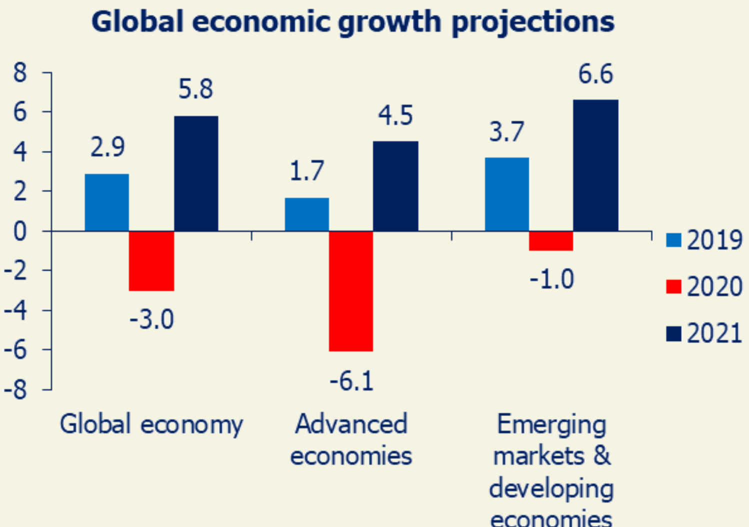
- **Economic losses most pronounced in the second quarter of the year** - a gradual recovery in the following period and a *solid and widely dispersed growth in 2021 of 5.8%*

- **A key assumption** - a gradual mitigation of the severity of pandemic in the second half of the year and a sequential reduction in restrictive measures

- **In case of slower pandemic management,** expectations for stronger decline for this and next year

- Amid sharp drop in demand, **all primary commodity prices are expected to fall,** energy in particular

* Due to the high level of uncertainty in current global economic conditions, the April 2020 WEO database projections are provided only through 2021.
Source: IMF, WEO database.



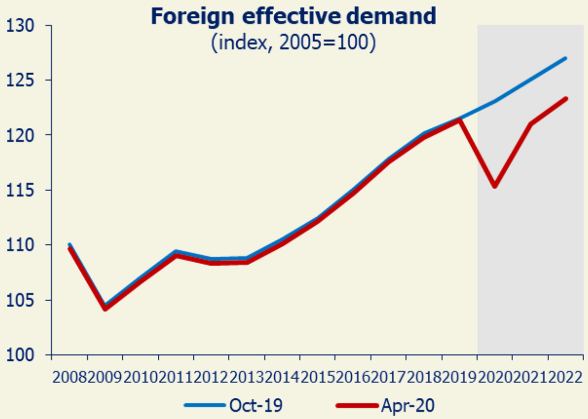
Source: IMF World Economic Outlook, April 2020.

External environment implications on foreign effective demand

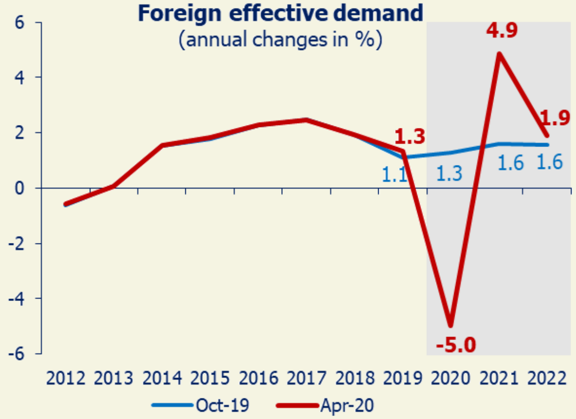
- **Foreign demand for our goods and services is expected to fall by 5% in 2020** (similar intensity as in 2008), and then to grow by 4.9% in 2021 and 1.9% in 2022 - significant downward correction compared to October forecasts of 1.3% growth in 2020 and 1.6% in the next two years

- **The downward correction reflects lower expectations for all our major trading partners** (decline from -2.6% to -9%), with the largest contribution of the German economy, which is our major trading partner

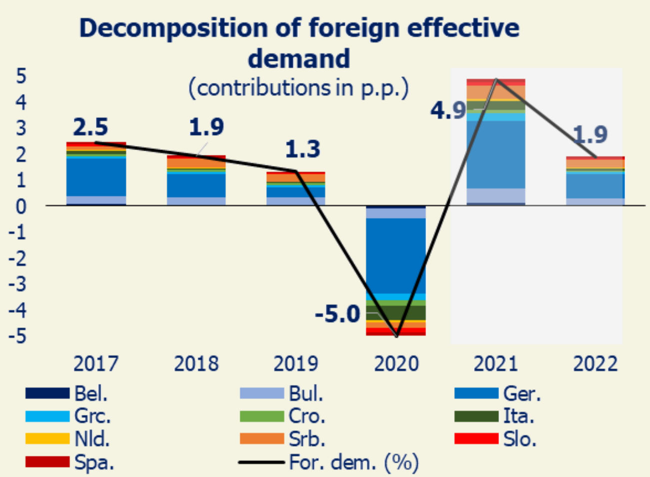
- **Risks** to the growth forecasts for our trading partners are mainly downward (high uncertainty about the duration of health crisis, pace of relaxation of measures and potential occurrence of a second wave of pandemics)



Source: Consesus Forecasts and NBRNM calculations.



Source: Consesus Forecasts and NBRNM calculations.

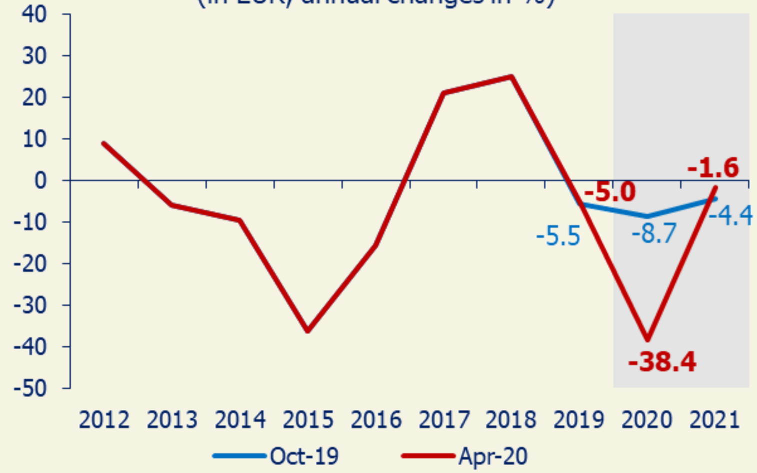


Source: Consensus Forecasts and NBRNM Calculations

External environment implications on import and export prices

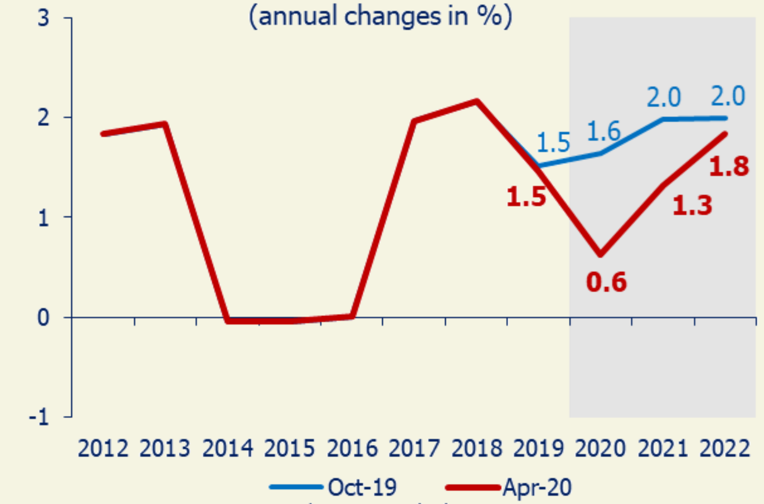
- **Generally lower import prices (foreign effective inflation)** compared to October, but still in the zone of positive changes of 0.6% and 1.3% for 2020 and 2021, respectively
- **Sharp downward correction of energy prices, especially in oil (nearly 40%)** - high supply, and reduced global demand, with a sharp decline in consumption due to reduced travel, transport and manufacture
- **Food prices** revised downwards for both years (except for wheat, which has been revised upwards for 2020) - amid a solid level of inventories and declining demand due to the pandemic, with possible logistical problems and export restrictions
- **Analyzing export prices,** higher metal price revisions (about 17% decline instead of growth)
- *Overall, this entails lower inflationary pressures, positive effect on imports and negative effect on exports*

Brent crude oil price
(in EUR; annual changes in %)



Source: IMF and NBRNM calculations.

Foreign effective inflation
(annual changes in %)



Source: Consesus Forecasts and NBRNM calculations.

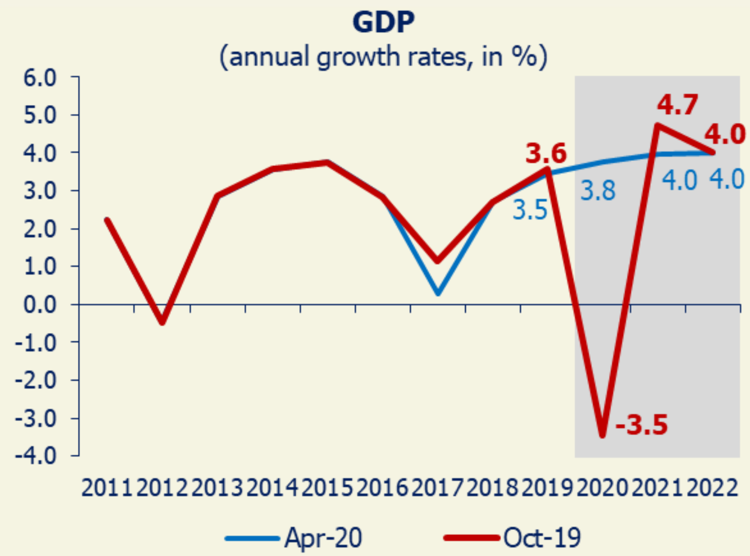
Forecast assumptions for the Macedonian economy

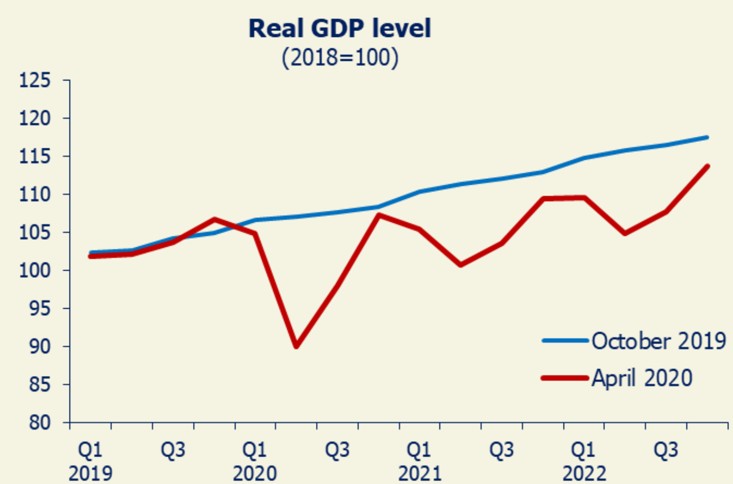
- **Unfavorable external environment with a sharp decline in foreign demand this year**, but a solid recovery next year, in line with the IMF forecasts
- **Domestic virus containing measures** to have the most pronounced adverse effects on consumption and investment in the second quarter, followed by a relaxation in restrictions
- **More expansive fiscal policy** aimed at protecting public health and mitigating the effects of the crisis this year, followed by stabilization of budget deficit in line with the mid-term Fiscal Strategy of December 2019
- **Continuation of public investment cycle,** but at weaker pace this year, and acceleration in the next
- **Maintaining favorable financial conditions** as a result of measures taken by the central bank
- **Existing export facilities, which are part of the production chains, more likely to be hit in the second quarter,** followed by gradual recovery

Macroeconomic scenario for 2020 - 2022

GDP forecast

- **After a solid growth of 3.6% of the Macedonian economy in 2019…**
- … faced with **global economic contraction and domestic measures** to curb the spread of the virus…
- …**we expect contracted economic activity** - a decline of **-3.5%** in 2020 and recovery of 4.7% in 2021, with a return to medium-term forecasts of 4% in 2022
- **Despite the expected recovery next year,** the level of economic activity remains lower than previously expected





Source: State Statistical Office and NBRNM calculations.

GDP forecast

- **Expectations for fall in all GDP components except in public consumption:**

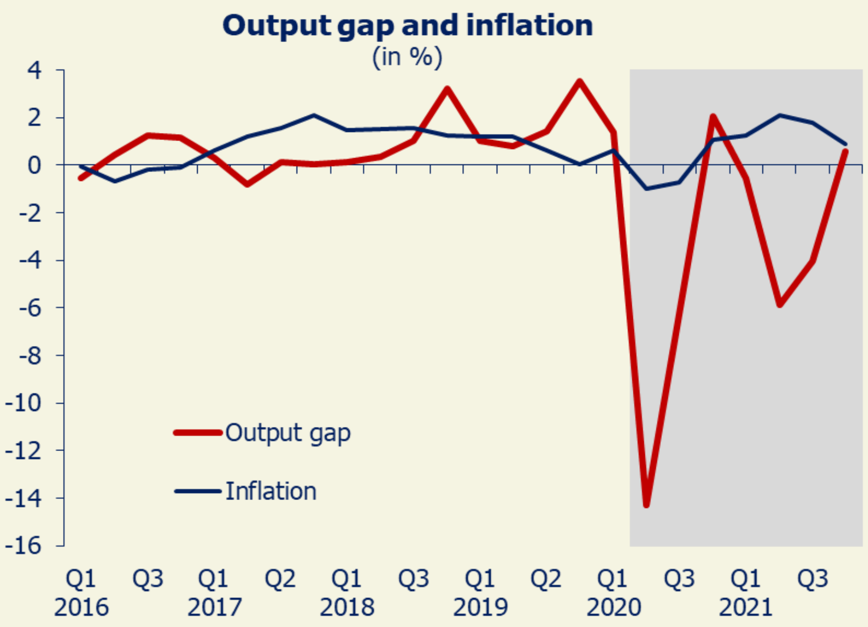
  - **Private consumption** - a decline of about 4% due to the declining disposable income amid unfavorable labor market and falling private transfers, reduced lending, increased uncertainty and restraint
  - **Gross investment** - down about 10% due to lower foreign and domestic - public and private investment, reflecting the increased uncertainty and slower credit support
  - **Exports** - down about 17%, due to reduced foreign demand, stagnation in supply chains and domestic restrictive measures
  - Reduced private and investment demand and declining exports will also reduce **imports** by about 15%

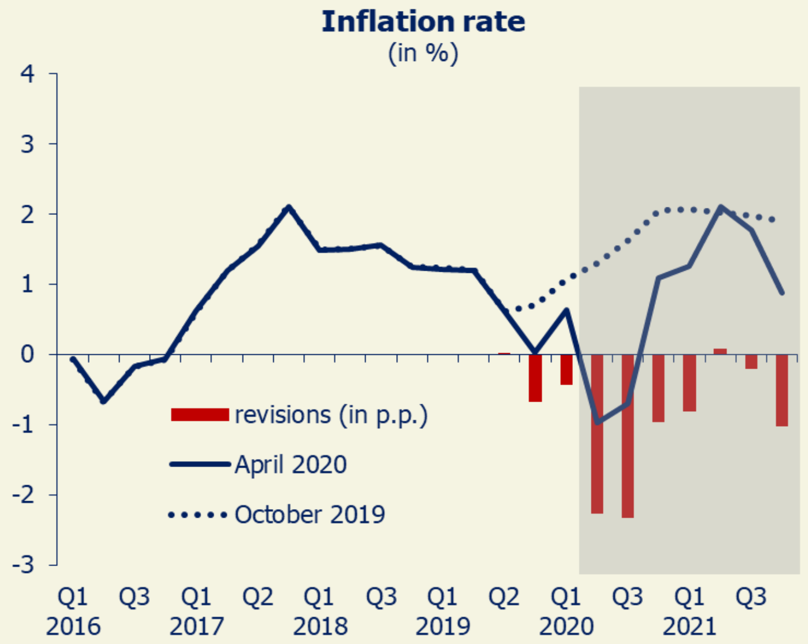
- **High uncertainty with pronounced downward risks - additional simulation**

	GDP	Private consumption		Gross capital formation		Exports of goods and services		Imports of goods and services		Public consumption		Domestic demand	Net exports
	%	%	*p.p.*	%	*p.p.*	%	*p.p.*	%	*p.p.*	%	*p.p.*	*contrib. in p.p.* **(Apr. 20)**	
2019	**3.6**	3.6	*2.4*	6.5	*2.2*	8.6	*5.1*	9.2	*-6.7*	4.4	*0.7*	*5.2*	*-1.6*
2020	**-3.5**	-4.3	*-3.1*	-10.4	*-3.3*	-17.1	*-11.9*	-15.4	*13.9*	6.6	*0.9*	*-5.5*	*2.0*
2021	**4.7**	6.1	*4.3*	9.8	*2.8*	25.0	*14.9*	21.6	*-17.1*	-1.5	*-0.3*	*6.9*	*-2.2*
2020-2021	**0.6**	**0.9**	***0.6***	**-0.3**	***-0.2***	**4.0**	***1.5***	**3.1**	***-1.6***	**2.5**	***0.3***	***0.7***	***-0.1***

Inflation forecast

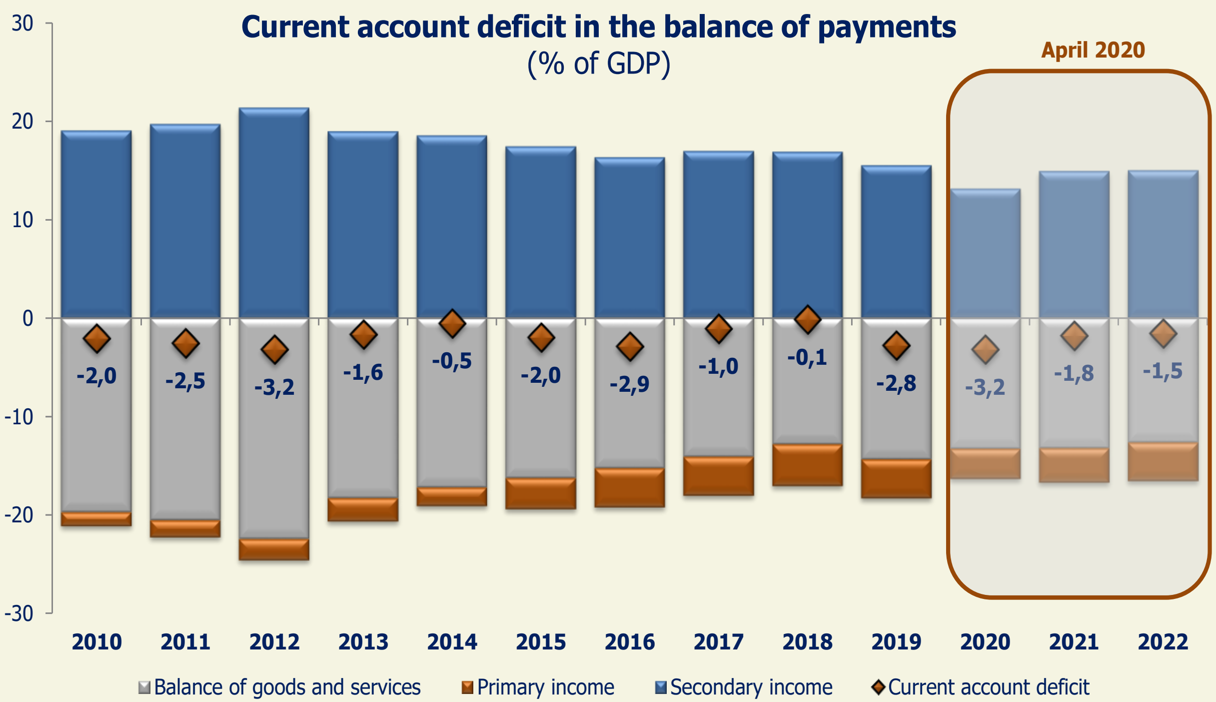
- **Downward inflation revision for this and next year: to about 0% for 2020 (from 1.5% in October) and to 1.5% for 2021 (from about 2% in October)**
- **Reasons behind the downward revision:** in the first quarter, inflation below forecasts (0.6% versus 1.8%), and downward revision of expectations for import prices and domestic demand
- **In the medium term, maintaining the October inflation forecast** at around 2%
- In the forecast horizon, **no expectations for pressures from the domestic demand** amid assessments of predominantly negative output gap
- **Risks** to the forecast inflation trajectory mainly attributed to the uncertainty surrounding the import prices of food and energy sources

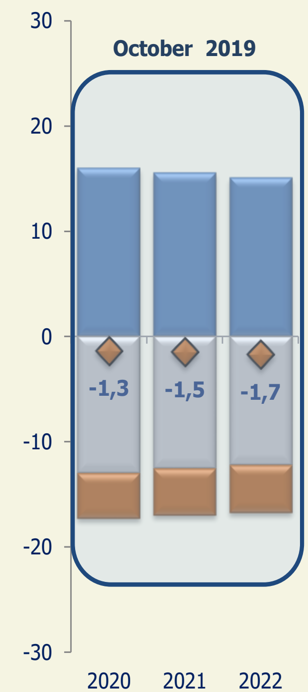




Balance of payments
- current account -

- **In 2020, current account deficit of 3.2% of GDP (wider compared to the October expectations for 1.3% deficit of GDP)**
  - reduced **private transfers** (reduced supply, especially due to lower remittances from abroad)
  - lower surplus in **services** (mainly travel and transport)
  - lower **trade deficit** (stronger effect of the fall in imports than exports due to lower import pressures of domestic demand and sizable fall in energy prices)
  - lower **primary income** deficit
- **In the period 2021 - 2022, gradual narrowing, with an average deficit of 1.6% of GDP, without changes compared to October**



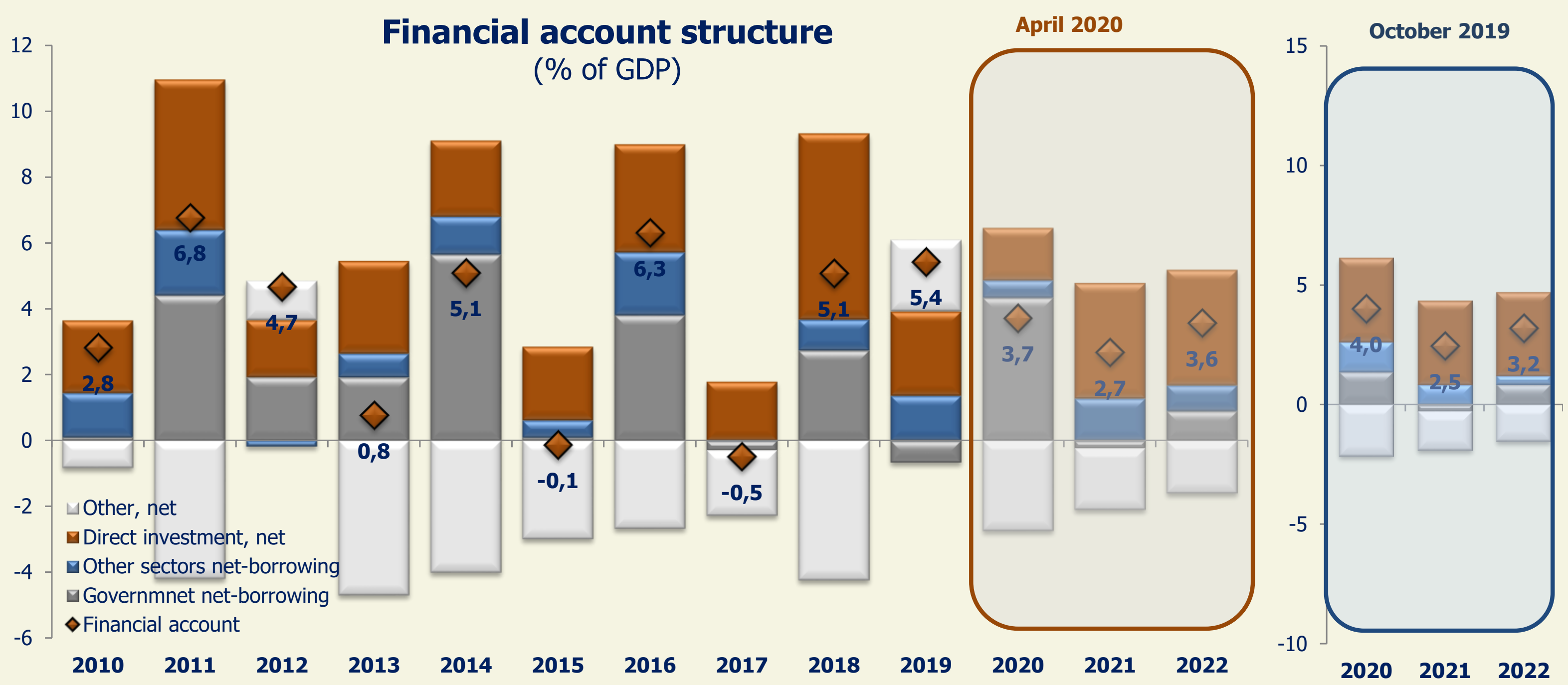


Balance of payments
- financial account -

- **Financial account inflows for 2020** (3.7% of GDP - lower compared to October) - mainly in the form of external government borrowing and direct investment, ensuring full current account deficit financing and additional moderate accumulation of foreign reserves

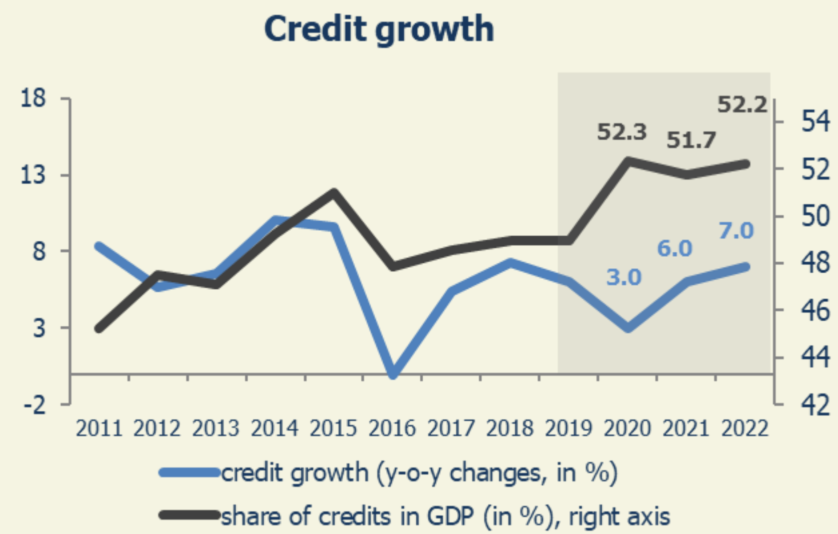
- In the following period (2021-2022), financial net inflows averaging 3.1% of GDP - mainly from direct investment

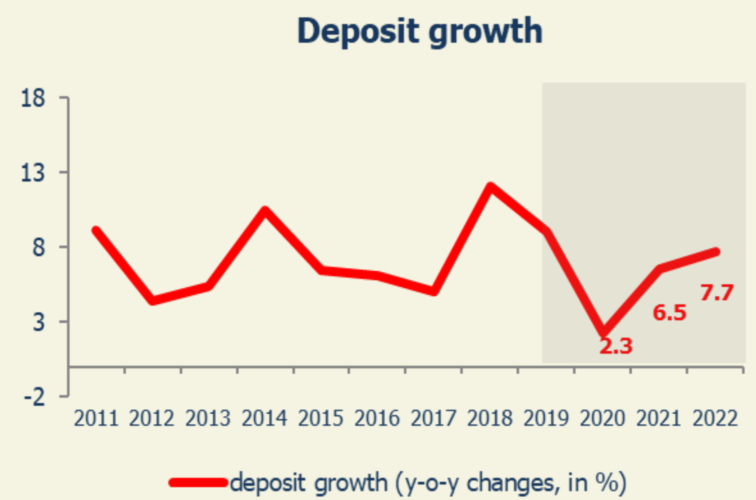
- Over the forecast horizon, **foreign reserves adequacy indicators** (ratio of reserves with the forecasted import of goods and services, with debt etc.) are in the safe zone



Deposit and credit growth

- **Solid deposit and credit growth in the first quarter of 7.9% and 5.8%, respectively**
- **Yet expectations for a slowdown in deposit growth of 2.3% and in credit growth of 3% this year,** followed by gradual acceleration to about 8% and 7%, respectively, in the medium term
- Adverse effects of the contracted economic activity on businesses and household income, and thus on savings
- On the other hand, the external government financing and the targeted measures to the affected sectors will have mitigating effects on the deposit base
- **Bank lending** will be determined by the assessments of the funding sources and risk perceptions; greater focus on restructuring the existing credit exposures - **the National Bank measures and favorable loans from the Development Bank with mitigating effects of the crisis**





Risks to the forecast

- Risks are an integral part of any forecast, but this time they are extremely high
- They arise from the external environment, but from the domestic context as well:
  - **Prolonged health crisis or second wave of the crisis could entail further contraction in global activity,** significant cross-sectoral spillover, adverse effects on corporate balance sheets, greater risk aversion and tightening of international financial markets
  - **The deteriorating external environment along with the protraction of the health crisis in our country** could slow down recovery of exports and domestic demand, reduce foreign exchange inflows, increase the risk of feedback loops between real and financial flows, hinder access to capital markets

- **In the case of risk materialization,** potential deviation from the forecast in all segments, including a sharper GDP fall

- **Simulation of twice as high fall of foreign effective demand in 2020,** i.e. a decline of 10% (versus 5%) would lead to **a stronger decline of GDP by 2.3 percentage points,** compared to the baseline forecast, with more pronounced adverse effects on exports and investment demand

Summary

- **The latest forecasts imply a complete redesign of the macroeconomic landscape for this year**
- In the short term, unfavorable effects are expected in several segments, as well as retention of the sound fundamentals which will be extremely important during the recovery
- Given solid foreign reserves and low inflation, **the National Bank has eased the monetary policy** and took additional measures to mitigate the effects of the crisis and support the economy
- **Policy rate cut** of 0.5 percentage points from the beginning of the year
- **Introduction of unconventional measure** to reduce banks' reserve requirement for the amount of newly approved and restructured loans to the affected sectors
- **Release of Denar 8 billion liquidity** through CB bills
- **Loosening of the regulatory framework** - aimed to alleviate the financial burden of the borrowers, while maintaining prudence, without jeopardizing financial stability
- **In the period ahead, the National Bank will closely monitor the trends** and changes in the domestic and external environment for the purposes of adequate monetary policy adjustment

THANK YOU FOR THE ATTENTION!