National Bank of the Republic of North Macedonia

Quarterly Report
August 2024

CONTENTS

Introduction

In the second quarter of 2024, the National Bank made additional changes in the monetary policy setup, as required by the economic conditions. The interest rate on CB bills remained 6.30%, simultaneously keeping the interest rates on overnight and 7-day deposit facilities at 4.20% and 4.25%, respectively. In conditions where the inflation dynamics does not deviate from the spring National Bank's forecasts, and the latest forecasts of the primary products prices on the stock markets have been revised moderately upwards, with the unstable geopolitical context further creating uncertainty and upward risks for the next period, *it was assessed that further caution in the monetary policy conduct is required.* The current level of interest rates, together with the changes in reserve requirement and macroprudential measures taken, is expected to contribute towards further inflation slowdown and exchange rate stability maintenance. The latest changes in the reserve requirement instrument, the application of which commences in June 2024 and are generally aimed at further support of the denarization process and increasing the long-term saving in the banking system, provide as well additional support to the prudent monetary policy. Regarding the European Central Bank (ECB) policy, at the latest meeting in June it was decided to cut the policy rates by 0.25 percentage points, in line with the market expectations. The ECB emphasized that despite the decrease, with the new level of interest rates, the monetary policy remained tight and prudent.

The global economic activity shows certain improvement despite the challenges. Namely, after the continuous deceleration in the last two years, the global growth dynamics is expected to stabilize, a perception which generally matches the April forecast. However, despite the improvement in the short-term prospects, the growth remains small in historical context, i.e. below the average in the decade preceding the pandemics. **The global risks remain downward despite the possibility for certain unexpected upward movements.** A possible escalation of geopolitical tensions could increase the raw materials prices, while further fragmentation pose a risk of further disruptions to trade chains. This could result in larger inflation inertia and could delay monetary easing. Keeping the interest rates higher for a longer period could result in global activity reduction. On the other hand, the possible faster slowdown of the global inflation than expected, according to the baseline scenarios, would also enable faster monetary easing. In addition, growth in the US could also be stronger than currently expected.

The latest indicators of the domestic economy suggest macroeconomic landscape that does not deviate much from the April forecasts. Namely, the real GDP in the first quarter registers annual increase of 1.2%, as opposed to the growth expectations of 1.7% according to the April forecast round. Analyzed by structure, the growth results from the positive contribution of the domestic demand, registering an increase in all three components, primarily in gross investments, in circumstances of growth in the investments in fixed assets and inventories. On the other hand, net exports made a negative contribution, given the decline in the exports and small increase in the import of goods and services. **Available high-frequency data on economic activity show early signs of acceleration in the annual growth in the second quarter of the year, with more favorable shifts, primarily in the services segment and construction activity.** Namely, for now, in the second quarter there is a the annual pace of the decrease in total trade decelerated, in real terms, while in the real turnover in catering, as well as in the construction works, the annual growth accelerated. On the other hand, the industrial output kept registering unfavorable trends, the reduction of which deepens in this period. For the time being, such achievements correspond to the April estimates for larger annual GDP growth in the second quarter of the year. For the entire year, the April baseline scenario suggests accelerated economic growth from 1% in 2023 to 2.6%, followed by its intensification to 3.6% in 2025. For 2026, a moderate growth acceleration is expected, in conditions of less favorable external environment, more stable environment and greater propensity for consumption and investments. **The risks for the economic prospects in a short run remain mainly downward.** Rising geopolitical tensions due to the war in Ukraine and the conflict in the Middle East are key risks in the short term, with the potential to cause significant disruptions in energy and commodity markets. In the medium term, a stronger commitment to capital projects, including the new European Union growth plan for the Western Balkans, which means access to additional European funds, could improve the economic prospects of the domestic economy.

In the second quarter of 2024, the annual inflation rate accelerated moderately to 3.9%. The acceleration is mostly associated with the inflation food component, partly influenced by the effect of short-term measures to reduce and freeze the prices of some food products in the domestic retail trade, which were lifted at the beginning of March. It slightly accelerates the growth of the energy component, according to the movement of oil prices on the world stock markets. Core inflation continues to decelerate on an annual basis, reflecting the previous tightening of monetary conditions. According to the April forecast, for 2024 it is expected that the average inflation will reduce to the level of 3.5%, after which it will stabilize at 2% in 2025, a level that will be preserved for the following 2026. Inflation risks still exist and are related mainly to the prices of primary commodities on world stock markets. Namely, extreme weather conditions, increased geopolitical tensions, as well as possible changes in policies could disrupt the balance between global demand and supply and affect prices.

In the second quarter of 2024, the lending activity of the banking sector remained solid. On an annual basis, the growth rate of the total loans accelerated slightly and this quarter equaled 6.4%, which is beyond the expectations in the April forecast. Observing the sources of financing, **the deposit base registered a quarterly growth in the second quarter, after the usual seasonal decrease in the first quarter, given solid annual deposit growth of 7.6%, which is below the expectations for the end of the second quarter according to the April forecast.** Favorable movements continue in terms of maturity and currency structure of savings (growth in denar and long-term deposits), reflecting the effects of the measures taken by the National Bank and stabilized expectations of economic agents.

The latest available data on the balance of payments indicate generally favorable movement, at slightly higher current account deficit, but simultaneously lower realized net outflows in the financial account than expected. Compared on an annual basis, the current account in the first quarter of 2024 recorded a deficit of 1.3% of GDP, against the realized surplus in the same period of the previous year, which mainly results from the higher deficit in the foreign trade in goods, and then from the lower surplus in secondary income. On the other hand, the balance of services slightly improved, while the deficit in primary income is almost unchanged. In the first quarter of the year, the financial account recorded net outflows of 0.9% of GDP, with net outflows in most categories, except direct investments, where significant net inflows were realized during this period. **Gross foreign reserves data for the second quarter indicate better performance than the expected in April forecasts, and they remain in the safe zone.**

In general, according to the latest realization of the macroeconomic indicators, the achievements in the key segments are currently close to the expectations from the latest forecast. Domestic inflation accelerated more moderately than it was forecasted in April, which was the case also with the domestic economic activity. The growth of the banks' deposit potential is slightly

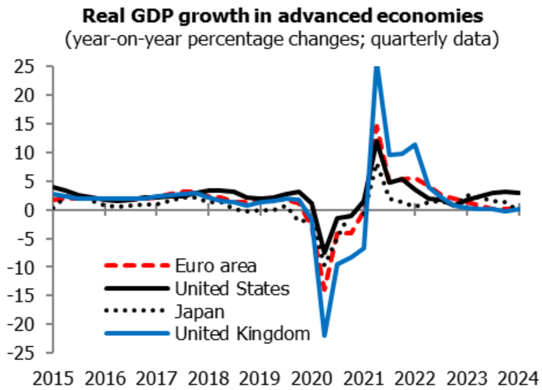
more moderate, but remains solid, and allows maintaining the credit growth, which slightly exceeds the projection. The external position of the economy is favorable and allows increase in the foreign reserves, which are maintained in the safe zone. ***However, the environment for conducting monetary policy remains vague, with the risks to the world and domestic economy on short and medium run still persisting.*** **Consequently, need for further caution in the monetary policy conduct and in general, the policies affecting demand in the economy is assessed.** ***The National Bank remains prepared to use all the necessary instruments and to take adequate measures that will contribute to the exchange rate stability maintenance, stabilization of inflation expectations and to medium-term price stability.***

I. Macroeconomic developments

1.1. International economic surrounding

Global economic activity continues to increase moderately in the first quarter of 2024, amid geopolitical tensions and tight financial conditions. In the euro area, which is our most important trading partner, economic activity recorded a slight annual growth in the first quarter of 2024, after stagnation in the past two quarters. Inflation at the global level shows a deceleration trend, but certain price pressures that arise mainly from core inflation still persist. In such conditions, the monetary policy in the developed countries did not change in the second quarter, except in the euro area, where after almost two-year increase in the policy rate, the ECB made a decision on their reduction by 0.25 percentage points. On the world stock markets, in the second quarter of 2024, the prices of primary commodities (oil, food and metals) recorded quarterly growth. According to World Bank forecasts in June 2024, the global economic growth is expected to stabilize at 2.6% in 2024. A slight acceleration of economic growth to 2.7% is expected for 2025 and 2026, supported by stronger investment growth and intensified global trade. Moreover, compared to the January forecasts, the expectations for 2024 have been revised upwards by 0.2 percentage points, while for 2025 they remain unchanged. Inflation is expected to decrease further, but more slowly compared to previous estimates.

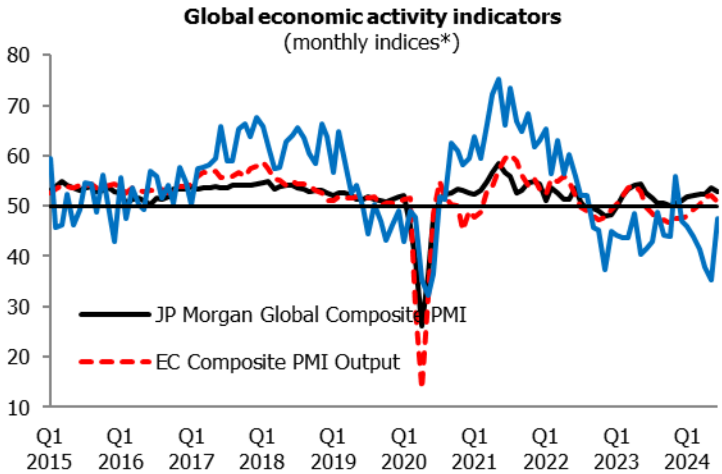
The global economic activity remains resilient, despite subsequent shocks and ongoing uncertainty, registering a growth in the first quarter of 2024, as well. Regarding developed countries, the improved better net export was the main factor for the UK's small annual growth of 0.2% (slight decline of 0.2% in the fourth quarter) and the growth of 0.4% in the euro area (0.2% in the previous quarter). The growth of the US economy decelerated slightly in the first quarter to 2.9% (3.1% in the previous quarter), but it is still the highest among developed countries, and the slowdown is mainly due to slightly weaker growth in private consumption and unfavorable shifts in net exports. On the other hand, economic activity in Japan reduced and for the first time after three years of constant growth, recorded a slight decline of 0.3% (growth of 1.2% in the fourth quarter), in conditions of less favorable trends in both domestic demand and in net exports. The emerging economies register further generally better performance compared to developed countries and maintain solid growth rates, although some countries face with moderately decelerated growth. Namely, in the first quarter of 2024, the Chinese economy continued to grow at a rate of 5.3% (5.2% in the previous quarter). India recorded a slight slowdown in growth, which amounted to 8.4% (8.8% in the fourth quarter), influenced by weaker growth in fixed asset investments. In Brazil, economic growth also slowed down to 1.7% (2.2% in the previous quarter), amid worsening in the net exports.



Source: OECD.

Source: OECD and Russia's statistical office.

As for the global growth estimates in the second quarter of 2024, the average value of the global PMI equaled 53.0 (52.1 in the first quarter), indicating favorable movements in the global economic activity in the following period. Annually, the global PMI index decreased by 1.4%.



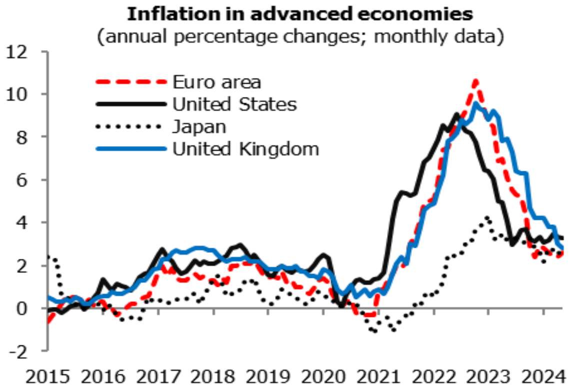
*The PMI index reflects the percentage of respondents that reported better bussiness conditions compared to the previous month and it can take values between 0 and 100. PMI=50 is considered as a reference value, indicating unchanged economic conditions. A PMI value over 50 is taken to indicate that the economy is expanding, while a PMI value below 50 suggests that the economy is contracting.
Source: Markit, ISM-Chicago.

The global economic growth[1] **is expected to stabilize to 2.6% in 2024, and that in the conditions of the still present geopolitical tensions and tight monetary policy, a slow investments growth and a moderate increase in the household consumption is expected, partly due to the already reduced savings and fiscal consolidation.** A slight acceleration of economic growth to 2.7% is expected for 2025 and 2026, supported by the increase in investments and strengthening of global trade. However, the projected average growth will be lower by 0.5 percentage points compared to the growth registered in the decade before the pandemic (average for the period 2010-2019). Moreover, compared to January forecasts, the expectations for 2024 are revised upward by 0.2 percentage points, while there are no changes for 2025. **The inflation is expected to keep decreasing, in conditions of restrictive monetary setup and deceleration of the wage growth trend,** but slower than previously expected. This is primarily due to the further high rise of services prices, which will keep the core inflation at a higher level. The risks in relation to the

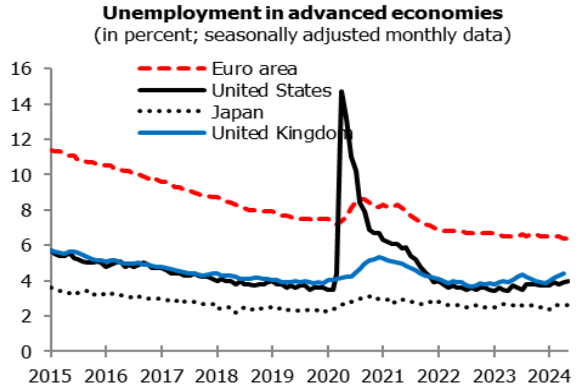
[1] The analysis in this section is based on the World Bank report "Global Economic Prospect" published in June 2024.

projected global economic growth are mainly downward and are related to the worsening of geopolitical tensions, which would contribute to the instability of the prices of primary commodities and the global trade slowdown. At the same time, a slower reduction in inflation may lead to a delay in the start of monetary easing and consequently, to a deterioration of financial conditions. China's weaker-than-expected growth, as well as climate change, are among the other unfavorable risks for a global growth.

Inflation at the global level mainly shows a deceleration trend, but certain price pressures persist, resulting mainly from the still high core inflation, as well as food. Among developed countries, the average inflation in the United Kingdom in the first two months of the second quarter slowed to 2.9% (3.9% in the first quarter), while average inflation rates in the euro area, the United States and Japan were similar as in the previous quarter and amount to 2.5%, 3.3% and 2.7%, respectively.



Source: Eurostat and national statistical offices.



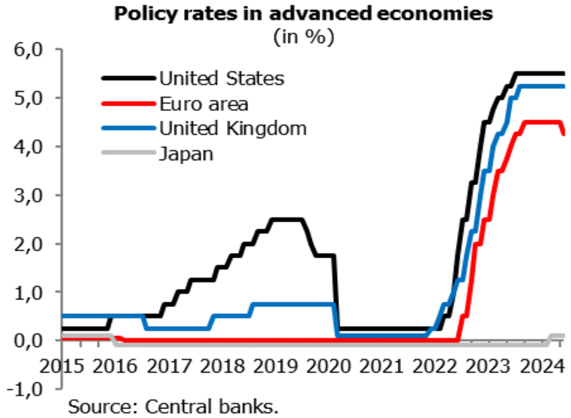
Source: Eurostat and UK's statistical office.

In the euro area, which is our most important trading partner, the economic activity registered a slight annual growth in the first quarter of 2024 of 0.4% (growth of 0.2% in the previous quarter). Namely, more favorable movements in net exports, together with household consumption and public consumption, have a positive contribution to the growth, as opposed to the decline in gross investments. In accordance with such achievements, in the ECB's June forecast, an upward correction was made for 2024, while the assessments for 2025 and 2026 are similar to those in March. Thus, in 2024 economic growth of 0.9% in the euro area is expected, followed by a forecasted acceleration and growth of 1.4% and 1.6% in 2025 and 2026, respectively.[2] Movements in the labor market in the euro area are stable, considering that the unemployment rate in the April - May period decreased minimally, reaching a historically bottom of 6.4%. The annual inflation in the euro area in the second quarter of 2024 averages 2.5% and is minimally lower than that in the first quarter (2.6%). According to the latest ECB forecasts, the inflation rate in 2024 would equal 2.5%, followed by its additional slowdown to 2.2% in 2025 and 1.9% in 2026, respectively, which is slight upward revision for 2024 and 2025 and unchanged forecast for 2026 compared March.[3]

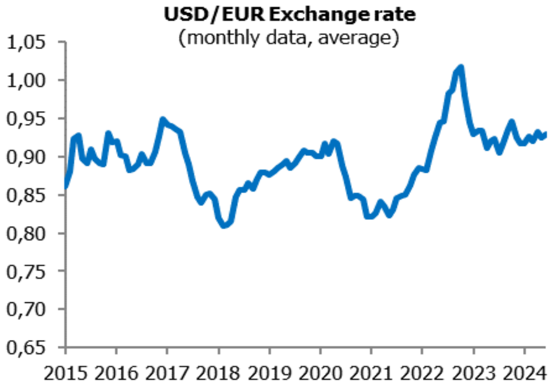
In the second quarter of 2024, central banks in developed countries mostly preserved the same policy rate at the same level, in conditions of a further, but slower reduction in the inflation rate, and estimated that this monetary setup will contribute to reducing inflation to the target level. Only the ECB reduced interest rates by 0.25 percentage points in June 2024, so that the interest rate on deposit facilities, of the basic refinancing operations and on marginal lending facilities were at the level of 3.75%, 4.25 % and 4.5%, respectively, simultaneously emphasizing that it maintains the monetary policy restrictiveness. At the same

[2] According to March 2024 forecasts, the economic growth was projected at 0.6% in 2024 and 1.5% in 2025 and 1.6% in 2026.
[3] In March 2024, the inflation in the euro area was forecasted at 2.3% in 2024, 2.0% in 2025 and 1.9% in 2026.

time, the portfolio within the Securities Purchase Program (APP) continues to decrease gradually and at a envisaged pace, while the full reinvestment of the matured securities within the Securities Purchase Program for immediate support of the economy due to pandemic (PEPP) stopped at the end of June 2024, so in the second half of the year the portfolio will decrease by Euro 7.5 billion per month on average, until the total cessation of reinvestments within this Program at the end of 2024. During the second quarter, the FED kept the policy rate in a range of 5.25% to 5.5% and continued to further reduce the portfolio of treasury bills and mortgage-backed securities, although since the beginning of June reduction pace slowed down by limiting the repurchase of government bonds to a maximum of US Dollar 25 billion (instead of the previous US Dollar 60 billion). The policy rate of the Bank of England remained at 5.25%, and the program to reduce the portfolio of securities in the central bank's balance sheet continues. In the second quarter of 2024, the Bank of Japan kept the policy rate at 0.1%, and at the same time, it will reduce the volume of purchase of government securities.



Source: Central banks.

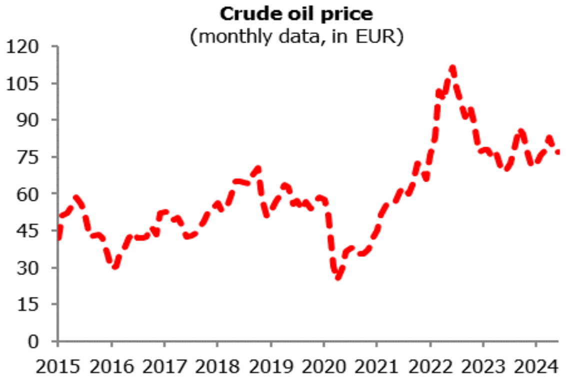


Source: Eurostat.

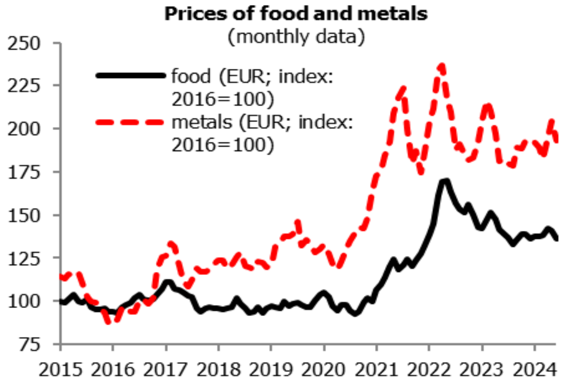
In the second quarter of 2024, the value of the US dollar against the Euro increased by 0.8% compared to the first quarter of 2024, signalizing the improved macroecomomic indicators for the USA. Analyzed on annual basis, the US dollar appreciated by 1.2%, and equaled Euro 0.93, on average, in this period.

In the second quarter of 2024, the primary commodities prices on world markets, denominated in euro, registered an increase. Thus, the average oil price in this period equaled Euro78.9 per barrel, which is higher by 4.6% compared to the previous quarter, i.e. by 10.1% annually. The upward movement in oil prices stems from increased demand in advanced economies at the start of the summer season, pressures from uncertainty related to tensions and attacks in Gaza, and the decision to extend the period of reduced supply by OPEC+ until the end of 2025. In addition, the prices of non-energy primary products index [4] (in euros), increased by 5.7% compared to the first quarter of 2024. Analyzed by groups of products, the primary metals[5] and food[6] price indices increased by 5.0% and 1.4%, respectively.

[4]This aggregate index includes the precious metals index, the food and beverages index, the agricultural raw materials index and the index of basic metals.
[5]This index includes the following metals: aluminum, cobalt, coper, iron, steel, molybdenum, nickel, tin, uranium, and zinc.
[6]This index includes the following food products: cereals, vegetable oil, meat, seafood, sugar and other food.

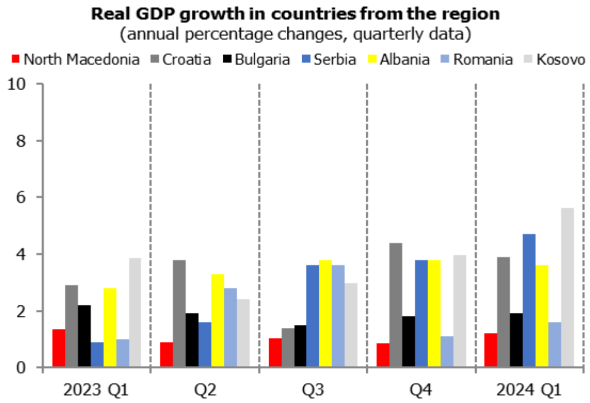


Source: IMF and NBRNM calculations.

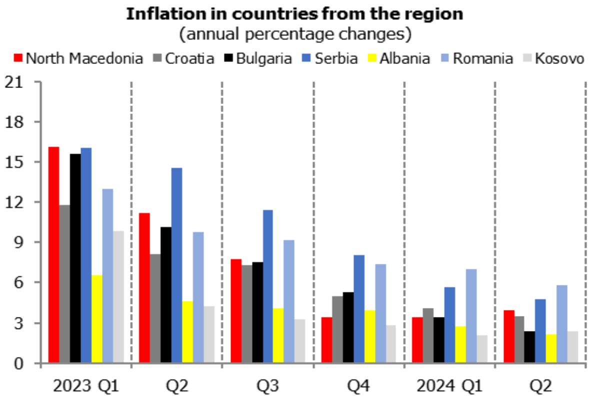


Source: IMF and NBRNM calculations.

In relation with the countries of the region, in the first quarter of 2024 the economic growth accelerated in almost all countries, with the exception of Croatia and Albania, which recorded smaller annual growth**.** A more significant acceleration of economic growth was registered in Kosovo, especially stronger growth in domestic demand, as well as Serbia, mainly due to higher growth in household consumption. **Inflation continues to slow down in the second quarter of 2024 in all analyzed countries of the region, except for Kosovo,** mainly under the influence of the slow rise in food prices.



Source: Eurostat and Agency of statistics of Kosovo



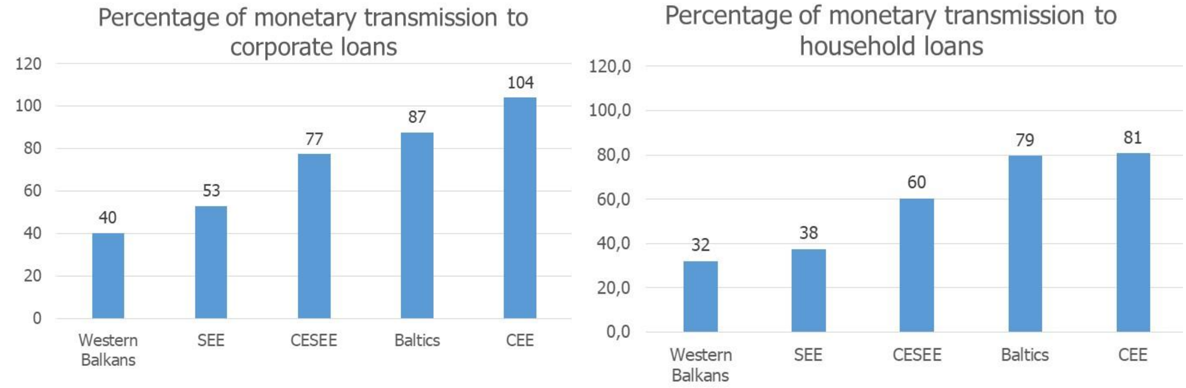
Source: Eurostat and national statistical offices.

Annex 1: Effects of the restrictive monetary policy on the growth

In the last few years, the global economy was stricken by multiple shocks that caused a slowdown in growth dynamics. Moreover, the latest episode of high inflationary pressures increased the need for aggressive monetary tightening, which implied tighter financing conditions. The series of increase in the interest rate has been extremely rapid and strong. Central banks acted swiftly and in almost all countries, the interest rates rose substantially and promptly. For example, the average increase in the interest rates (bottom to top) for the CESEE region was around 600 basis points (bp), with a range between 275 and 1240 bp. However, in the euro area, the policy interest rate increased by a total of 450 bp from July 2022.

The debate in the central banking community has been predominantly focused on whether the monetary policy setup is restrictive enough to control the inflation, or prevent it from rising further. However, there has also been a lot of discussion about whether and to what extent such a setup could be detrimental to the economic recovery. The transmission channels to the real economy are multiple and the impact is conditioned by very specific characteristics, such as excess liquidity in the system, the interest rates structure (fixed or variable), the exposure of households and enterprises to credit financing, the state of real estate markets, etc. In other words, all these characteristics define how strong the transmission of interest rates can be and which sectors of the economy can be most affected. **Despite the possible heterogeneous impact, the tightening of financial conditions was evident everywhere.** For example, in the wider CEE region and the euro area countries, the response of interest rates to a rise in the prime rate ranged from 0.2 to just over 1. What most countries had in common was a much stronger transmission to companies than to households.

Chart 1
Reaction of corporate and household interest rates to changes in the policy rate, in % (from lowest to highest level)

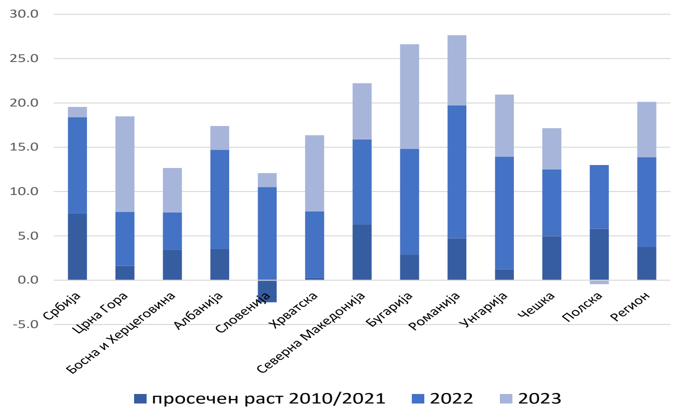


Source: ECB, IMF, Central banks and NBRNM calculations.

Source: ECB, IMF, Central banks and NBRNM calculations.

The tight financing conditions affected credit dynamics, thus limiting the financial support through the banking system. The increase in lending in the region slowed down by about 4 percentage points (pp) in just one year. Despite the slowdown, credit flows continued, except in countries with credit contraction (for example, Poland). All this indicates that the monetary policy setup, together with the readiness of the banking system, was calibrated in a way not to cause a "hard landing of the economies", that is, to avoid the economies falling into recession.

Chart 2
Annual growth of loan rates (in %)



Source: Central banks’ web sites.

Although the effects of the monetary policy can be seen based on the delay and it may be too early to draw conclusions, the same conclusion as above can be drawn

from the data on the economic growth in the region. Real growth rates in the region slowed to an average of 1.3% in 2023, half of the average growth in the previous decade. However, almost all countries show positive growth, while the number of countries with economic contraction is small (Hungary, the Czech Republic and the Baltic countries). The medium-term forecast shows an average growth of close to 3%, in other words, a return to the average growth observed before the pandemic period. Although this is only a conclusion based on data, statistics show that a "hard landing of the economies" in the region has been avoided.

Table 1
Gross domestic product (real growth rates, in %)

	2010-2019	2020	2021	2022	2023	2024-2029
Estonia	3,6	-1,0	7,2	-0,5	-3,0	1,6
Latvia	2,3	-3,5	6,7	3,0	-0,3	2,3
Lithuania	3,6	0,0	6,3	2,4	-0,3	2,3
Baltic countries	**3,2**	**-1,5**	**6,8**	**1,6**	**-1,2**	**2,1**
Czech Republic	2,5	-5,5	3,6	2,3	-0,4	1,9
Hungary	2,8	-4,5	7,1	4,6	-0,9	3,0
Poland	3,7	-2,0	6,9	5,3	0,2	3,1
Slovakia	3,1	-3,3	4,8	1,8	1,2	2,6
Slovenia	2,0	-4,2	8,2	2,5	1,6	2,6
CEE	**2,8**	**-3,9**	**6,1**	**3,3**	**0,3**	**2,6**
Albania	2,6	-3,3	8,9	4,8	3,3	3,4
Bosnia and Herzegovina	2,2	-3,0	7,4	4,2	1,8	2,9
Bulgaria	2,1	-4,0	7,7	3,9	1,8	2,8
Croatia	1,1	-8,6	13,8	6,3	2,8	2,7
Kosovo	4,6	-5,3	10,7	4,3	3,3	3,9
Montenegro	2,9	-15,3	13,0	6,4	6,0	3,1
North Macedonia	2,6	-4,7	4,5	2,2	1,0	3,6
Romania	3,1	-3,7	5,7	4,6	2,1	3,5
Serbia	1,9	-0,9	7,7	2,6	2,5	4,0
SEE	**2,6**	**-5,4**	**8,8**	**4,4**	**2,7**	**3,3**
CESEE region	**2,7**	**-4,3**	**7,7**	**3,6**	**1,3**	**2,9**

Source: World Economic Outlook, IMF, April 2024.

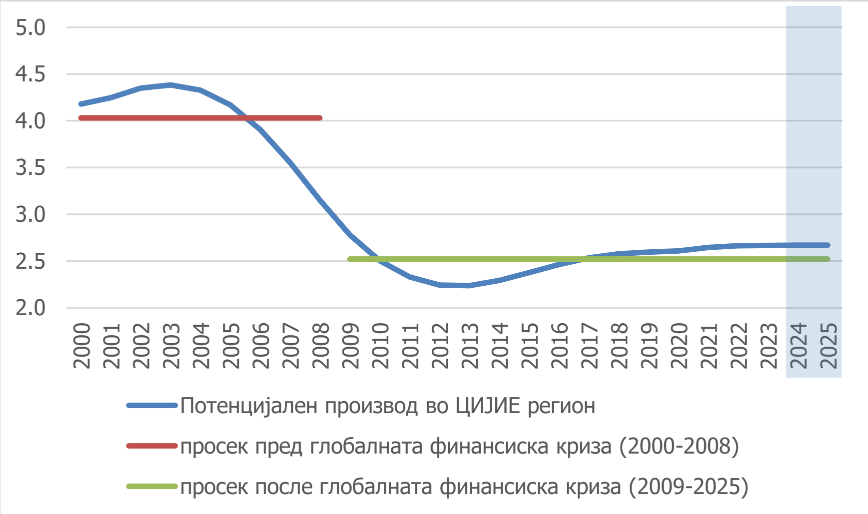
The conclusions for the euro area are similar. Thus, the restrictive monetary policy affected the economic activity. The economic activity in the euro area stagnated in 2023, but it began recovering at the beginning of 2024. (Lane, 2024)[7]. **For the euro area, there are empirical estimates on how the monetary setting affect the economic activity. In short, they conclude that the restrictive policy was transmitted at different speed and intensity to different areas of the economy.** The velocity and the intensity of transmission depend on several factors, including the importance of foreign demand and foreign competition, reliance on domestic versus global supply chains, household and corporate balance sheets, the sensitivity of investment and consumption to interest rates, and conditions on the labour market. **Estimates suggest that the maximum impact of the monetary policy tightening on activity levels is greater in manufacturing than in services, with the highest impact being registered in the fourth quarter of 2023.** In addition, it is greater for business and residential investment than for private consumption,

[7] Philip R. Lane (2024), The analytics of the monetary policy tightening cycle, a lecture at the Stanford Graduate School of Business, 2 May 2024.

further strengthening the transmission on business investments also in the first quarter of 2024 (Battistini and Gareis, 2023)[8].

Of course, whenever tighten the monetary policy setup, the central bank's goal is to reduce inflation by temporarily curbing the demand. It is therefore important that central banks communicate openly and explain the reasons behind their decisions and the objectives of these decisions. In order to ensure price stability and credibility of monetary policy, it is important not to delay unduly the achievement of low inflation, and that inflation expectations remain anchored. **In fact, the central banks' focus on stability ensures a stable environment, which is most conducive to growth.** However, let's remember that the central bank and its monetary policy are not long-term drivers of growth, nor a substitute for deeper structural reforms. Thus, reviving growth dynamics requires addressing deep-rooted structural issues that will provide sufficient support to the underlying drivers of growth and raise the potential growth of the region. Namely, if we look at the data**, the potential growth in the region in the period preceding the global financial crisis hovered around 4% on average, but since then it has slowed down to only 2.5% on average [9].** This is an even more complex issue at a time of serious global challenges the solving of which requires much greater efforts.

Chart 3
Potential output in the CEE region (annual growth rates, %)



Source: NBRNM calculations based on Hodric - Prescott filter (with annual data on the period 1980 - 2025), through the IMF's World Economic Outlook data, from April 2024

1.2. Domestic supply

In the first quarter of 2024, the activity in the domestic economy registered a real annual increase of 1.2%, and it accelerated compared to the growth of 0.9% in the previous quarter. Moreover, also in this quarter there are no significant changes in terms of structure, that is, the growth is still largely due to the positive contribution of "trade, transport and hospitality" group of activities. On the other hand, agriculture recorded a strong annual decrease for the second quarter in a row and made a significant negative contribution, with the performance of industry and

[8] Battistini and Gareis (2023), Monetary policy and the recent slowdown in manufacturing and services, European Bulletin Boxes, ECB, number 8/2023.
[9] NBRNM calculations based on Prescot – Holdrick filter and data from the IMF's World Economic Outlook, April 2024.

construction also having an impact, although more moderately. The GDP registered real increase of 0.5% on a quarterly basis. The high frequency data on the supply side available for the period April-May 2024 mainly indicate more favorable movements. The estimates of the managers about the business conditions of the companies for the second quarter of 2024 are favorable in trade, while more unfavorable in the construction sector, services sector and industry. The expectations in the forthcoming period are generally less favorable, except in construction.

In the first quarter of 2024, real GDP growth slightly equaled 1.2% annually (growth of 0.9% in the previous quarter), amid further quarterly growth of 0.5% (seasonally and calendar adjusted). Analyzing the production side of GDP, the growth in the first quarter largely stems from the positive contribution of the group of activities "trade, transport and catering", with an additional positive contribution of the activities "arts, entertainment and recreation; other services;", "professional, scholar and technical activities; administrative and auxiliary services", "public administration and defense; education; health and social work" and "information and communication". On the other hand, agriculture recorded again a significant negative contribution, with unfavorable movements in this quarter also being registered in construction activity and industry.

GDP and components - annual growth rates (in %)

	annual growth rates, in %								
	2019	**2020**	**2021**	**2022**	Q1 2023	Q2 2023	Q3 2023	Q4 2023	Q1 2024
Agriculture	**0,1**	**2,5**	**-8,7**	**-5,0**	-0,2	0,1	2,0	-15,3	-19,7
Industry	**1,4**	**-6,7**	**2,2**	**-1,2**	-0,8	0,1	-1,7	1,6	-1,2
Manufacturing	**2,6**	**-4,8**	**6,1**	**-2,7**	-3,2	-1,8	-1,2	1,9	-0,2
Construction	**5,5**	**-4,0**	**-6,0**	**8,1**	18,9	-14,8	-13,0	5,5	-2,5
Trade and transport	**6,7**	**-10,6**	**7,6**	**0,0**	3,4	4,4	1,9	2,3	6,9
Information and communication	**6,8**	**4,5**	**12,2**	**15,1**	7,0	3,3	5,4	2,2	2,5
Financial and insurance activities	**0,4**	**-0,1**	**-0,1**	**-1,4**	3,8	3,9	6,6	3,5	-0,1
Real estate activities	**0,2**	**1,1**	**7,0**	**19,0**	3,6	4,1	5,6	1,6	0,1
Professional, scientific and technical activitiess	**8,0**	**-8,7**	**14,5**	**9,2**	1,4	3,6	5,5	2,0	7,5
Public administration	**5,2**	**3,2**	**4,0**	**-7,2**	-4,5	-0,9	-0,2	0,1	0,7
Art, enetertainment and recreation; Other service activities	**9,6**	**-22,6**	**17,2**	**8,4**	-0,4	1,9	2,7	-2,0	19,6
Gross Domestic Product	**3,9**	**-4,7**	**4,5**	**2,2**	**1,4**	**0,9**	**1,0**	**0,9**	**1,2**

*From the release for GDP of 03.06.2024
Source: State Statistical Office and NBRNM calculations.

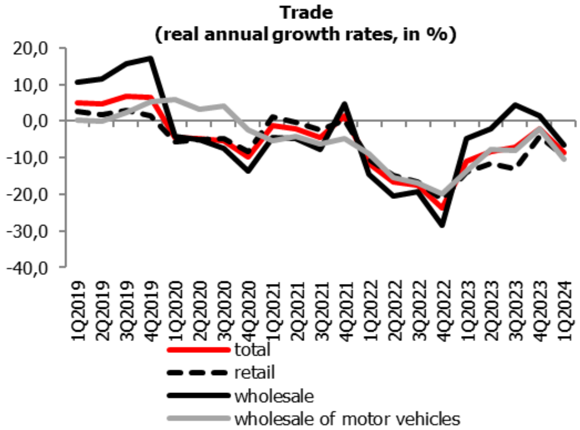
GDP and components - Contributions to the GDP growth (in percentage points)

	contribution in GDP growth, in p.p.									
	2019	**2020**	**2021**	**2022**	**2023**	Q1 2023	Q2 2023	Q3 2023	Q4 2023	Q1 2024
Agriculture	**0,0**	**0,2**	**-0,7**	**-0,4**	**-0,3**	-0,1	0,0	0,3	-1,2	-1,2
Industry	**0,3**	**-1,2**	**0,4**	**-0,2**	**0,0**	-0,1	0,0	-0,3	0,3	-0,2
Manufacturing	**0,3**	**-0,6**	**0,8**	**-0,4**	**-0,1**	-0,4	-0,2	-0,2	0,2	0,0
Construction	**0,3**	**-0,2**	**-0,3**	**0,5**	**-0,1**	0,7	-0,7	-0,9	0,4	-0,1
Trade and transport	**1,3**	**-2,1**	**1,5**	**0,0**	**0,6**	0,6	0,8	0,4	0,4	1,3
Information and communication	**0,2**	**0,2**	**0,5**	**0,6**	**0,2**	0,3	0,2	0,2	0,1	0,1
Financial and insurance activities	**0,0**	**0,0**	**0,0**	**0,0**	**0,1**	0,1	0,1	0,2	0,1	0,0
Real estate activities	**0,0**	**0,1**	**0,7**	**2,0**	**0,4**	0,4	0,5	0,6	0,2	0,0
Professional, scientific and technical activitiess	**0,3**	**-0,3**	**0,5**	**0,4**	**0,1**	0,1	0,1	0,2	0,1	0,3
Public administration	**0,6**	**0,4**	**0,5**	**-0,9**	**-0,2**	-0,6	-0,1	0,0	0,0	0,2
Art, enetertainment and recreation; Other service activities	**0,3**	**-0,7**	**0,5**	**0,2**	**0,0**	0,0	0,1	0,1	-0,1	0,6
Gross Domestic Product	**3,9**	**-4,7**	**4,5**	**2,2**	**1,0**	**1,4**	**0,9**	**1,0**	**0,9**	**1,2**

*From the release for GDP of 03.06.2024
Source: State Statistical Office and NBRNM calculations.

Source: NBRNM calculations.

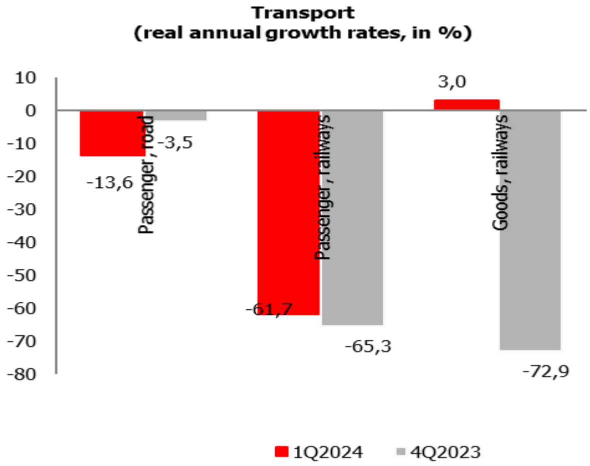
Analyzed by high-frequency data, **in the first quarter of the year the total trade turnover registered a real annual decrease,** in conditions of a decline in all three types of trade (wholesale trade, retail trade and trade in motor vehicles). In the period April-May, the movements in the total trade turnover are favorable, i.e. the real annual decrease in the total turnover slows down significantly, in conditions of a slow decline in all three types of trade. The perceptions of the corporate managers in the sector "retail trade" on the business conditions during the second quarter of 2024 are more favorable compared to the same quarter in the previous year, while the expectations for the forthcoming period are less favorable.



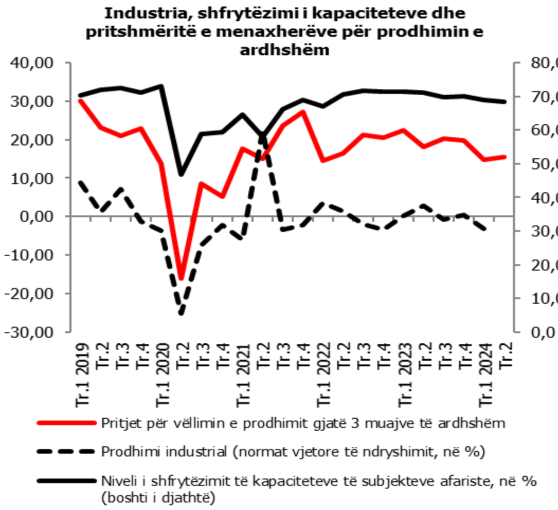
Source: State Statistical Office.

Source: Retail survey of EC, State Statistical Office and

In terms of **transport**, in the first quarter of 2024 there is a small rise in freight rail traffic compared to the substantial fall in the previous quarter, and more favorable changes are also noted in passenger rail traffic, which recorded a smaller drop compared to the one in the previous quarter. On the other hand, passenger road traffic experienced a slightly stronger fall compared to the previous quarter.

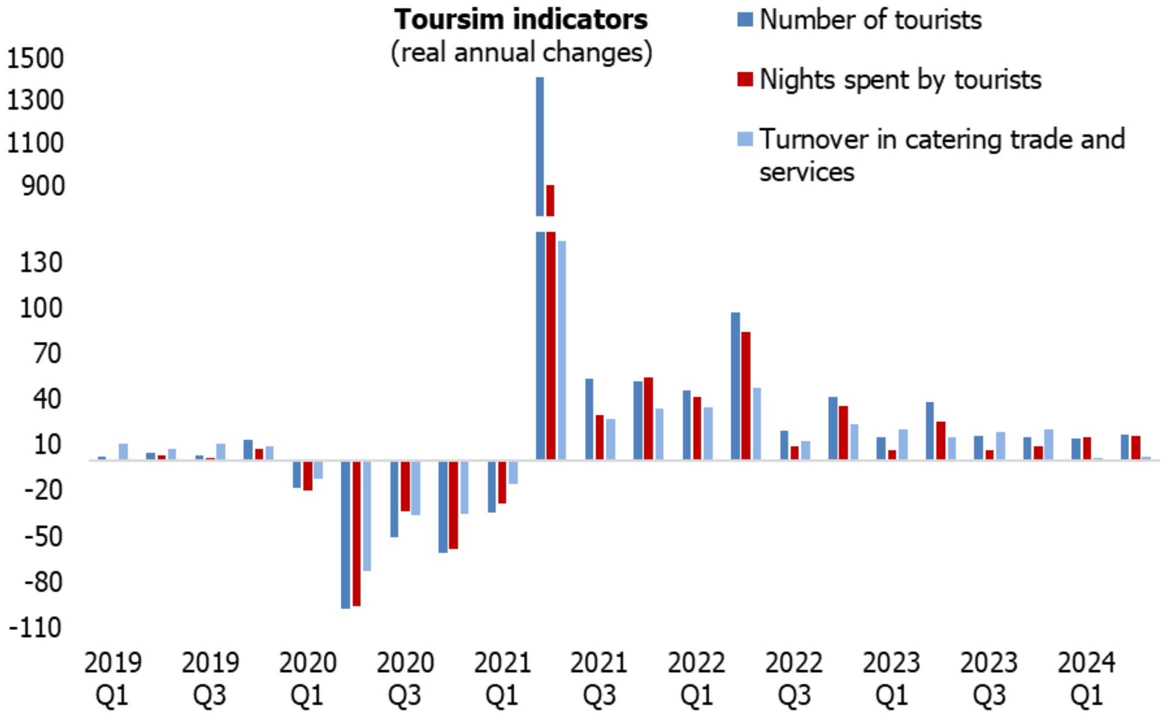


Source: State Statistical Office.



Burimi: Enti Shtetëror Statistikor dhe Anketa e KE-së për industrinë.

Within the **catering sector**, in the first quarter of 2024, the number of tourists and overnight stays, as well as the total turnover in catering, continue to record real growth on an annual basis. The turnover in the hospitality industry in April recorded a real annual growth, slightly higher compared to the increase in the previous quarter, with further solid growth in the number of tourists and overnight stays. The perceptions of the corporate managers in the services sector on their business situations during the second quarter of 2024 are less favorable compared to the same quarter in the previous year, with the expectations for the upcoming period in terms of demand also being less favorable.

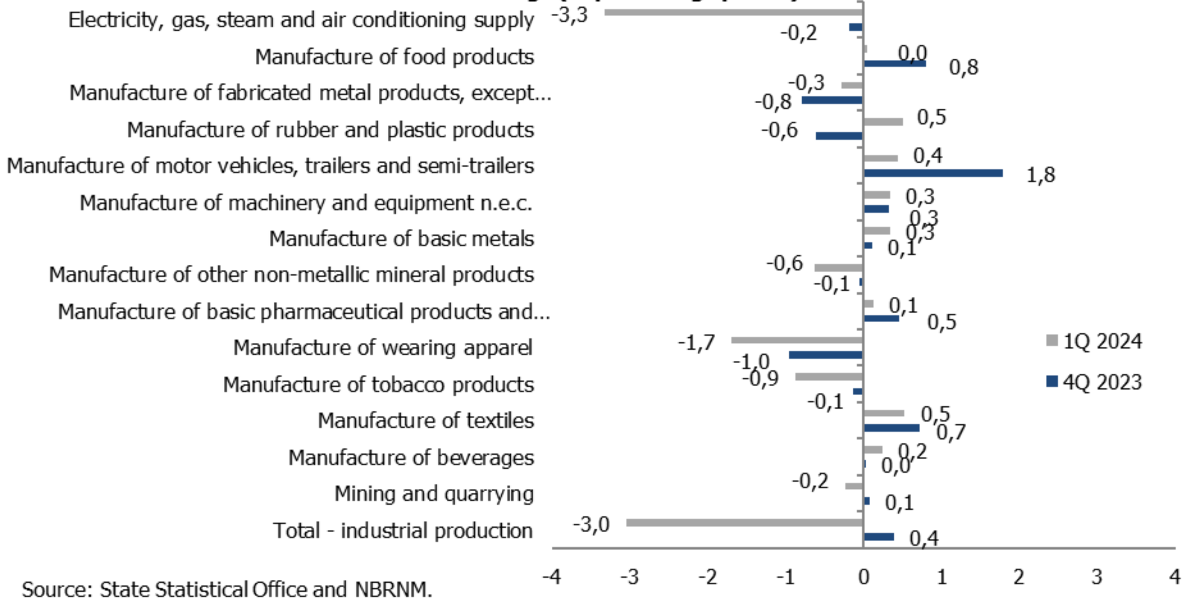


Source: SSO and NBRNM calculations.

In the first quarter of 2024, industrial output[10] **declined by 3.1% annually,** as opposed to the slight rise of 0.4% in the preceding quarter, primarily as a result of the energy sector, and less of manufacturing industry and mining. By activity, within the manufacturing industry, the most significant negative contribution is made by the production of clothing and the production of tobacco products. On the other hand, the most significant positive contribution is made by the production of electrical equipment, the production of rubber and plastic products, the production of textiles, as well as the rest of the manufacturing industry. In the April-May period, the decline in industrial output deepens, and the decline is driven by the negative contribution of energy, the manufacturing industry (in conditions of a significant negative contribution of clothing production and the production of tobacco products), as well as mining. The industrial sector managers have less favorable perceptions of the business conditions in the second quarter of 2024, compared to the same quarter last year, with less favorable expectations in terms of the movement of production in the upcoming period, as well.

[10] The analysis of trends in industry uses SSO's monthly data for the industrial output indices.

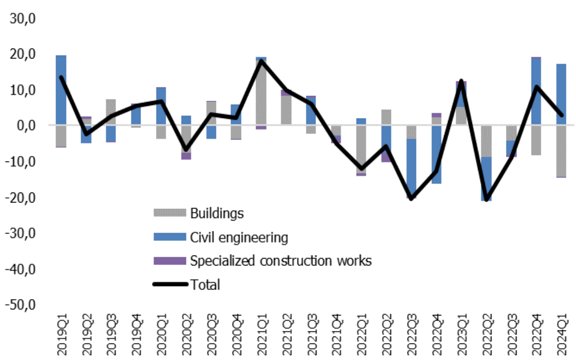
Contributions of selected industries to the total industrial production, annual rate of change (in percentage points)



Source: State Statistical Office and NBRNM.

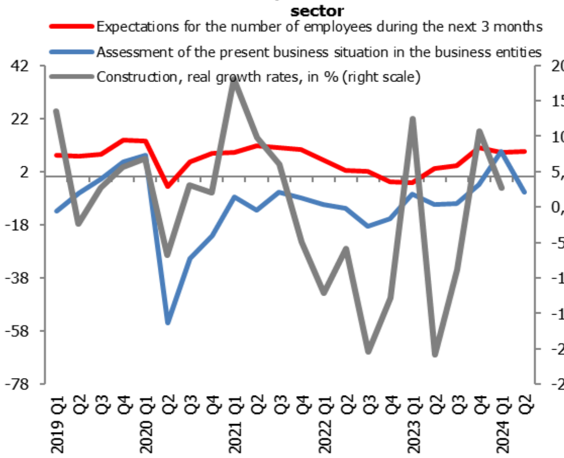
According to the high frequency data for the construction sector, in the first quarter of 2024, a decline was observed in buildings construction and specialized construction works[11], as opposed to the increase in civil engineering. In April, construction recorded high real growth on an annual basis, as a result of growth in the three categories (civil engineering, buildings construction and specialized construction works). Perceptions of the corporate managers in the construction sector for the movement of their activity in the second quarter of 2024 were less favorable compared to the same quarter last year, yet the expectations for the following period are more favorable.

Completed construction works (contributions to the real growth, in p.p.)



Source: State statistical office and calculations of NBRNM

Construction and expectations of the construction sector



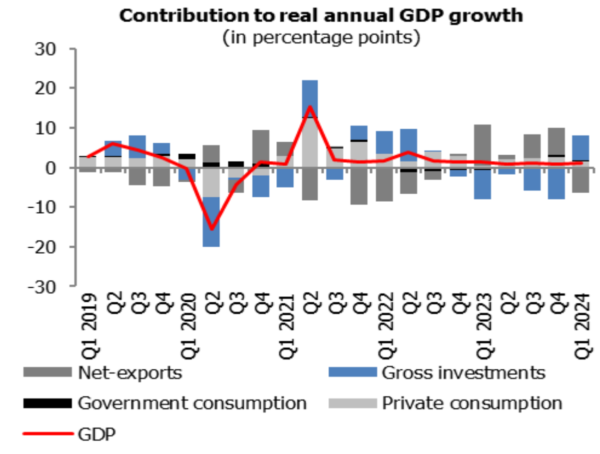
Source: Construction survey of EC, State Statistical Office and NBRNM.

[11] Specialized construction works are the new category that the SSO started to publish from May 2024 within the data on completed construction works for April, and which includes the categories "demolition and preparation of a building site", "electric installations, plumbing and sewerage installations and other construction installation works", "completed construction works" and "other specialized construction works".

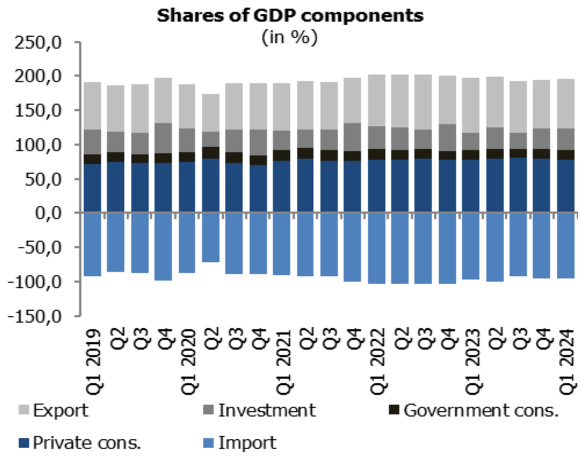
1.3. Aggregate demand

Observed by the aspect of the demand, the real annual GDP growth of 1.2% in the first quarter of 2024 is entirely due to the domestic demand, in conditions of growth in all components. The highest growth was registered in gross investments, the positive contribution of which to the GDP growth was the highest. Namely, after a strong drop in 2023, the gross investments recorded a high growth in this quarter, supported by the growth of investments in fixed assets and inventories. On the other hand, net exports have a negative contribution to GDP growth, which is due to the decrease in exports, which indicates a certain stabilization, after the solid growth in the previous period. A minimal increase was observed in the import of goods and services.

Structural analysis of the GDP[12] in terms of demand shows that also in the first quarter of 2024 the growth entirely results from positive contribution of the domestic demand, amid increase in all components. The growth of gross investments is particularly noticeable, in conditions of growth of investments in fixed assets, that is, in machinery and equipment and in transport equipment, as well as increase in inventories. Both private and public consumption recorded growth, although slower. On the other hand, net exports made a negative contribution, given the decline in the exports and minimal increase in the import of goods and services.



Source: State Statistical Office and NBRNM calculations.



Source:SSO and NBRNM calculations.

	Real annual growth rates (%)								Contributions to real annual growth (in p.p.)**							
	2021	**2022**	**2023**	**2023-Q1**	**2023-Q2**	**2023-Q3**	**2023-Q4**	**2024-Q1**	**2021**	**2022**	**2023**	**2023-Q1**	**2023-Q2**	**2023-Q3**	**2023-Q4**	**2024-Q1**
Private consumption	8,8	3,8	2,4	0,7	2,8	2,8	3,3	2,0	5,7	2,6	1,7	0,5	1,9	2,0	2,2	1,4
Government consumption	0,9	-5,0	-0,6	-4,3	-1,1	-3,0	5,6	2,4	0,1	-0,8	-0,1	-0,7	-0,2	-0,5	0,8	0,5
Exports of goods and services	14,3	11,4	-0,1	6,6	-1,4	-5,0	0,1	-7,8	8,2	7,5	-0,1	4,8	-1,0	-3,8	-0,1	-6,1
Imports of goods and services	14,8	12,4	-5,8	-5,0	-2,0	-9,8	-6,5	0,2	-10,4	-10,1	5,5	4,7	1,9	9,3	6,1	-0,1
Gross capital formation	3,7	9,4	-16,7	-22,3	-4,8	-18,7	-20,5	23,6	0,9	3,0	-6,0	-8,0	-1,7	-6,0	-8,2	5,6
Domestic demand	*6,5*	*4,2*	*-3,1*	*-6,0*	*0,3*	*-3,0*	*-3,6*	*6,8*	*6,7*	*4,8*	*-4,4*	*-8,2*	*0,0*	*-4,5*	*-5,2*	*7,5*
*Net exports**	*16,3*	*15,2*	*-21,6*	*-35,8*	*-3,8*	*-26,3*	*-21,3*	*35,8*	*-2,2*	*-2,6*	*5,4*	*9,5*	*0,9*	*5,5*	*6,0*	*-6,2*
Statistical discrepancy									*0,0*	*0,0*	*0,0*	*0,0*	*0,0*	*0,0*	*0,0*	*0,0*
GDP	**4,5**	**2,2**	**1,0**	**1,4**	**0,9**	**1,0**	**0,9**	**1,2**	**4,5**	**2,2**	**1,0**	**1,4**	**0,9**	**1,0**	**0,9**	**1,2**

**decrease represents lower deficit*
*** Contribution components do not sum to total GDP due to statistical discrepancies in real amounts.*
In order to comply with the official real growth rates, the statistical discrepancy is included in the aggregate GDP.
Source: SSO and NBRNM calculations.

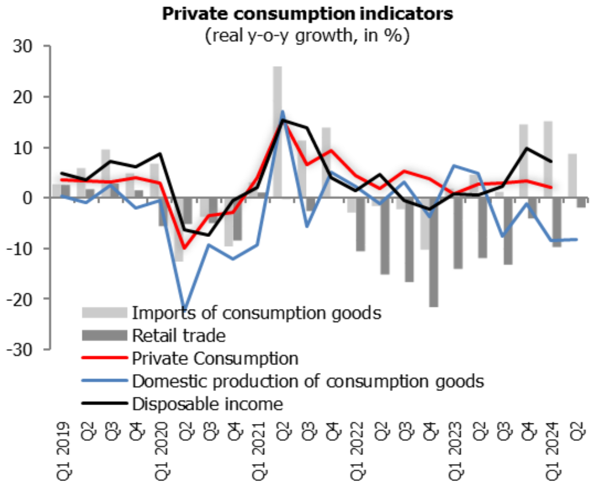
[12]The quarterly changes of the GDP and its components are calculated using seasonally and calendar adjusted SSO data.

1.3.1. Private consumption

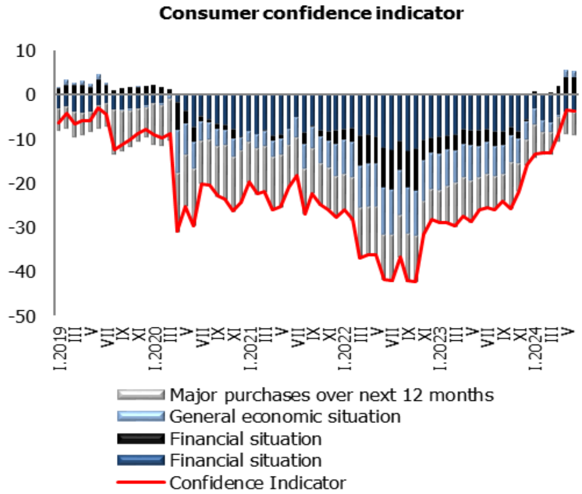
In the first quarter of 2024, the private consumption continued to grow, yet slower, registering an annual growth of 2% and a quarterly decline of 0.5% (annual growth of 3.3% and quarterly increase of 0.8% in the previous quarter). Private consumption is supported by real disposable income, which continued to grow, although at a more moderate pace. Real growth was observed in the average paid wage,[13] and pensions bill[14]. On the other hand, private transfers recorded a real decline, deeper compared to the previous quarter. Part of household consumption continues to be financed based on bank loans, the growth of which is more moderate. Amid uncertainty from the war in Ukraine and the conflict in the Middle East, and their impact on consumer prices, some of the economic measures adopted in 2023 to protect living standards were still in place in the first quarter of 2024[15] in order to maintain household consumption.

The available private consumption data[16] for the second quarter of 2024 mainly indicate its further increase. Namely, in this period as well, an annual growth was observed in some of the components of the disposable income, i.e. in wages and pensions, although somewhat slower, with slow real growth also being recorded in household borrowings and the import of consumer goods. In addition to this, an accelerated growth was registered in gross VAT revenues. On the other hand, retail trade on a real basis and domestic production of consumer goods continued to decline, but more slowly. In addition, the results of the Lending Survey from June show net easing of the credit conditions, at net increase in the demand for total household loans. The consumer confidence indicator[17] points to more favorable perceptions for the second quarter of 2024 relative to the previous quarter, especially compared to the same period in 2023.

[13] For more details, see section 1.3. Employment and wages.
[14] In September 2023, pensions increased by 5.3% nominally according to the regular adjustment with the new methodology which follows two indicators, i.e. 50% of the increase in the average wage and 50% of the increase in the consumer prices, according to the official data of the State Statistical Office. This harmonization happens twice a year, in March and September (for more information see the following link).
[15] On 19 September 2023, the Government adopted a decision on reducing the prices of some food products by at least 10% and freezing the reduced prices. The Decision is valid from 20 September to 31 November 2023 and the highest prices of some of the food products are determined at the level of prices (excluding the promotional pricing) applied as of 1 August 2023 in retail trade, i.e. the prices of these products are reduced by at least 10%. For more details, please visit the following link: https://vlada.mk/node/34532. The Government of RNM decided to extend the implementation of the measures regarding the guaranteed prices of basic food products and the prescribed highest trade margin in the trade of fresh fruits and vegetables until the end of February 2024 (link). On December 9, 2023, the Government adopted another set of anti-crisis measures divided into 4 categories: 1) Measures to support citizens and households (support for pupils and students from low-income families, support for vulnerable categories of citizens, pensioners and households with lower income, support to farmers); 2) Measures to support the economy (more favorable loans for liquidity and investments, subsidizing contributions for higher salaries); 3) Measures to support the public sector (municipalities and public enterprises); and 4) Systemic measures that contribute to mitigating the effects of the price and energy crisis. (https://finance.gov.mк)
[16] Data on wages are given as of April 2024, while data on household loans, pensions, retail trade, domestic production of consumer goods, import of consumer goods and gross revenues from VAT refer to the period April-May 2024.
[17] European Commission's Consumer Survey as of June 2024. The chart shows consumer confidence index as a net percentage of responses. This index is an integral component of the total index of economic confidence.



Source: State Statistical Office , Ministry of Finance and NBRNM calculations.

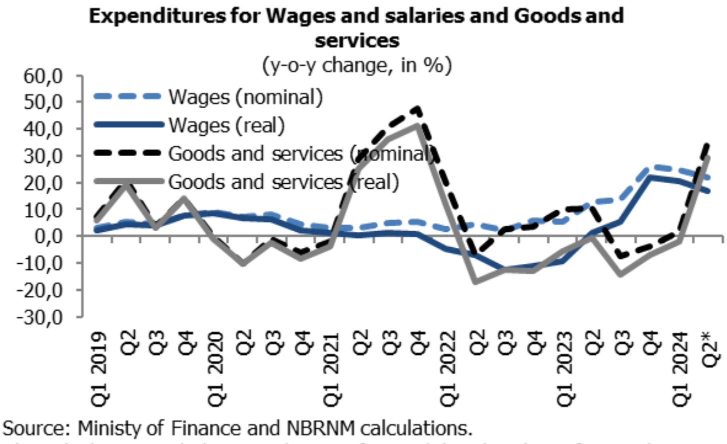


Source: European Commision and NBRNM's calculation.

1.3.2. Public consumption

In the first quarter of 2024, the growth of public consumption was more moderate and equaled 2.4% (5.6% in the previous quarter), amid quarterly fall of 2.7%. According to the budget data, the performance results from the decelerated increase in the expenditures based on wages and transfers to the local authorities, amid further real decrease in the expenditures based on goods and services.

The Budget realization for the period April-May 2024 point to a real annual growth of public consumption, with growth being registered in all main categories.

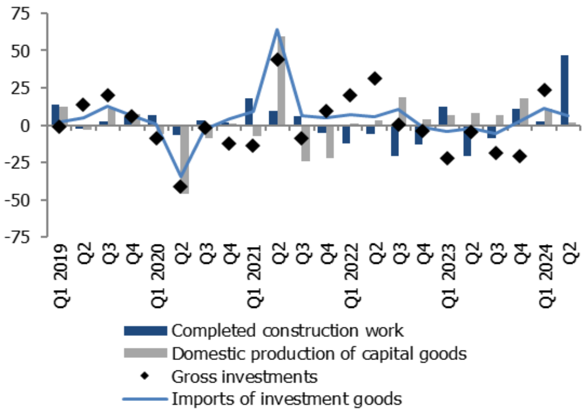


Source: Ministy of Finance and NBRNM calculations.
The calculations include expenditures of Consolidated Budget of Central Government and Funds, deflated by CPI.

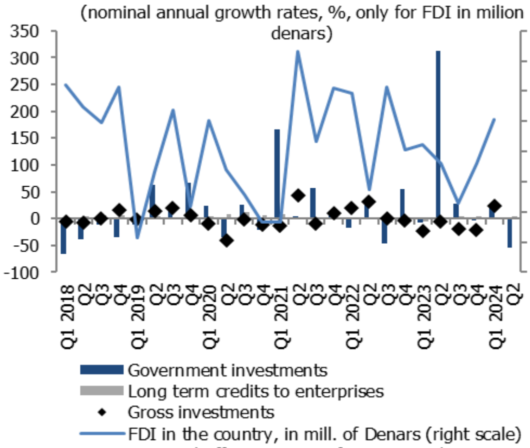
1.3.3. Investment consumption

After a strong annual decrease in gross investments in 2023, mainly due to the effect of inventory depletion, in the first quarter of 2024 they registered double-digit real annual and quarterly growth rates of 23.6% and 20.7%, respectively. Thus, the gross investments are the component with the highest individual positive contribution to GDP growth in this quarter. Such movements on an annual basis are the result of the growth of investments in fixed assets, that is, in machinery and equipment and in transport equipment, as well as the growth of inventories. Analyzed by the indicative categories for investments in fixed assets, after the decline in the previous quarter, in this quarter real growth was observed in state capital investments and in foreign direct investments, and higher growth rates were recorded in income from profit tax and the import of working capital. Construction works performed and the domestic production of capital goods, as well as the long-term corporate loans are still registering a growth, although slower compared to the previous quarter.

As for the high-frequency data on gross investments[18] for the period April - May 2024, a growth was registered in the completed construction works, import of means of operation, domestic production of capital goods, inventories of finished products, profit tax, with continuing credit support to companies. In addition, the results of the Lending Survey for the second quarter point of 2024 to net easing of the overall credit conditions, given net increase in the demand for corporate loans. On other hand, a decrease was registered in government capital investments due to the high comparison base, related to the advance payments for infrastructure projects related to corridor 8 and 10 last year, with a larger decrease in total industrial output.



Source: State Statistical Office, Ministry of Finance and NBRNM



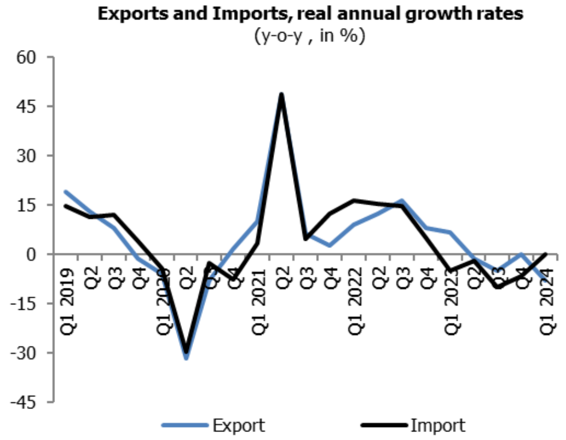
Source: State Statistical Office, Ministry of Finance and NBRNM calculations.

1.3.4. Net external demand

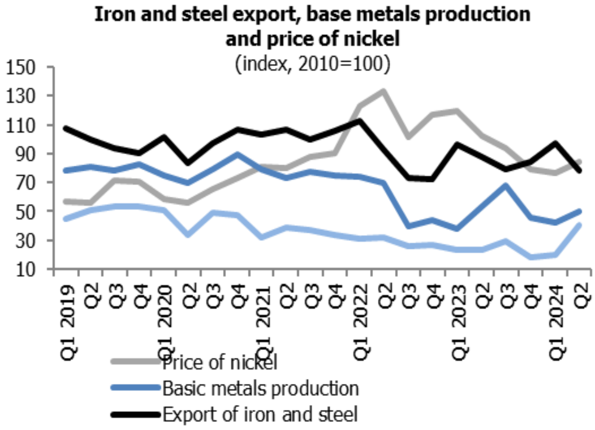
After five quarters of constant positive contribution, due to the larger downward adjustment of imports (depletion of raw materials and energy stocks), in the first quarter of 2024, net exports had a negative contribution to the GDP growth. In conditions of minimal growth in the import of goods and services, these achievements fully reflect the decline in exports. Thus, the export of goods and services, which almost stagnated in the last quarter of 2023, in the first quarter of 2024 registered a more significant annual fall of 7.8% (quarterly decline of 2.8%), reflecting the stabilization of exports, after the relatively high realization in the previous year, as well as the weaker growth of export demand for individual products. In conditions of decline in exports, but growth in domestic demand, total imports recorded minimal real growth in the first quarter of 0.2% on an annual basis (with a quarterly growth of 2.4%), on a relatively low comparison basis.

[18] Data on completed construction works and stocks of manufactured articles are as of April 2024, while data on long-term corporate loans, government capital investments, industrial production, imports of investment products and domestic production of capital goods refer to the April - May 2024 period.

Foreign trade data for the period April-May 2024 indicate possible increase in deficit compared to the same period last year, in conditions of nominal fall in the export and growth in the import of goods.



Source: State Statistical Office.



Source: State Statistical Office, IMF monthly database and NBRNM

1.4. Employment and wages

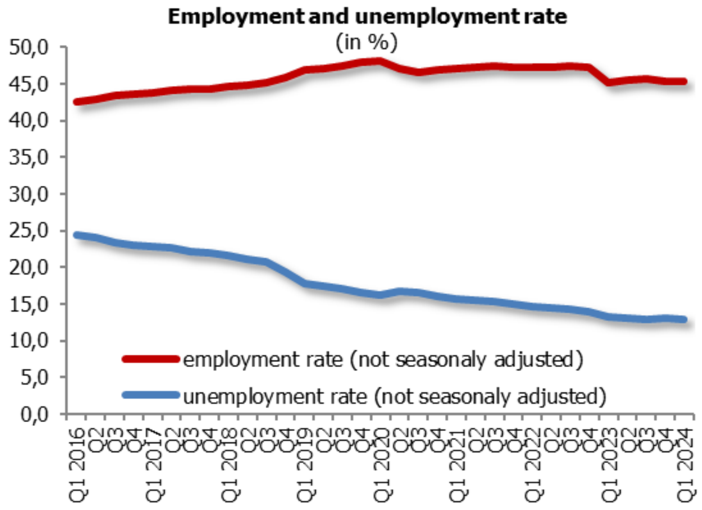
In the first quarter of 2024, the labor market registered moderate positive developments on an annual basis. Thus, the employment rate is 45.4% and is higher by 0.3 percentage points compared to the first quarter of 2023, in conditions of growth in the number of employees by 0.6%.The unemployment rate registered a decrease, reducing to the level of 12.9% at annual decline in the number of unemployed of 2.7%. In the first quarter, the active population recorded a slight increase on an annual basis (by 0.2%), with a minimal annual growth also being recorded with the inactive population (by 0.1%). In accordance with the surveys, the optimism of corporate managers in terms of the new employments in the second quarter of 2024 increased compared to the perceptions in the previous quarter. In terms of the labor cost, in the first quarter of 2024 the wages continued to grow on an annual basis, but slightly more slowly compared to the previous quarter.

In the first quarter of 2024, at the labour market,[19] moderate positive developments on annual basis were registered. Thus, in the first quarter of 2023, the employment rate remained at 45.4%, which is by 0.3 percentage points a higher level compared to the same quarter of the previous year, in conditions of an increase in the number of employees of 0.6% on an annual basis. Analyzed by activity, the biggest contribution to the annual growth in the number of employees is made by the activities related to "agriculture, forestry and fishing", followed by "construction", "accommodation facilities and food service activities", "public administration and defense; mandatory social insurance", and "administrative and auxiliary service activities". In terms of the economic status[20], the increase in the number

[19] Starting from this quarterly information, we reintroduce the annual analysis based on the comparable data from 2023 onwards, because the comparability in 2023 with other years by quarter was limited when the new Regulation (EU) no. 2019/1700 of the European Parliament and the Council for Social Statistics and the corresponding executive regulation of the Commission (EU) no. 2019/2240 for the area of the workforce was implemented, while the previous Regulation (EC) no. 577/98 was repealed. The implementation of the new regulation caused changes in the research, starting from the changes in questionnaire, changes in the order of the questions, modifying and removing current and adding new questions, changes in the scope and definition of employment and unemployment.

[20] The classification by economic status applies to the following groups: **employers** - persons who operate their own business entity or engages independently in their own shop, or farm owners who hire other employees; **employees** - persons who work in

of employed persons is explained with the growth in the categories "own account workers" and "unpaid family workers", while there is a decrease in "employees" and "employers" category.



Source: State Statistical Office, Labour Force

Note: LFS 2021 and 2022 use data from the 2021 census, while the data since Q1 2023 include methodological change, thus causing statistical break in the series.

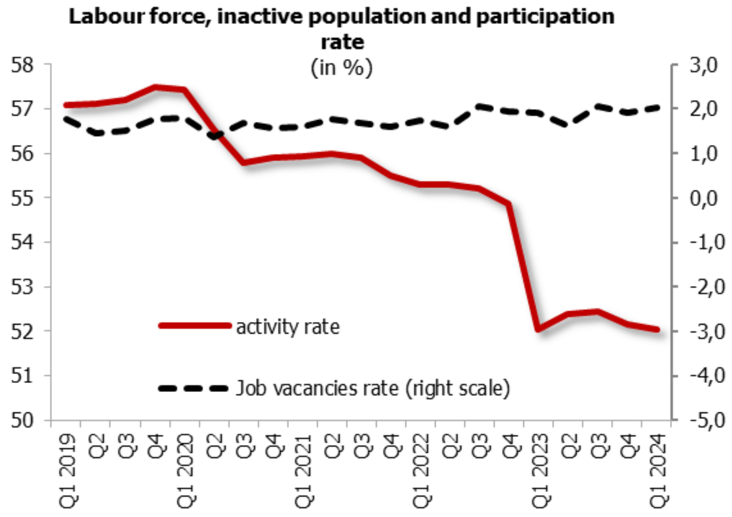
The business tendency surveys[21], on average, mainly point to more favorable expectations of the corporate managers with regard to the increase in the number of employees in the second quarter of 2024 compared to the previous quarter, given more favorable expectations with all sectors. Compared to the same quarter of the previous year, the expectations are less favorable.

Source: European Commission, Business and consumer surveys.
*Managers employment expectations for the next 3 months in the companies in the four sectors: industry, services, retail trade and construction .

government institutions, business entities in public, mixed, cooperative and undefined ownership or for private employer; **own-account workers -** persons who operate their own business entity, company, engage independently in their own business and work on a farm in order to generate income, while not hiring other employees; **unpaid family workers** - persons who work without pay in a business entity, shop or farm (owned by a family member).

[21] Source: European Commission, business tendency surveys, employment expectations in the next 3 months in industry, services, retail trade and construction (surveys conducted in April, May and June 2024).

The vacancy rate[22] is maintained on a relatively stable level, so in the first quarter of 2024 it equals **2%** (1.9% in the respective quarter of 2023). Analyzed by activity, the highest vacancy rates were registered in "administrative and auxiliary service activities" (3.6%), "art, entertainment and recreation" (3.5%), "accommodation and food service activities" (3.2%), "construction" (2.8%) and "trade" (2.8%).



Source: State Statistical Office.

Note: LFS 2021 and 2022 use data from the 2021 census, while Q1 2023 includes methodological change, thus causing structural break in the series.

In the first quarter of 2024, labor supply registered slight positive movements. Thus in the first quarter, the total labor force registered an increase by 0.2% annually, while the activity rate is minimally higher and equaled 52.1% (52% in the same quarter of 2023).

The stronger rise in the demand relative to supply of labor force in the first quarter of 2024 resulted in further fall in unemployment. Thus, the number of unemployed persons on an annual basis decreased by 2.7%, which caused a decrease in the unemployment rate, which was reduced to 12.9% (13.3% in the first quarter of 2023).

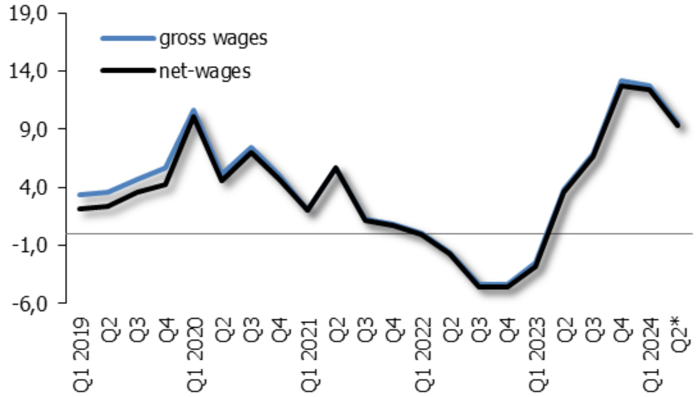
The average net and gross wages paid in the first quarter of 2024 recorded a high growth, but still slightly more moderate than the growth in the previous quarter. Thus, net and gross wages in the first quarter registered an annual growth of 16.3% and 16.6%, respectively, growth of 16.6% and 17%, respectively in the previous quarter). The annual wage growth in this quarter mostly reflects the increase in wages of public sector employees [23] in September 2023 in conformity with the new collective agreement. In addition, the increase in wages is partly the result of the increase in the minimum gross wage of 12.15%

[22] The job vacancy rate is defined as the ratio between the number of job vacancies and the total number of jobs. Usually, the job vacancy rate is considered along with the unemployment rate (a relationship known as the Beveridge Curve). The value of these two indicators provides labor market information about any skill mismatch. More precisely, if both indicators are moving simultaneously, the fluctuations are temporary, cyclical, and when the unemployment rate is decreasing, amid stable vacancy rate, these are structural changes, i.e. improved labor market efficiency.

[23] In July 2023, the Government signed a new Labor Agreement for the public sector, which includes increase in the wages by 10% from September 2023, an additional increase in September 2024 if the annual inflation rate in the first six months of 2024 exceeds 3% (the gross wage increases in the amount of up to 3%) and a review of the wage determining methodology from March 2025 which links the basic gross wage to the average gross wage in the country by increasing the complexity ratio by at least 5%. Also, the complexity ratio at the workplace will be harmonized with the nominal growth of GDP, if it is lower than the increase in the average gross wage.

in March 2024 and, consequently, the linear increase in wages in the state administration[24], as well as the transmission effect of the increase in the wages of the state officials in April 2023 and the increase in the wages of the healthcare workers[25] in May 2023. The growth in the minimum wage was driven by the existence of certain structural factors, such as lack of labor force in some labor market segments. Analyzing by activity, an annual wage growth was recorded in all economic activities, especially in: "public administration and defense", "education", "administrative and support service activities", "electricity, gas, steam and air-conditioning", "water supply", "wastewater removal, waste management and environment", "art, entertainment and recreation", "health and social work activity", as well as in "manufacturing industry". In conditions of growth in consumer prices of 3.4%, **real net and gross wages in the first quarter increased by 12.5% and 12.8%, respectively on an annual basis, which is slight deceleration compared to the increase in the preceding quarter.** In April 2024, the annual growth in the nominal average net wage decelerated more substantially and equaled 13.7%, while the real net wage increased by 9.3%.

Average gross and net-wages
(annual real changes in %)



Source: State Statistical Office.
*Data in Q2 is with last available data, April 2024.

1.5. Inflation

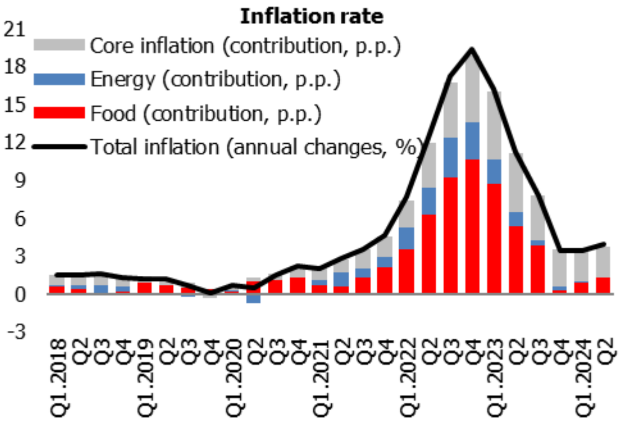
In the second quarter of 2024, the annual inflation rate accelerated moderately to 3.9% (3.4% in the previous quarter). This dynamic results from the food prices dynamics, while the contribution of other components remained almost unchanged. From the aspect of individual categories, the acceleration of the food component is mainly due to the growth of prices in "milk, cheese and eggs" and "bread and cereals" categories, which in the previous quarter recorded an annual decrease, as a result of lifting the domestic measures for reducing and freezing the prices of some food products. In terms of the factors that would influence the future short-term dynamics of consumer prices, in the second quarter the prices of

[24] In accordance with the latest amendments to the growth of the minimum wage (Official Gazette of the Republic of North Macedonia No. 68/24) from March 2024, the minimum net wage increased by Denar 2,392. The minimum gross wage, from March 2024 to February 2025, is Denar 33,352 (previously Denar 29,739), i.e. the minimum net wage is Denar 22,567 (previously Denar 20,175). This increase is calculated in accordance with the methodology from March 2022, which will adjust the minimum wage, and is calculated in accordance with the increase of the average wage paid in the RNM for the previous year and the consumer price index - 50% of the increase of each indicator, respectively. Moreover, it is defined that the minimum wage cannot be lower than 57% of the average net wage paid in the RNM for the previous year.
[25] https://vlada.mk/node/33235

domestic manufacturers of industrial products increased sightly, in contrast to the decline in the previous quarter, while imported inflation continues to slow down. In terms of the inflation expectations in the next period, the National Bank Survey showed that the economic analysts further expect its further deceleration, which is similar to the projected inflation dynamics of the National Bank and international institutions.

1.5.1. Current inflation

In the second quarter of 2024, the annual inflation rate intensified moderately and equals 3.9%[26], which is primarily due to the accelerated growth of food prices, and slightly, to energy prices.



Source: State statistical office and NBRNM calculations.

The annual increase in food prices in the second quarter of 2024 accelerated and averaged 3.5% (2.4% in the previous quarter). This movement of food prices is mostly due to the price growth in "milk, cheese and eggs" and "bread and cereals" categories, which recorded an annual decline in the previous quarter. This is mainly related to the lifting of domestic short-term measures related to the reduction and freezing of prices of some food products in retail trade, which were in effect until February 2024.[27]. On the other hand, the annual growth of vegetable prices show a significant slowdown, due to the shift of the fresh vegetables season, which partially neutralizes the growth in the other categories. However, growth in fruit prices, along with price growth in the categories "bread and cereals" and "milk, cheese and eggs" are the main components of food growth in the second quarter. From the aspect of the factors for the future inflation movement, in this period, the world prices of basic food products and the selling prices of domestic food producers kept declining, although less intensively, while the growth of foreign effective food prices, denominated in euros[28] keeps decelerating.

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[26] On a quarterly basis, domestic consumer prices increased by 1.9%, and by 1.2% seasonally adjusted.

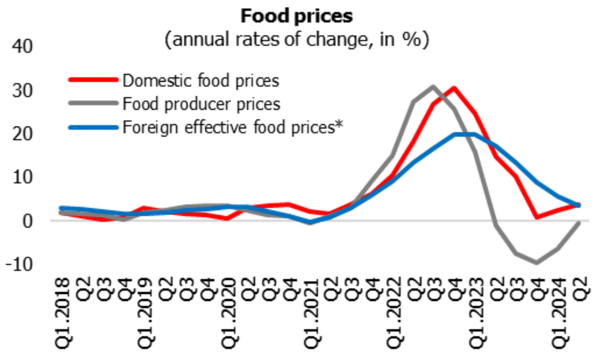
[27] On 19 September, the Government of the RNM adopted a decision on reducing the prices of products within 24 categories of bakery, milk, meat industry and agriculture of at least 10% in relation to their prices as of 1 August 2023 and to freeze them at that level, while retail traders were required to label these products with "guaranteed price" (link). Also, on 26 September, the Government prescribed, by a special decision, the highest trade (profit) margin in the trade in fresh fruits and vegetables in a total amount of up to10% in wholesale trade and of up to 15% in retail trade (link). These decisions were initially valid until November 2023, but then their validity was extended until February 2024 (link). On 28 September, the Government adopted a decision on reducing the import duties (trade margins and duties) on the imports of fresh vegetables, with validity until February 2024 (link).

[28] Data on sales prices of domestic food producers and foreign effective food prices refer to the first two months of the second quarter of 2024.

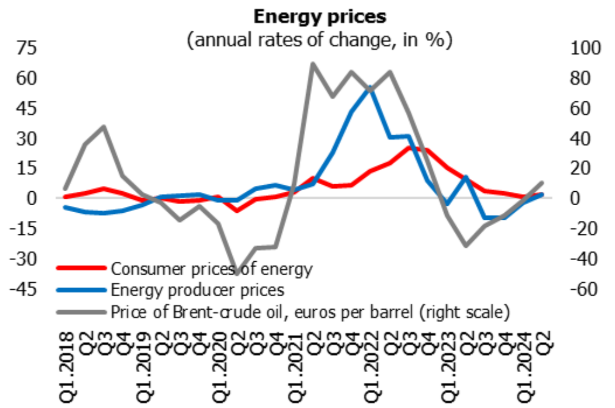
	annual changes, in %							contributions to annual changes, in p.p.						
	2023				2023	2024		2023				2023	2024	
	Q1	Q2	Q3	Q4		Q1	Q2	Q1	Q2	Q3	Q4		Q1	Q2
Consumer price index - all items	**16,1**	**11,2**	**7,7**	**3,4**	**9,4**	**3,4**	**3,9**	**16,1**	**11,2**	**7,7**	**3,4**	**9,4**	**3,4**	**3,9**
Food	24,6	14,5	10,2	0,8	11,8	2,4	3,5	9,0	5,5	3,9	0,3	4,5	0,9	1,3
Energy	15,3	9,2	3,6	2,3	7,3	0,5	1,8	2,0	1,2	0,5	0,3	0,9	0,1	0,2
Electricity	14,0	14,0	8,1	8,1	10,9	2,7	2,7	1,0	1,0	0,6	0,6	0,8	0,2	0,2
Heat energy	14,2	14,2	4,3	2,3	8,4	3,5	3,5	0,1	0,1	0,0	0,0	0,0	0,0	0,0
Fuels and lubricants	4,2	-14,3	-13,3	-8,6	-8,5	-2,4	3,9	0,1	-0,4	-0,4	-0,2	-0,2	-0,1	0,1
Food and energy (volatile prices)	22,2	13,2	8,5	1,1	10,7	1,9	3,1	11,0	6,7	4,4	0,6	5,5	1,0	1,5
Core inflation calculated by the NBRNM (total index - food and energy (categories 01.1, 04.5, 07.2.2))	10,2	9,1	6,9	6,0	8,0	5,0	4,8	5,2	4,5	3,3	2,8	3,9	2,4	2,4
Overall index excluding energy, liquid fuels and lubricants and unprocessed food (SSO)	15,8	11,2	7,2	3,7	9,3	3,3	4,6							
Overall index excluding energy, liquid fuels and lubricants, unprocessed food, tobacco and alcoholic beverages (SSO)	16,6	11,4	7,2	3,4	9,4	2,7	4,5							

Source: State Statistical Office and NBRNM calculations.

After the deceleration in the growth in the last period, the increase in energy prices intensified slightly in the second quarter of the year, and equaled 1.8% (0.5% in the preceding quarter), which is fully due to the shifts in domestic prices of oil derivatives, which increased in this quarter, as opposed to the decrease in the preceding quarter. This situation matches the movements of crude oil, the increase of which is linked with the higher consumption in the developed economies due to the beginning of the summer season and reduced supply, given further limitation of the production by OPEC+ and war conflicts. However, the electricity prices still contribute the most to the annual rise in the prices of the energy component, due to the transmission effect of the price growth in last July[29].



* Foreign effective food prices are calculated as weighted sum of food prices in countries that are major trade partners with North Macedonia in the domain of food import.



Source: State statistical office and NBRNM calculations.

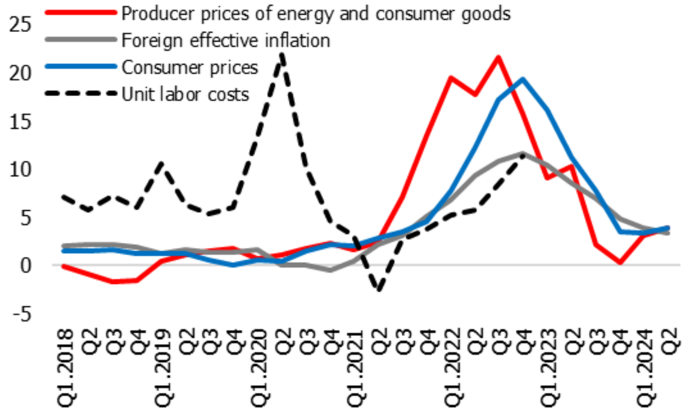
The core inflation continued to slow down also in the second quarter of 2024 and reduced to 4.8% annually (5.0% in the previous quarter). The slowdown in core inflation is mainly a reflection of the weaker growth in tobacco prices compared to the previous quarter, resulting from the equalization of the comparison basis, due to the application of the increased excise taxes since April in the previous year[30]. However, the services prices in restaurants and hotels continue to contribute the most to the core inflation (about 20%), with the prices of personal hygiene products, tobacco and the category "furniture, household goods and household maintenance" having also a more significant contribution. Regarding other inflation sub-indices, which exclude the most volatile prices, they registered an accelerated

[29] In conformity with the data of the State Statistical Office, in July 2023 the average price of electricity for households increased by 4.3%, compared to June (press release).
[30] In conformity with the adopted amendments to the Law on Excis, the excise on cigarettes increased by Denar 0.23 per piece, applied by January 2024. As for the other tobacco products, see the amendments on the following link. However, the excises are forecasted to increase every year until 2030.

growth in this quarter. Thus, the total index, excluding energy[31], liquid fuels and lubricant oils (for transport) and unprocessed food registered an annual growth equaled 4.6% (3.3% in the previous quarter), while the increase in the total index, excluding energy, liquid fuels and lubricant oils (for transport), unprocessed food, tobacco and alcoholic beverages, reached 4.5% (2.7% in the previous quarter).

In the second quarter of 2024, **producer prices** recorded a minimal annual growth of 0.5%[32], against the decline in the first quarter (of 1.4%). At the same time, the growth in the prices of consumer goods has the biggest contribution to the overall growth in production prices, and to a lesser extent, energy prices, which recorded growth after three quarters of annual decline. From the aspect of the individual activities, the growth is mostly driven by the increase in the production prices of beverages, energy and textiles. **Hence, producer prices of energy and consumer goods**, as an aggregate category and a factor that influences the dynamics of consumer prices, registered an increase of 3.9%, which is slight acceleration compared to the growth in the previous quarter (3.1%). **On the other hand, the foreign effective inflation**[33]**,** as an indicator of imported inflation, in the second quarter registered slower growth, which equaled 3.4% (3.9% in the previous quarter).

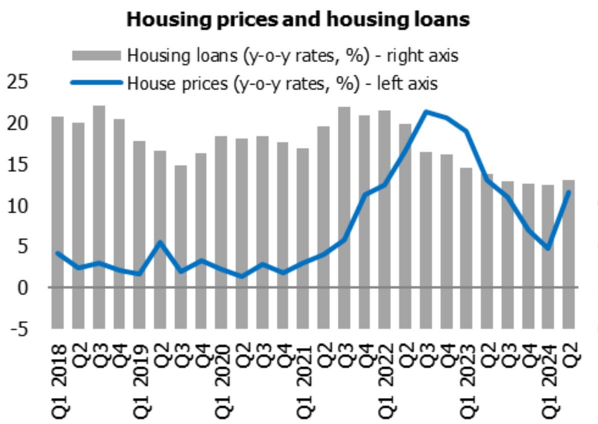
Factors affecting consumer prices
(annual rates of change, in %)



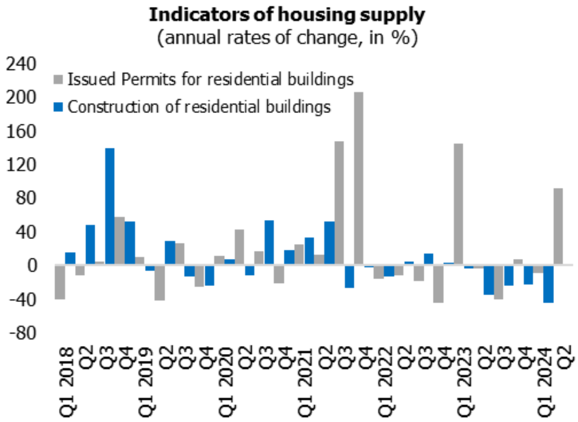
Source: State statistical office and NBRNM calculations.

In the second quarter of 2024, **the growth of the housing prices** accelerated, measured by the Hedonic index[34], which have risen by 11.5% on an annual basis (4.7% in the previous quarter). Regarding the supply, in the first quarter of 2024, the value of constructed residential buildings recorded a severe drop on an annual basis, which intensified and equaled 44.5%. After the fall in the previous quarter in the value of issued approvals for the construction of residential buildings, the available data for the second quarter of 2024[35] for now indicate high annual increase, in conditions of low comparison basis. Analyzing housing demand, slight acceleration of the annual growth in the housing loans in this period has been registered.[36]

[31] The energy category includes electricity, gas, liquid and solid fuels for heating and central heating.
[32] The analysis of producer prices of industrial products uses data for the first two months of the second quarter of 2024.
[33] The calculation of foreign effective inflation derives from the weighted sum of consumer price indices of the countries that are major partners of the Republic of North Macedonia in the field of import of consumer goods. The weight structure is based on the normalized shares of nominal imports from each country in the total nominal imports in the period 2016-2018. The calculation of this indicator includes Bulgaria, Germany, Greece, France, Italy, Austria, Slovenia, Croatia, Serbia, Poland and Spain. The data refers to the first two months of the first quarter of 2024.
[34] Hedonic index of housing prices, prepared by the National Bank on the basis of notices of sale in the capital city, and published by real estate agencies. The apartment price is a function of the apartment size, location, floor, use of central heating and construction date.
[35] The analysis refers to the first month of the second quarter of 2024.
[36] Available data for the first two months of the second quarter of 2024.



Source: NBRNM. Index of housing prices is calculated by the employees of the NBRNM based on the data from the daily newspapers.



Source: SSO and NBRNM calculations.

1.5.2. Inflation expectations

Regarding the expected trend of the inflation rate, domestic and international institutions predict a downward trend in the growth of consumer prices in the coming period. The expectations of the surveyed economic analysts given in the **Inflation Expectations Survey and the expectations for the movement of real GDP**[37], conducted in June 2024 are similar, according to which they project the inflation rate to decrease to the level of 3.9% in 2024, 3.0% in 2025 and 2.7% in 2026, in line with the expectations of more moderate price pressures due to the gradual stabilization of food and energy prices, the measures taken by policy makers, as well as the slowdown in foreign inflation.

Forecasts and expectations for the inflation rate

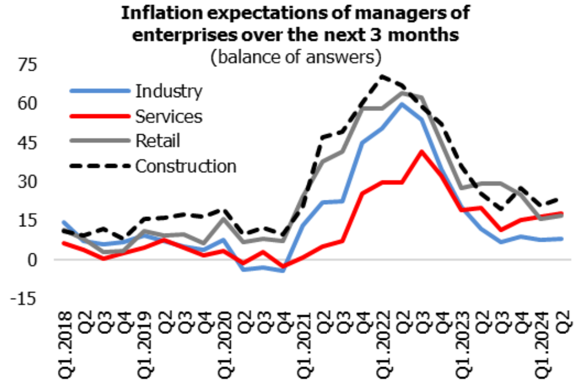
	2024	2025	2026
Economic analysts	3,9	3,0	2,7
IMF	4,0	2,5	2,0
Consensus Forecast	3,7	2,8	
Ministry of Finance	3,6	2,0	2,0
NBRNM	3,5	2,0	

Source: Inflation and real GDP growth expectations survey, June 2024; IMF, World Economic Outlook, April 2024; Consensus Forecast, June 2024; Ministry of Finance, Revised Fiscal Strategy of the Republic of North Macedonia 2024-2028, December 2023; and NBRNM, April 2024.

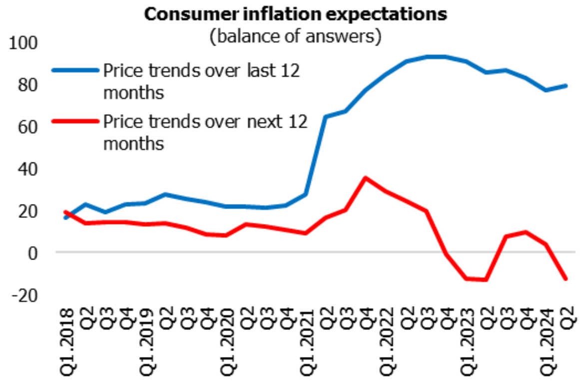
Weaker pressures from food and energy prices have a favorable effect on expectations for future short-term price movements in the manufacturing industry segment, as well as on consumer expectations for price changes, expressed in surveys. Thus, within the **corporate sector**[38], in the second quarter of 2024, on average, the expectations for the price fluctuations in the next three months are more favorable in the manufacturing industry, where a decrease in the number of company managers who expect an increase in the prices of their products is observed. On the other hand, in retail trade, construction and the service sector, there is a slight deterioration of that ratio compared to the previous quarter. In **terms of consumer expectations for price changes in the next 12 months**[39], they improved, that is, the

[37] In October 2017, the National Bank modified its Inflation Expectations Survey. New Inflation and Real GDP Expectations Survey is conducted on a sample of economic analysts, extending the Survey subject in line with the practice of the European Central Bank (ECB). The Survey results can be found at the following link.
[38] European Commission's business tendency surveys in industry, retail trade, construction and services sector as of June 2024.
[39] European Commission's Consumer Survey as of June 2024.

number of people who expect a decrease in prices in the next 12 months is increasing, as opposed to those who expect price growth.



Source: European Commission.
Data for the corresponding quarter are mean values from monthly data.



Source: European Commission.
Data for the corresponding quarter are mean values from monthly data.

1.6. Balance of payments

In the first quarter of 2024, the current account recorded a deficit of 1.3% of GDP, as opposed to the surplus registered in the same period last year. The expansion of the trade deficit in this quarter (of 1.2 percentage points of GDP) is the main factor for the deterioration compared to last year. This change is mainly the result of the drop in exports, which reflects the stabilization after the high growth in the previous year among some companies in the automotive industry segment and lower energy exports. The realizations of the secondary income, the surplus of which, after the record high levels, stabilized and in this quarter decreased by 1 percentage point of the GDP also acted in this direction. On the other hand, the changes in services are still favorable and had a positive impact on the current account balance. Regarding the financial account, during the first quarter net outflow in almost all categories were realized, except in direct investments, which registered significant net inflows. Foreign reserves remained within the safe zone.

	2023					2024	2023					2024
	Q1	Q2	Q3	Q4	I-XII	Q1	Q1	Q2	Q3	Q4	I-XII	Q1
	In millions of euros						% of GDP					
I. Current account	**92,8**	**-124,9**	**239,2**	**-111,7**	**95,3**	**-185,0**	**0,7**	**-0,9**	**1,8**	**-0,8**	**0,7**	**-1,3**
Goods and services	**-347,8**	**-577,4**	**-326,3**	**-591,2**	**-1842,7**	**-509,9**	**-2,5**	**-4,2**	**-2,4**	**-4,3**	**-13,5**	**-3,5**
Credit	2432,0	2487,3	2493,0	2527,9	**9940,2**	**2289,9**	17,8	18,2	18,3	18,5	**72,8**	**15,7**
Debit	2779,7	3064,7	2819,3	3119,1	**11782,8**	**2799,9**	20,4	22,4	20,6	22,8	**86,3**	**19,2**
Goods	-601,0	-592,6	-620,5	-762,2	**-2576,3**	**-811,9**	-4,4	-4,3	-4,5	-5,6	**-18,9**	**-5,6**
Services	253,3	15,2	294,2	171,0	**733,7**	**301,9**	1,9	0,1	2,2	1,3	**5,4**	**2,1**
Primary income	**-185,1**	**-185,1**	**-192,2**	**-186,3**	**-748,6**	**-193,2**	**-1,4**	**-1,4**	**-1,4**	**-1,4**	**-5,5**	**-1,3**
Secondary income	**625,6**	**637,5**	**757,7**	**665,7**	**2686,6**	**518,2**	**4,6**	**4,7**	**5,5**	**4,9**	**19,7**	**3,6**
II. Capital account	**0,2**	**-0,5**	**-0,5**	**-0,7**	**-1,6**	**0,0**	**0,0**	**0,0**	**0,0**	**0,0**	**0,0**	**0,0**
Net lending (+) / net borrowing (-) (balance from current and capital account)	93,0	-125,4	238,6	-112,5	**93,8**	**-185,0**	0,7	-0,9	1,7	-0,8	**0,7**	**-1,3**
III. Financial account	**-174,4**	**-167,9**	**575,2**	**-684,5**	**-451,6**	**136,6**	**-1,3**	**-1,2**	**4,2**	**-5,0**	**-3,3**	**0,9**
Direct investment	-143,3	-122,4	-51,2	-206,2	**-523,1**	**-235,9**	-1,0	-0,9	-0,4	-1,5	**-3,8**	**-1,6**
Portfolio investment	-438,5	20,0	414,9	37,3	**33,8**	**76,2**	-3,2	0,1	3,0	0,3	**0,2**	**0,5**
Currency and deposits	124,0	120,1	268,1	-99,0	**413,2**	**174,6**	0,9	0,9	2,0	-0,7	**3,0**	**1,2**
Loans	163,7	-174,0	-7,9	-384,9	**-403,2**	**23,6**	1,2	-1,3	-0,1	-2,8	**-3,0**	**0,2**
Trade credit and advances	115,3	-10,8	-48,9	-31,8	**23,8**	**98,3**	0,8	-0,1	-0,4	-0,2	**0,2**	**0,7**
Other accounts receivable/payable	5,0	0,1	0,1	0,1	**5,2**	**-0,3**	0,0	0,0	0,0	0,0	**0,0**	**0,0**
IV. Special drawing rights (Net incurrence of liabilities)	0,2	0,2	0,1	0,1	**0,7**	**-0,1**	0,0	0,0	0,0	0,0	**0,0**	**0,0**
V. Net errors and omissions	**-0,7**	**9,8**	**30,9**	**20,8**	**60,8**	**29,7**	**0,0**	**0,1**	**0,2**	**0,2**	**0,4**	**0,2**
VI.Reserve assets	**266,7**	**52,3**	**-305,6**	**592,8**	**606,1**	**-291,9**	**2,0**	**0,4**	**-2,2**	**4,3**	**4,4**	**-2,0**

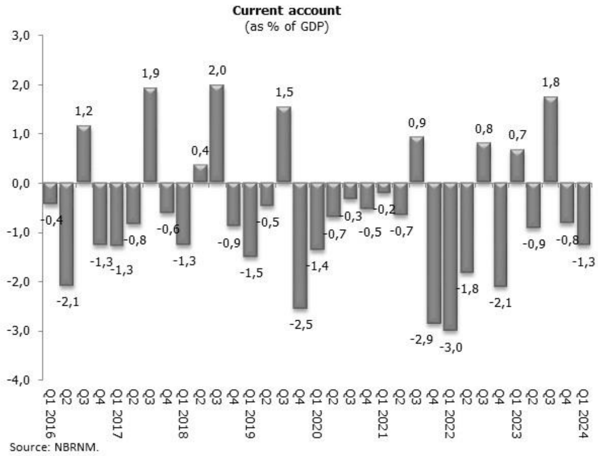
Source: NBRNM.

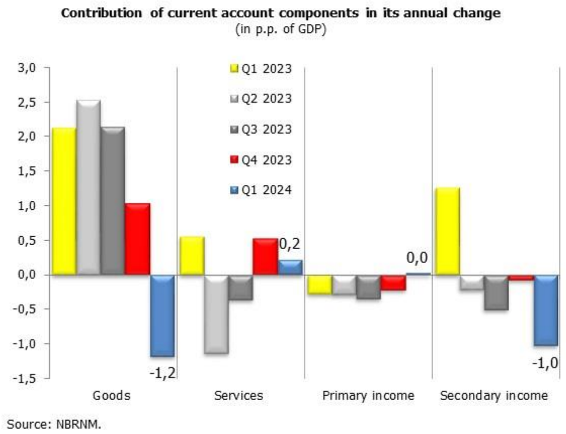
1.6.1. Current account

In the first quarter of 2024, the balance of payments' current account registered a deficit totaling Euro 185 million, or 1.3% of GDP[40]. Compared to the same period last year, there is a deterioration of 2.0 percentage points of GDP, primarily due to the widening of the negative trade balance, as well as lower surplus with the secondary income. The trade deficit in the first quarter of the year widened by 1.2 percentage points of GDP annually, primarily due to the decrease in the import of goods by 2.4 percentage points of GDP, given simultaneous decrease, although more moderate, in the import of goods (of 1.2 percentage points of GDP). Analyzed by the trade balance components, the weaker performance in the trade of goods is a result non-energy balance, given simultaneous improvement in the energy balance. The decrease in exports mostly results from the reduced export activity of part of the production facilities in foreign ownership related to the automotive industry, after the high growth in the previous period, as well as from the reduced export of energy. In addition, the lower export of iron and steel and ore had an impact in this direction. On the import side, the reduction of import pressures in the energy component continues, especially in the case of natural gas, which is also due to the narrowing of the energy balance on an annual basis. In addition, there is a decrease in the import of some of the raw materials for the automotive industry, corresponding to the lower export activity of some of these companies. The reduced surplus in the secondary income, as a result of the lower official and private transfers, which after the record high amounts are gradually stabilizing, also contributed to the deterioration in the current account. On the other hand, the balance of services improved

[40] The calculations use the projected amount of the nominal GDP (from April 2024).

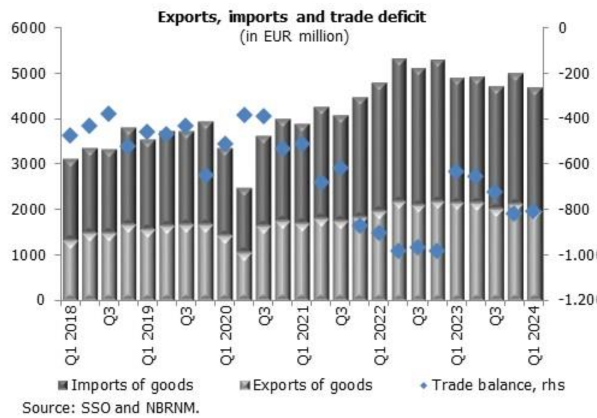
slightly, primarily as a result of higher net inflows in other business services and in telecommunications, computer and information services.

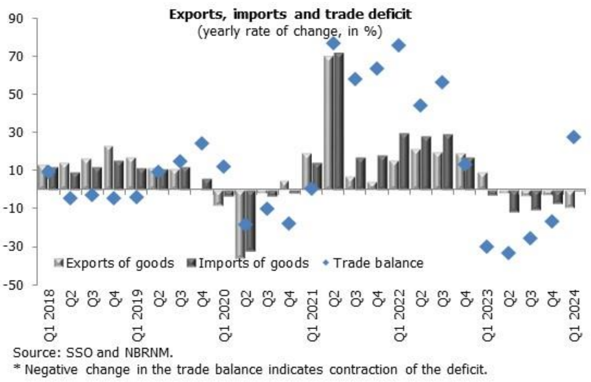




Annex 2: Foreign trade in goods and movement of the Nominal and the Real Effective Exchange Rate (NEER and REER)[41]

Foreign trade amounted to Euro 4,667.3 million in the first quarter of 2024, i.e. 32.1% of GDP, which compared to the same quarter of the previous year is a decrease of 4.5% (or 3.7 percentage points of GDP). This largely results from the reduced export of goods, while the decline in the import of goods has significantly slowed down.



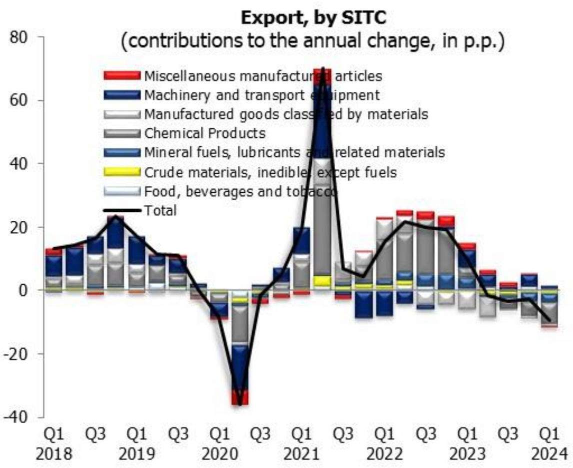


In the first quarter of 2024, the export of goods registered a decrease of 9.2% on an annual basis. The main contribution to the substantial fall in the exports in this period was made by the negative export performance of part of the production facilities from the automotive industry in foreign ownership, which can be perceived from the lower export of chemical products. The export of energy also recorded a negative contribution, due to the lower export of electricity, which is the result of the reduced export quantities and prices, with other export categories being affected in this regard, as well. The export of equipment and

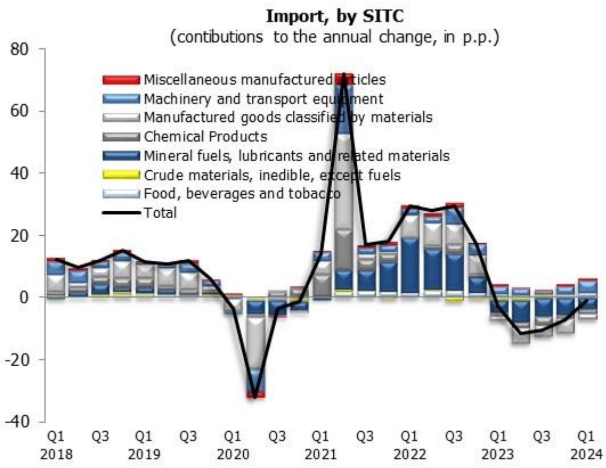
[41] According to the Foreign Trade Methodology, data on export of goods are published on an f.o.b. basis, and on import of goods, on a c.i.f. basis.

machinery and food is an exception, where growth has been recorded on an annual basis. Namely, the other segments of the automotive industry continued registering solid export performance, which influenced towards increase in the export of equipment and machinery in the first quarter of 2024. Regarding food, the export further increase and it is dispersed in several sub-categories. **In the first quarter of 2024, the import of goods declined slightly by 0.8% on an annual basis, again mainly due to the reduced import pressures in energy**, especially the reduced import of natural gas and oil derivatives, but also with an additional lower import of the raw material component for the industry. The significant reduction in the prices of electricity and natural gas had a dominant impact on the decline in energy imports in this quarter. The import of precious metals, as a raw material component of part of the foreign-owned export facilities, as well as the import of inorganic chemical products and iron and steel also contributed to the decline in imports during this period. On the other hand, during this quarter, a higher import of vehicles, as well as other categories of equipment and machinery was registered. **The performance in both foreign trade components in the first quarter of 2024 resulted in trade deficit widening by 27.5% on an annual basis,** in conditions of a deficit in the non-energy balance, given simultaneous decrease in the deficit in the energy balance.

The latest available data for the period April- May 2024 indicate a further decline in the export and simultaneous increase in the import component of foreign trade compared to the same period of the previous year. The annual decline in exports mainly results from lower exports of chemical products, as well as lower exports of energy, vehicles and ores. On the other hand, the annual decline in these categories is mitigated by the growth of the export of equipment and machinery. The growth on the import side in this period is mostly caused by the higher import of vehicles, as well as the import of equipment and machinery and food. On the other hand, there is a decrease in the import of natural gas and in the import of ores.



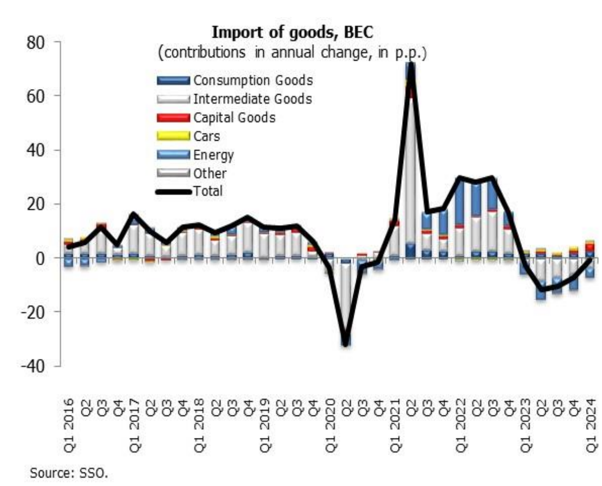
Source: SSO and NBRNM.

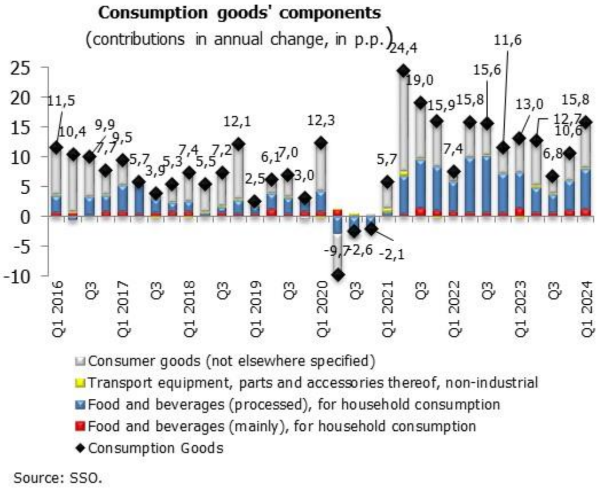


Source: SSO and NBRNM.

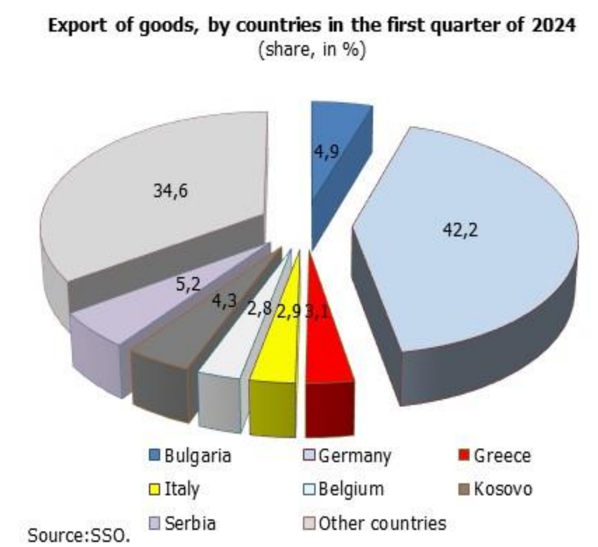
Analyzing imports of goods in the System of National Accounts (SNA), in the third quarter of 2024, the imports reduced due to the energy imports, as well as imports of intermediate products. The import of private consumption goods[42] increased during this quarter, with the highest contribution being made by the import of consumer goods not elsewhere mentioned, as well as the import of food and beverages (processed) mainly for households.

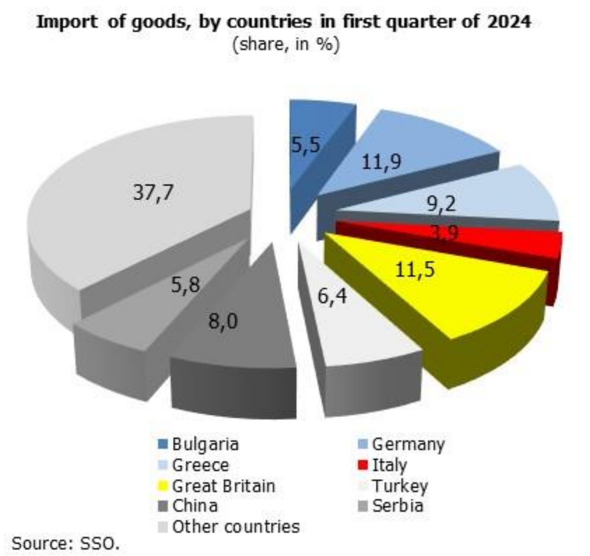
[42] The import of private consumption goods is analyzed as import intended for private consumption, approximated through the import of consumer goods and the estimated import of passenger vehicles for personal use.

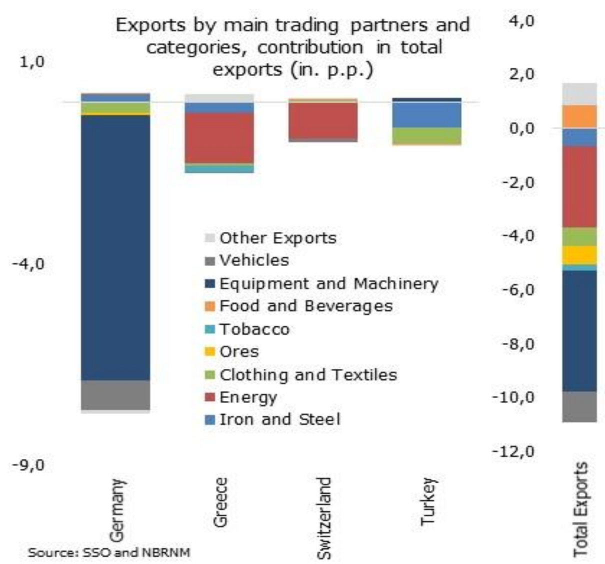


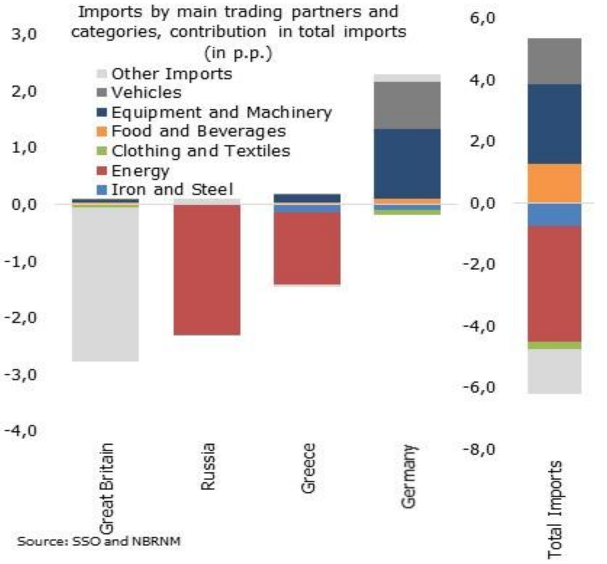


The foreign trade analysis, by trading partner, shows that in the first quarter of 2024, the European Union was the major trading partner of the domestic economy, making up 63.4% of total foreign trade. The analysis of the **export** side shows that the decrease on an annual basis mainly results from the export to Germany, in the conditions of the decline in the export of various products of the chemical industry. An additional contribution to the decline is the reduced export of energy to Greece and the reduced export of iron and steel to Turkiye. At the same time, such achievements were mitigated by the increased export of electrical control panels or distribution of electricity to the Czech Republic, as part of the export of the automotive sector. From the aspect of individual countries on the import side, the analysis shows that the biggest contribution to the annual decrease in imports is lower imports from Great Britain, as a result of the decrease in import of precious metals and inorganic chemical products, as well as lower import of energy from Russia and Greece. On the other hand, the **import** of equipment and machinery and vehicles from Germany has increased, as well as the import of energy from Bulgaria and equipment and machinery from Turkiye. Regarding the foreign trade ***balances*** by partner, the higher annual trade deficit was mostly due to the lower surplus in the trade with Germany, and less to the higher negative balance in the trade with Turkiye and Bulgaria.

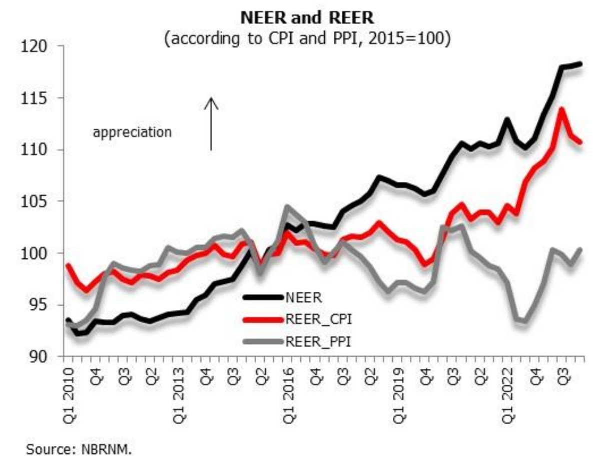


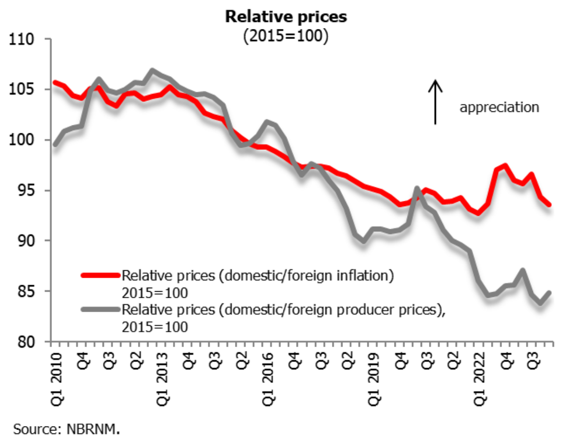






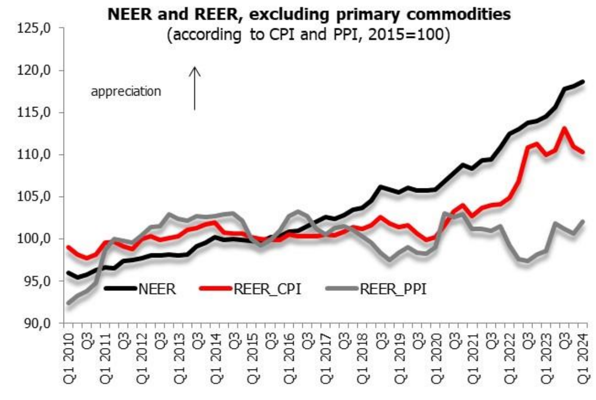
In terms of the price competitiveness indicators, in the first quarter of 2024, the REER deflated by consumer prices appreciated by 1.7% annually, while the REER deflated by producer prices appreciated by 3.4%. Such achievements are a reflection of the appreciation of the nominal effective exchange rate of the denar, which recorded an annual increase of 4.3%, primarily due to the depreciation of the Russian ruble and the Turkish lira against the domestic currency. On the other hand, the favorable performance in relative prices continued, i.e. the relative consumer prices and the relative producer prices reduced by 2.5% and 0.8%, respectively, on an annual basis.



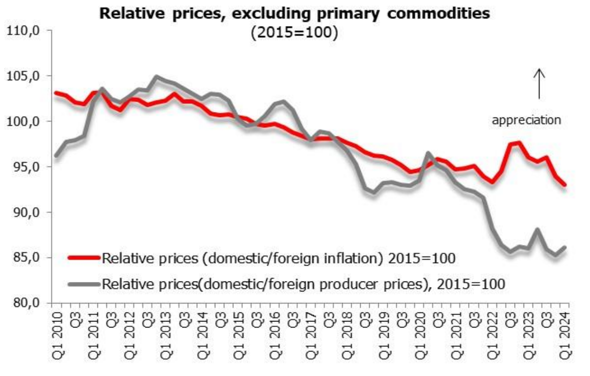


The analysis of the REER indices, measured by using weights based on the foreign trade without primary products, shows that the REER deflated by consumer prices appreciated slightly by 0.3% annually, while REER based on producers prices appreciated by3.6%. The nominal effective exchange rate appreciated by 3.5% due to the depreciation of the Turkish lira relative to domestic currency. Moreover, the relative consumer prices registered a decline of 3.1%, while the relative producer prices registered slight rise of 0.1% annually.

Regarding the price competitiveness indicators for the period April-May 2024, the REER deflated by consumer prices and producers prices appreciated by 1.9% and 2.0%, respectively. At the same time, the NEER appreciated by 3.5%, which is largely due to the depreciation of the Turkish lira and Russian rouble against the denar. Simultaneously, on the basis of the calculation by using weights based on the foreign trade without primary products, the REER index deflated by consumer prices appreciated by 1.1%, while the REER index deflated by producer prices appreciated by 2.7%. Moreover, the NEER appreciated by 3.4%, which is largely due to the depreciation of the Turkish lira against the domestic currency.



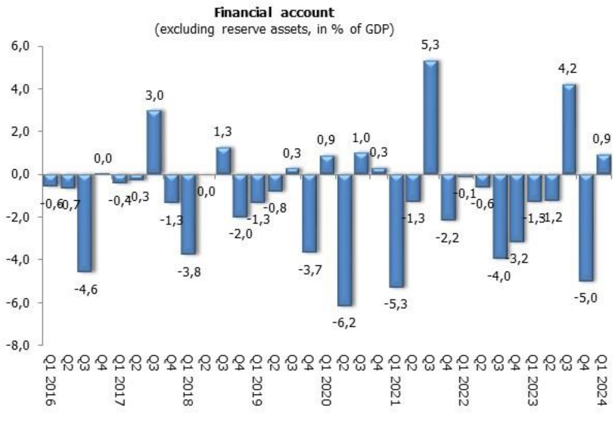
Source: NBRNM.



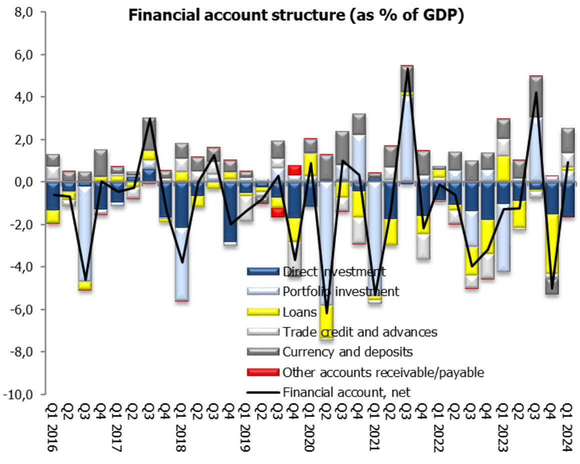
Source: NBRNM.

1.6.2. Financial account

In the first quarter of 2023, the financial account in the balance of payments registered net outflow of Euro 136.6 million, or 0.9% of GDP. At the same time, this financial account performance is mostly due to net outflows in the "currency and deposits" category, given simultaneous net outflows in the banking sector and in other sectors. In addition, this quarter registered net outflows in trade credits and advances, as well as in portfolio investments and loans. On the other hand, net inflows in foreign direct investments in the first quarter of the year were registered, mainly as a result of realized net inflows in the non-debt component, i.e. reinvested profit and equity, with simultaneous small inflows on a net basis and in intercompany lending.



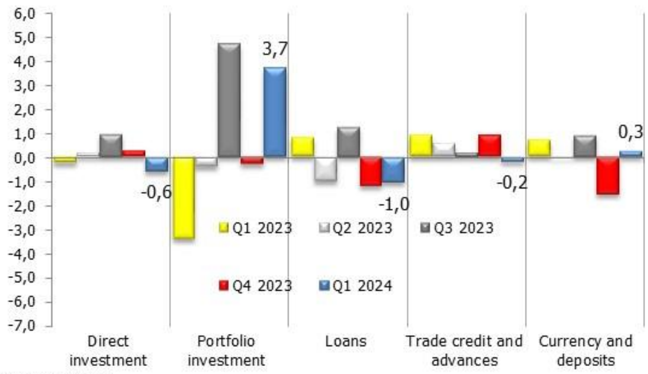
Source: NBRNM.



Source: NBRNM.

The annual analysis points to worse performance in financial flows in the first quarter of 2024, having in mind the realized net outflows, as opposed to the net inflows in the same period of the preceding year. At the same time, the greatest contribution to this performance in the financial account accounts for the realized net outflows in portfolio investments, as a result of the repayment of liabilities based on previously issued debt securities on international markets by the Government.[43] At the same time, in the "currencies and deposits" category, higher net outflows were registered compared to the same period of the previous year (higher net outflows in the banking sector). On the other hand, lower net outflows were recorded in loans and trade credits and advances on an annual basis. In the same direction were the higher net inflows of foreign direct investments, mainly under the influence of realized net inflows in intercompany lending (as opposed to outflows on a net basis in the same period of the previous year), with a simultaneous positive impact on the non-debt component, as well.

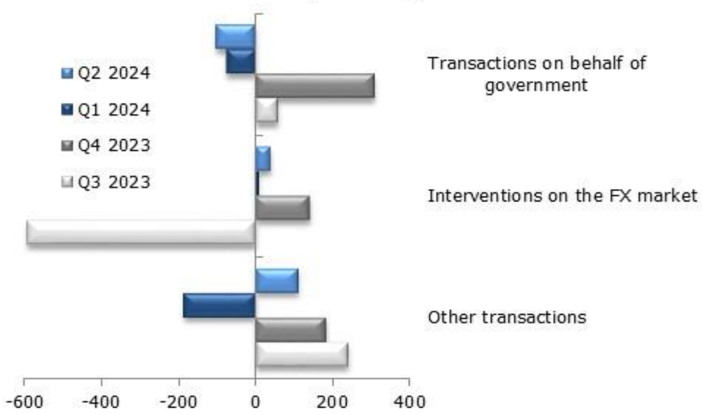
Contributions to the annual change in the financial account
(in p.p. of GDP)



Source: NBRNM.

At the end of the first quarter of 2024, the gross foreign reserves were valued at Euro 4287.1 million, which is a decrease of Euro 251.4 million compared to the previous quarter. Analyzed by the factors of change, **the decrease in the foreign reserves mostly stems from other transactions, caused by the foreign reserves management operations, which are temporary,** and less to the transactions for the account of the Government (a result of the regular servicing of liabilities to abroad, including the repayment of the first installment of the bond issued on the German market.

Factors of change of the foreign reserves, in quarters
(in EUR mil.)



Source: NBRNM

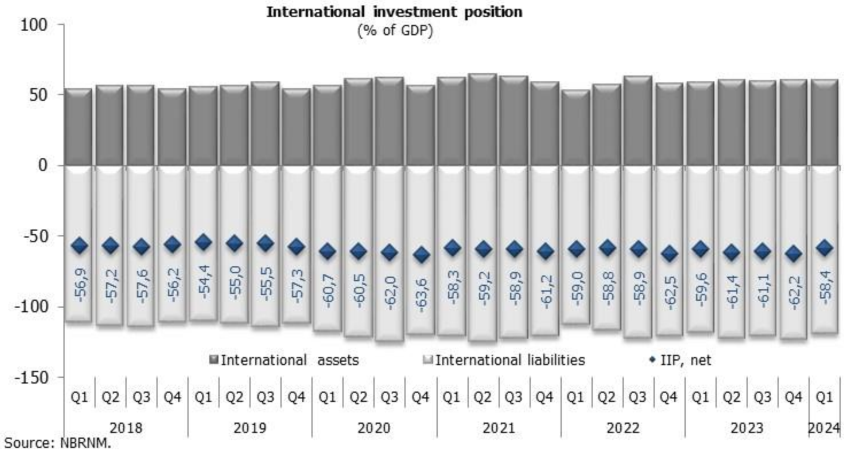
At the end of the second quarter of 2024, the gross foreign reserves were valued at Euro 4337.5 million, which is an increase of Euro 50.5 million, compared to the previous

[43] In March 2024, an installment based on the bond issued on the German securities market was paid – Namensschuldverschreibungen (NSV)

quarter. Analyzed by factors of change, the increase in the foreign reserves mostly results from the other transactions.

1.6.3. International investment position and gross external debt

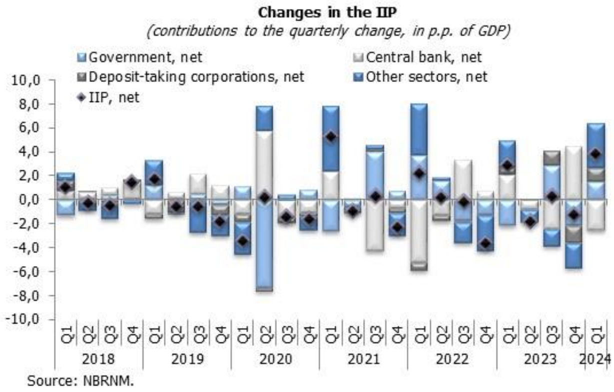
At the end of the first quarter of 2024, the net international investment position of the Macedonian economy was negative and amounted to Euro 8,506.2 million, or 58.4% of GDP. Compared to the end of the previous quarter, the net debt position narrowed by 3.8 percentage points of GDP, which is due to the decrease in international liabilities (of 3.9 percentage points of the GDP), at almost unchanged international assets.[44] The sectoral analysis shows that the improvement of the net debt position mainly results from the reduced net liabilities of the other sectors (mainly on the basis of direct investments), and to a lesser extent from the lower net liabilities of the Government (on the basis of debt securities[45]) and depositary institutions (mainly based on currencies and deposits).

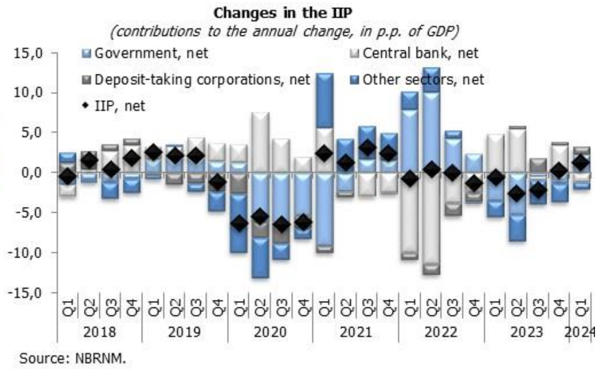


Annually, the negative international investment position narrowed by 1.2 percentage points of GDP[46], amid more evident increase in the international assets, compared to the increase in the international liabilities (of 2 percentage points and 0.8 percentage points of GDP[47], respectively). From a sectoral point of view, the narrowing is mostly due to the reduced net liabilities of the Government (on the basis of debt securities), to a lesser extent to the lower net liabilities of the depository institutions. The lower net assets of the central bank, as well as

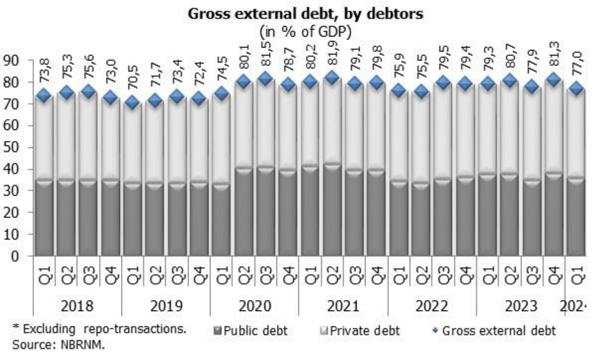
[44] In absolute amounts, the net debt position of the Macedonian economy in the first quarter of 2024 recorded a quarterly growth of Euro 6.1 million, with an increase in international funds of Euro 547.4 million and an increase in international liabilities of Euro 553.5 million.
[45] In March 2024, first installment of the bond („Namensschuldverschreibungen" – NSV) issued in 2022 on the German market was paid, in the amount of Euro 250 million with maturity of three years and interest rate on the 6-month EURIBOR, plus margin of 3.75%.
[46] In absolute amounts, the net debt position of the Macedonian economy in the first quarter of 2024 registered an annual growth of Euro 365.8 million.
[47] In absolute amounts, in the first quarter of 2024, international funds recorded an annual growth of Euro 832.5 million, while international liabilities recorded an annual growth of Euro 1,198.3 million.

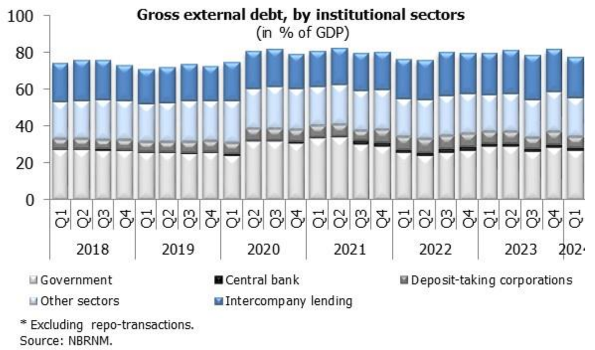
the higher net liabilities of the other sectors, had the opposite effect.





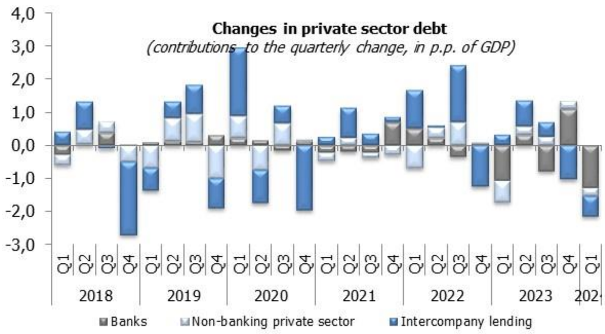
At the end of the first quarter of 2024, the balance of the gross external debt was Euro 11,789.4 million, or 81% of GDP, which is a decline of 3 percentage points of GDP, compared to the previous quarter. *By excluding the effect of the specific foreign reserves management activities of the National Bank*[48]*, the gross external debt amounts to 77% of GDP and registers a quarterly drop by 4.2 percentage points of GDP*[49], amid equal drop of both public and private debt (each by 2.1 percentage points of GDP[50]). The change in the public debt mainly results from the reduced debt of the central government based on debt securities, while the fall in the private debt is a reflection of the lower liabilities in all sectors, but mostly the reduced short-term liabilities in the banking sector based on currencies and deposits.



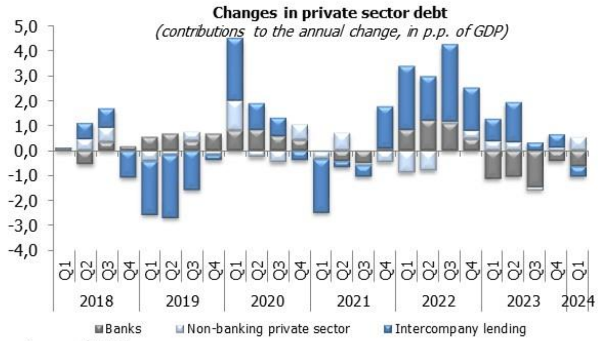


At the end of the first quarter, the gross external debt registered an annual decrease of 2.2 percentage points of GDP[51], in conditions of larger fall in public and private debt, (of 1.7 and 0.5 percentage points of GDP, respectively[52]). The annual decline in public debt is due to the reduced obligations of the central government based on debt securities. The better net position of the private sector on an annual basis is a reflection of the lower debt with the banks, as well as the lower intercompany lending with capital-related entities.

[48] The specific foreign reserves management activities of the central bank include repo agreements and other foreign reserves management operations.
[49] In absolute amounts, the gross external debt of the Macedonian economy in the first quarter of 2024 registered a quarterly growth of Euro 118.3 million.
[50] In absolute amounts, the public and the private external debt in the first quarter of 2024 registered a quarterly growth of Euro 39.1 million and 39.1 million,, respectively.
[51] In absolute amounts, the bottom of the Macedonian economy in the first quarter of 2024 registered an annual growth of Euro 390.8 million.
[52] In absolute amounts, the public and private external debt in the first quarter of 2024 registered an annual growth of Euro 90.1 and 90.1 million, respectively.

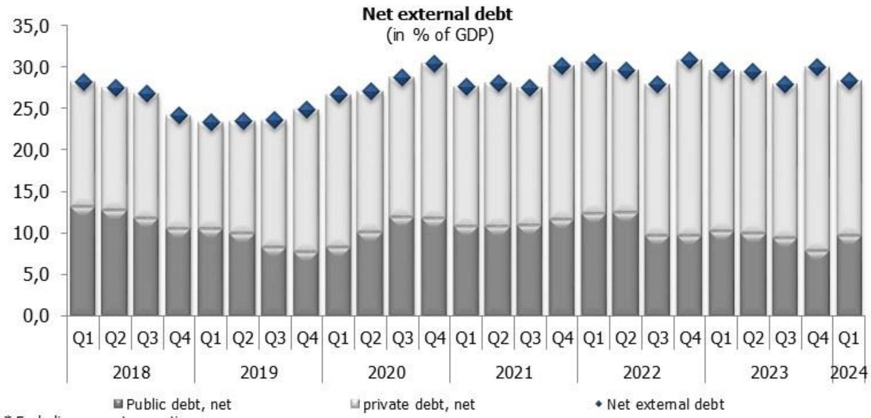


Source: NBRNM.



Source: NBRNM.

As of 31.3.2024, net external debt equaled Euro 4,132 million, or 28.4% of GDP, which is a quarterly fall of 1.6 pp of GDP[53], driven by the fall in the private net debt (of 3.4 percentage points of GDP), at simultaneous growth of the public net debt (of 1.8 percentage points of GDP).



* Excluding repo-transactions.
Source: NBRNM.

External debt ratio of the national economy remains in the safe zone. Except the gross external debt to GDP ratio which remains in the zone of highly indebted countries, all other solvency and liquidity ratios point to low indebtedness of the domestic economy. However, the high structural share of liabilities on direct investments in gross external debt, as a form of financing foreign capital companies, as well as liabilities on trade credits as an instrument for international trade financing, mitigates the risk profile in terms of the debt position of the economy. The level of gross external debt excluding trade credits and intercompany debt is lower and equals 46.7% of GDP[54], which is an indicator of moderate indebtedness.

[53] In absolute amounts, the net debt bottom of the Macedonian economy in the first quarter of 2024 registered an annual growth of Euro 39 million.
[54]Refers to debt without repo agreements.

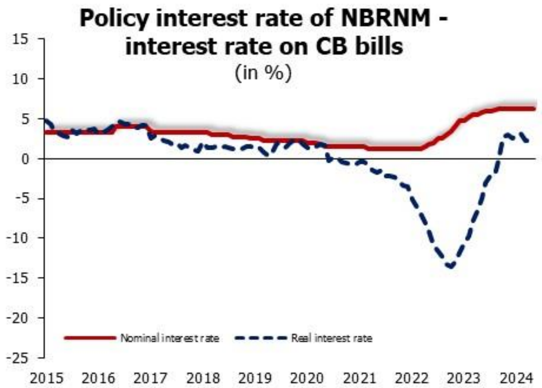
Indicators for external indebtness	Solvency				Liquidity		
	Interest payments/ Export of goods and services and other inflows	Gross debt/ Export of goods and services and other inflows	Gross debt/ GDP	Debt servicing/ Export of goods and services and other inflows	Foreign reserves/ Short-term debt	Foreign reserves/ Short-term debt, with residual maturity**	Short-term debt/ Overall debt
	in %				ratio	ratio	in %
31.12.2010	3,22	140,4	59,7	13,9	1,49	0,99	27,9
31.12.2011	3,12	148,4	64,6	16,8	1,78	1,18	25,2
31.12.2012	2,92	142,1	67,6	13,1	1,64	1,03	26,7
31.12.2013	2,51	137,3	67,3	15,8	1,64	1,08	23,3
31.12.2014	3,01	149,1	74,0	17,2	1,82	1,13	22,3
31.12.2015	2,69	143,9	73,2	20,0	1,69	1,13	21,3
31.12.2016	2,37	149,39	79,33	14,89	1,65	1,16	21,93
31.03.2017	2,69	138,68	76,61	12,72	1,47	1,00	23,53
30.06.2017	2,69	140,69	77,72	12,72	1,33	0,88	24,19
30.09.2017	2,69	138,24	76,37	12,72	1,26	0,86	24,57
31.12.2017	2,69	139,17	76,88	12,72	1,32	0,89	23,94
31.03.2018	2,22	132,80	78,27	15,77	1,30	0,93	25,06
30.06.2018	2,22	135,55	79,89	15,77	1,27	0,96	25,61
30.09.2018	2,22	135,98	80,14	15,77	1,30	0,98	25,59
31.12.2018	2,22	131,37	77,42	15,77	1,42	1,04	25,75
31.03.2019	2,05	119,55	74,37	8,89	1,40	0,98	25,81
30.06.2019	2,05	121,51	75,59	8,89	1,37	0,97	26,39
30.09.2019	2,05	124,39	77,38	8,89	1,37	0,97	27,62
31.12.2019	2,05	123,15	76,61	8,89	1,56	1,02	25,52
31.03.2020	2,45	121,76	73,94	16,79	1,39	0,95	26,63
30.06.2020	2,45	121,76	73,94	16,79	1,39	0,95	26,63
30.09.2020	1,91	129,93	80,75	13,61	1,72	0,98	22,93
31.12.2020	1,91	122,30	77,94	13,61	1,93	1,11	20,38
31.03.2021	2,19	127,34	83,90	16,27	1,93	1,18	21,49
30.06.2021	2,19	129,98	85,63	16,27	1,89	1,18	22,03
30.09.2021	2,19	125,62	82,76	16,27	1,77	1,30	22,21
31.12.2021	2,19	126,62	83,42	16,27	1,79	1,29	21,50
31.03.2022	1,77	118,00	83,09	9,38	1,27	0,95	25,97
30.06.2022	1,77	117,29	82,59	9,38	1,20	0,89	26,32
30.09.2022	1,77	123,63	87,06	9,38	1,35	0,90	26,89
31.12.2022	1,77	123,38	86,88	9,38	1,51	0,97	24,73
31.03.2023	2,35	112,37	84,29	14,70	1,63	1,01	23,61
30.06.2023	2,35	114,38	85,79	14,70	1,60	0,98	23,84
30.09.2023	2,35	110,44	82,84	14,70	1,50	1,02	24,44
31.12.2023	2,35	115,20	86,41	14,70	1,81	1,18	22,57
31.03.2024	2,97	106,38	81,56	12,44	1,65	0,98	23,11
*Moderate indebtedness criterion**	*12 - 20%*	*165 - 275%*	*30 - 50%*	*18 - 30%*		*1,00*	

II. Monetary policy[55]

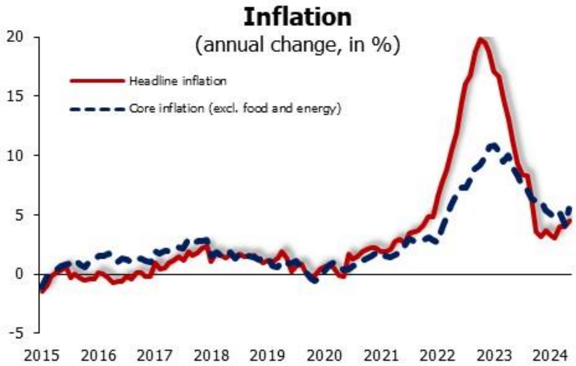
During the second quarter of 2024, the National Bank made no changes in the policy rate, i.e. it was kept at 6.3%, appropriate to the conditions in the economy. Also, there we no changes either in other monetary and macroprudential instruments. This decision is based on the expectations that the current level of interest rates, together with the changes in reserve requirement and macroprudential measures taken, are still expected to further slow the inflation down and maintain the exchange rate stability. Moreover, the latest changes in reserve requirement, the implementation of which started in June, provide further support to the prudent monetary policy. In the second quarter of 2024, the European Central Bank reduced the policy rates by 0.25 percentage points, stressing that despite the reduction, the monetary policy remains tight and prudent. The foreign reserves level remained adequate and in the safe zone, while banks' deposit base and lending registered a solid annual growth rate. However, the conditions for the monetary policy conduct remains vague. The National Bank will continue to carefully monitor the risks in the domestic and global economy and, if necessary, will act using all available instruments, in order to maintain the stability of the exchange rate and price stability.

[55] For more information on the new monetary measures, see the National Bank website: https://www.nbrm.mk/content/MPI%20publikacii/03%202024%20Hronologija_na_promenite_vo_postavenosta_na_monetarnite_instrumenti_na_Narodnata%20banka.pdf

During the second quarter from 2024, the National Bank preserved the policy rate at 3.25%. Interest rates on overnight and seven-day deposit facilities remained unchanged, i.e stood at 4.2% and 4.25%, respectively. The offered amount of CB bills remained unchanged at Denar 10,000 million, with the changes in the reserve requirement so-far, which encourage lending to projects related to domestic production of electricity from renewable sources, being further implemented. When making a decision to maintain the current monetary policy setup, the main emphasis was placed on the need for inflation stabilization and long-term inflation expectations. Namely, the current level of interest rates, together with the latest changes in reserve requirement, the implementation of which commences in June, as well as macroprudential measures taken, are still expected to further slow the inflation down and maintain the exchange rate stability through prudent monetary policy conduct.



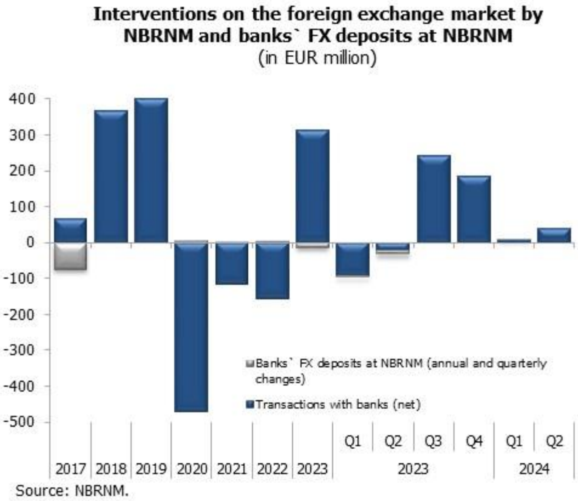
Source: NBRNM.

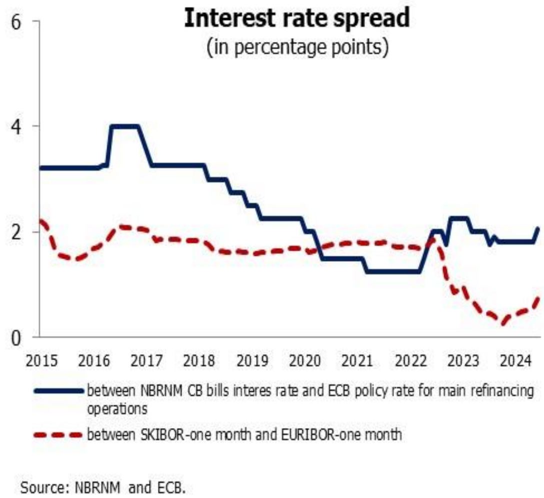


Source: SSO and NBRNM.

The performance[56] of the main macroeconomic indicators in the domestic economy suggest the need for further caution in conducting policies. The economic growth in the first quarter of 2024 accelerated slightly, matching the National Bank forecasts, yet more moderate than expected. In May 2024, the inflation moderately accelerated and equaled 4.5% annually, amid positive contribution to the growth of both core inflation and other components. However, the inflation in May does not deviate from the trajectory within the National Bank spring forecasts. According to these forecasts, an average inflation of 3.5% is expected for 2024. As for the primary commodities prices on the markets, the latest forecasts have been revised slightly upward, with a minor decline this year, while the uncertain geopolitical context still creates uncertainty and upside risks for the coming period. All this imposed the need for further caution in conducting monetary policy. The situation on the foreign exchange market remains favorable and contributes to net purchase of foreign currency by the National Bank since the beginning of the year, amid solid inflow of foreign currency on the currency exchange market. The level of foreign reserves at the end of May is appropriate for maintaining the stability of the exchange rate of the domestic currency. In the monetary sector, the data as of May 2024 indicate further increase in the banks' deposit potential, similar to the expectations, amid slightly faster credit growth than forecasted.

[56]It refers to the available information during the second quarter of 2024 that was taken into account when making the decisions on the monetary stance in that period.

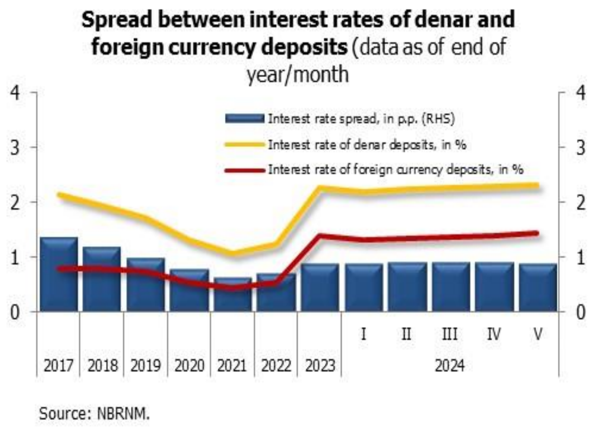




Given the applied monetary strategy, when making monetary decisions, the setup of the European Central Bank (ECB) policy is also taken into account, which lowered the policy rates by 0.25 percentage points in the second quarter of 2024, i.e. it reduced the interest rate on basic refinancing operations to the level of 4.25%, which is in line with the market expectations. The ECB pointed out that despite the decrease, with the new level of interest rates, the monetary policy remains tightened and prudent. Thus, the National Bank and the ECB's policy rates spread in June 2024 equaled 2.05 percentage points (increase compared to the previous quarter of 0.25 percentage points). Regarding the indicative market interest rates on 1m SKIBOR and 1m EURIBOR, the spread between them increased by 0.2 percentage points at the end June 2024, compared to the previous quarter.

Regarding the deposit interest rates in the domestic economy, in May 2024 the interest rates on denar and foreign currency deposits recorded insignificant changes, compared to the previous quarter, while the interest spread remained unchanged and amounted to 0.9 percentage points. Regarding the newly accepted[57] total deposits, the interest rate spread in May did not change compared to the end of the previous quarter and equaled 0.8 percentage points, in conditions of an equal reduction in denar interest rates (from 2.8% in March to 2.7% in May) and on foreign exchange interest rates (from 2.1% in March to 2.0% in May).

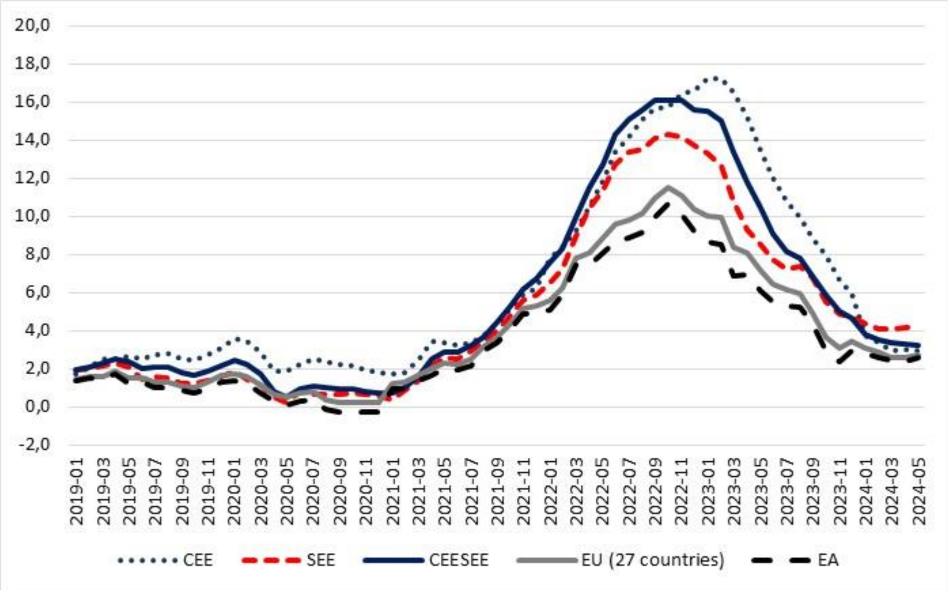
[57] Regarding the interest rates on newly approved loans, one should have in mind that they are characterized with variable movements. Interest rate volatility on newly approved loans results from the fact that they are determined by the volume of newly approved loans (which can vary from month to month) and their interest rate.



Annex 3: Is monetary easing a reality anytime soon?

In most countries of the CESEE Region, inflation trends are favorable. Namely, with the increase in interest rates, inflation visibly slowed down, so that in the region it is currently hovering around 3.5% on an annual level, compared to the reached maximum of over 16%. Undoubtedly, this is an expected result, taking into account the rapid and strong monetary tightening, and thus the tightening of the overall financial conditions, in global terms. Apart from monetary measures, the easing of supply-side pressures also contributed to slower price growth. Namely, inflation was initially instigated by disrupted supply chains, additionally stirred up by exceptional increase in food and energy prices. Thus, after the military attack on Ukraine, world food prices increased by 60% in just one year, while energy prices reached historical peaks. In the last period, these inflationary pressures are gradually decreasing, evident through the drop in food and energy prices, with the situation with the supply chains being normalizing and coming close to the pre-pandemic levels. All this reduces the pressure on prices globally.

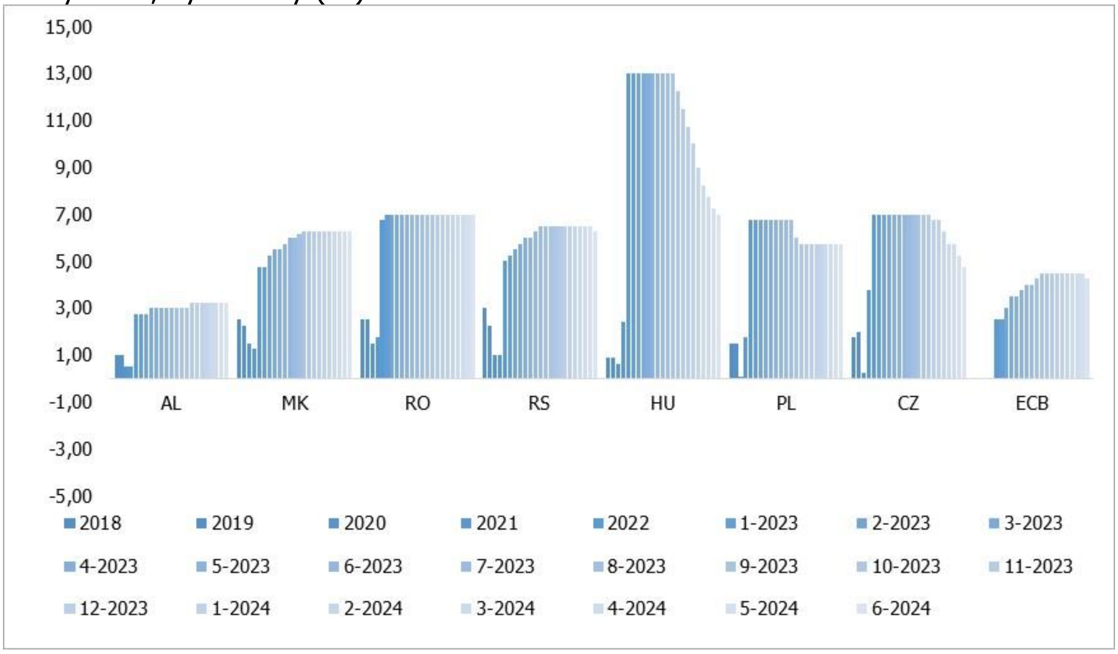
Chart 1
Inflation, by region
(annual rates, in %)



Source: Eurostat, inflation according to HICP.

However, taking into account the constant uncertainty, although the pressure on prices is decreasing, it is still too early to conclude that inflation has been brought down to a sustainable level. Pronounced geopolitical risks still threaten the stability of the global commodity market. The impact on prices from the Middle East conflict has been generally moderate so far, but it brings high uncertainty and risks. An additional risk factor is an increase in nominal and real wages in the region, as a result of the need to maintain purchasing power, but also as a result of the restrictiveness on the labor market under the influence of structural factors. Not less significant is the future behavior of companies and their policy on profit margins. Therefore, central banks must continue to closely monitor the situation and remain vigilant in future, as premature policy normalization could disrupt the ongoing process of disinflation. In some countries in the region, such as Hungary, Poland and the Czech Republic, the central banks have started reducing the policy rates since the end of last year, and from the middle of this year, Serbia, as well, began reducing the interest rate.

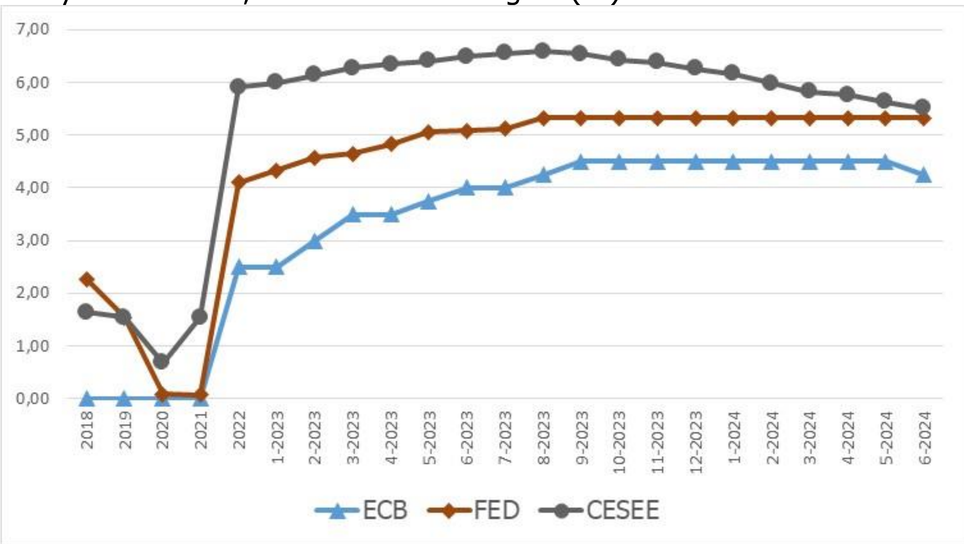
Chart 2
Policy rates, by country (%)



Source: National central banks, ECB.

The monetary tightening so far by the National Bank has been driven by the current economic and financial conditions in the domestic economy. The direction of future interest rate changes will depend on several key indicators. First, it is the inflation dynamics and the slowing down of inflationary pressures on a more permanent basis. The second important indicator of the foreign exchange market, having into consideration our strategy for maintaining a stable exchange rate of the denar against the euro. Currently, the trends are favorable and the market is stable, supported by a significantly reduced trade deficit, high private transfers and inflows of foreign direct investments. The ECB's monetary policy also plays an important role, as our currency is pegged to the euro. The ECB has kept interest rates unchanged since last October, maintaining a restrictive monetary policy setup, and this June it lowered interest rates for the first time (by 25 basis points), which was explained by the fact that inflation in the euro area is decreasing and it is gradually approaching the goal, but that it still remains in the restrictive zone. However, decisions will further depend on data and whether key macroeconomic data are consistent with the expectations and risk assessments. The ECB's latest forecasts that euro area inflation will likely exceed the target until 2025 have significantly shaken investor confidence for further reductions, with market expectations for just one more reduction for this year prevailing. Unexpectedly higher price pressures since the beginning of the year and stronger economic data for the US have also shifted the expectations for decreasing the policy rate by the FED. Namely, investors anticipate a rate cut of less than 40 basis points by the end of the year (versus expectations for a decrease of over 150 basis points that prevailed at the beginning of 2024).

Chart 3
Policy rates of ECB, FED and CESEE Region (%)

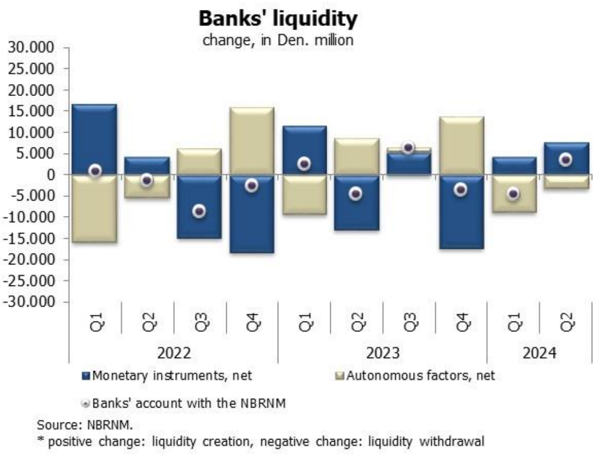


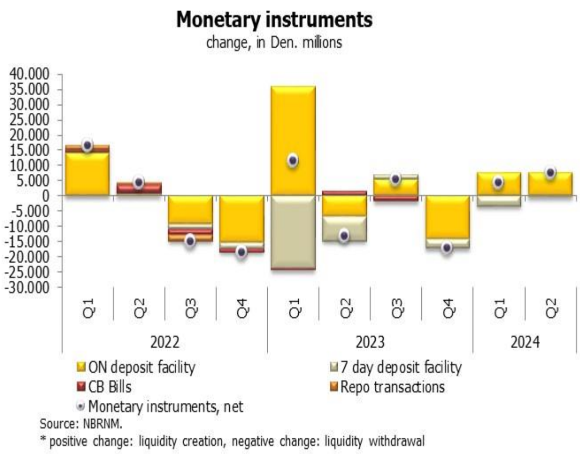
Source: National central banks, ECB, IMF.

During the last decision-making on the direction of the monetary policy, the interest rate remained unchanged, with the main emphasis when making the decision to maintain the current monetary policy setup being put on the need to stabilize both inflation and inflation expectations on a more permanent basis. It is estimated that the context for monetary policy conduct remain vague, so further careful monitoring of the inflation dynamics and factors is needed, as well as prudent conduct of the macroeconomic policies that affect the demand in the economy, as well as the labor market. The National Bank monitors the performance regularly, as well as its influence on the primary objective and if the conditions are met, it makes room for monetary relaxation in the forthcoming period.

2.1. Banks' liquidity

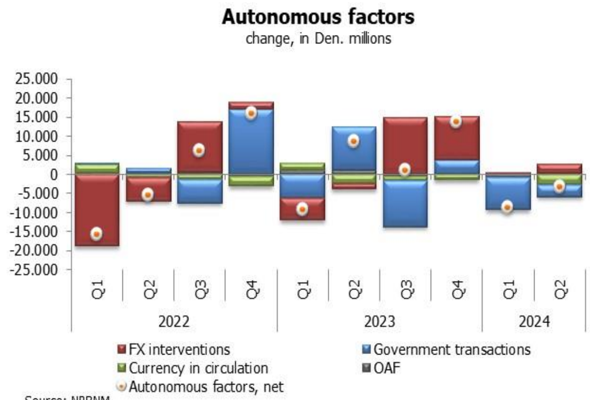
In the second quarter of 2024, the banks' denar liquidity increased, which fully results from the change in the monetary instruments, while the autonomous factors acted towards liquidity creation.



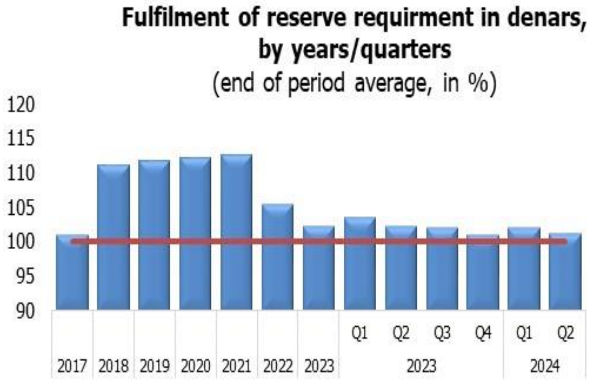


The autonomous factors, net, in the second quarter of 2024 contributed towards liquidity withdrawal from the banking system by Denar 3,255 million. Such change with the autonomous factors arise from the Government transactions and currency in circulation, while the foreign currency interventions led to slight liquidity growth.

In such circumstances, monetary instruments, banks' investments in deposit facilities (overnight and seven-day) decreased by Denar 7,619 million in the second quarter of 2024, which contributed to liquidity creation in the banking system. At the same time, overnight deposits decreased by Denar 7,720 million, while 7-day deposits increased by Denar 101 million. The basic instrument - CB bills, remained unchanged and at the end of the second quarter of 2024, it equaled Denar 10,000 million.



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



Source: NBRNM

During the second quarter of 2024, the banks continued to have more allocated funds on the accounts with the National Bank than the determined amount of the reserve requirement in denars, on average by about 1.2%.

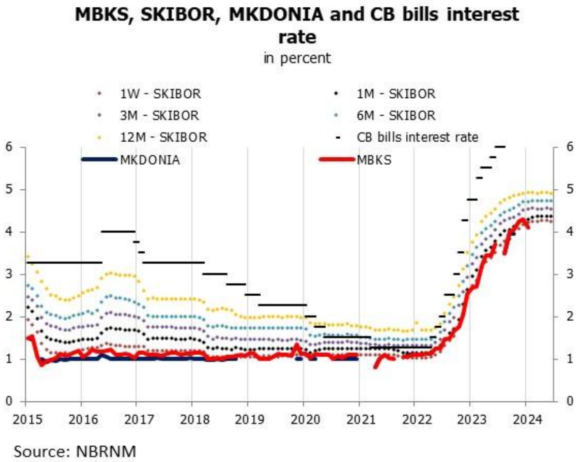
III. Financial market developments

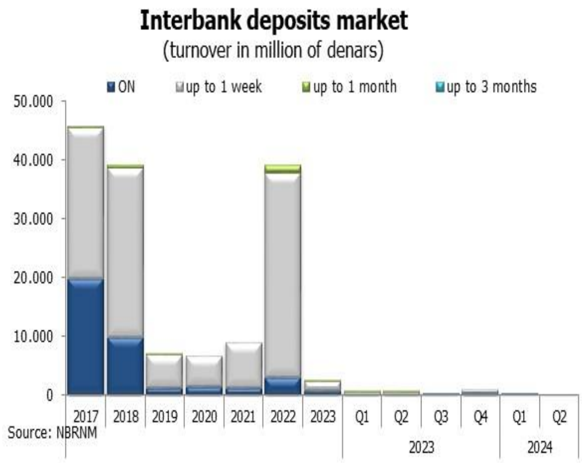
In the interbank deposit market in the second quarter of 2024, no trading activities were recorded. SKIBOR's average quotes were relatively stable, and did not show any significant movement. In the primary government securities market, the new issues were mainly with longer maturities, while the secondary securities market reported no trade securities. The stock exchange turnover on the Macedonian stock market decreased by 21.7% compared to the previous quarter, while the MBI -10 registered a quarterly increase of 9.0%. The indices on the regional stock exchanges moderately increased, on average by 6.6% quarterly. In the international financial markets during the second quarter of the 2024, volatility indices on the bond and stock markets, i.e. MOVE and VIX indices registered divergent change, but jointly, indicate moderate uncertainty reduction on the global capital markets. Most of the spreads between the yields of Macedonian and German Eurobonds narrowed compared to the previous quarter, amid more evident increase

in the yields of German government bonds, compared to the increase in the yields of Macedonian Eurobonds.

3.1. Unsecured interbank deposit market

In the second quarter of 2024, no activities within the interbank deposit market (MBKS) were registered, i.e. there is no trading, in conditions of an unchanged policy rate of the National Bank. Last quarter, only overnight transactions were recorded, but during the second quarter, there is no record of realized trading on the interbank deposit market of any maturity.

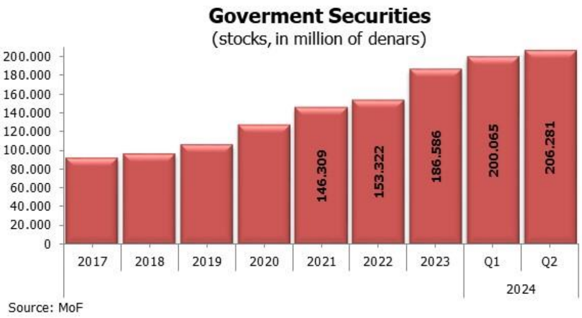


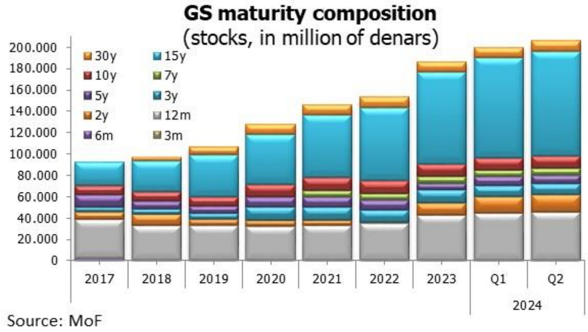


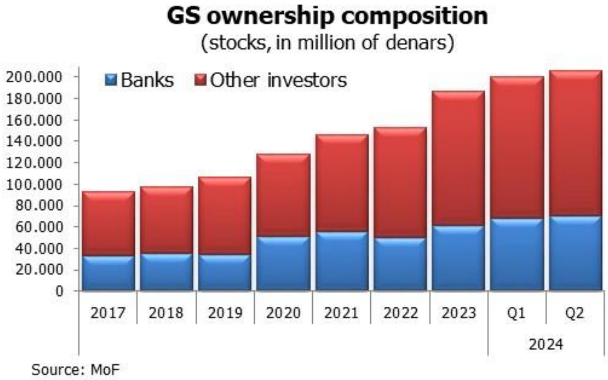
3.2. Government securities market

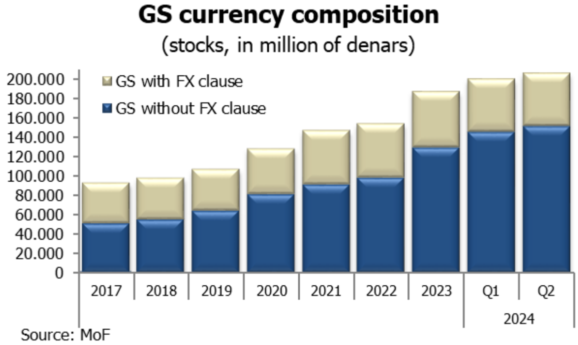
The stock of government securities issued on the primary market in the second quarter of 2024 increased by Denar 6,216 million or 3.1% on a quarterly basis and reached Denar 206,281 million. At the same time, the quarterly growth mainly stems from the securities with longer maturities, i.e. fifteen-year and two-year government bonds (with an increase of Denar 5,083 and Denar 1,104 million, respectively), while the balance of five-year and ten-year government bonds decreases (a fall of Denar 409 and 208 million, respectively). Analyzing the structure of government securities, government bonds remain dominant category, with a share of 78.1%. Thus, the fifteen-year government bonds still make up most of the maturity structure of government securities of 47.8% (46.7% in the previous quarter), which is in line with the guidelines from the Fiscal Strategy of the Ministry of Finance for issuing government bonds with longer maturities, in order to optimize debt payment and reduce refinancing risk.[58] Also, in this quarter, the two-year the share of the bonds in the maturity structure of government securities raised slightly to 8.1% (7.8% in the previous quarter). Analyzing maturity, the rest of the government securities registered a minor decrease in their share compared to the previous quarter. Analyzing the currency structure, denar government securities without currency clause maintained their dominant share, making up 73.0% of total government securities (72.4% in the previous quarter). From the aspect of the ownership structure, in this quarter the share of the banks minimally increased to 34.2% (34.1% in the previous quarter), at the expense of a corresponding reduction in the share of other investors to 65.8% (65.9% in the previous quarter). Within other investors, the pension funds remain dominant (with a share of 46.8%).

[58] Revised Fiscal Strategy for 2024-2028, Ministry of Finance, December 2023.

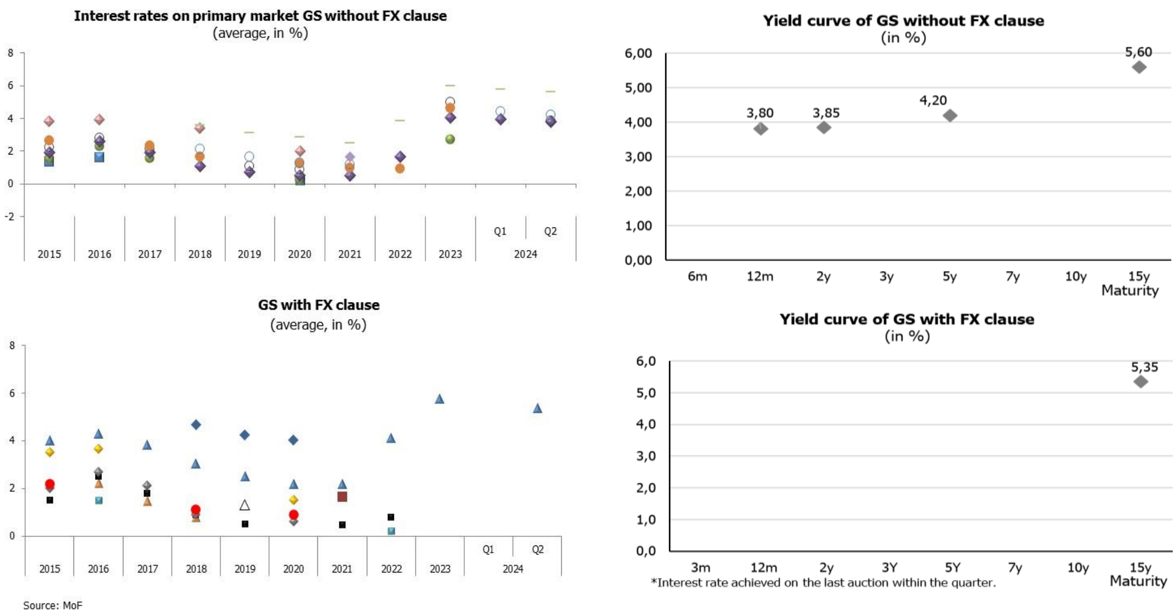




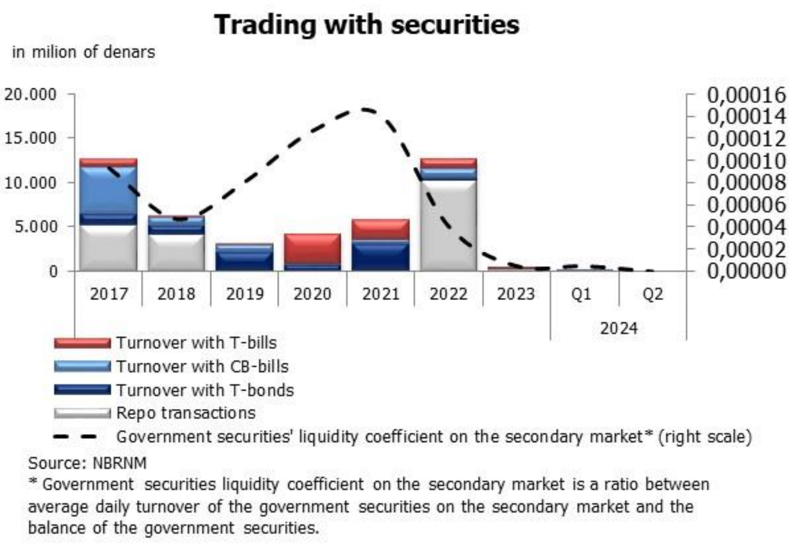




In the second quarter of 2024, interest rates on issued government securities, set by the Ministry of Finance, registered moderate downward changes. Thus, in the segment of government securities without a currency clause, twelve-month treasury bills, two-year, five-year and fifteen-year government bonds were issued in the primary market with interest rates of 3.80%, 3.85%, 4.20% and 5 .60%, respectively (in the previous quarter twelve-month, five-year and fifteen-year treasury bills were issued with average weighted interest rates of 3.94%, 4.4% and 5.77% respectively, while two-year government bonds were last issued in the last quarter of 2023, with an average weighted interest rate of 4.7%). In addition, within the segment of treasury bills with a currency clause, fifteen-year government bonds with an interest rate of 5.35% were issued in the primary market (fifteen-year government bonds with a currency clause were last issued in the last quarter of 2023 with an interest rate of 5.9%).

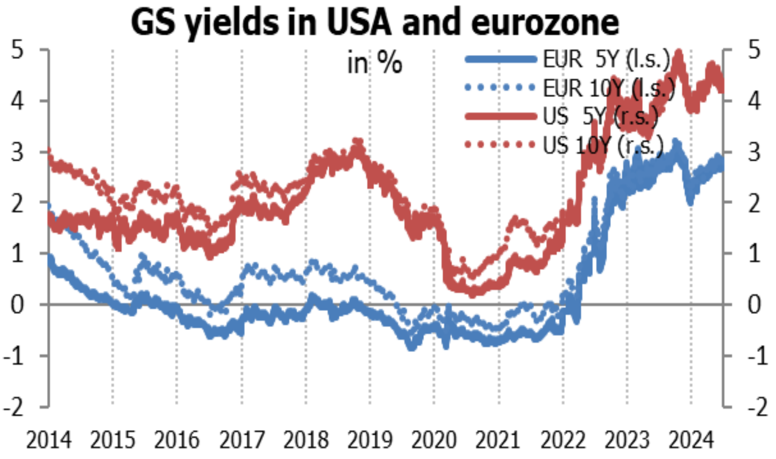


In the second quarter of 2024, no securities were traded on the secondary market, as opposed to the previous quarter, when amount of Denar 62 million was traded in this segment, i.e. government bonds with residual maturity of ten to fifteen years (with average yield of 5.9%). Such changes indicate moderate decrease in the liquidity ratio[59], when there is no trade of securities on the secondary market during the second quarter.



In the second quarter of 2024, on the US financial market, the yields on the 10-year treasury bills increased and equaled 4.4%, on average (4.1% in the previous quarter). The euro area also registered developments, where the yields from the 10-year treasury bills also increased and equaled 2.8%, average (2.6% in the preceding quarter).

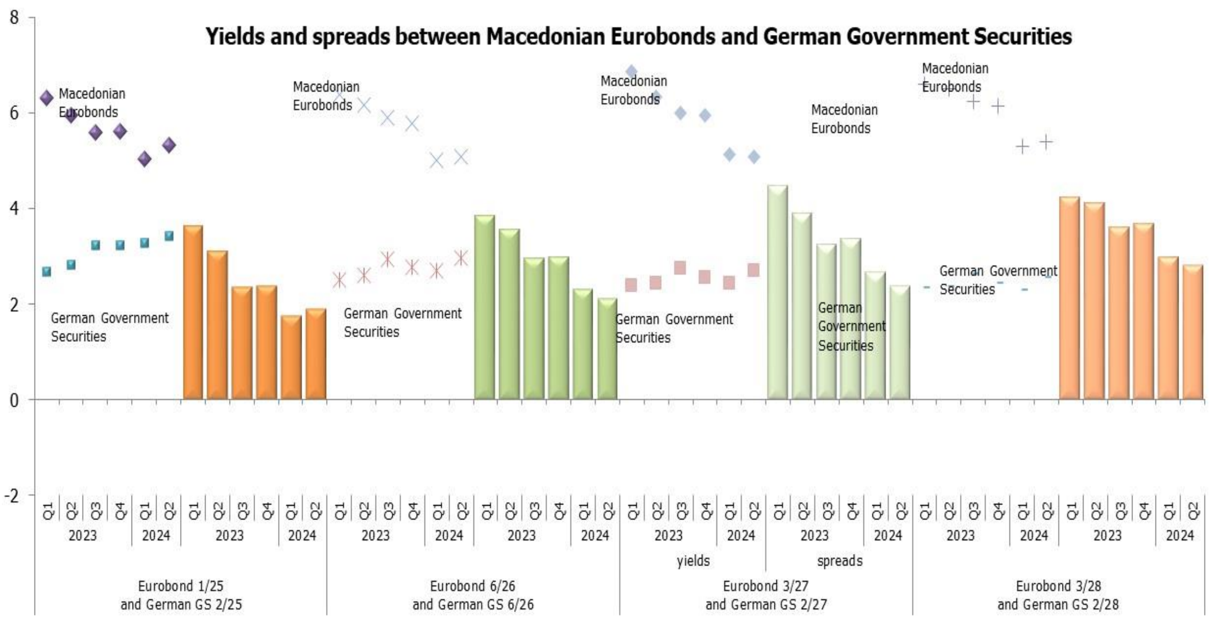
[59]The liquidity ratio on the secondary market is the correlation between the average daily turnover and the stock of government securities.



Source: Bloomberg.

In the second quarter of 2024, the yields of the Macedonian Eurobonds[60] registered slight upward movement, compared to the more pronounced increase in the yields in relevant German government bonds. This resulted in minor narrowing in most of the spreads between Macedonian and German bonds, which on average, equaled 2.1 percentage points, 2.4 percentage points and 2.8 percentage points, respectively. The only exception is the spread of the Macedonian Eurobond issued in January 2018, where there is a slight upward movement of the spread to 1.9 percentage point.

(1.8 percentage points in the last quarter). (1.8 percentage points in the preceding quarter).

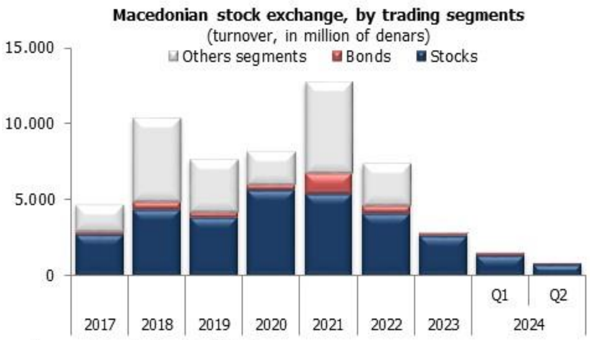


Source: Bloomberg.

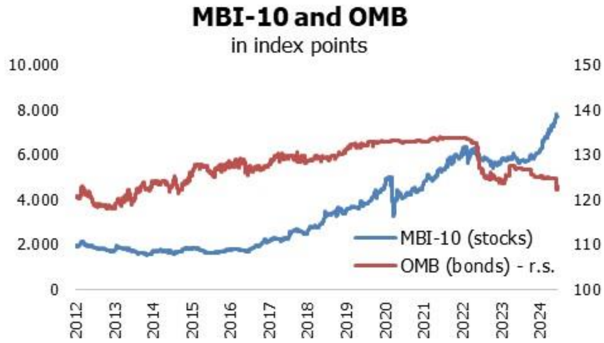
[60] These include the Macedonian Eurobonds issued in January 2018, in June 2020, March 2021 and March 2023. Eurobonds are issued in the nominal amount of Euro 500 million, Euro 700 million, Euro 700 million, and Euro 500 million, respectively, with a maturity of 7, 6, 7 and 4 years, respectively, and annual interest rates of 2.75%, 3.675%, 1.625% and 6.96%, respectively.

3.3. Stock markets

At the end of the second quarter of 2024, the value of Macedonian stock exchange index MBI-10 increased by 9% (increase of 15.5% of previous quarter) and equaled 7,705 index points. The total stock exchange turnover registered a quarterly reduction of 21.7% (after the increase of 89% in the previous quarter), due to the decreased turnover in shares and bonds. The value of the bond index (OMB) during the quarter registered slight downward change by 2 index points, compared to the previous quarter and equaled 123 index points.

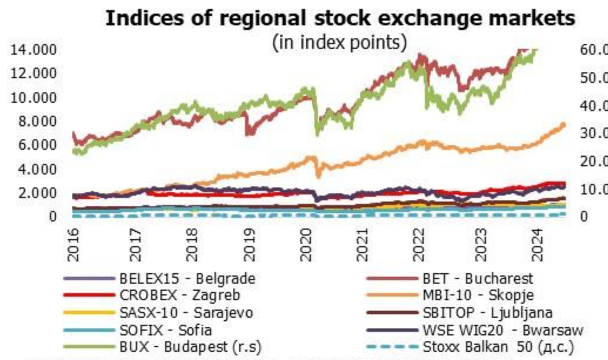


Source: Macedonian Stock Exchange

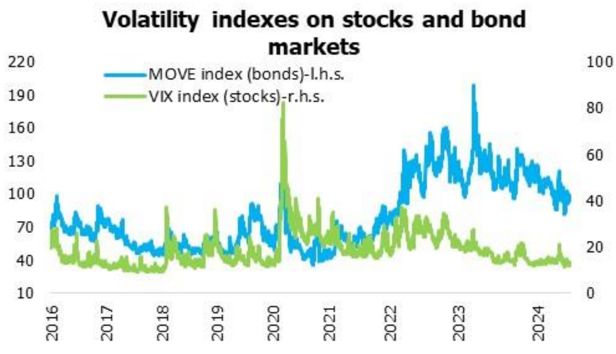


Source: Macedonian Stock Exchange

In the second quarter of 2024, stock exchange indices of the region registered a moderate quarterly growth, which averaged 6.6% (increase of 8.9% in the previous quarter). Moreover, all regional indices increased, except Croatian and Serbian, which registered minor decrease. Furthermore, during the second quarter of 2024, volatility indices on the bond and stock markets, i.e. MOVE and VIX[61] indices recorded a daily divergent movements, i.e. the MOVE index decreased by 7% on average (after the decrease of 12% in the previous quarter), while VIX increased by 3% on average (after the decrease of 11% in the previous quarter). The movements of both indices, observed jointly, indicate a further moderate reduction in the uncertainty and volatility at the global capital markets.



Source: Macedonian stock exchange, national stock exchange markets.



Source: Chicago Board Options Exchange (CBOE)

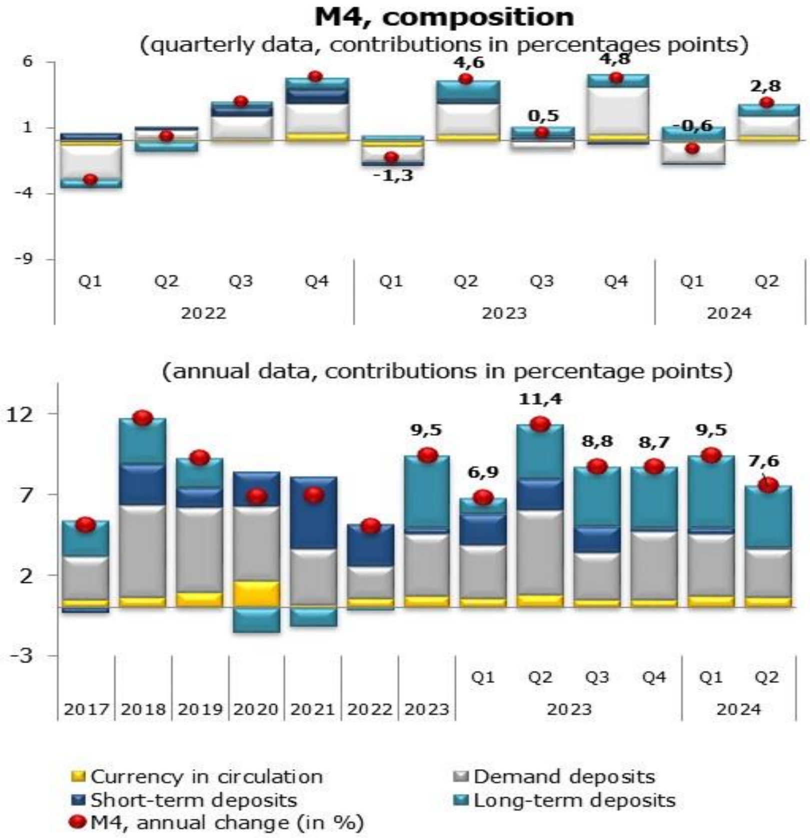
[61] The MOVE Index (Merrill Lynch Option Volatility Estimate) shows the implicit volatility in the US government securities markets. The VIX Index (Volatility Index) is constructed based on the implied volatility of S&P500 index options. Investors use both indices as indicators of the conditions and expectations for the financial markets volatility. Downward path in indices indicates a decrease in volatility.

IV. Monetary and credit aggregates

After the usual seasonal decline in the first quarter of 2024, the second quarter registered a quarterly growth of brad money M4 as a result of almost all subcategories. The growth was contributed the most by the most liquid components (demand deposits and currency in circulation). The favorable trends in saving continue this quarter, considering the growth of long-term and denar deposits, and in accordance with the measures taken so far by the National Bank, which are aimed at supporting denarization and saving in the longer term. In the second quarter, an increase in the credits of both sectors was registered, slightly larger with enterprises than households. The results of the Bank Lending Survey (BLS) for the second quarter point to net tightening of the overall credit conditions and net increase in the credit demand in both sectors.

4.1. Monetary aggregates

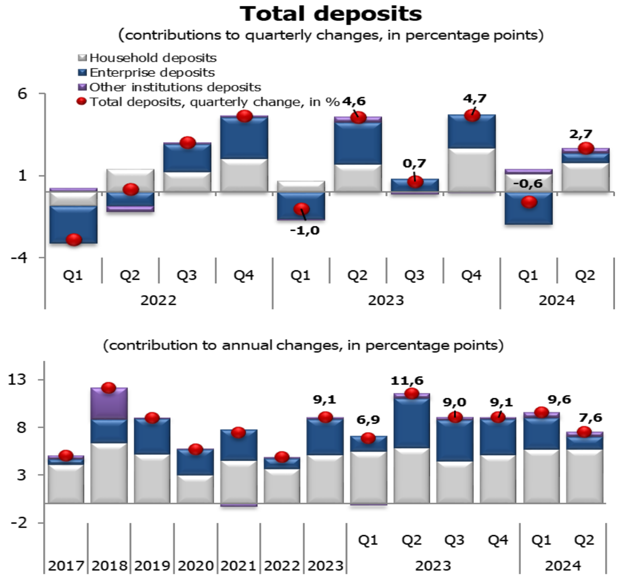
During the second quarter of 2024, broad money M4 registered a quarterly growth of 2.8% (a decrease of 0.6% in the first quarter). Structurally speaking, the increase results from the growth of almost all components of the money supply. The largest growth is observed in demand deposits, as the most liquid component of the money supply (with a contribution of 1.5 percentage points), followed by the growth of cash in circulation (contribution of 0.3 percentage points). Long-term deposits also recorded an increase (with a contribution of 0.9 percentage points), while short-term deposits stagnated. By **currency structure**, most of the growth (2.2 percentage points arise from the denar deposits (with demand deposits), given slight positive contribution also of foreign currency deposits (of 0.2 percentage points). Moreover, the share of foreign deposits in M4 was 38.3% at the end of the second quarter, which is by 0.8 percentage points less compared to the end of the first quarter. Annually, the monetary aggregate M4 registered more moderate growth of 7.6% (9.5% at the end of the first quarter).



Source: NBRNM.

Total financial system deposits[62] in the second quarter of 2024 increased by 2.7% on a quarterly basis (after the quarterly fall of 0.6% in the previous quarter). **Regarding sectors**, deposit growth was observed in all sectors, with the most significant one being registered in household deposits (with a contribution of 1.8 percentage point), followed by the growth of corporate deposits and deposits of other sectors (with a contribution of 0.6 percentage points and 0.3 percentage points, respectively). By **currency**, the denar deposits (including demand deposits) registered more pronounced growth, relative to the one in the foreign currency deposits (contribution of 2.4 and 0.3 percentage points, respectively). In terms of **maturity**, long-term deposits are growing (1.0 percentage point), while short-term deposits are stagnating, which indicates the retention of favorable trends in savings. **On an annual basis**, the growth of total deposits at the end of the second quarter slowed down moderately and amounted to 7.6% (9.6% at the end of the first quarter), with a high comparative basis from the end of the second quarter of last year.

[62] Data refer to non-government deposits in banks and savings houses, funds of other financial institutions on the accounts with the National Bank and funds of local government authorities on the accounts with the National Bank. The data are consistent with the methodological changes of the National Bank from June 2018. For more information on the methodological changes visit: http://www.nbrm.mk/monetarna_statistika_i_statistika_na_kamatni_stapki.nspx.



Source: NBRNM.

Total deposits

	2022				2023				2024	
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2
quarterly change, in %										
Total deposits	-2,9	0,2	3,0	4,7	-1,0	4,6	0,7	4,7	-0,6	2,7
contributions to quarterly growth, p.p.										
Deposit money	-2,8	0,7	1,9	2,5	-1,3	2,5	-0,5	3,9	-1,7	1,7
Denar deposits	-1,0	-0,9	0,3	0,7	0,3	1,0	0,4	0,4	0,9	0,7
FX deposits	0,9	0,3	0,9	1,5	0,0	1,0	0,8	0,4	0,2	0,3
Short-term deposits	0,6	0,3	0,7	1,2	-0,2	0,4	0,4	-0,3	-0,1	0,0
Long-term deposits	-0,7	-0,9	0,4	1,0	0,5	1,7	0,8	1,1	1,2	1,0
Households	-0,9	1,4	1,2	2,0	0,7	1,7	0,0	2,7	1,1	1,8
Enterprises	-2,2	-0,9	1,7	2,5	-1,7	2,5	0,8	2,0	-2,0	0,6
Other institutions deposits	0,2	-0,3	0,1	0,1	-0,1	0,4	-0,1	0,0	0,3	0,3

Source: NBRNM.

The growth in **household deposits** accelerated in the second quarter of the year (quarterly rate of 2.7% compared to the moderate growth of 1.7% in the first quarter). Analyzing **by currency,** the increase mostly results from the growth of denar deposits (including demand deposits), amid further increase in foreign currency deposits (contributing by 2.0 percentage points and 0.8 percentage points, respectively). By **maturity structure**, the increase was driven by the long-term deposits (contributing by 1.3 percentage points), given minor contribution of short-term deposits (of 0.2 percentage points). **Annually**, the increase in total household deposits equaled 8.9% in the second quarter of 2024 (8.7% at the end of the first quarter).

Corporate deposits registered a significant increase of 2.1% in the second quarter of 2024 (as opposed to the fall of 6.7% in the first quarter). As for the **currency structure,** the increase is fully due to the denar deposits (including demand deposits), given a decrease in the foreign currency deposits. From a **maturity** point of view, long-term deposits grew, while short-term deposits declined. **Annually**, corporate deposits increased by 4.7% at the end of second quarter of 2024 (increase of 12.2% at the end of the first quarter), in conditions of higher basis registered in the same period of the previous year.[63]

[63]The high basis of the corporate deposits in the second quarter of 2023 was partly due to government transfers to ESM for energy needs.

Household deposits										
	2022				2023				2024	
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2
quarterly change, in %										
Total household deposits	-1,4	2,1	1,9	3,1	1,0	2,6	0,0	4,2	1,7	2,7
contribution to quarterly change of total deposits. in p.p.										
Deposit money	-1,8	1,1	0,7	2,5	-0,2	1,2	-1,1	3,1	0,0	1,3
Denar deposits	-1,4	-0,8	0,0	0,7	0,5	0,9	0,5	0,7	1,2	0,7
FX deposits	1,8	1,8	1,2	-0,1	0,8	0,4	0,6	0,4	0,5	0,8
Short-term deposits	0,9	1,3	0,7	-0,6	0,1	-0,5	-0,2	-0,9	0,2	0,2
Long-term deposits	-0,4	-0,3	0,5	1,2	1,1	1,8	1,3	2,0	1,5	1,3

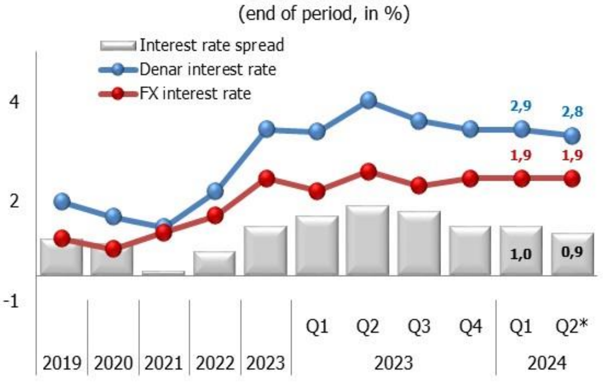
Source: NBRNM.

Enterprise deposits										
	2022				2023				2024	
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2
quarterly change, in %										
Total household deposits	-7,8	-3,2	6,3	9,3	-5,8	9,4	2,8	6,9	-6,7	2,1
contribution to quarterly change of total deposits. in p.p.										
Deposit money	-6,0	-0,4	4,7	3,2	-4,5	5,5	0,2	6,0	-6,0	2,1
Denar deposits	-0,4	-0,2	1,1	0,5	0,6	1,4	0,8	0,4	0,3	0,3
FX deposits	-1,4	-2,6	0,4	5,7	-1,9	2,5	1,8	0,5	-0,9	-0,3
Short-term deposits	-0,6	-0,8	0,9	5,4	-1,1	2,2	2,2	1,2	-1,8	-1,1
Long-term deposits	-1,1	-2,0	0,7	0,7	-0,2	1,7	0,4	-0,3	1,1	1,1

Source: NBRNM.

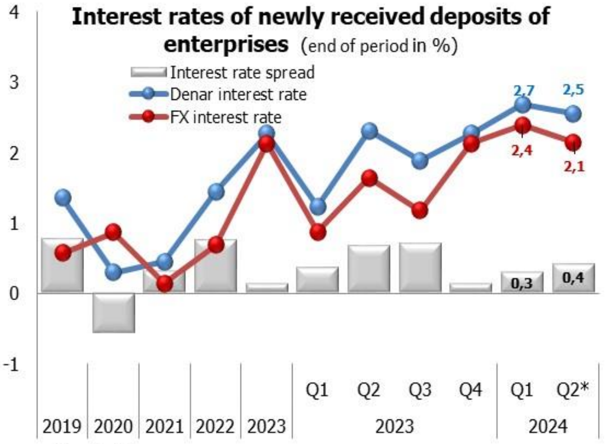
The analysis of the returns[64] on the new savings shows that in May, the interest rates on the newly accepted[65] denar and foreign currency deposits of **the households** were 2.8% and 1.9%, respectively (2.9% and 1.9%, respectively in March). In such circumstances, the interest rate spread between the new denar and foreign currency savings of households in May equaled 0.9 percentage points (1.0 percentage points in the first quarter). As for the **corporate sector**, interest rates on newly accepted denar and foreign currency deposits in May equaled 2.5% and 2.1%, respectively (2.7% and 2.4%, respectively in March). With such shifts, the interest rate spread between the newly accepted denar and foreign currency corporate deposits at the end of May equaled 0.4 percentage points (0.3 percentage points in the first quarter). From the aspect of the total received deposits (denar and foreign currency), the interest rates on the corporate deposits at the end of May amounted to 2.2%, i.e. they grew compared to March by 0.1 percentage point, while for households they are unchanged and amount to 1.8%.

Interest rates of newly received deposits of households
(end of period, in %)



*end of May
Source: NBRNM.

Interest rates of newly received deposits of enterprises (end of period in %)



*end of May
Source: NBRNM.

[64] Data on interest rates are in accordance with the methodological changes of the National Bank from June 2018. For more information on the methodological changes visit:
http://www.nbrm.mk/monetary statistics of the interest rates.nspx.
[65] Note that the interest rates on newly accepted deposits typically vary. Volatility of interest rate on newly accepted deposits results from the fact that they result from the volume of newly accepted deposits (which varies from month to month) and their interest rate.

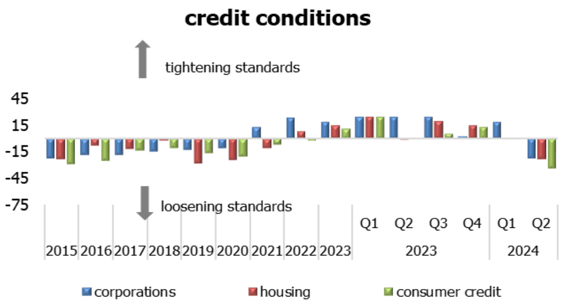
4.2. Lending activity

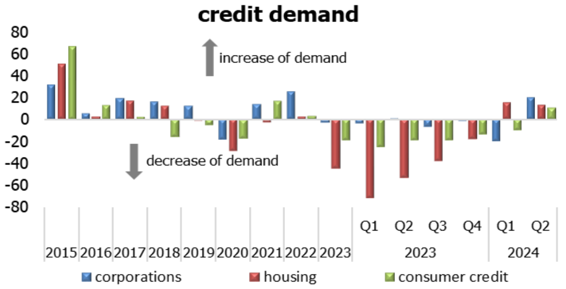
Banks' lending activity in the second quarter of the year grew by 2.9% compared to the first quarter. **Lending Survey** conducted in the second quarter of 2024, shows net relaxation of the **lending terms** in both sectors (enterprises and households), as opposed to net tightening of the conditions in the Survey made in the first quarter. Regarding the **demand for loans**, it registered net increase in the second quarter, in both sectors, as well, as opposed to the net decrease in the previous survey. For the third quarter of 2024, the banks expect net easing of the lending terms and net increase in the demand, in both sectors.

Total credits of private sector

	2022				2023				2024	
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2
quarterly change, in %										
Total credits of private sector	2,6	2,7	1,1	2,6	0,0	2,6	0,5	1,9	1,0	2,9
Contribution in quarterly change of total credits (in p.p.)										
Denar credits	1,3	1,1	-0,2	1,2	-0,3	1,3	0,7	1,7	1,1	3,0
Foreign currency credits	1,3	1,6	1,4	1,4	0,4	1,3	-0,3	0,2	-0,1	-0,1
Short-term credits	1,4	0,5	-0,1	0,5	-0,4	0,1	-0,5	0,1	0,5	0,0
Long-term credits	1,3	2,0	1,2	2,5	0,6	2,5	1,0	1,8	0,2	2,8
Households	0,8	1,3	0,8	0,7	0,6	1,1	0,7	0,9	0,7	1,3
Corporations	1,8	1,3	0,3	1,9	-0,6	1,5	-0,3	1,0	0,3	1,7

Source: NBRNM.



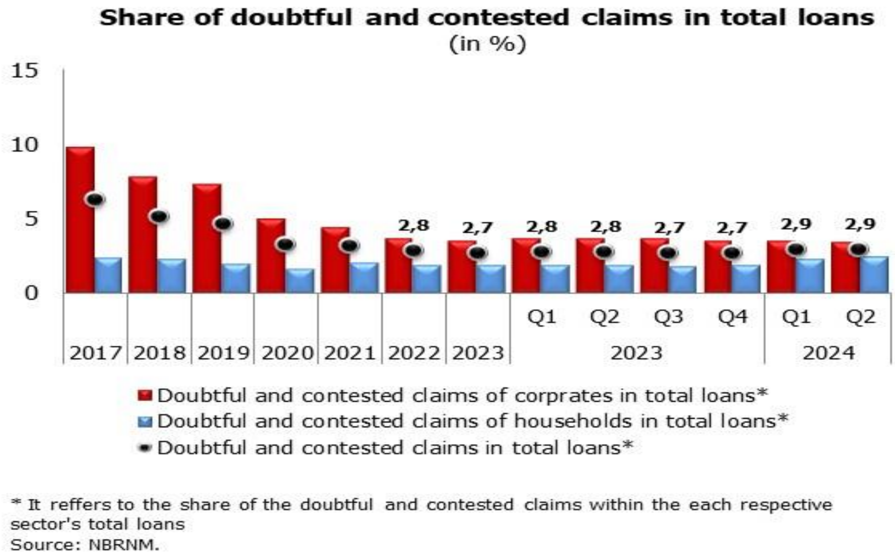


Source: Bank lending Survey, NBRNM.

The sector structure analysis of the total private sector loans shows a quarterly increase in loans with both enterprises and households (with a contribution of 1.7 percentage points and 1.3 percentage points, respectively). By **currency**, the increase stems from the denar loans (with a contribution of 3.0 percentage points), amid negative contribution of the foreign currency loans[66]. The analysis from the aspect of the **maturity structure** shows that increase was registered in the long-term loans (with a contribution of 2.8 percentage points), given stagnation of the short-term loans in this quarter. The share of **doubtful and contested claims** in total loans remained at the level of 2.9%.[67]

[66] Foreign currency loan data also include denar loans with currency clause.

[67] Since the beginning of 2024, new Decision on the methodology for credit risk management has been enforced, published in the Official Gazette of the Republic of North Macedonia No. 57/23, which enables further harmonization with the regulatory requirements effective in the European Union and improves the stability of the banking system. The Decision prescribes a new method of determining the non-performing credit exposures, strengthens the criteria for monitoring and control of the quality of the banks' credit portfolio and improved the rules for credit exposure restructuring. The new methodological changes in determining of the non-performing loans may lead to their growth, at least in the initial period after the implementation of the Decision, which is more an effect of the different approach in determining the non-performing status (counting the days of delay), than of the changed creditworthiness of the clients.



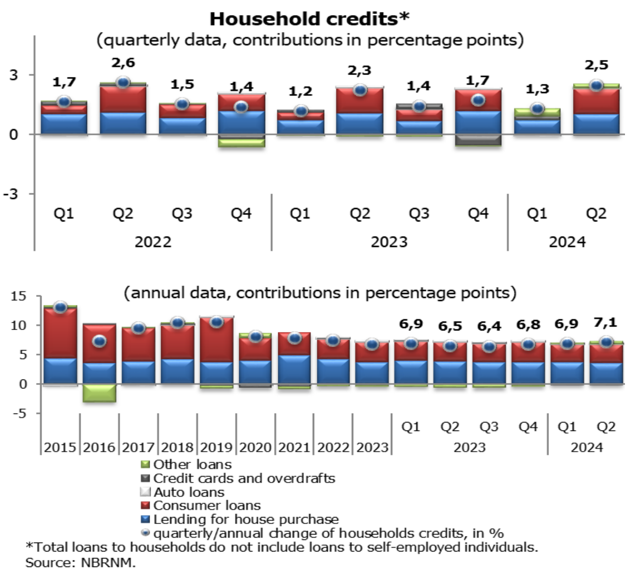
Annually, total loans at the end of the second quarter of 2024 grew by 6.4% (6.1% at the end of the first quarter). In conditions of more intensive loan growth compared to deposits, loan-to-deposit ratio increased and in the second quarter equaled 83.1% (82.9% at the end of the first quarter).

In the second quarter of 2024, **the lending to the households sector** registered a quarterly growth of 2.5% (an increase of 1.3% in the previous quarter). This growth mostly results from the growth of consumer loans, the growth of residential loans and the more moderate growth of other loans, with car loans, credit cards and overdraft remaining unchanged. The results of the **Bank Lending Survey** for the second quarter of this year, regarding the household sector, indicate a net increase in the demand for total loans, amid net relaxation of the overall credit standards. **By currency**, larger contribution was made by denar loans compared to the more moderate increase in foreign currency loans. Analyzing the **maturity structure**, the growth arises fully from the increase in the long-term loans, amid unchanged short-term loans. **Annually,** at the end of the second quarter of 2024, total household loans increased by 7.1% (increase of 6.8% in the first quarter).

Total credits of households

	2022				2023				2024	
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2
quarterly change, in %										
Total credits of households	1,6	2,6	1,5	1,4	1,2	2,2	1,5	1,7	1,3	2,5
Contribution in quarterly change of household credits (in p.p.)										
Denar credits	1,0	1,3	0,5	0,1	0,3	0,8	0,9	0,6	0,7	1,6
Foreign currency credits	0,6	1,3	1,0	1,3	0,8	1,4	0,5	1,1	0,6	0,9
Short-term credits	0,2	0,1	0,0	-0,2	0,2	0,0	0,3	-0,3	0,2	0,0
Long-term credits	1,3	2,4	1,5	1,9	1,0	2,2	1,2	2,0	0,7	2,2

Source: NBRNM.



In the second quarter of 2024, the amount of **total loans extended to the corporate sector** increased by 3.5%. According to the results of the **Lending Survey** for the second quarter of 2024, the banks indicate net increase in the total corporate loan demand, amid net relaxation of credit standards. By currency, lending in domestic currency is increasing, as opposed to foreign currency loans, which are decreasing. According to the maturity structure, the growth is driven by the long-term loans, while short-term loans registered a decrease. **On annual basis,** the total corporate loans registered an increase of 5.8% at the end of the second quarter (5.4% at the end and of the previous quarter).

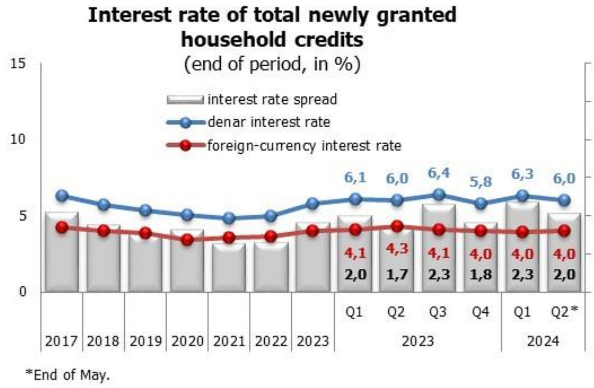
Total credits of corporations

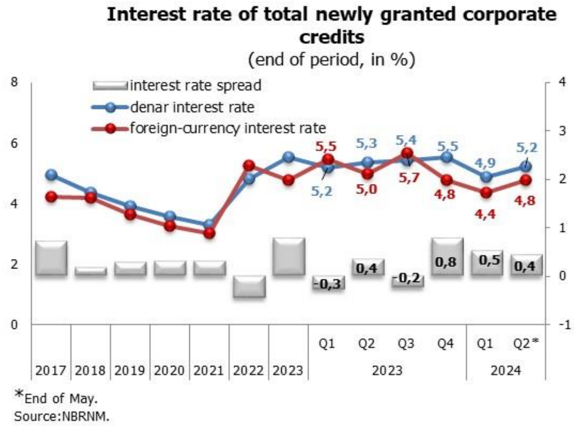
	2022				2023				2024	
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q2
quarterly change, in %										
Total credits of corporations	3,7	2,8	0,7	3,9	-1,3	3,1	-0,6	2,1	0,7	3,5
Contribution in quarterly change of corporation credits (in p.p.)										
Denar credits	1,7	0,9	-1,0	2,4	-1,1	2,0	0,5	2,9	1,5	4,6
Foreign currency credits	2,0	1,8	1,8	1,5	-0,2	1,1	-1,1	-0,7	-0,8	-1,1
Short-term credits	2,7	0,9	-0,3	1,3	-1,4	0,3	-1,3	0,6	0,8	-0,1
Long-term credits	1,3	1,5	1,0	3,1	0,2	2,6	0,7	1,6	-0,3	3,5

Source: NBRNM.

According to the data on the interest rates[68] on newly approved loans[69] in May, the interest rates on denar and foreign currency loans to households equaled 6.0% and 4.0%, respectively (6.3% and 4.0%, respectively in March). In such conditions, the interest rate spread between the new denar and foreign currency lending to households narrowed to 2.0 percentage points. (2.3 percentage points in the first quarter). **Regarding corporations,** the interest rates on newly approved denar and foreign currency loans equaled 5.2% and 4.8%, respectively 4.9% and 4.4%, respectively in March), thus the interest rate spread between the new denar and foreign currency corporate lending reduced and equaled 0.4 percentage points. (0.5 percentage points in the first quarter). Regarding **total loans** granted to the private sector, at the in May the interest rates on household and corporate loans amounted to 5.7% and 5.3%, respectively, which is a minimal increase in households of 0.1 percentage point and unchanged level in enterprises, compared to March 2024.

[68] Data on interest rates are in accordance with the methodological changes of the National Bank from June 2018. For more information on the methodological changes visit: http://www.nbrm.mk/monetarna_statistika_i_statistika_na_kamatni_stapki.nspx.
[69]Note that the interest rates on newly approved loans are volatile. Volatility of interest rate on newly approved loans depends on the volume of newly approved loans (which can change from month to month) and their interest rate.



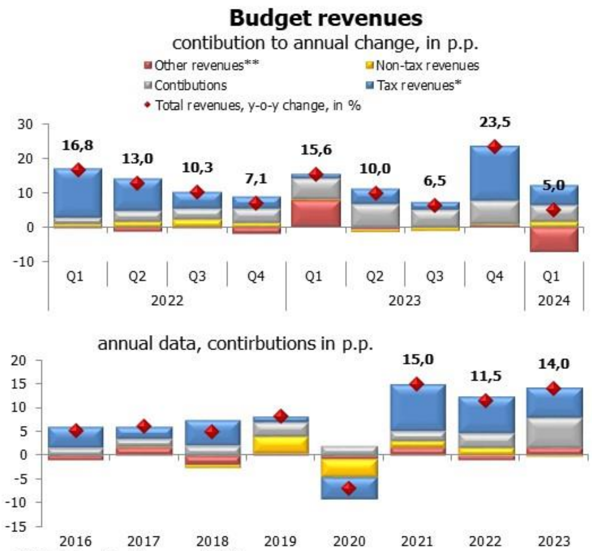


V. Public finance

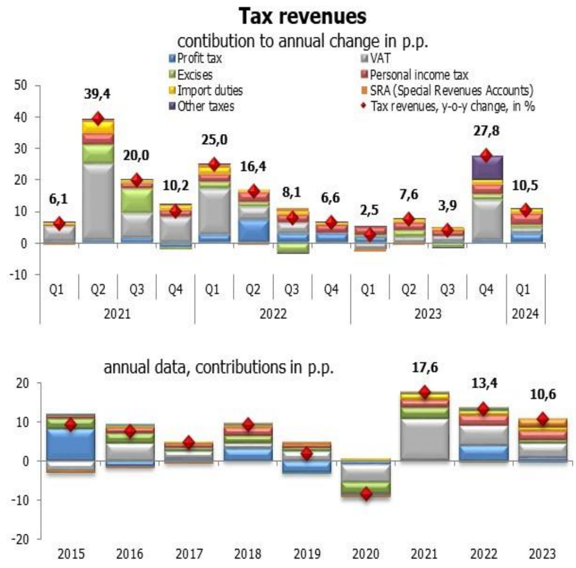
In the first quarter of 2024, there was a slowdown in the growth of budget revenues to 5.0% on an annual basis and an accelerated annual growth of budget expenditures of 20.9%, which contributed to the budget deficit widening on an annual basis, up to 1.6% of GDP (0.4% of GDP in the same quarter of the previous year). In the period January-May 2024, the budget deficit was 2.3% of GDP, which is around 61.3% of that planned for 2024, entirely financed by government borrowing on the domestic and foreign market, amid accumulated government deposits with the National Bank. At the end of the first quarter of 2024, the total public debt equaled 60.2% of GDP.

In the first quarter of 2024, **total revenues** in the Budget of the Republic of North Macedonia[70] registered decelerated growth, which equaled 5.0%, on an annual basis (23.5% in the fourth quarter of 2023). All categories of budget revenues contribute to this dynamic of slow growth (except non-tax revenues, the growth of which slightly accelerated), and mostly the decrease in foreign donations, within the rest of revenues, because of their higher base than in the same period last year.[71] Within other categories, the slower growth in taxes has a more significant share, with a contribution of 5.7 percentage points to the growth (against the positive contribution of 15.9 percentage points in the previous quarter), as well as in contribution income (with a contribution of 4.8 percentage points against the contribution of 6.6 percentage points in the previous quarter).

[70] Central budget and budgets of funds.
[71] In March 2023, the foreign donations increased owing to the EU grant, which amounted to Euro 72 million intended for coping with energy crisis.

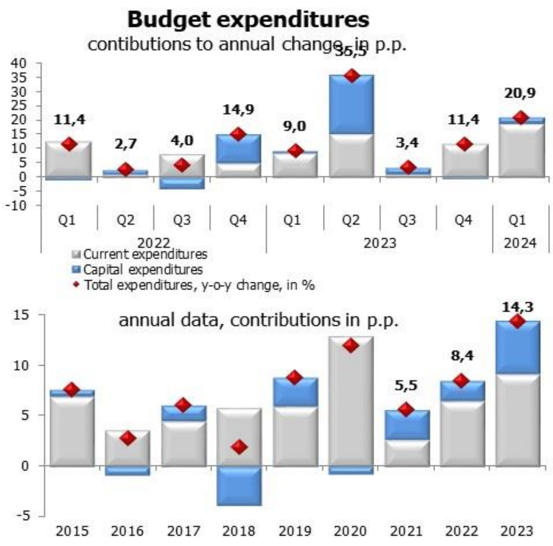


* It includes Tax Revenues (SRA).
**Other revenues includes capital revenues, foreign donations and revenues from due loans.
Sources: Ministry of finance and NBRNM`s calcualtions.

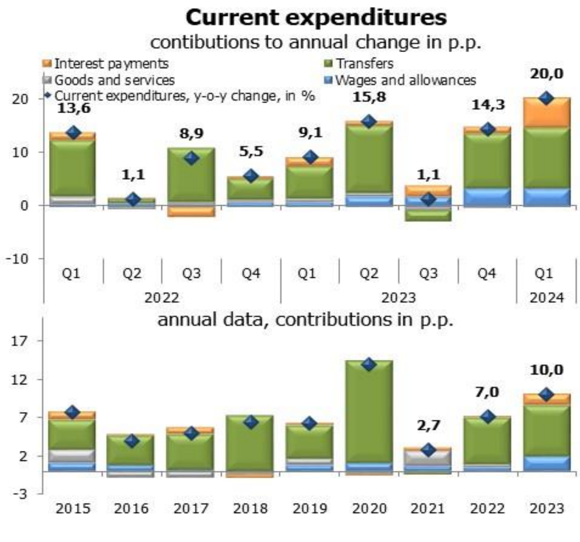


Source: Ministry of finance and NBRNM`s calculations

Annual growth in total **tax revenues** slowed significantly to 10.5% in the first quarter of 2024. Such performance results from the growth slowdown of the revenues from indirect taxes, mostly from the VAT revenues (with a contribution of 1.7 percentage points), as well as from excise taxes and import duties (contributions of 1.3 percentage points and 1.2 percentage points, respectively). As a contrast, a slight growth acceleration was registered in direct taxes, both in personal income tax and profit tax (with contributions of 3.4 percentage points and 2.9 percentage points, respectively).



Source: Ministry of finance.

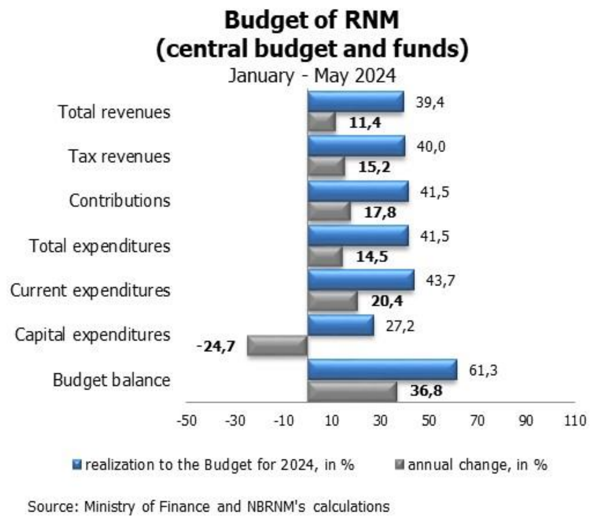


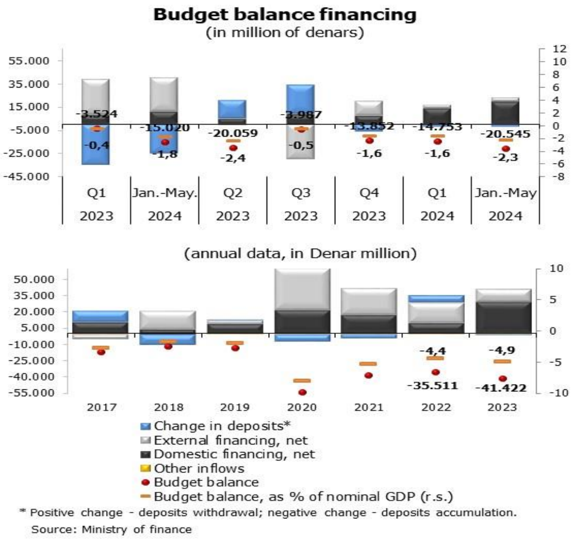
Source: Ministry of finance and NBRNM`s calcualtions.

The total budget expenditures in the first quarter of 2024 registered intensified growth dynamics on an annual basis, with a rate of 20.9%. By structure, the increase in the total expenditures arise from the current expenses, amid slight increase in capital costs. The annual increase in the current expenditures mostly stems from the “transfers” category[72] (a

[72] Transfers category include pension expenses, social security costs, health care costs and other transfers (mainly subsidies). The transfer intensification in the first quarter of 2024 is due to the pension increase in March, according to the regular 5.3% adjustment

contribution of 11.1 percentage points), with more moderate contribution accounting for the increase in "interest payments", "wages and compensations" and "goods and services" categories (of 5.6 percentage points, 3.2 percentage points and 0.1 percentage point, respectively).





In the first quarter of 2024, the Budget deficit was Denar 14,753 million or 1.6% of GDP, which is better realization compared to the same period last year (deficit of 0.4% of GDP). The realized deficit in the first quarter was primarily financed through net government borrowings from abroad[73], and on domestic market, amid accumulation of government deposits with the National Bank.

BUDGET OF REPUBLIC OF NORTH MACEDONIA (Central budget and budgets of funds)

	2023					2024			2023							
	Budget 2023	First Reallocation Budget 2023	Second Reallocation Budget 2023	Q4	Total 2023	Budget 2024		Jan.-Feb. 2024	Q1		Q2		Q3		Q4	
									Annual changes, in %	Contributions in annual changes, in p.p.	Annual changes, in %	Contributions in annual changes, in p.p.	Annual changes, in %	Contributions in annual changes, in p.p.	Annual changes, in %	Contributions in annual changes, in p.p.
TOTAL REVENUES	**282.052**	**282.052**	**282.052**	**79.669**	**277.144**	**310.097**		**44.641**	**15,6**	**15,6**	**10,0**	**10,0**	**6,5**	**6,5**	**23,5**	**23,5**
Tax revenues and contributions	250.689	253.205	253.205	72.987	250.355	279.044		40.601	8,3	7,6	12,5	11,3	8,3	7,4	24,9	22,5
Taxes*	162.600	162.235	162.235	47.082	157.733	178.067		25.058	2,5	1,5	7,6	4,5	3,9	2,3	27,8	15,9
Contributions	88.089	90.970	90.970	25.905	92.622	100.977		15.543	20,0	6,0	21,3	6,9	16,3	5,1	19,8	6,6
Non-tax revenues	19.894	17.962	17.962	4.736	16.882	20.394		3.560	6,1	0,4	-6,9	-0,5	-8,9	-0,7	4,1	0,3
Capital revenues	2.800	2.800	2.800	672	2.071	3.210		170	-31,3	-0,2	-64,5	-0,6	5,7	0,1	30,7	0,2
Foreign donations	8.669	8.085	8.085	1.274	7.836	7.449		310	533,7	7,8	-18,4	-0,3	-21,4	-0,3	29,7	0,5
TOTAL EXPENDITURES	**324.810**	**324.811**	**324.810**	**93.521**	**318.566**	**343.638**		**55.807**	**9,0**	**9,0**	**35,5**	**35,5**	**3,4**	**3,4**	**11,4**	**11,4**
Current expenditures	276.059	279.888	279.833	77.714	275.042	298.459		50.333	9,1	8,4	15,8	14,8	1,1	1,0	14,3	11,6
Capital expenditures	48.751	44.923	44.977	15.807	43.524	45.179		5.474	8,3	0,6	359,0	20,6	38,4	2,4	-0,7	-0,1
BUDGET DEFICIT/SURPLUS	**-42.759**	**-42.759**	**-42.758**	**-13.852**	**-41.422**	**-33.541**		**-11.166**								
Financing	42.759	41.966	42.758	13.852	41.422	33.541		11.166								
Inflow	**94.876**	**94.058**	**94.973**	**18.256**	**84.942**	**78.595**		**23.138**								
Other inflows	0	0	0	414	1.275	0		188								
Foreign loans	66.876	65.885	65.978	15.753	47.600	43.164		9.839								
Deposits	-5.626	-14.838	-22.119	-6.171	-89	-4.332		-6.261								
Treasury bills	33.616	43.001	51.114	8.260	36.156	39.753		19.372								
Sale of shares	10	10	0	0	0	10		0								
Outflow	**52.117**	**52.092**	**52.215**	**4.404**	**43.520**	**45.054**		**11.972**								
Repayment of principal	52.117	52.092	52.215	4.404	43.520	45.054		11.972								
External debt	36.506	36.428	36.551	3.351	36.046	26.429		1.878								
Domestic debt	15.611	15.664	15.664	1.053	7.474	18.625		10.094								
Other outflows	0	0	0	0	0	0		0								

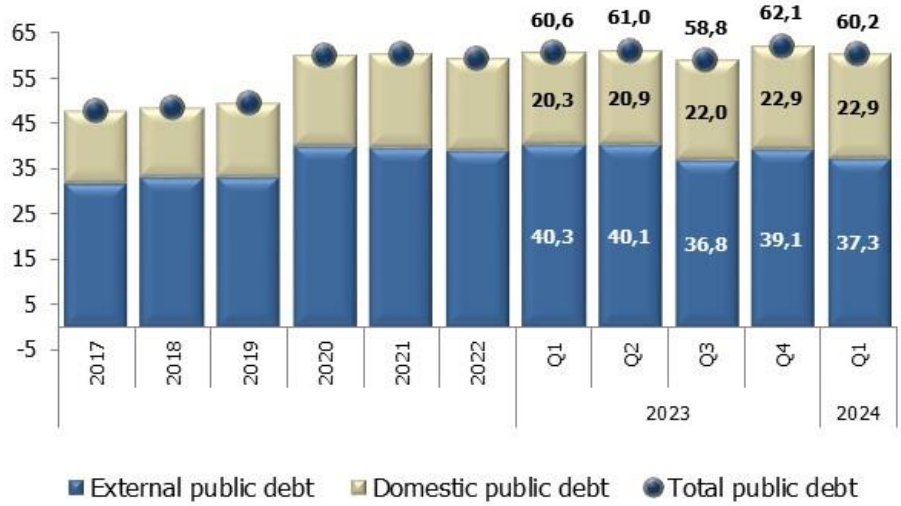
* Includes Special Revenues Accounts (SRA)
Source: Ministry of Finance and NBRNM calculations.

with the new methodology, which follows two indicators, i.e. 50% of the increase in the average wage and 50% of the increase in the consumer prices, according to the official data of the State Statistical Office. In addition, transfers are also growing due to the payment of financial support to socially vulnerable categories of citizens in accordance with the ninth set of anti-crisis measures, provided for by the Law on Financial Support of Socially Vulnerable Categories of Citizens for Dealing with the Energy and Price Crisis, which are also in force in 2024.

[73] In January 2024, the second tranche of Euro155 million was withdrawn as part of the PLL program (Precautionary and Liquidity Line) of the International Monetary Fund.

In the period January-May 2024, total budget revenues grew by 11.4% on an annual basis. This mostly results from the better performance of tax revenues, and additional but more moderate contribution is made by contribution revenues and non-tax revenues, while revenues from foreign donations and capital revenues show a decline. At the same time, budget expenditures went up by 14.5% on an annual basis, which is mainly contributed by higher current expenditures (primarily due to higher transfers), while capital expenditures recorded a decline[74]. In the period January - May 2024, the budget deficit equaled Denar 20,545 million, or 2.3% of GDP[75], representing 61.3% of the planned 2024 deficit. The deficit was largely financed through net borrowing on the domestic market and less on foreign market, amid accumulation of government deposits with the National Bank.

Public debt in % of GDP



Source: MoF and NBRNM calculations.

At the end of the first quarter of 2024, total public debt[76] equaled 60.2% of GDP, which is a reduction of 1.8 percentage points of GDP compared to the end of the previous quarter. This is largely due to the reduction of the external debt, while the internal debt remains unchanged. Analyzed by debt structure, the total government debt decreased by 1.3 percentage points and equaled 51.8%, while the debt of public enterprises (guaranteed and unguaranteed)[77] decreased by 0.5 percentage points of the GDP and reduced to 8.4% of the GDP. Compared to the same period of 2023, at the end of the first quarter of 2024 the total public debt decreased by 0.4 percentage points of GDP.

[74] Capital expenditures are lower due to the comparison base effect of April 2023 when a higher amount was paid for financing the road infrastructure project for the Corridors 8 and 10d.
[75] The analysis uses the National Bank's April forecasts for the nominal GDP for 2024.
[76] The public debt is defined under the Law on Public Debt (Official Gazette of the RM No. 62/05, 88/08, 35/11, 139/14 and 98/19) as the sum of government debt and debt of public enterprises established by the state or municipalities, municipalities within the City of Skopje and the City of Skopje, and companies that are entirely or predominantly owned by the state or by the municipalities, the municipalities within the City of Skopje and the City of Skopje.
[77] According to the amendments to the Law on Public Debt from May 2019, the non-guaranteed debt of public companies and joint stock companies established by the government or municipalities, municipalities within the City of Skopje and the City of Skopje is included in public debt (Official Gazette of the RM No. 62/05, 88/08, 35/11, 139/14 and 98/19).

VI. Analytical appendices

Annex 1: Inflation and inflation perceptions and expectations - analysis of different consumers' opinion about the inflation in North Macedonia

Inflation expectations play a key role in the transmission mechanism of monetary policy, and therefore they represent an important part of the information set for central bank analyses. Information on inflation expectations can be quantitative and qualitative and there are several ways to be measured: they can be derived from financial market instruments, as well as through surveys of professional forecasters and surveys of businesses and households/consumers. In conditions of rapid inflation growth, the inflation expectations become even more important. Namely, when economic agents believe that inflation will rise, they may spend more and save less to optimize their consumption and investment in the longer term, as well as increase their wage demands. In addition, inflation expectations also play an important role in the process of determining the wages and prices by companies and in that respect are an important determinant of future inflation. Hence, it is of particular importance for monetary policy holders to have more information on how inflation expectations are formed and what is their relationship with realized inflation. On the other hand, it is also important to take into account the inflation perceptions i.e. the past movements in the inflation, as they may also affect consumer behavior and the formation of their inflation expectations.

Previous research [78] and experience confirm the important role of inflation expectations for the setting and implementation of monetary policy, with special attention being paid to consumer expectations. They point to several general conclusions about consumer perceptions and expectations: (1) the average perceptions/expectations about the inflation, presented in quantitative indicators, are mainly higher than the realized inflation, but their movements are in the same direction; and (2) social demographic characteristics affect the creation of the inflation expectations – for example, younger consumers, women, individuals with lower level of formal education, as well as those belonging to lower income groups, usually register higher inflation perceptions and expectations[79].

The purpose of this box is to verify such conclusions drawn from the previous literature in the case of North Macedonia. Data from the Consumer Survey of the European Commission, from May 2012 to December 2022, were used for the analysis. These are qualitative answers to the following two questions related to perceptions and expectations about inflation, respectively:

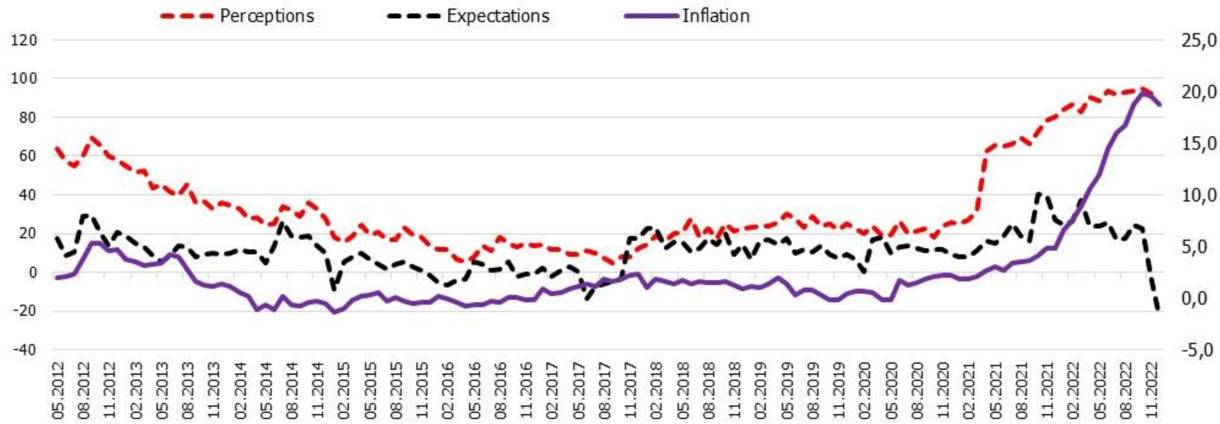
Question 5: How do you think consumer prices have changed over the last 12 months? They:
 	
a) significantly increased (++);
b) moderately increased (+);
c) slightly increased (=);
d) remained almost unchanged (-);
e) reduced (--);
f) don't know (DK)
	Question 6: Compared to the past 12 months, how do you expect consumer prices to move in the next 12 months? They are going to:
	
	a) increase faster (++);
	b) increase at the same rate (+);
	c) increase at slower rate (=);
	d) remain the same (-);
	e) decrease (--);
	f) don't know (DK).

[78] ECB Economic Bulletin, Issue 2/2021; Arioli et al. (ECB, 2017); Di Nino et al. (ECB blog, 2022); Pizzinelli (IMF F&D September, 2022); Weber et al. (2022); Andre et al. (2022) и други.
[79] More information at ECB Economic Bulletin, Issue 2/2021 and stated references.

The advantage of the qualitative surveys data is that they can help to obtain very quick and timely information. Thus, in the absence of quantitative response, they provide solid initial information to form an opinion about the inflation movements. However, when using qualitative information from surveys, one should take into account the shortcomings that they have, as opposed to working with quantitative data, so the results should not be taken for granted.

Having in mind the qualitative nature of the responses given in the Survey, they provide information only on the direction of the price changes in the last as well as the future 12 months. In that regard, as can be seen in Chart 1, the results show that the **consumer perceptions and expectations mainly move in the same direction with the realized inflation, which is similar as in the euro area.** However, by period, the movements diverged slightly, which was evident at the beginning of 2016 and in 2017, as well as at the beginning of the pandemic and at the end of 2021 and 2022, as well as in highly uncertain periods, preceded by stable prices.[80]. Therefore, it can be stated that in conditions of low and stable inflation, the consumer perceptions and inflation expectations with the realized inflation are aligned more than in situations of increase in the inflation rates that emerges after period of low inflation and higher uncertainty. Similar conclusions can be drawn from the researches in the euro area[81] in accordance with the period the analysis referred to, where the biggest divergence emerged with the introduction of euro, as well as at the beginning of the pandemic, i.e. highly uncertain periods. *Additionally, what is notable in our case is that although there was a high rise in inflation in 2022, due to the post-pandemic disruption of global supply chains, the energy crisis, as well as the effects of the war in Ukraine, the inflation expectations of households remained stable, and as of the end of the year they even entered the negative zone, which corresponds to expectations of a decrease in inflation in the coming period.* This indicates that the measures taken by the National Bank, as well as the strengthened communication with the public, supplemented by short-term economic measures, contributed to a relatively quick stabilization of inflationary expectations[82].

Chart 1 Qualitative consumer responses to inflation perceptions and expectations and the rate of realized inflation
(left axis: response balances; right axis: annual inflation rate in %)



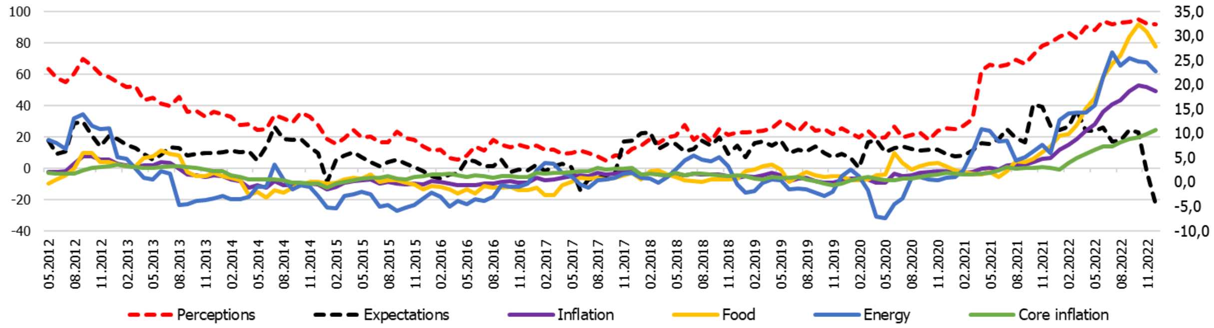
Source: European Commission, SSO and NBRNM calculations.
Note: The latest observations pertain to December 2022. Qualitative responses to the questions for the inflation perceptions and expectations are presented as balances of responses to the questions five and six, which are part of the Consumer Confidence Survey, conducted by the European Commision. With both, perceptions and expectations, the balances of the responses

[80] More information on the consumer price movements for the respective years at Annual Reports of the National Bank.
[81] More information at ECB Economic Bulletin, Issue 2/2021 .
[82] More information on the measures taken at Годишен извештај на Народната банка за 2022 година.

are calculated as a+(b/2)-(d/2)-e, where a-e are percentages of consumers who responded with a, b, c and e.

Chart 2 below shows perceptions and expectations of inflation and actual inflation and its main components: food, energy and core inflation. Similar to chart 1, also this chart presents that, in addition to inflation, the expectations and the perceptions move in the same direction with the main components, especially the energy and food components. Additionally, table 1 shows the correlation calculation, from which it can be seen that there is a higher correlation between the perceptions of inflation and the realized inflation, in total and by main components. Given that we are talking about simultaneous correlations (or how similarly the variables move in the same time period), such results are expected, because consumers have a relatively clearer idea of the current developments with the prices, and hence their perceptions are close to the performance. Regarding inflation expectations, correlations are higher with realized inflation after 12 months, suggesting that consumer inflation expectations contain useful information about future inflation and can serve as its leading indicator. Analyzing by the main inflation components, the contemporaneous correlations of both expectations and perceptions are higher with the energy and food components of the inflation, and lower with core inflation. Similar results were obtained also in the euro area survey, which show a weaker correlation of consumer expectations with the core inflation. This points to a greater mutual influence of energy and food prices on future price expectations, given that consumers consider these goods necessary, use them daily and monitor their prices closely, which directly affects their daily consumption decisions.

Chart 2 Qualitative consumer responses to inflation perceptions and expectations and realized inflation and its main components
(left axis: response balances; right axis: Annual inflation rates and its main components in %)



Source: European Commission, SSO and NBRNM calculations.
Note: The latest observations pertain to December 2022

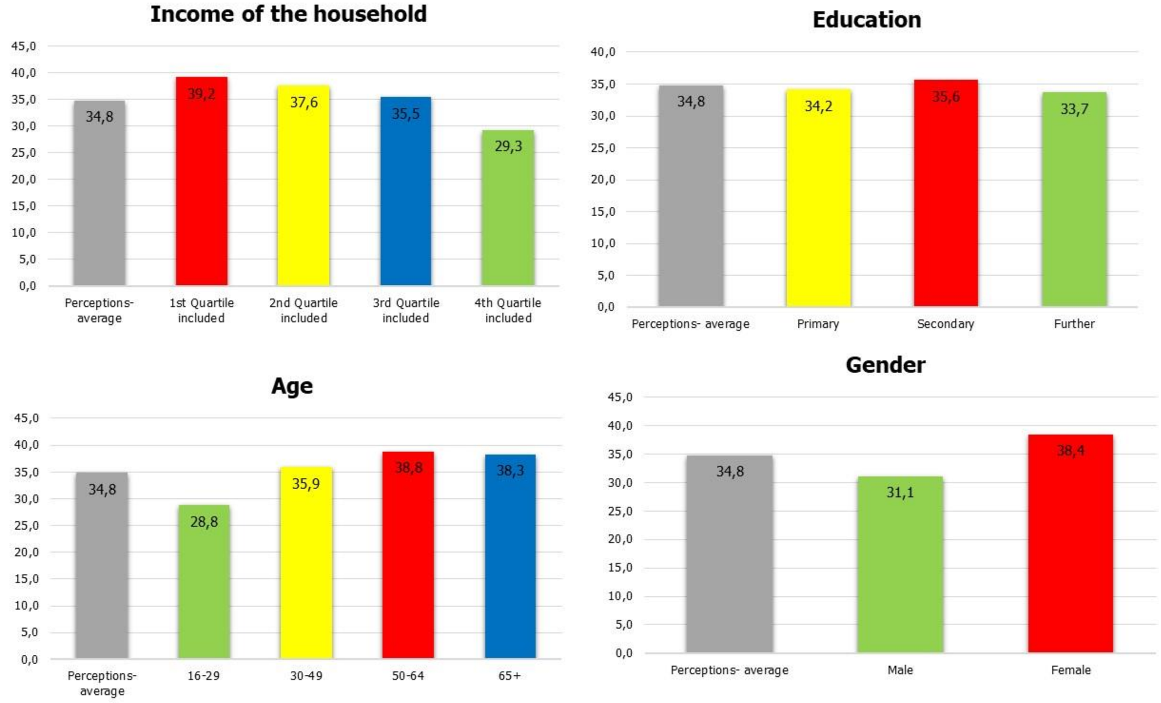
Table 1: Correlations between qualitative consumer responses to inflation perceptions and expectations and realized inflation and its main components

	Perceptions	Expectations	
	Contemporaneous correlations	Contemporaneous correlations	Correlation with inflation 12 months ahead
Inflation	0,819	0,272	0,508
Food	0,776	0,248	0,573
Energy	0,843	0,398	0,307
Core inflation	0,741	0,153	0,443

Source: European Commission, SSO and NBRNM calculations.

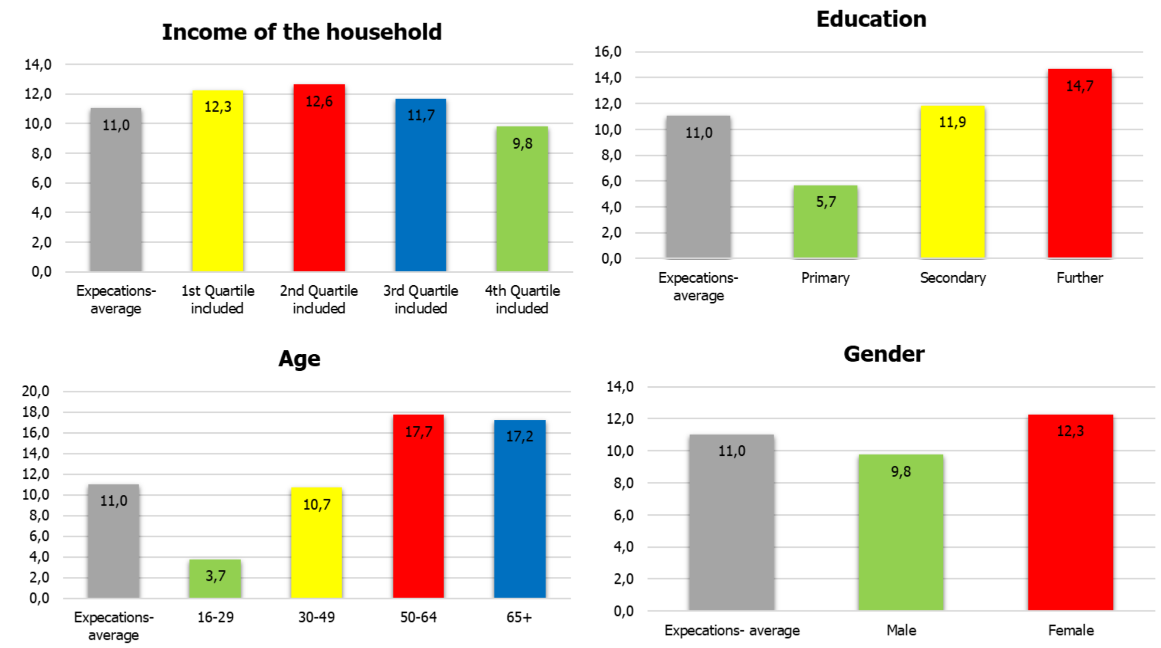
The second part of the analysis refers to an examination of how the **sociodemographic characteristics of households** affect the formation of perceptions and expectations about inflation. In this case, too, the qualitative responses from the European Commission's Consumer Survey were used, analyzed according to several characteristics: household income, education, age and gender.

Chart 3 Consumers' perceptions of inflation according to their sociodemographic characteristics (Balance of responses)



Source: European Commission and NBRNM calculations.
Note: The analysis refers to the period May 20012 to December 2022.

Chart 4 Consumers' inflation expectations according to their sociodemographic characteristics (Balance of responses)



Source: European Commission and NBRNM calculations.
Note: The analysis refers to the period May 20012 to December 2022.

As can be seen from the charts, in the case of North Macedonia, the different sociodemographic characteristics contribute to respondents having different perceptions and expectations about inflation. Some of the findings presented so far in the literature have been proven in the case of North Macedonia. In doing so, although it is important to take into account the sociodemographic characteristics of the respondents, the literature states that it is difficult to explain reliably such results. Thus, in **terms of income**, households with a lower level of income have higher perceptions and expectations of inflation. One of the reasons is the ability to cover the costs of living (those who pay off their expenses more easily and quickly have usually a higher income and lower perceptions and expectations of inflation).[83] This is also verified by the findings that the households with lower level of income are exposed to more flexible and more variable prices compared to the households with higher level of income[84]. **Regarding the gender**, women generally have higher perceptions and expectations of inflation, compared to men. This, in part, can be explained by the level of financial literacy of the respondents. Namely, people who have a lower level of financial literacy, on average, have higher perceptions and expectations about inflation, while the findings so far point to somewhat lower financial literacy among women.[85] In addition, according to some researches, the different roles in the households that women and men have, the different involvement in shopping, and thus also in observing prices, are also a factor. Namely, research indicates that men pay more attention to the prices of transport, clothing and housing when forming their perceptions and expectations about inflation.[86] However, it is emphasized that such differences are very small when both men and women are equally involved in household chores. On the other hand, **in terms of age**, in contrast to the findings in the literature, our younger population has lower perceptions and expectations about inflation, compared to the older population. **In terms of education,** people with the highest education have the lowest perceptions of inflation, which is similar to previous research, but at the same time, they also have the highest expectations for inflation, which is not the case with the results of previous findings.

In summary, in the absence of quantitative data, the analysis made with the qualitative data represents a solid basis for further research, and it could be useful for policy makers in the direction of obtaining more detailed information about the inflationary perceptions and expectations of households and their links with the realized inflation. In that respect, they are important for central banks because they affect the consumer behavior, wage dynamics, transmission to inflation, as well as the effectiveness of policies and communication strategies. Inflationary perceptions also affect the formation of inflationary expectations themselves, and thus the effectiveness of monetary policy and the ability to attain its goals. By monitoring and influencing expectations, central banks can better achieve their primary goal of price stability, thereby maintaining overall macroeconomic stability. This can be proven by the successful stabilization of expectations in 2022 by the National Bank. In addition, the sociodemographic characteristics of households influence the formation of their perceptions and expectations about inflation, so in that direction the communication of central banks with the public regarding the measures taken to maintain a stable price level, which should to consider these factors as well. The findings in our case largely confirm the general findings of previous research in global frameworks.

[83]More information at EU consumers' quantitative inflation perceptions and expectations: an evaluation, April 2017 and stated references.
[84]Working materials: Income-specific inflation rates and the effects of monetary policy: The case of North Macedonia, 2021.
[85] More information at OECD (2020), OECD/INFE 2020 International Survey of Adult Financial Literacy
[86] More information at Gender roles produce divergent economic expectations, May 2021 и What drives inflation expectations of women and men?, September 2022 and stated references.

Annex 2: Price and financial stability – two sides of the same coin

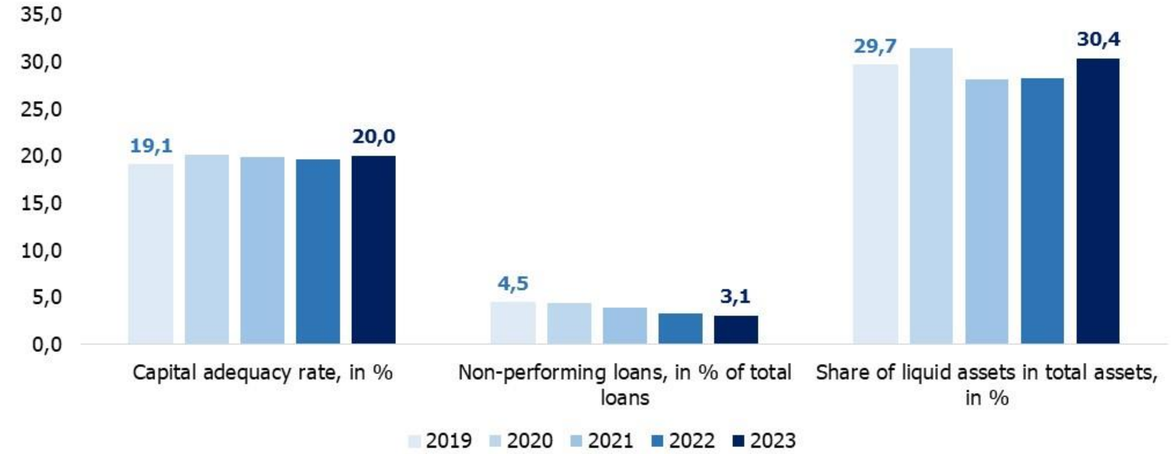
Monetary policy and the policies to maintain financial stability are substantively linked, given that changes in interest rates can have an impact on financial markets, and developments in financial markets can in turn affect the monetary policy effectiveness. In fact, it is generally accepted now that financial stability is a prerequisite for price stability, and the reverse is also true. If we look historically, within the last decade and a half, when inflation was low, central banks were able to implement accommodative policies and support economic growth, while contributing to the maintenance of financial stability. Seen from today's perspective, it is clear that there is a trade-off between managing inflation and financial stability, because, as recent experience has shown, raising interest rates to deal with inflation can potentially increase risks in the financial system. **Therefore, monetary policy and financial stability have now begun to be perceived as two complementary policies, i.e. two sides of the same coin.** The International Monetary Fund (IMF, 2013) describes this post crisis paradigm as one in which both monetary policy and macroprudential policy are used for counter cyclical management: monetary policy primarily aimed at price stability, macroprudential policy primarily aimed at financial stability, and microprudential policy a policy focused on the safety and stability of individual financial institutions. This view is supported by a growing number of empirical findings on the effectiveness of macroprudential policy in maintaining financial stability, which is strengthened in cases where it is used as a complement to monetary policy. For example, a recent Bank for International Settlements (BIS) paper analyzing 157 episodes of monetary tightening finds that tightening macroprudential policy, whether before or during a monetary tightening, helps reduce the likelihood of financial shocks, thus increasing the room for maneuver of central banks in the fight against inflation. Practical experience during the pandemic also showed that macroprudential policy measures could complement monetary policy, contributing to the overall resilience of banks' credit activity. **At the same time, their mutual relations are complex, which can create challenges for policy makers in certain context.** For example, monetary tightening to deal with high inflation can lead to increased risks for financial institutions, especially if it is unexpected, rapid, follows a long period of loose monetary policy, and if it interacts with other factors such as weaknesses in risk management, prudential regulation and supervision. The stress in the US with the collapse of the two banks serves as an example of the impact that the rapid and sudden tightening of asset valuations may have, which was the cause of their collapse. **This is closely related to the possible risk that central banks could eventually abandon their efforts to bring inflation under control, raising the issue of "financial dominance", which refers to the possible trade-off between the higher costs of reducing inflation and concerns about financial stability.**

The solution to this significant trade-off is to have a strong, capitalized and resilient banking system, as well as a non-banking financial sector, and effective instruments for maintaining financial stability, both macroprudential and bank resolution tools. The stronger the banks' balance sheets and the better the instruments, the lower the risk of financial dominance and the greater the room for maneuver for the monetary policy to remain focused on price stability.

Regarding the first prerequisite - the condition of the banking system, it is important that the banks in the Central Eastern and Southeastern Europe (CESEE)

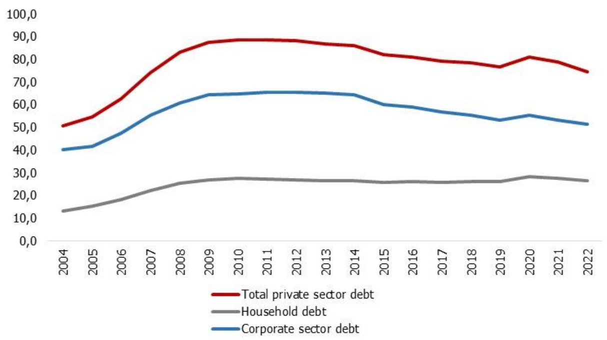
region entered this crisis in a relatively solid state with strong capital and liquidity positions that were generally built before the pandemic and remained at appropriate level. According to data from the end of 2023, the capital adequacy ratio is 20% on average for the region, while the liquidity ratio (liquid assets as opposed to total assets) is around 30%. Loan portfolios are of high quality, that is, low rates of non-performing loans (around 3% on average), which are better compared to pre-pandemic levels. The risks have not materialized, and the profitability remained solid. However, there is no room for complacency, so there is a need of constant vigilance and policy adaptability in order to prevent vulnerabilities that could again test the resilience of the banking system in the future. This particularly applies to the indirect credit risk arising from households and the corporate sector, which persists in the current environment of high interest rates. Since the global financial crisis, important steps have been taken in the region to improve the adequacy of banks' non-performing loans provisions, enable their timely write-offs and sales, and develop NPL markets. This contributed to reducing non-performing loans to historically low levels. However, the challenge is to prevent them from accumulating again, as this would pose a risk to the soundness of banks' balance sheets and their lending capacity.

Chart 1 Indicators for the banking systems in CESEE countries, averages for the region



Source: Central banks' websites and IMF database on the financial stability indicators.

Chart no. 2 Debt of the private sector in CEEC countries
(averages, in % of GDP)



Source: IMF Global Debt Database.

The analyses of the debt burden of the households shows that it is sustainable and below the vulnerability thresholds in all CESEE countries[87]. Household debt increased during the pandemic, but has since returned to previous levels (about 26% of GDP on average in 2022). However, to get a more accurate image of household vulnerability, a more comprehensive approach is needed that analyzes risks from multiple aspects. **One such analysis is the Austrian National**

[87] Vulnerability threshold for household debt is derived from the MIP Scoreboard used by the European Commission to assess potential risks and macroeconomic imbalances in the EU countries. Vulnerability threshold for corporate debt is derived from the MIP Scoreboard used by the European Commission to assess potential risks and macroeconomic imbalances in the EU countries.

Bank's recent survey[88] of nine CESEEE economies,[89]which finds that the risk in the household sector is significant and should be closely monitored. According to the research, the participation of vulnerable households in the region is close to 15%, with the debt exposed to risk constituting slightly more than 20% of the total debt. However, large differences are evident between countries, with the share of debt at risk ranging from 36% and 32% in Bosnia and Herzegovina and Romania to 11% in Hungary. In North Macedonia, the share of debt at risk is estimated to be slightly below 30%. **Higher costs for debiting are source of vulnerability also for the enterprises, especially for heavily indebted companies.** On the positive side, the corporate sector managed to exit from the pandemic in relatively good condition, with the strong post-pandemic recovery helping companies to generate some reserves. Currently, indebtedness is at the pre-pandemic level (around 51%). However, the rise in reference interest rates increased the interest burden on private borrowers who have variable rate loans. As the IMF's analysis shows, in developing countries the debt exposed to risk (the part of the debt with an indicator of coverage of interest expenses with operating profit that is lower than 4) is 70-80% for small and medium-size enterprises and about 50% for large companies. In the domestic economy, the share of corporate debt, whose indicator for the coverage of interest expenses with operating profit is less than 3, is about 42%. In addition, debt is sensitive to shocks that may negatively affect profitability and shocks related to higher financing costs, which may further worsen debt indicators. As the IMF's scenario analysis (presented in the April 2023 Global Financial Stability Report) shows[90], after the shock, debt at risk increases by 6 percentage points and 14 percentage points for small and medium-size enterprises, respectively. Undoubtedly, during the crisis, the corporate sector weakened, and some companies could not cope with the consequences of the triple shock that led to high energy costs, high material and production costs, and increased labor costs, while simultaneously tightening financial conditions. The risk of insolvency was emphasized, which was evident through the increased number of filed requests for opening bankruptcy proceedings. In the EU, after falling in 2020, bankruptcy proceedings recorded a double-digit growth rate between Q3 2022 and Q3 2023, reaching historically high levels since data collection began in 2015. However, in the second half of the year the situation stabilized, with the index of bankruptcy proceedings gradually normalizing towards the pre-pandemic levels. Overall, private debt in CESEE appears to be under control for the time being and according to the latest data, it is on a downward path to the level of around 75% of GDP, while in all countries it is below the vulnerability threshold.[91] However, it is necessary to remain vigilant.

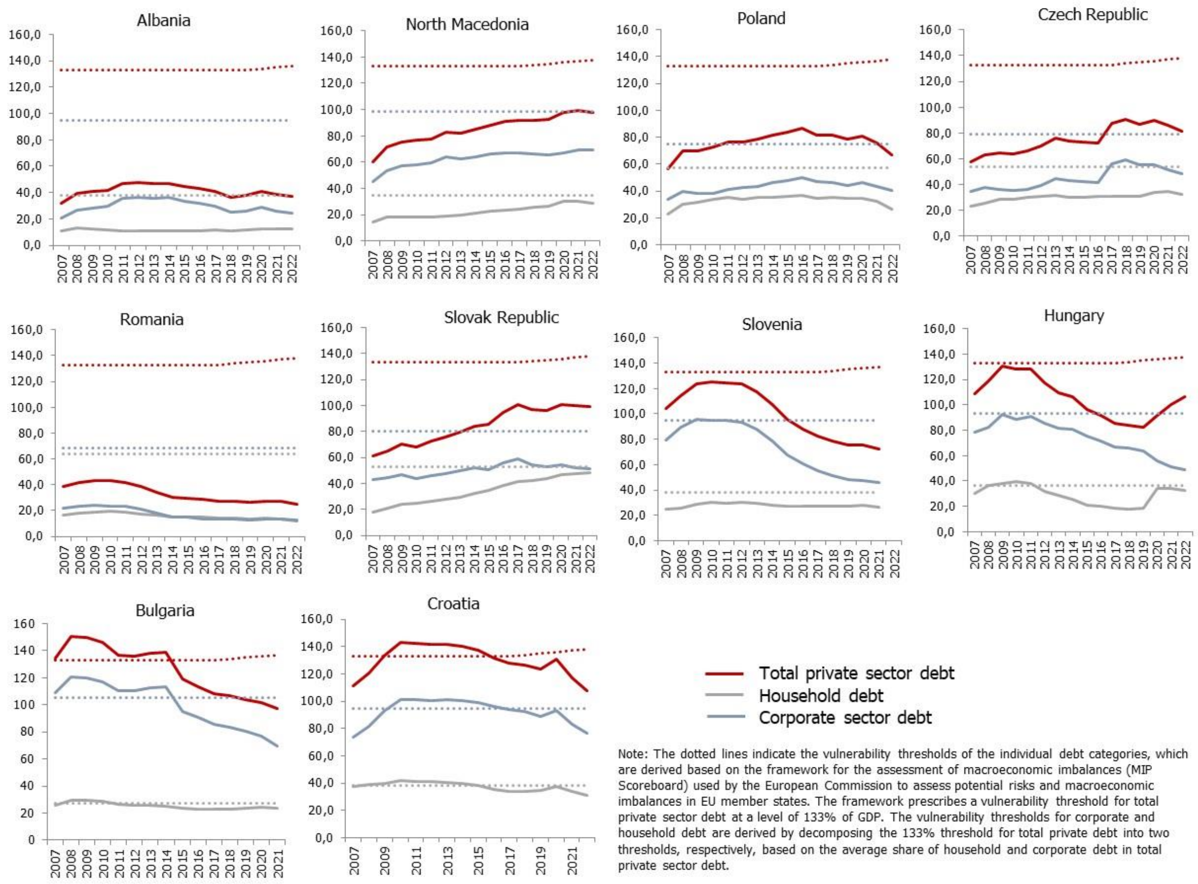
Chart 4 Private sector debt relative to the vulnerability thresholds in the CESEE countries, in % of the GDP

[88] Financial vulnerabilities and debt at risk of CESEE borrowers: a cross-country analysis, Financial Stability Report 44, November 2022. The analysis uses newly available data at micro level about nine CESEE economies on household indeptedness obtained from the OeNB Euro Survey 2020 and 2021.

[89] CESEE-9 countries are Bulgaria, the Czech Republic, Croatia, Poland, Hungary, Romania, Bosnia and Herzegovina, North Macedonia and Serbia.

[90] The analysis is based on corporate data from the second quarter of 2022, when inflation was close to the peak in several countries. Earnings and interest rate shocks are applied that are calibrated to approximate those during previous recessionary episodes, including inflationary recessions and the global financial crisis. In general, for firms, earnings before interest and taxes are assumed to fall by 20 percent, while the effective interest rate (which takes into account the fact that not all debt is floating) rises by 200 basis points, both currently. The magnitude of the interest rate shock is broadly consistent with that used in the corporate stress test of the 2020 United States Financial System Stability Assessment.

[91] Vulnerability threshold for corporate debt is derived from the MIP Scoreboard used by the European Commission to assess potential risks and macroeconomic imbalances in the EU countries.



Source: National Bank calculations based on the IMF global debt data

Regarding the second prerequisite - the availability of effective instruments for maintaining financial stability, it should be noted that in the period after the Global Economic Crisis, the authorities from the entire region strengthened the regulation and supervision of the banking sector, in line with the global regulatory reforms. It has helped banks to face with the recent consecutive crises with reformed and strong capital and liquidity buffers that have been maintained. Both macroprudential frameworks and banks' capital positions were strengthened, which was also enabled through the introduction of measures related to capital buffers, in order to mitigate systemic risks in conditions of enduring uncertainty. To strengthen financial stability, the counter cyclical capital buffer and the systemic risk capital buffer were actively managed. In the last few years, some countries acted through the counter cyclical capital buffer, introducing it for the first time (such as Croatia and North Macedonia), while others (such as Croatia, Slovenia, Serbia and Montenegro) continued with the application of or have introduced the capital buffer for systemic risk. This was further supported by the banks' solid profitability as a "natural" source of maintaining capital positions. Measures aimed at borrowers were also introduced to ensure a high quality of credit demand and to reduce the risks. **In the Macedonian context, even before the last crisis, there was a long history of implementing macroprudential measures to limit vulnerabilities in the banking sector, while the macroprudential instruments were constantly being improved.** Such experience enabled active use of the macroprudential policy even in the current circumstances in order to strengthen further the banks' resilience, in conditions when the economy was transitioning to an environment with higher interest rates. In 2022, a countercyclical capital buffer was introduced for the first time, the rate of which was increased four times, to the level of 1.5%, in order to act preventively and further strengthen the capital strength of domestic banks. In 2023, for the first time, macroprudential measures aimed at the quality of credit demand were introduced, while prescribing the limits for DSTI and LTV indicators. Although banks previously generally applied prudential standards for household loans, the introduction of macroprudential measures is expected to limit further the risks of their excessive borrowing, as well as the risks of the real estate market, thus increasing the banks' resilience. In the next period, policy makers should remain focused on additional strengthening of macroprudential supervision and improvement of macroprudential instruments, which will support the resilience of the financial sector and make more room for maneuvers in the monetary policy in order to achieve the goals of monetary and financial stability.

In short, recent history de facto shows that, even in periods of high inflation, when strong tightening is necessary, financial stability can be ensured and financial dominance avoided if there is an appropriate regulatory and supervisory framework and adequate instruments to maintain financial stability accompanied by appropriate communication by central banks. Moreover, considering that the interest rate of the monetary policy has a wide influence throughout the economy, there is general agreement that the financial stability set is a better tool for dealing with vulnerabilities in the financial system, at least as a first line of defense. Hence, there is a need to close further the regulatory gaps, including fully implementation of the Basel III reforms and strengthening regulatory oversight, including on smaller institutions that are not considered systemic, as it has recently been shown that they too can be a source of systemic risk. The importance of macroprudential instrumentation and supervision is particularly emphasized, given that recent research indicates that a tightening of prudential policy, whether before or during a monetary tightening, helps to reduce the likelihood of financial stress, thus increasing the room for maneuver of central banks in the fight against inflation. The bottom line is that regulators and supervisors are important players that allow monetary policy makers to focus on their core mandate, which is the price stability maintenance.