

National Bank of the Republic of North Macedonia



**Quarterly Report
November 2021**

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Introduction

In the third quarter of 2021, the NBRM maintained the policy rate at a historic low of 1.25% and thus a relaxed monetary policy. Such monetary stance supports credit flows in the economy and increases liquidity in the banking system aimed to mitigate the effects of the protracted pandemic on the domestic economy. The relaxed monetary policy is conducted with foreign reserves at a comfortable level, and within the safe zone. In the third quarter, the National Bank continued purchasing foreign currency on the foreign exchange market, which contributes to further policy space building. Analyzing price movements, despite the acceleration, inflation remains under the influence of supply-side factors and temporary supply-demand mismatches caused by the pandemic. Price pressures are assessed as temporary, and inflation remains within a controlled range and so far does not require a monetary response. In the credit market, the activity of banks remains solid, supported also by the further deposit growth. Despite the relatively favorable developments, the risk balance in this period registered pronounced unfavorable risks associated with the uncertain health conditions, supply chain disruption and volatility in primary commodities markets.

In the period between the two forecasts, the economic parameters are generally as expected. The domestic economic recovery continued at the expected pace, the external position is still favorable, with faster growth of foreign reserves compared to expectations, while inflation under the influence of global and temporary factors was moderately above forecasts. **The assessments of the fundamental factors that define the economic trajectory remain almost unchanged.** Mitigating the epidemiological situation and stabilizing the external environment, restoring optimism and confidence of economic agents, strengthening the investment cycle supported by private and public investments and labor market recovery are all factors that in this forecast vintage are considered key assumptions underlying the baseline macroeconomic scenario. **However, in this forecast vintage, the risks are more pronounced.** Due to unequal access to vaccines, the rapid spread of the delta strain, and the threat of new, more contagious vaccine-resistant virus mutations, the dealing with the health crisis is still uncertain. Also, the supply-demand mismatches and the so-called bottlenecks in the global supply and production chains, as well as the accelerated growth of primary commodity prices are significant risk factors in this forecast vintage.

The main indicators of the external economic environment of the domestic economy somewhat changed between the two forecast rounds. Thus, compared to April, the current perceptions of the **foreign effective demand** show higher growth in 2021 (of 4.1%, compared to the growth estimates of 3.6% in April), and slightly higher growth in 2022. (of 4.3%, compared to expectations for growth of 4.1% in April). Analyzing the **foreign effective inflation**, compared to the April forecasts, an upward revision was made for 2021 (inflation of 2.2%, as opposed to the inflation estimates of 1.4% in April), but also a moderate upward correction for 2022 (expected inflation of 2%, compared to the inflation forecast of 1.6% in April). **The latest forecasts for the changes in the prices of primary commodities on the world stock markets point to higher growth in 2021, as well as small growth in most of them in 2022, contrary to the April expectations for a small decline.** However, the movements of the prices of primary commodities are extremely volatile and under the strong influence of the pandemic developments, which creates greater uncertainty about their future trajectory and effects on the domestic economy, in both short and long term.

The October perceptions for growth of the Macedonian economy are unchanged compared to the April estimates. The easing of the containment measures and the improvement of confidence with the start of mass vaccination have led to a significant recovery in domestic demand. Despite the gradual reduction of government support, solid economic performance is expected driven by private consumption. However, the increased virus spread in mid-August prompted the introduction of certain containment measures. Although the forecast does not envisage an introduction of strict measures, the economic recovery still depends on the pandemic development. **In such circumstances, GDP growth of 3.9% is forecast for 2021, followed by further growth at unchanged pace, i.e. growth of 3.9% is expected in the next 2022 (without changes compared to the April observations).** Observing the structure of activity for 2021, a large positive contribution compared to the April estimates is expected from domestic demand, with a more negative contribution of net exports. Recovery of the foreign demand is expected this year and next, which will have a stimulating effect on the export activity and further offset of losses from 2020. However, given the expected higher import pressures,



reflecting the high import component of exports as well as the faster recovery of domestic demand, net exports will make a negative contribution to growth. The current situation in automotive industry related to the disruptions in the global supply chains is a risk factor for the prospects of this part of the export sector. Within the domestic demand, in this forecast round, household consumption is expected to make the largest positive contribution in 2021, unlike in April when an equal contribution from investment and private consumption was expected. The growth of disposable income, amid rising wages and remittances, improving consumer confidence, maintaining credit support to households, as well as accumulated savings underly the expectations for further solid performance of private consumption. On the other hand, the presence of structural weaknesses in the labor market and the slower recovery of the activity rate are possible downside risks. Investments would have positive, lower though, contribution to growth in 2021, amid expected public sector support, mainly through infrastructure construction, as well as through government credit-guarantee scheme. Public consumption is expected to make a negative contribution to growth, with unchanged intensity, compared to the April perceptions. For 2022, just like in the April cycle, there are expectations for a positive contribution from the domestic demand and a negative, weaker though, contribution from the net export, compared to the estimates for 2021. **In the medium term, further solid growth is expected, i.e. growth rate of 4% in 2023 (as estimated in April), and growth of 4% in 2024.** The downside risks to forecasts remain strong, especially in the short term. Uncertain epidemiological situation, rising energy prices, disruptions in supply chains, possible faster tightening of global financial conditions are the main unfavorable risks to the forecasts. Positive medium-term risks still include the favorable effects of the NATO membership and the progress in the EU accession process, as well as the latest development and investment plans of the country¹ which are not directly embedded in the current medium-term scenario and which if implemented, would be a stimulus for economic growth in the medium term.

Regarding the future price trajectory in the domestic economy, the latest forecasts point to inflation of 3.1% in 2021, compared to the April estimates for inflation rate of about 2.2%. Most of the current upward pressures are due to factors on the supply side, related to the prices of primary commodities on the world stock markets, with the transmission effect of last year's regulatory increase in prices, as well as certain pandemic-specific factors amid relaxation of containment measures. These factors are expected to normalize next year. **Consequently, for 2022, the inflation rate is expected to slow down to 2.4% (expected inflation of 2% in the April scenario).** In general, the estimates are that the current increase in inflation will be temporary, in line with the expectations for stabilization of movements in the second half of 2022. At the same time, no significant transmission effects from the current price growth are expected, given the estimates for moderate demand recovery. **For the period 2023 - 2024, the inflation is expected to average about 2%. Given the protraction of the pandemic,** the international markets still report great volatility in the prices of primary commodities, and thus uncertainty about the movement of import prices, both in short and long term.

Credit activity of the banking system is still considered a great supporter of economic growth. The latest credit market assessments in the forecast horizon indicate faster than expected credit activity in 2021 and solid growth rates for the next three years. Given the increased credit support in the first three quarters of 2021 and the expectations for its continuation by the end of the year, for 2021, the credit growth would be 7.1% (5.8% in the April forecast). Solid credit growth pace would continue in the period 2022 - 2023, and would average about 7% (similar to the April forecast) and would gradually accelerate to 7.8% in 2024. The estimates for acceleration of the credit growth over the forecast horizon rely on the assumptions for stable expectations, deposit growth and favorable capital and liquidity position of the banks. Regarding the sources of financing, having in mind the solid growth of the total deposits in the first three quarters of 2021, it is expected that the growth for the whole 2021 will be 7.1%, slightly more moderate compared to the expected growth of 7.5% with the April forecast. In the next two years, amid assessment for faster economic growth and maintenance of high propensity to save in banks, the annual deposit growth is expected to average 7.5% (7.7% in the April forecast), while in 2024, the deposit growth would amount to 8%.

The assessments for the external position of the economy, according to the performance so far, and within this cycle of forecasts are favorable. The medium-term forecast of the balance of payments continues to indicate a moderate current account deficit, supported by financial flows,

¹ According to the Plan for Accelerated Economic Growth 2022 - 2026.



with the foreign reserves still on the upside. However, within these forecasts, a slightly larger current account deficit is expected, especially during 2021 and 2022, due to higher import pressures from demand than expected and a larger effect on the balance of payments from rising energy prices. Advances in vaccination and the increasing availability of vaccines worldwide have helped the demand to recover, which is not followed by the supply of certain products and raw materials, causing imbalances followed by rapid growth in energy prices and other primary commodities on the world stock markets. Within the latest forecasts, **the current account deficit of the balance of payments is expected to moderately increase in 2021 to 3.8% of GDP (2.9% in the April forecasts).** Such expectations are mainly a reflection of the higher trade deficit, and less of primary income. Regarding the foreign trade, growth is expected in the export component, supported by the foreign demand and the favorable conjuncture on the world metals markets. However, imports are growing rapidly, in part due to price factors, which will be further pronounced by the end of the year. Such changes also mean expectations for widening of the trade deficit. On the other hand, better performances are forecast in current transfers, a category that recovered faster than expected from the negative shock in the previous year and is expected to exceed the pre-pandemic level by the end of the year. In the balance of services, the forecasts are more favorable, due to the good export performance in this category, especially noticeable in other services (mainly ICT services). **According to the expectations for stabilization of the movements in the global economy in the second half of 2022, the current account deficit would remain at 3.8% of GDP in 2022 (compared to the expected 2.3% in April),** amid forecast stabilization of the negative balance in trade in goods and services, a slightly lower primary income deficit, as well as relatively stable net inflows from current transfers. **Analyzing the financial account, in the period 2021-2024, current transactions are forecast to be largely financed through external government borrowings and foreign direct investment.** Foreign reserves adequacy ratios show that they remained in the safe zone over the forecast horizon.

In general, the latest estimates for the next four years (2021-2024) confirm the expectations for recovery of the domestic economy from the pandemic which would reach the pre-crisis level in 2022 and are basically unchanged compared to the April forecasts. The current scenario indicates a moderate acceleration of inflation in 2021, which will be temporary and influenced by supply-side factors, after which it is expected to gradually decrease to 2% in the medium term. The external position remains stable, with the baseline scenario assuming the maintenance of favorable financial conditions globally and unimpeded access to capital markets. Consequently, foreign reserves will remain in the safe zone throughout the forecast horizon. **The estimates are surrounded by high uncertainty, with mostly downward risks and associated primarily to the future unfolding of pandemic.** *The main downward risk is the supply and distribution of vaccines and the vaccination pace,* which could additionally slow down the process of mass vaccination, as well as the uncertainty in terms of the effectiveness of the vaccines to the new more contagious variants. This could lead to reintroduction of stricter containment measures, and lower consumer and investor confidence, which would adversely affect domestic demand and growth on a global scale. *An additional risk is the current protracted mismatch of supply and demand,* which could lead to more pronounced and long-term disruptions in supply and production chains, price pressures and need to normalize monetary policy faster than expected, and therewith, to early tightening of financial conditions. On the other hand, *positive risk* is the potential improvement of the international cooperation in the field of vaccination, which would speed up pandemic management and increase confidence of economic agents and thus private sector consumption and investment. *The National Bank continues to carefully monitor the developments and risks in the domestic and external environment, in order to adequately adjust the monetary policy setup.*

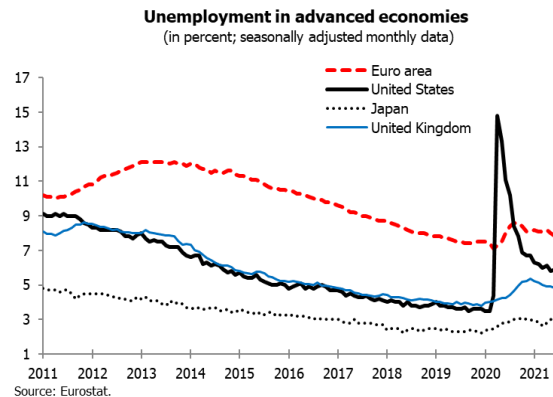
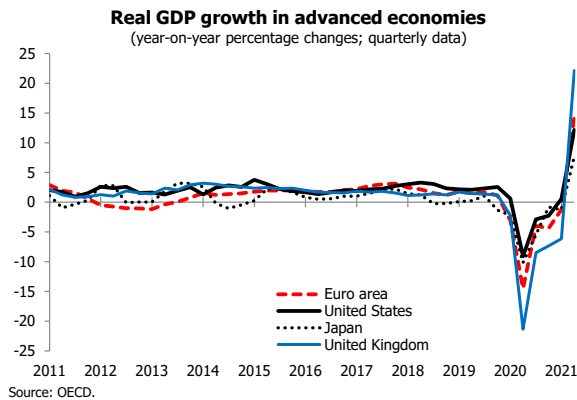


I. Macroeconomic developments

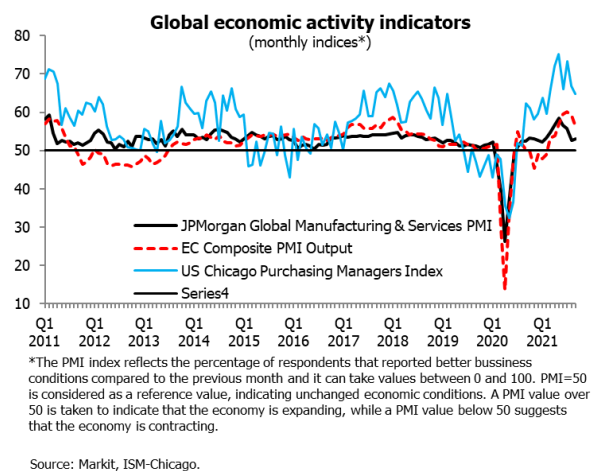
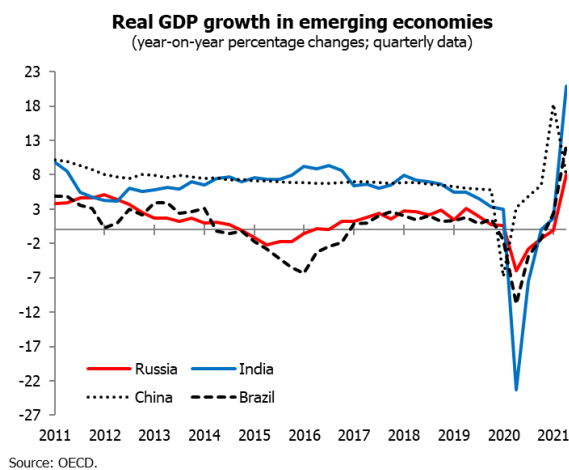
1.1. International economic surrounding

High growth rates of the global economic activity were registered in the second quarter of 2021. Although the high performances are primarily a result of the low base effect from the last year, due to severe restrictions introduced as a protection against COVID-19, the more favorable developments in the second quarter are also related to the gradual economic recovery, reduction of the restrictive measures, initiated mass immunization and further stimulating fiscal and monetary policy. In the second quarter, an annual growth of 14.2% was registered in the Euro area, as our major trading partner, compared to the decline of 1.2% in the first quarter, mostly due to the significant growth of domestic demand, especially private consumption. According to the October estimates by the IMF, the global economic activity in 2021 and 2022 is still expected to recover, with growth rates of 5.9% and 4.9%, respectively, followed by an expected moderate growth of about 3.3% in the medium term. Minimal downward correction was made only in the estimates for 2021, which largely reflected the expectations for a lower growth in developed countries, as well as in low income developing countries. The estimates are still accompanied by significantly high uncertainty, where the risks are mainly downward and are primarily related to the further development of the pandemic and the adjustment of the stimulating policies, especially in developed countries.

Global economic activity registered significant growth in the second quarter of 2021. This is partly a result of the low base effect from the previous year, when tough measures for public health protection were introduced due to the spread of the coronavirus, and partly a result of the gradual economic recovery, reduction of current restrictive measures and further stimulating fiscal and monetary policy. Analyzing developed countries, largest movement of the economic activity was registered in the United Kingdom, which recorded an annual growth of 23.6% (decline of 5.8% in the first quarter). The positive performance is mostly a result of the growth in domestic demand, especially private consumption, amid negative contribution from net exports. The euro area also registered double-digit growth of 14.2% (decline of 1.2% in the first quarter), which is the largest growth since its founding. This upward shift is mostly a result of the significant growth in the domestic demand, whereby all member states registered more significant positive performances. The USA economy registered accelerated economic activity, with a growth of 12.2% (growth of 0.5% in the previous quarter), mainly driven by the significant private consumption, as well as investments. The Japanese economy registered a solid annual growth rate of 7.7% (compared to the decline of 1.3% in the first quarter), as a result of the more favorable performances in all GDP components.



Larger emerging economies registered a positive development of the economic activity in the second quarter, with a growth structure similar to developed economies. Moreover, the Indian economy registered the highest annual growth within this group, of 20.9% (1.6% in the first quarter), driven by the significant growth of private consumption and investments, amid negative contribution of the public consumption and net exports. The Brazilian economy also registered significant acceleration of the economic activity, realizing an annual growth of 12.4% (2.3% in the first quarter), which mostly stems from the strong growth in private consumption, amid improved performances in other GDP components as well. The Chinese economy continued its solid economic performances, registering an annual growth rate of 7.9% (18.3% in the previous quarter), influenced by the private consumption and net exports. Russia registered a revival of the economic activity, with an annual growth of 8.1% (decline of 0.1% in the first quarter), which mostly stems from the significant growth of domestic demand, especially private consumption.



Regarding the global growth estimates in the third quarter of 2021, the global PMI index in the third quarter averaged 53.8 (compared to 57.2 in the previous quarter), which is a quarterly decline of 6.1%. These movements are result of the reduced activity in the manufacturing and service industries, especially in the Asian region. Divergent movements were registered, regarding the estimates in the surveys for the euro area and the USA. Namely, the indicators in the euro area point to expectations for a small quarterly growth in the third quarter of the year, while there is a slight deceleration in the USA, due to decreasing availability of raw materials and workers in making new orders.

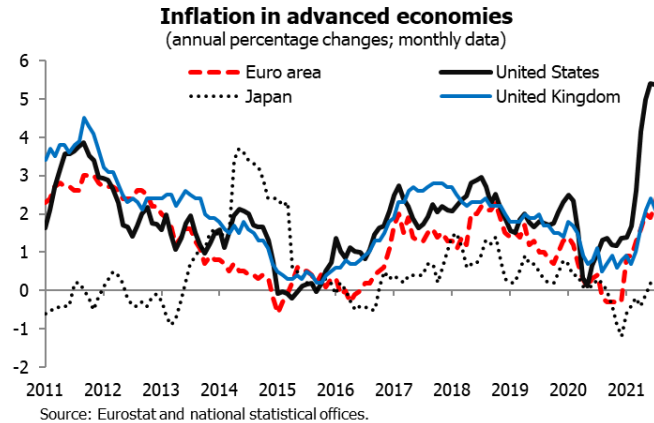


According to the latest IMF estimates, the global economic activity is expected to grow by 5.9% in 2021 and 4.9% in 2022. Moreover, a minimal downward correction (of 0.1 percentage points) for 2021 was made according to the latest estimates, compared to the June forecast, while the estimate for 2022 remains unchanged. The downward revision for 2021 reflects the expectations for a lower growth in developed countries, partly due to the disruption in supply chains, as well as the lower growth of low income developing countries, mainly due to difficulties in dealing with the spread of the pandemic. However, these downwards estimates are almost entirely compensated with the prospects for faster growth in the countries exporting primary commodities, as well as in certain developing countries, in the short term. In the medium term, stabilization of the global growth is expected to average 3.3%. Moreover, the gross domestic product in certain economies is expected to exceed the pre pandemic mid-term forecasts, largely due to the expectations for continuing expansionary economic growth supporting policies in the US, which include measures for increasing the potential (infrastructure projects). On the other hand, more pronounced losses in the production are expected in the emerging economies and developing countries due to the slower immunization process and generally smaller stimulating packages compared to advanced economies.

The forecasts on the global economy growth are characterized by great uncertainty, in terms of the development of the pandemic, the inflation prospects and changes in the global financial conditions. The risk balance is mainly unfavorable both in the short and the medium term. *The downward risks* to growth refer to the occurrence of new more transmissible and more deadly variants of COVID-19, long-term mismatch of supply and demand, price pressures and normalization of the monetary policy faster than expected, as well as possibly lower fiscal stimulus in the USA and volatility in financial markets. Possible larger social unrests, less favorable climate shocks, cyber-attacks, as well as intensified tensions in trade and technology² are additional downward risks. On the other hand, *the upward risks* for the future growth are mainly related to faster production of vaccines and immunization pace that would increase the confidence of consumers and companies, contributing to the growth of consumption and investments and consequently strengthen the economic recovery. Furthermore, the pandemic has accelerated the changes in many sectors of the economy, through greater automation and transformation of working positions which could rely on technological platforms for distance work, which might result in significant growth of productivity.

Accelerated inflation was registered in the third quarter of 2021 globally, mainly influenced by the growth of energy prices. Namely, an average annual inflation rate of 5.3% is registered in the USA in the period July-August, compared to the rate of 4.8% in the second quarter, mostly due to temporary factors related to the pandemic. The United Kingdom and the Euro area registered same growth rate of prices of 2.6% (compared to 2% and 1.8%, respectively in the first quarter of 2021). Japan also registered slight upward movement of prices in July, with an average inflation rate of 0.2% (compared to -0.1 in the previous quarter).

² Based on the risks, the IMF works on two alternative (downward) scenarios, whereby in the first one the inflation expectations in the USA are assumed to grow in the next three years more than expected, while in the second scenario, the implications of living with endemic COVID-19 in the medium term. According to the first scenario, the level of the global GDP as well as in the USA is expected to be lower by about 1.25 percentage points until 2026, but the decline in the emerging countries would be more significant, for more than 1.5 percentage points by the end of (2025-2026), which is approximately four times more than the decline of the GDP in the developed economies (excluding the USA). According to the second scenario, the global GDP is expected to be lower by more than 1 percentage points until 2025, with a gradual recovery and approximation to the baseline scenario. The developed economies are expected to be strongly affected by the emerging economies, which is mostly due to assumptions for greater restraint regarding vaccination.



The economic activity in the Euro area, amid low base effect, grew significantly in the second quarter of 2021, reaching an annual growth of 14.2%, which is a significant improvement compared to the decrease of 1.2% in the first quarter of the year. The upward movement was mostly encouraged by the loosening of restrictive measures, whereby the domestic demand, especially private consumption had the largest contribution, amid growth of the real disposable income and significant decrease of the saving rate. Significant improvement of the economic activity, with positive annual growth rates, is registered in all Euro area countries, the highest registered in Ireland, Spain, France and Italy. According to the September forecasts, the ECB projected the real growth of the GDP in 2021 to 5%, and is expected to be more moderate in 2022 and to amount to 4.6% and 2.1% in 2023. The forecasts for 2021 are revised upward, compared to the expectations for June, while for 2022 they are minimally revised downwards³. Consequently, in the latest forecasts, the pre-crisis level of the GDP (the end of 2019) is expected to be reached by the end of 2021, i.e. one quarter earlier than previously forecasted. As of the labor market in the Euro area, the unemployment rate in July decreased and amounted to 7.6% (8% in the first quarter of 2021). The annual inflation rate in the Euro area for the period July-August 2021 accelerated to 2.6% (1.8% in the previous quarter), mainly influenced by the higher energy and food prices, amid growth in demand. According to the September forecasts, the ECB estimated the inflation rate in the Euro area to 2.2% in 2021, mainly driven by temporary upward factors⁴, followed by a slowdown of 1.7% and 1.5% in 2022 and 2023, respectively. An upward revision for the entire forecasting period was made, compared to the June forecasts⁵, mostly due to the expectations for demand recovery, continuous pressures that arise from the disrupted supply chains and upward effects from the prices of primary commodities, including oil.

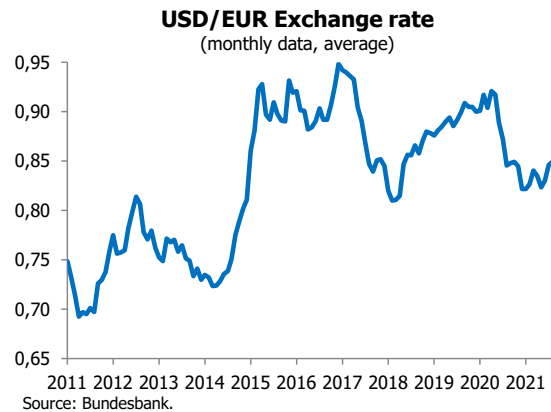
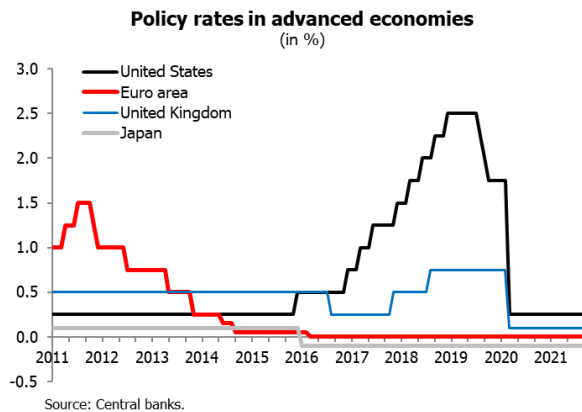
In the third quarter of 2021, developed countries continued with stimulating monetary policy for support of the economic growth. Namely, the FED kept the interest rate spread to a level of 0-0.25% and continued with the measures for purchase of long-term securities, in the total amount of US Dollar 120 billion until further significant progress is reached in the labor market, and the interest rate reaches, and after a while moderately exceeds 2% for a certain period. Therefore, at the meeting in July, the FED confirmed the decision for keeping the interest rate of the reserve requirement and excess reserves of 0.15%, in power since 29 July, in order to support smooth functioning of the short-term markets, and at the same time kept the interest rate of repo and reverse repos overnight, to 0.25% and 0.5%, respectively. The

³ In June, the growth of the GDP in the euro area was projected to be 4.6% in 2021, 4.7% in 2022 and 2.1% in 2023.

⁴ According to the forecasts by the ECB, one of the most significant temporary factors that will contribute to the growth of prices in 2021 are: growth of the energy inflation amid strong base effect; strong growth of the input costs due to disrupted supply; single increase in prices of services due to decreased limitations related to COVID-19; and Germany's interruption of VAT rate reduction measure.

⁵ In June, the growth of the inflation in the euro area was projected to be 1.9% in 2021, 1.5% in 2022 and 1.4% in 2023.

FED meeting in September suggested that if the economic growth mostly continues at the same pace, the appropriate thing to do will be to reduce the purchase of bonds. The bank of England kept the interest rate unchanged at the level 0.1% in the third quarter and continued with the government bonds purchase measures (in total amount of GBP 895 billion)⁶ to support the economy. Moreover, it announced that if the economy moves in line with the forecasts, a moderate tightening of the monetary policy might be expected, due to achieving the inflation goal in the medium terms. The ECB started implementing the new revised monetary strategy⁷ since July. Despite that, the ECB interest rates remained unchanged during the third quarter of 2021, along with the prolonged previously undertaken measures for maintaining favorable financial conditions during COVID-19 pandemic. However, at the meeting in September, the ECB reported that as a result of the favorable conditions of financing, the net purchase of assets within the securities purchase program for urgent support of the economy due to the pandemic will have a more moderate pace than in the previous two quarters. The bank of Japan also kept its interest rate (-0.1%), and prolonged the previously adopted measures for stimulating the economic activity.

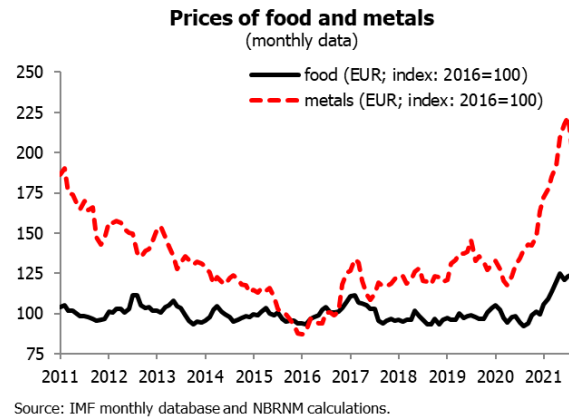
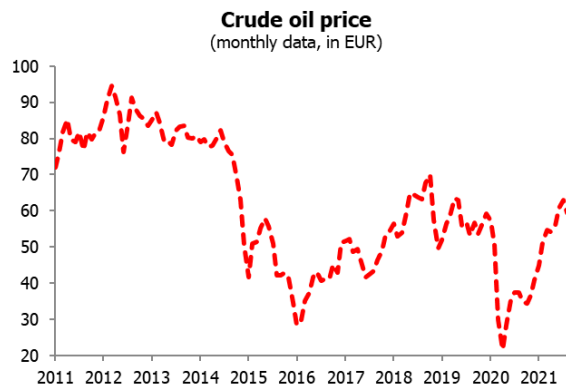


The value of the US dollar in the third quarter of 2021, registered a slight appreciation of 2.2% on a quarterly basis, averaging to euro 0.85. Such change was mostly a result of the increased interest by the investors in the US Dollar, amid increased risk of the impact of the new coronavirus variants on the global economic growth, as well as the expectations for reduction of the monetary stimulus by the FED earlier, compared to the previous expectations. On the other hand, the value of the US Dollar on an annual basis against the euro registered a slight depreciation of 0.8%.

The price of oil continued to grow in the third quarter of the year, registering a quarterly growth of 8.8%, where the average price equaled Euro 61.9 per barrel. Moreover, the oil price reflects the decreased level of inventories of oil in the US, amid simultaneous fast growth in demand for oil, mainly supported by the greater global economic activity amid reduced restrictive measures worldwide. Analyzed annually, the oil price registered significant growth of 69.5%, which is mostly due to the low base effect from the previous year.

⁶ At the regular meeting in August and September, the Bank of England decided to keep the volume of corporate bonds purchase to non-financial investments to GBP 20 billion and to continue the current government securities purchase program, with a target amount of GBP 875 billion, whereby the total amount of assets purchase from these measures equals to GBP 895 billion.

⁷ According to the latest strategy, reaching a price stability is still the main objective of the monetary policy, while the major changes refer to definition of the target inflation (2% symmetrical target inflation in the medium terms), as well as to extension of the scope of inflation by including housing costs. For more information see the following [link](#):



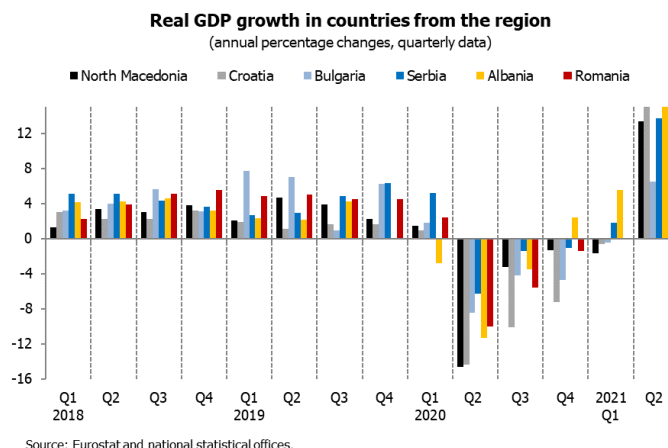
The prices of non-energy primary products⁸ (in Euros) in the period July-August 2021 registered a quarterly growth of 2%. Analyzed by groups of products, the growth stems from the increase in prices of food and metals. Therefore, the index of basic metals⁹ registered an annual growth of 2.3%, amid growth in prices of most of the metals, among which the nickel. The growth in prices of metals was mostly encouraged by the increased demand by the industry for electric cars and other industries related to the process of transition towards pure energy. The index of food prices¹⁰ registered an increase of 1.5%, mostly a result of the growth in prices of meat and sugar. The growth in sugar price was mostly a result of the investor's concerns over the adverse weather conditions in Brazil, the largest producer of sugar in the world, while the growth of the meat prices was due to increased demand in Asia, amid reduced supply. Analyzed on an annual basis, the growth in prices of non-energy primary products, in euros, equaled 27.6%.

In the second quarter of 2021, all countries in the region registered significant increase of the economic activity, as a result of the positive contribution of the domestic demand, especially private consumption. Moreover, Albania registered the highest annual growth in the region of 17.9% (increase of 5.5% in the first quarter), while Croatia, Serbia and Romania registered double digit growth of 16.1%, 13.7% and 13%, respectively (compared to the decline of 0.7%, increase of 1.8% and decline of 0.2%, in the previous quarter, respectively). The Bulgarian economy registered a growth rate of 6.4% (decline of 0.5% in the first quarter).

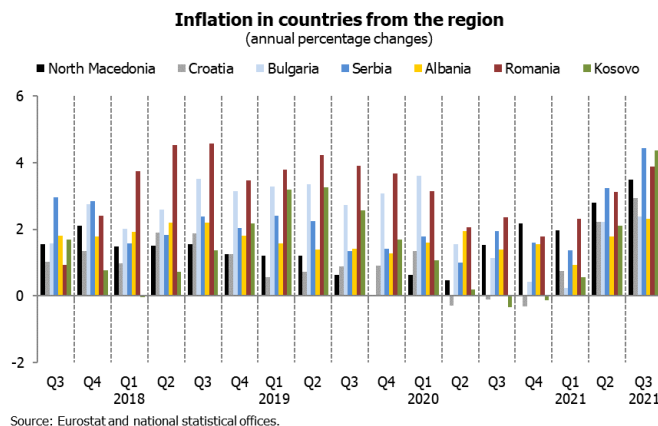
⁸ This aggregate index includes the index of precious metals, the index of food and beverages, the index of agricultural raw materials and the index of basic metals.

⁹ This index includes the following metals: Aluminum, cobalt, copper, iron, steel, molybdenum, nickel, tin, uranium, and zinc.

¹⁰ This index includes the following food products: Cereals, vegetable oil, meat, sea food, sugar and other food.



In the third quarter of 2021, all countries in the region registered an acceleration of the annual inflation rate. Moreover, the accelerated growth of inflation, in almost all countries, is mostly a result of the high growth in prices of food and energy, except in Croatia, where the acceleration is due to the growth in prices of food and core inflation.



1.2. Domestic supply

In the second quarter of 2021 the domestic economy registered real growth of 13.1% on an annual basis, after the continuous annual fall in the previous four quarters under the influence of the outburst of COVID-19 pandemic. The high growth rate in the second quarter is primarily a result of the low base effect from the same period last year, when tough measures were undertaken to prevent the spread of COVID-19. However, the stabilization of the epidemiological situation and the initiated mass immunization had a positive effect on the growth, and had a favorable influence on consumer confidence in the country during the second quarter. Therefore, the group of activities "trade, transport and catering" which were previously mostly affected by the health and economic crisis caused by the COVID-19, have the largest impact on the growth of the GDP, with a solid positive contribution from industry, due to the favorable performances in the manufacturing industry. Given the prolonged character of the pandemic, the level of the GDP in the first half of the year is still



lower than the pre-pandemic level, despite the strong dynamics of the economic recovery. High-frequency data on the supply side available for the period July-August 2021 mainly indicate a further annual growth in the economic activity in the third quarter of the year, but at a significantly slower pace, compared to the growth in the previous quarter. The perceptions of the corporate managers for the business situations of the companies in the manufacturing industry, retail trade, construction and service sector in the third quarter of 2021, as well as their expectations for the forthcoming period, are generally more favorable compared to the expectations from the previous quarter.

In the second quarter of 2021 the domestic economy registered a significant real growth of 13.1% on an annual basis (amid growth of 0.3% on a quarterly basis, seasonally adjusted), **which is a significant improvement compared to the decline in the previous quarter (-1.9%).** These performances are primarily a result of the low base effect from the previous year, given the undertaken strict measures to protect the spread of COVID-19 in that period, and the stabilization of the epidemiological situation during the second quarter and the initialized mass immunization in the country had an additional effect. Structurally, the group of activities "trade, transport and catering" have the largest positive contribution in the second quarter, with a significant positive contribution by the industry due to the favorable performances in manufacturing industry.

GDP and components- annual growth rates (in %)

| | annual growth rates, in % | | | | | | | | | | | |
|---|---------------------------|-------|-------|------|-------|---------|---------|---------|---------|---------|---------|--|
| | 2016 | 2017 | 2018 | 2019 | 2020 | Q1 2020 | Q2 2020 | Q3 2020 | Q4 2020 | Q1 2021 | Q2 2021 | |
| Agriculture | -0.4 | -12.5 | 8.3 | -0.3 | 1.7 | 2.5 | 4.0 | 5.2 | -3.2 | 0.3 | 0.4 | |
| Industry | -3.0 | 1.4 | 5.3 | 5.2 | -10.0 | -3.9 | -25.1 | -10.4 | -0.6 | -6.7 | 11.4 | |
| Manufacturing | -1.5 | 1.6 | 6.2 | 2.4 | -10.6 | -2.1 | -30.5 | -9.1 | 0.0 | -6.2 | 19.7 | |
| Construction | -2.8 | 1.6 | -11.0 | 3.0 | -2.1 | 1.4 | -12.0 | 3.4 | -1.4 | 1.7 | -0.4 | |
| Trade and transport | 8.7 | 7.1 | 5.0 | 4.8 | -7.9 | -1.5 | -28.2 | -2.3 | -0.1 | -0.4 | 46.0 | |
| Information and communication | 7.2 | 7.6 | -4.1 | 6.2 | 2.8 | 12.9 | -3.5 | 3.3 | -0.4 | -0.9 | 5.7 | |
| Financial and insurance activities | 1.5 | 1.9 | 2.6 | 0.1 | -1.6 | 0.3 | -6.5 | -1.0 | 1.0 | -0.7 | 4.6 | |
| Real estate activities | -3.2 | -1.6 | 0.1 | 0.5 | 1.0 | 5.0 | -1.7 | -1.3 | 2.0 | 0.5 | 2.2 | |
| Professional, scientific and technical activities | 11.5 | 8.8 | 7.9 | 3.4 | -2.4 | -1.6 | -2.8 | -3.7 | -1.6 | -0.3 | 3.3 | |
| Public administration | 3.5 | -2.2 | 2.0 | 0.8 | -1.0 | -1.6 | -0.6 | -1.3 | -0.4 | -2.9 | 0.6 | |
| Other service activities | 7.2 | 3.1 | 6.6 | 4.2 | 0.4 | 7.6 | 4.5 | -6.6 | -3.6 | -3.8 | -0.1 | |
| Gross Domestic Product | 2.8 | 1.1 | 2.9 | 3.2 | -4.5 | 0.9 | -14.9 | -3.3 | -0.7 | -1.9 | 13.1 | |

*From the release for GDP of 06.09.2021

Source: State Statistical Office and NBRNM calculations.

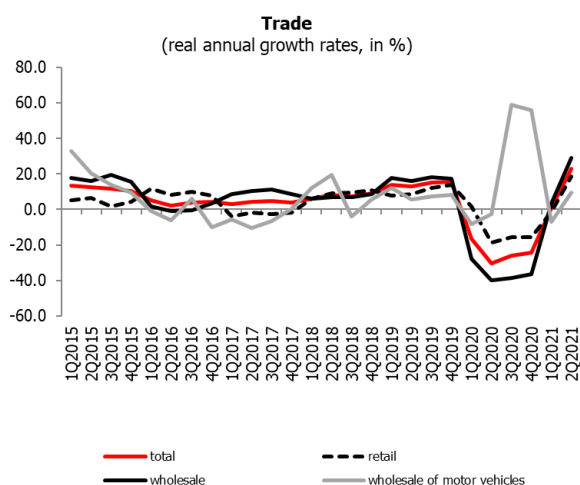


GDP and components-Contributions to the GDP growth (in percentage points)

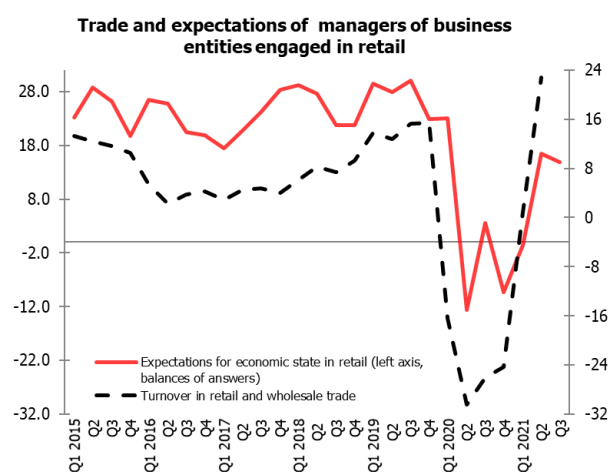
| | contribution in GDP growth, in p.p. | | | | | | | | | | |
|---|-------------------------------------|------------|------------|------------|-------------|------------|--------------|-------------|-------------|-------------|-------------|
| | 2016 | 2017 | 2018 | 2019 | 2020 | Q1 2020 | Q2 2020 | Q3 2020 | Q4 2020 | Q1 2021 | Q2 2021 |
| Agriculture | 0.0 | -1.1 | 0.7 | 0.0 | 0.1 | 0.2 | 0.3 | 0.4 | -0.3 | -0.1 | 0.0 |
| Industry | -0.5 | 0.2 | 0.9 | 1.0 | -1.8 | -0.7 | -4.5 | -1.9 | -0.1 | -1.2 | 1.8 |
| Manufacturing | -0.2 | 0.2 | 0.8 | 0.3 | -1.4 | -0.3 | -4.2 | -1.2 | 0.0 | -0.8 | 2.2 |
| Construction | -0.2 | 0.1 | -0.7 | 0.2 | -0.1 | 0.0 | -0.6 | 0.2 | -0.1 | 0.0 | 0.0 |
| Trade and transport | 1.6 | 1.3 | 1.0 | 0.9 | -1.6 | -0.3 | -5.7 | -0.5 | 0.0 | -0.1 | 7.9 |
| Information and communication | 0.2 | 0.2 | -0.1 | 0.2 | 0.1 | 0.5 | -0.1 | 0.1 | 0.0 | 0.0 | 0.2 |
| Financial and insurance activities | 0.0 | 0.1 | 0.1 | 0.0 | 0.0 | 0.0 | -0.2 | 0.0 | 0.0 | 0.0 | 0.1 |
| Real estate activities | -0.4 | -0.2 | 0.0 | 0.1 | 0.1 | 0.6 | -0.2 | -0.1 | 0.2 | 0.0 | 0.2 |
| Professional, scientific and technical activities | 0.4 | 0.3 | 0.3 | 0.1 | -0.1 | -0.1 | -0.1 | -0.1 | -0.1 | 0.0 | 0.2 |
| Public administration | 0.4 | -0.3 | 0.2 | 0.1 | -0.1 | -0.2 | -0.1 | -0.2 | -0.1 | -0.4 | 0.2 |
| Other service activities | 0.2 | 0.1 | 0.2 | 0.1 | 0.0 | 0.2 | 0.1 | -0.2 | -0.1 | -0.1 | 0.0 |
| Gross Domestic Product | 2.8 | 1.1 | 2.9 | 3.2 | -4.5 | 0.9 | -14.9 | -3.3 | -0.7 | -1.9 | 13.1 |

Source: NBRNM calculations.

Analyzed by high-frequency data, the turnover in trade realized a significant real growth on an annual basis in the second quarter of the year, which is a significant acceleration, after the low growth in the previous quarter. Moreover, a significant real growth on an annual basis is registered in all three types of trade- wholesale trade, retail trade and trade in motor vehicles). Total trade turnout in the period July-August 2021 continued to register high real annual growth, yet slightly more moderate compared to the growth in the second quarter. Moreover, the favorable performances in the total trade are due to high growth of wholesale trade and retail trade, while the trade in motor vehicles registered a decline. The perceptions of the corporate managers in the "retail trade" sector of their turnover during the third quarter of 2021 are more favorable compared to the previous quarter. Moreover, the expectations for the following period from the aspect of employments and prices are more favorable compared to the previous one, amid slightly less favorable expectations regarding demand and business activity.

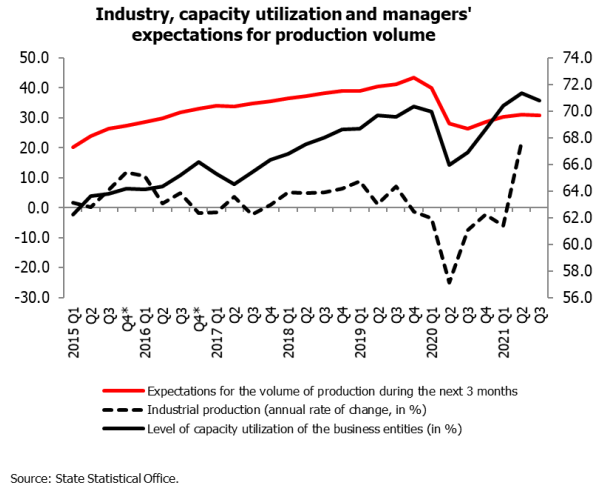
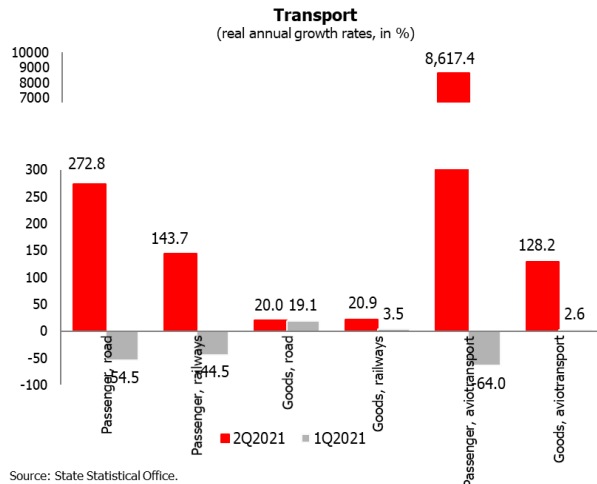


Source: State Statistical Office

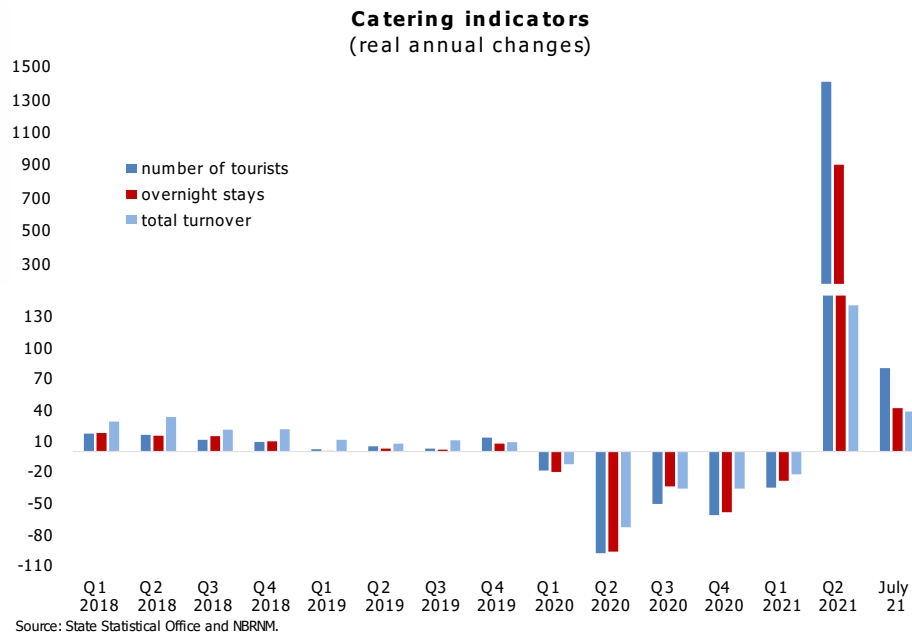


Source: Retail survey of EC, State Statistical Office and NBRNM.

In the second quarter of 2021, the **transport** registered more favorable performances, especially in all types of passenger traffic that realized a significant growth rate, after the decline in the previous quarter. The freight traffic (air, railway and road) also registered real annual growth, with accelerated dynamics compared to the previous quarter.

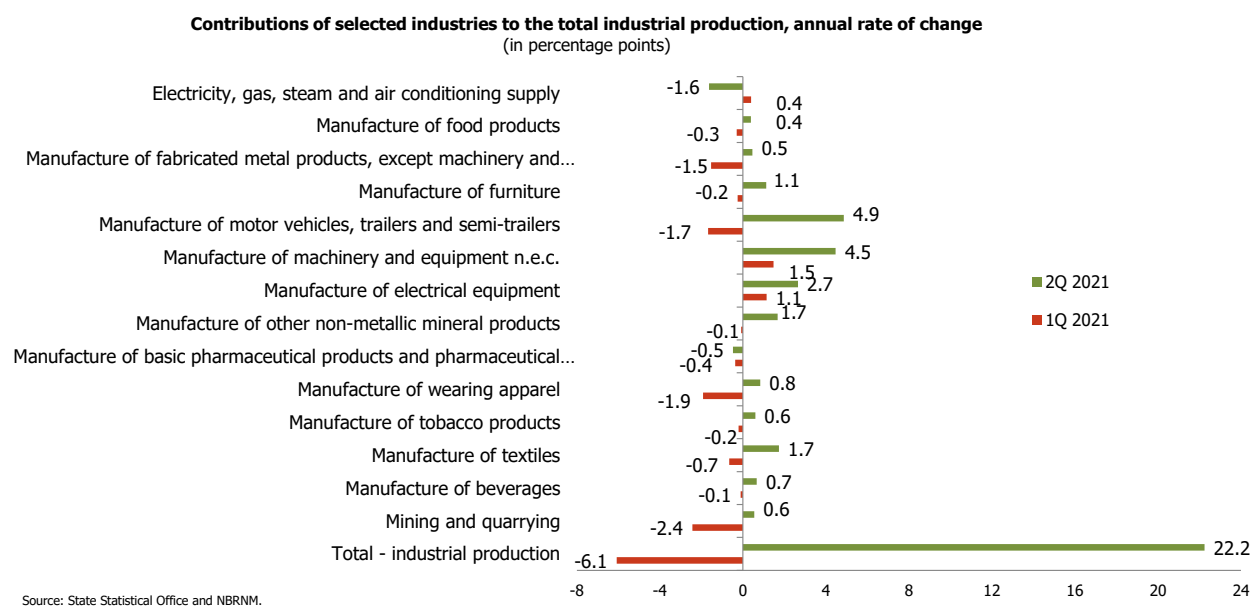


In the second quarter of 2021, **the catering** registered a significant real growth on an annual basis of the number of tourists, overnight stays, as well as total turnover, which is an improvement compared to the decline in the previous quarter in these categories. Moreover, the growth in number of tourists and overnight stays is a result of the increased number and overnight stays of both, foreign and domestic tourists. The catering in July also registered high annual growth rates in total number of tourists, overnight stays, as well as total real turnover, yet at a more moderate pace compared to the growth in the second quarter in all three categories. The perceptions of the corporate managers in the service businesses of their business situation, demand and employment in the third quarter of 2021, are more favorable compared to the estimates in the previous quarter, and the expectations for the next period are also more favorable from the aspect of employment and prices, amid slightly less favorable expectations regarding demand.



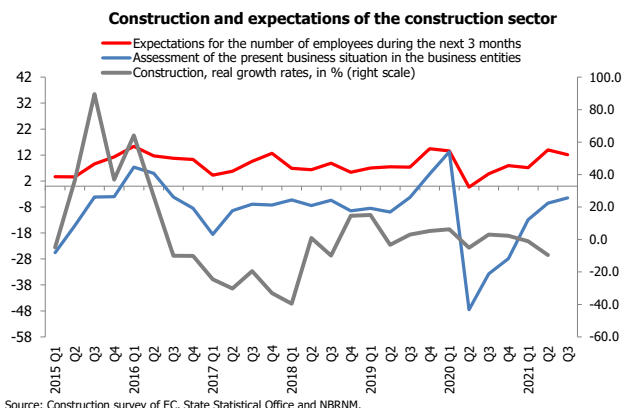
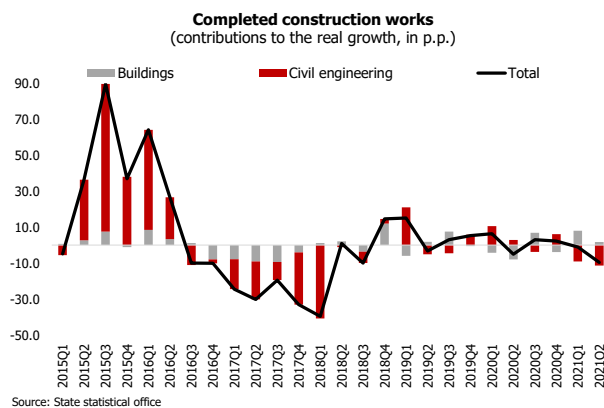
The industrial output in the second quarter of the year registered a significant real growth of activity of 22.2% on an annual basis, which is a significant improvement after the decline of 6.1% in the previous quarter. Analyzed by activities, through the index of Industrial

output¹¹, the positive contribution of the manufacturing industry is the most influential, the mining has a less positive contribution, while the energy sector registers a slight decline. The growth in the second quarter within the manufacturing industry is widely dispersed, and the most pronounced positive contribution is made by the group of activities in which the foreign export facilities, such as production of motor vehicles, production of machines and devices and the production of electrical equipment are active. The group of traditional activities such as production of textile and clothing, production of other non-metallic minerals and production of beverages also registers a positive contribution, as well as the production of chemicals and chemical products and furniture manufacturing. On the other hand, more pronounced negative contribution is registered in the production of basic pharmaceutical products and pharmaceutical preparations. In the period July-August 2021, the Industrial output registered a slight real annual decline of 0.9%. Observed by main activities, the manufacturing industry has the largest negative contribution, with a small negative contribution from the energy sector, while the activity in mining increased. The managers from the industrial sector have more favorable perceptions of the business situation in the third quarter of 2021, compared to the previous quarter, as well as more optimistic expectations from the aspect of the production development, prices and employment for the forthcoming period.



On the other hand, the construction sector registered real fall in the second quarter of the year, on an annual basis. According to the available high frequency data on the construction sector, a real annual fall is registered in the second quarter of total completed construction works (faster decline compared to the one in the previous quarter), which is entirely due to the high decline in civil engineering, while the construction registered growth, yet at a slower pace compared to the one in the previous quarter. In July, the decline of the value of completed construction works widened on an annual basis, mainly due to the high decline in civil engineering, and also a lower decline in construction. When it comes to the perceptions of the corporate managers in the construction companies, of their activity movement in the third quarter of 2021, they are less favorable compared to the previous quarter. On the other hand, the expectations for the next period are more favorable, from the aspect of number of orders and pricing, while the expectations for employments are less favorable.

¹¹ The analysis of trends in industry uses data on the SSO's monthly data for the industrial output indices.

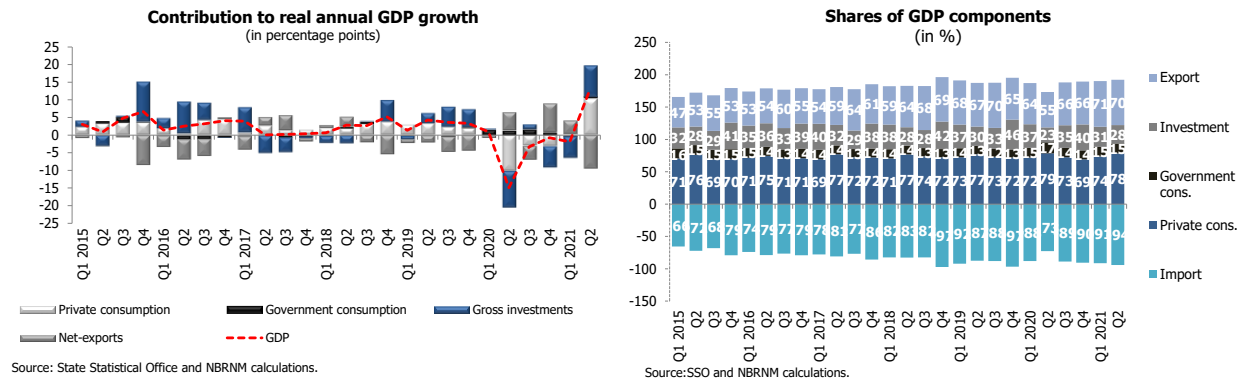


1.3. Aggregate demand

Observed from the aspect of demand, the high real annual growth of the GDP of 13.1% in the second quarter of 2021 is entirely a result of the positive contribution of domestic demand, amid growth in all three components, while the net export had a negative contribution. Thus, the private consumption registered significant acceleration of the growth in conditions of fast growth of the disposable income primarily driven by the growth in private transfers and wage bill, amid low base effect, as well as stabilization of the epidemiological situation. Gross investments also registered high growth, amid simultaneously higher public consumption. On the other hand, the negative contribution of the net exports is a result of the higher growth of imports than exports, although both components registered significant acceleration of the growth dynamics.

The structural analysis of the GDP¹² components from the aspect of demand, shows that the high growth in the second quarter is entirely explained by the positive contribution of domestic demand, while the net export had a negative contribution. These performances in the economy in this period are primarily a result of the low base effect from the last year, when the impact of the pandemic was the strongest, as well as the stabilization of the epidemiological situation during the second quarter and the initiated mass immunization in the country. Observed by individual components, all components of domestic demand registered a growth. Thus, in conditions of high growth of the disposable income, the private consumption registered a significant acceleration of the growth, and after a fall in two consecutive quarters, the gross investments also registered high growth. The public consumption also registered an increase in this quarter, after the fall at the beginning of the year. Unlike the previous two quarters, when the net exports had a positive contribution, it registered a negative contribution to the GDP in this quarter, amid higher growth in import than in export. However, both components registered significantly accelerated growth compared to the growth in the previous quarters.

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



| | Real annual growth rates (%) | | | | | | | | | Contributions to real annual growth (in p.p.)** | | | | | | | | |
|-------------------------------|------------------------------|------|-------|---------|---------|---------|---------|---------|---------|---|------|------|---------|---------|---------|---------|---------|---------|
| | 2018 | 2019 | 2020 | 2020-Q1 | 2020-Q2 | 2020-Q3 | 2020-Q4 | 2021-Q1 | 2021-Q2 | 2018 | 2019 | 2020 | 2020-Q1 | 2020-Q2 | 2020-Q3 | 2020-Q4 | 2021-Q1 | 2021-Q2 |
| Private consumption | 3.7 | 3.5 | -5.6 | -0.3 | -13.0 | -4.1 | -4.3 | 0.4 | 12.9 | 2.5 | 2.3 | -3.7 | -0.2 | -8.9 | -2.7 | -2.8 | 0.3 | 9.4 |
| Government consumption | 1.5 | -0.8 | 10.1 | 10.7 | 9.8 | 13.5 | 6.6 | -2.2 | 2.9 | 0.2 | -0.1 | 1.4 | 1.6 | 1.4 | 1.8 | 0.9 | -0.4 | 0.6 |
| Exports of goods and services | 12.8 | 7.2 | -10.9 | -5.9 | -30.8 | -8.4 | 1.3 | 8.6 | 45.0 | 7.1 | 4.4 | -6.8 | -3.7 | -19.1 | -5.4 | 0.8 | 5.1 | 22.7 |
| Imports of goods and services | 10.7 | 8.9 | -10.5 | -3.7 | -29.4 | -2.4 | -7.2 | 2.0 | 46.7 | -7.4 | -6.4 | 8.0 | 2.9 | 21.6 | 1.7 | 5.9 | -1.4 | -28.3 |
| Gross capital formation | 1.7 | 9.5 | -10.2 | 1.0 | -34.4 | 4.2 | -13.0 | -16.6 | 38.4 | 0.5 | 3.1 | -3.5 | 0.3 | -9.8 | 1.3 | -5.6 | -5.4 | 8.6 |
| Domestic demand | 2.9 | 4.7 | -5.3 | 1.3 | -15.9 | 0.0 | -6.3 | -4.9 | 16.5 | 3.2 | 5.3 | -5.8 | 1.8 | -17.4 | 0.3 | -7.5 | -5.6 | 18.6 |
| Net exports* | 4.9 | 13.8 | -9.5 | 2.6 | -24.8 | 20.9 | -24.6 | -15.4 | 52.0 | -0.3 | -2.1 | 1.3 | -0.9 | 2.5 | -3.7 | 6.7 | 3.6 | -5.5 |
| Statistical discrepancy | | | | | | | | | | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| GDP | 2.9 | 3.2 | -4.5 | 0.9 | -14.9 | -3.3 | -0.7 | -1.9 | 13.1 | 2.9 | 3.2 | -4.5 | 0.9 | -14.9 | -3.3 | -0.7 | -1.9 | 13.1 |

*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.

1.3.1. Private consumption

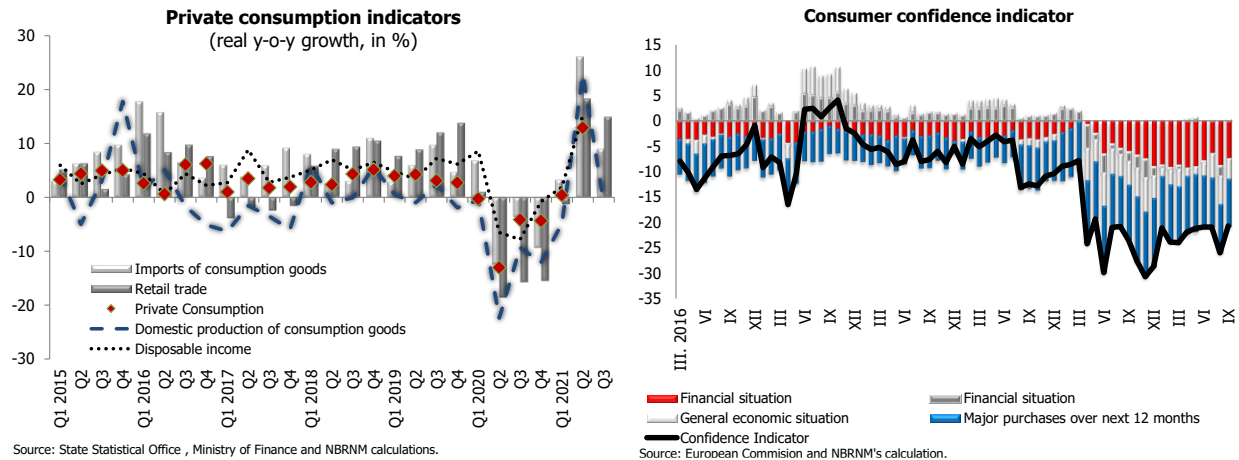
After the strong decline in 2020, as well as the slight annual growth in the beginning of 2021, the private consumption registered a double-digit annual growth in the second quarter of 12.9% and a quarterly growth of 1.1%. Although reflecting the low base effect from the previous year in one part, such movements are still a result of more favorable shifts in line with the gradual stabilization of the epidemiological situation, amid initiated mass immunization of the population, which also affected the gradual return of consumers' confidence, with favorable movements in the labor market, amid further solid credit support. Thus, from the aspect of financing consumption, the disposable income registered a strong growth in the second quarter, amid enhanced growth in private transfers, which substantially decreased in the previous period, due to the pandemics and reduced movement of the population worldwide, with an additional influence from the growth in wage bills¹³. At the same time, the amount of paid pensions continued to grow, as well as the solid growth of banks' lending to households.

Indicators of the movements in **private consumption**¹⁴ for the third quarter of the year suggest further annual growth, but at a more moderate pace. Thus, the growth of the retail trade, gross revenues from VAT and import of consumer goods continued in this period and was more moderate compared to the growth in the previous quarter. On the other hand, the high growth in the second quarter was followed by a decline in domestic production of consumer goods. The available data regarding the funding sources of

¹³ The wages in the sectors mostly affected by the pandemic and the restrictive measures undertaken for dealing with it, were paid in the second quarter, due to the inability for timely wage payment for February and March 2021. For more details, see section 1.3. Employment and wages.

¹⁴ From the indicators for personal consumption, data on turnover in retail trade, pensions, domestic production of consumer goods, imports of consumer goods and household loans refer to the period July -August 2021, while net wages are as of July 2021.

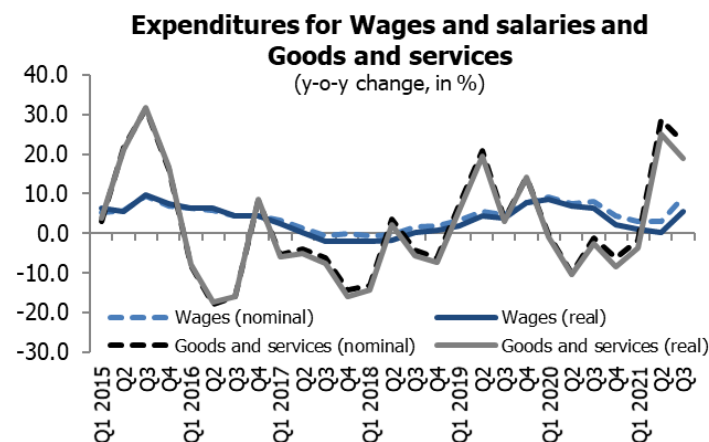
private consumption, also indicate further growth of disposable income, but at a slower pace, in conditions of more moderate wage growth and small decline in the stock of pensions, amid further growth in household loans as well. On the other hand, the results of the Bank lending Survey from September show a slight net tightening of the credit standards and further net increase in demand of total loans to households. The consumer confidence indicator for the third quarter of 2021 points to less favorable expectations of the overall economic and financial condition, compared to the previous quarter.



1.3.2. Public consumption

After the decline in the first quarter of 2021, the public consumption in the second quarter registered an annual growth of 2.9% (quarterly growth of 5.0%). According to budget data, such growth is mostly due to higher costs of goods and services, while higher growth rates are observed in transfers to the Health Fund. The wage expenses continue to grow, yet at a slower pace, while the transfers to the local authorities registered a decline again.

Regarding the fiscal data for the period July-August 2021, the budget performances point to further, yet more moderate growth of **public consumption**, amid growth in the cost of goods and services and wage expenses, but lower costs in Health Insurance Fund.

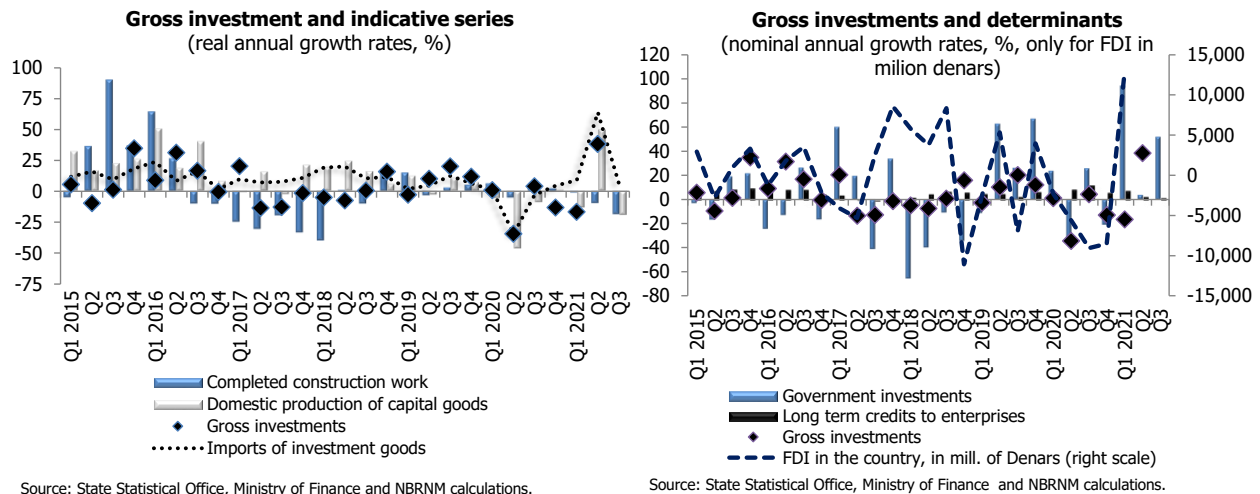


Source: Ministry of Finance and NBRNM calculations.
The calculations include expenditures of Consolidated Budget of Central Government and Funds, deflated by CPI.

1.3.3. Investment consumption

After the decline of gross investments at the end of 2020 and the beginning of 2021, they registered a high double-digit annual growth in the second quarter of 2021 of 38.4% (quarterly growth of 12.1%). Similar to private consumption, such movements mostly reflect low base effect from the last year, as well as favorable shifts in line with the stabilization of the epidemiological situation and initiated immunization in the country. Regarding the indicative categories of investments, a high growth in import of machinery and equipment is registered, as well as increase of foreign direct investments. The domestic production of capital goods also registered high growth rates, with positive movements in other indicative categories for investments, amid growth in the income from profit tax, government capital investments and long term corporate loans, which still grew somewhat slower. Negative movements in this quarter on an annual basis were registered only in completed construction works.

The high frequency data on the **gross investments**¹⁵ for the period July-August 2021 moved in different directions. Thus, in this period, the total industrial output registered small annual decline, while the fall in domestic production of capital goods was more pronounced (as opposed to the growth in the previous quarter). The construction also registered a decline. On the other hand, positive movements were registered in government capital investments, corporate tax, and the growth in import of investment products and long-term corporate loans also continues. The results of the Lending Survey for the third quarter point to further net tightening of overall credit conditions and further net increase of demand for corporate loans.



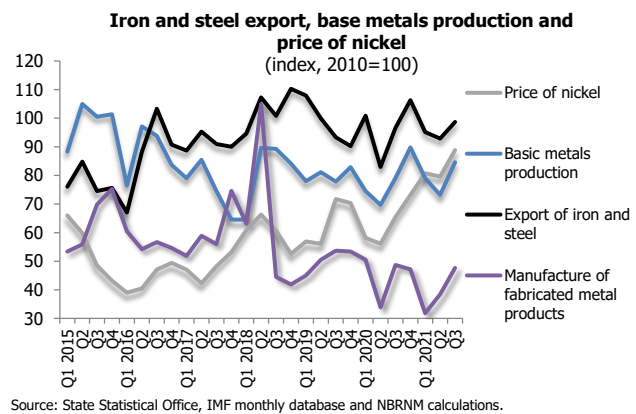
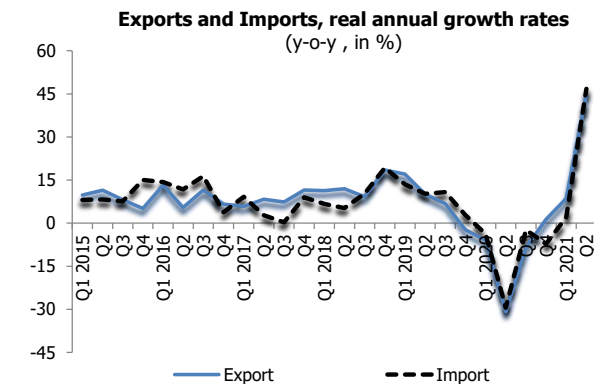
1.3.4. Net external demand

After two quarters of positive contribution, the net export in the second quarter of 2021 had a negative contribution to the GDP, amid higher growth of import than export. However, both components registered accelerated annual growth, which is partly due to low base effect. Thus, the export registered a high annual growth of 45.0% (quarterly growth of 0.4%). The enhanced export activity in part of the export-oriented capacities from the automotive industry had the largest positive contribution for the growth, as well as the improved performances in export of iron and steel, driven by more favorable price situation. Therefore, the export is a component with the highest positive individual contribution to the GDP in this quarter. Amid growth in domestic demand and export, the import registered a significant annual growth of 46.7% (amid quarterly growth of 7.3%).

¹⁵ Data on the completed construction works are as of July 2021, while data on long-term corporate loans, government capital investments, Industrial output, and imports of investment goods and domestic production of capital goods refer to the period July-August 2021.



Foreign trade data in the period July-August 2021 indicate possible deficit expansion in the third quarter of the year compared to the same period last year, amid higher growth of the import than the export of goods.

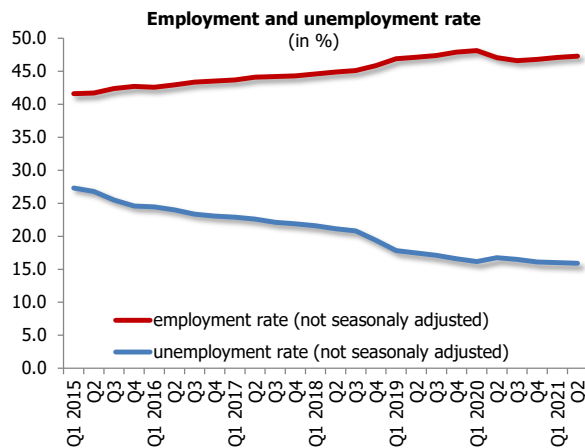


1.4. Employment and wages

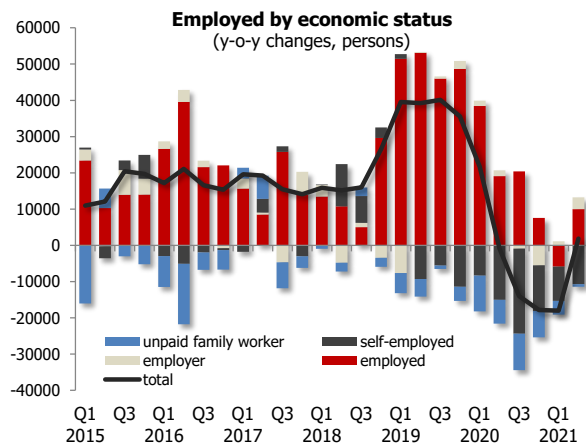
Labor market developments, during the second quarter of 2021, indicate gradual improvement of the situation in this segment of the economy, under the influence of stabilization of the epidemiological condition and initialized mass immunization. Thus, the number of employees registered a slight annual growth of 0.2% since the beginning of the pandemic. At the same time, the number of unemployed decreased by 5.9%, which contributed to further decrease of the unemployment rate, which reduced to 15.9%. Such movements also affected the labor supply, by slower decrease of the active population, which is a trend since the beginning of the COVID-19. The business tendency Surveys point to improved expectations from the managers of companies regarding the new employments in the third quarter of 2021, compared to expectations for the previous quarter, also expecting positive trends to continue in the following period, yet at a more moderate pace. The competition indicators also registered more favorable shifts, so the labor productivity registered an accelerated growth in the second quarter, while unit labor costs registered a decrease, after five years of continuous growth.

The labor market shows signs of gradual recovery from the consequences of the health and economic crisis caused by the COVID-19 pandemic. Namely, the number of employees increased in the second quarter of 2021 (by 0.2% on an annual basis and by 1.3%¹⁶ on a quarterly basis), following a steady decline in the previous four quarters. Analyzed by individual activity, the activities related to "health and social work", "information and communication", "trade", "public administration and defense", "education", and "professional scholar and technical activities" have the largest contribution to the growth of employment. However, activities related to "accommodation facilities and catering services", "agriculture", as well as activities related to "arts, entertainment and recreation" continue to make pronounced negative contribution. Regarding the economic status, the increased number of employees is explained with the growth in the categories "employees" and "employer", while "own account workers" and "unpaid family workers" still show negative movements.

¹⁶ Analysis of quarterly dynamics of employment, unemployment and total active population is made by using seasonally adjusted data.



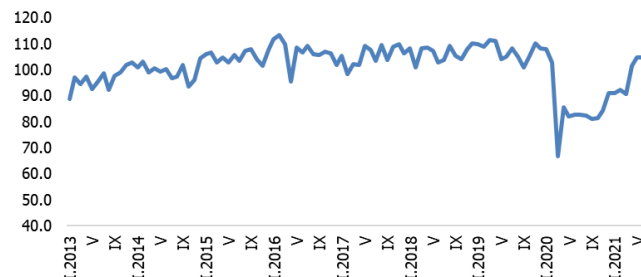
Source: State Statistical Office, Labour Force Survey.



Source: State Statistical Office, Labour Force Survey.

In the second quarter of 2021, the employment rate amounted to 47.3%, which is an annual growth of 0.2 percentage points, according to the growth in the number of employees. The aggregated signals from business tendencies surveys¹⁷ generally indicate a growing optimism among the managers from business entities regarding the expectations for employment in the third quarter of 2021, amid stabilization of the third pandemic wave, as well as enhanced immunization in the country. On the other hand, according to the surveys conducted in August, certain decrease of the optimism is noted regarding the expectations for increased number of employees in the next period in accordance with the spread of the fourth pandemic wave related to delta variant of COVID-19.

Employment expectations indicator*
(composite indicator of employment expectations, seasonally adjusted)



Source: European Commission, Business and consumer surveys.

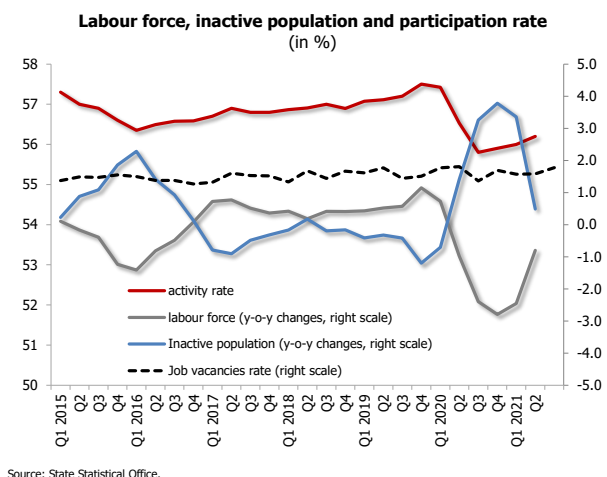
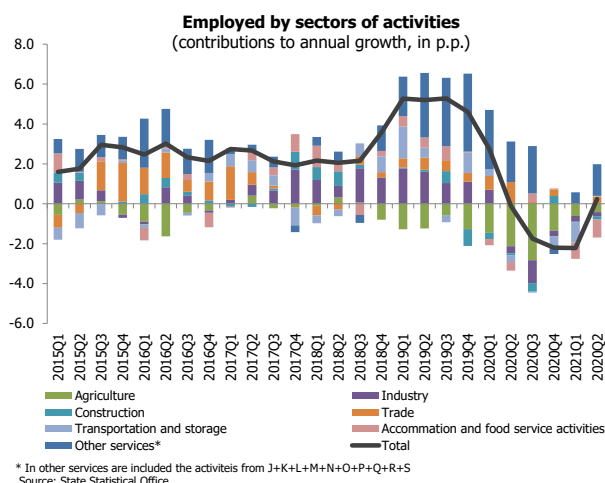
*Managers employment expectations for the next 3 months in the companies in the four sectors: industry, services, retail trade and construction.

In the second quarter of 2021, the job vacancy rate¹⁸ equals 1.8% (1.4% in the same quarter of 2020). The job vacancy rate has been relatively stable over a long period, which points to possible improvement of the connection process of the supply with the demand for skills in the labor market.

¹⁷ Source: European Commission for business trends, expectations for employments in the next 3 months in industry, services, retail trade and construction (Surveys conducted in July, August and September 2021).

¹⁸ 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 placement of these two indicators gives information on labor market performance in terms of potential mismatches between demand profiles and those available on the job market at a given moment (skill mismatches). In particular, if both indicators are moving simultaneously, they are temporary, cyclical fluctuations, while in the case of the unemployment rate decreasing, with a stable vacancy rate, these are structural changes that is, improving the efficiency of the labor market.

Analyzed by activities, the highest vacancy rates are generally registered in activities which are mostly affected by the pandemic, activities that require digital skills, as well as activities which register continues growth of their activity. Thus, the highest vacancy rates are registered in "accommodation facilities and catering services" (4.6%), "mining and quarrying" (4.6%), "information and communications" (3.4%), "administrative and ancillary services" (3.1%), "transport and storage" (2.8%), as well as "construction" (2.7%).



Similar to demand, the supply of labor force in the second quarter also registered a gradual improvement. Namely, total active population in the second quarter registered a slight decrease of 0.8% on an annual basis, which is a significant slowdown compared to the annual decline in the previous quarter (2.5%). According to this, the activity rate was also improved, and in the second quarter amounted to 56.2% (56% in the previous quarter).

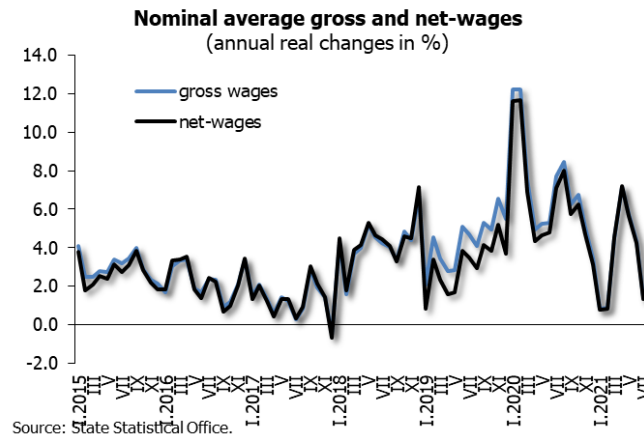
The small rise in the demand amid further, albeit significantly slower decline in supply of labor force in the second quarter of 2021 resulted in further fall in unemployment. Thus, the number of unemployed in the second quarter decreased by 5.9% annually, while the unemployment rate reduced to 15.9% (annual and quarterly fall of 0.8 and 0.1 percentage points, respectively). Such movement of the unemployment rate is a result of the positive movements in the number of employees, as well as the further increase of the inactive population, yet at a significantly slower pace (growth of 0.5% compared to the growth of 3.4% in the previous quarter).

The average paid net and gross wages in the second quarter registered further annual growth. Thus, the net and gross wages in the second quarter registered an annual growth of 8.6% and 8.7%, respectively (growth of 4% in the previous quarter, respectively). The growth of wages and their acceleration is partly a result of comparative basis due to the initial effect in the beginning of the pandemic and partly of the increase of the minimum wage by 1.7% in April 2021, according to the regular legal adjustment¹⁹ complemented with the low base effect, due to postponement of the regular adjustment of the minimum wage last year²⁰. Analyzing the labor market, these movements of wages stem from certain structural factors, such as the non-compliance between the labor supply and demand (additionally pronounced in the pandemic when the rate of inactivity also grows), and hence the lack of labor in certain segments, also as an effect of the crisis which is pronounced through the decrease in the number of

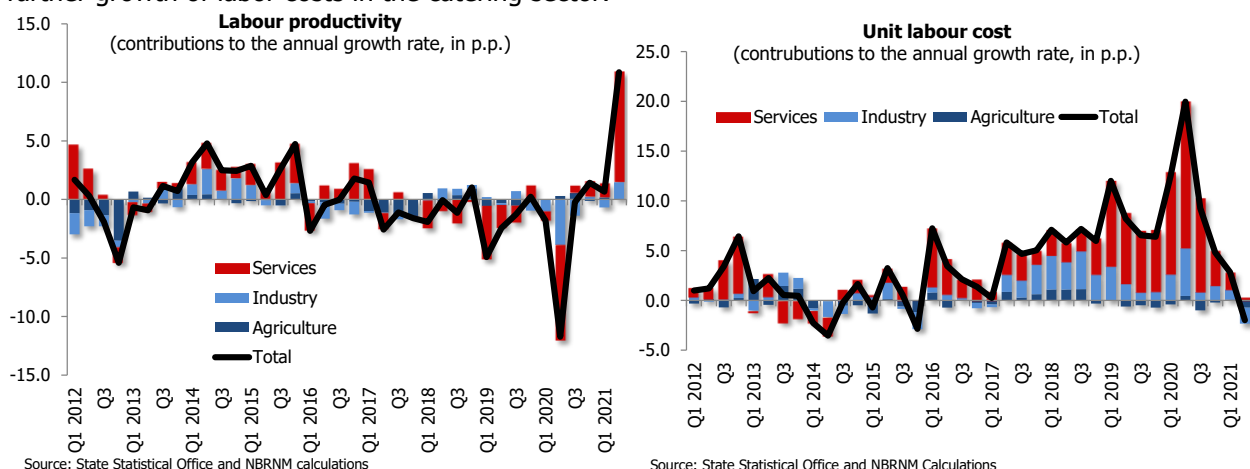
¹⁹Regular adjustment for increasing the minimum wage (with the increase for the previous year of the average wage paid in the RNM, the consumer price index and the real GDP growth-one third of the growth of each indicator, respectively) was made in April 2021. According to the announcement of the Ministry of Labor and Social Policy, published in the Official Gazette of the Republic of North Macedonia No. 80/21 enforcing the Law on Minimum Wage in the Republic of Macedonia Official Gazette of the Republic of North Macedonia No. 12.30/14, 180/14, 81/15, 129/15, 132/17 and 140/18 and Official Gazette of the Republic of North Macedonia No. 124/19 and 239/19), the minimum net wage increased by Denar 260 or 1.7%. The minimum wage in gross amount, starting from April 2021 to March 2022 is Denar 22,146 (previously Denar 21,776), i.e. the minimum wage in net amount is Denar 15,194 (previously Denar 14,934).

²⁰The adjustment of the minimum wage with an increase of 3% was made in July 2020 instead in April 2020.

employees with wage lower than the average. Therefore, analyzed by activities, an annual growth of wages was registered in activities which were mostly affected by the tough measures last year, introduced in the beginning of the pandemic, such as "art, entertainment and recreation", "accommodation facilities and catering services", professional, scientific and technical activities", "trade", "manufacturing industry", as well as "transport and storage". There is a significant growth in "information and communication" due to the large demand for digitalization. Amid growth in consumer prices of 2.8%, **the real annual growth of net and gross wages in the second quarter amounted to 5.7%**. In July 2021, the nominal annual growth of the average net wage decelerated and amounted to 4.8%. This wage dynamics is primarily due to the base effect, given that the recovery of wages continued last year in July, after the initial effect in the beginning of the pandemic, due to the tough measures, amid simultaneous depletion of the base effect of the delayed increase in minimum wage in July 2020.



The labor productivity²¹ continued to improve in the second quarter of 2021, registering a significant growth rate of 10.9% (an increase of 0.7% in the previous quarter). The growth of productivity in the second quarter is a result of significant growth of the economic activity compared to the increase in employment. Analyzed by sectors, the growth of productivity mostly stems from the service sector, complemented by productivity growth in industry. **The unit labor costs registered an annual decline of 2%, after a five-year consecutive growth (growth of 2.8% in the previous quarter)**. The decline in labor costs is due to the higher productivity growth than the growth of gross wages. Therefore, most of the decrease in unit labor costs is explained with the lower costs in industry and agriculture, amid further growth of labor costs in the catering sector.



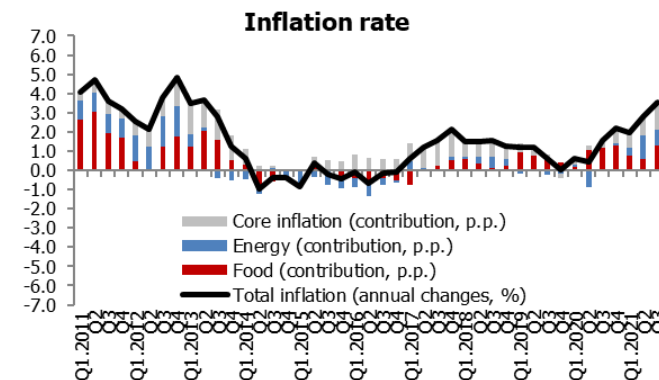
²¹ Total labor productivity is a weighted sum of productivity of each sector. Sector productivity is the ratio of the sector's value added to the number of employees.

1.5. Inflation

Domestic consumer prices in the third quarter of 2021 rose by 3.5% annually, which compared to the previous quarter, is a moderate acceleration of the annual inflation rate. Annual increase in prices was registered in all three main components of the inflation index. In the first nine months of the year, the annual inflation rate averaged 2.8%. Moderate upward inflationary movements are driven by supply side factors such as food and energy prices on world stock markets, transmitted effect of last year's administrative and regulatory increase in prices as well as pandemic-specific factors amid relaxation of containment measures. Regarding the factors likely to affect future short-term rate of consumer prices, there is still an acceleration of the growth rate of domestic producer prices and foreign imported inflation, which are currently assessed as temporary, while unit labor costs went down in the second quarter of 2021, after years of steady growth. In the absence of pressures from domestic demand, these factors, as before, are not expected to cause more serious prolonged upward pressures on the prices of final products. Regarding the inflation expectations in the period ahead, according to the National Bank Survey, economic analysts expect an inflation rate of 2.8% this year, and subsequent moderate slow down to 2.5% in 2022 and to 2.3% in 2023. Such expectations are generally in line with the National Bank forecasts, as well as the expectations of international institutions.

1.5.1. Current inflation

In the third quarter of 2021, the annual inflation rate was 3.5% (2.8% in the previous quarter)²². The acceleration of consumer price growth in this period was mainly driven by the increased contribution of food and core inflation. The energy component also made a positive contribution, although it is slowing down due to the exhaustion of the transmitted effect of the increase in the price of electricity in August last year, amid further annual growth of oil derivatives prices, which follow the price movement on world stock markets. In general, the rise in domestic prices reflects changes driven by food and energy prices on world stock markets, transmitted effects of last year's administrative and regulatory changes, as well as changes in demand and supply-side constraints during the pandemic.



Source: State statistical office and NBRNM calculations.

²² On a quarterly basis, domestic consumer prices increased by 1.4%, and by 1.5% seasonally adjusted.



Core inflation in the third quarter was 2.9% on an annual basis (2% in the previous quarter). The growth, as well as the mild acceleration of the core inflation is primarily a result of the higher air traffic prices, in accordance with the increased international travel amid smaller containment measures. This effect is complemented by the higher restaurant and hotel services prices, which in part is related to the reduced capacity due to the containment measures, the continued positive contribution of tobacco prices as a result of regulatory amendments²³, and less to the prices of pharmaceutical products, cars, footwear, as well as IT equipment. The other inflation sub-indices, which exclude the most volatile prices, also increased in the third quarter of 2021, with a moderate acceleration compared to the previous quarter. Thus, the total index, excluding energy²⁴, liquid fuels and lubricants (for transport) and unprocessed food registered an annual growth of 2.9% (2.2% in the previous quarter), while the total index excluding energy, liquid fuels and lubricants (for transport), unprocessed food, tobacco and alcoholic beverages registered an annual growth of 2.8% (2.1% in the previous quarter).

| | (annual changes, in %) | | | | | | | | | (contributions to annual changes, in p.p.) | | | | | | | | |
|--|------------------------|------|-------|-------|-------|-------|------|------|------|--|-----|------|------|------|------|------|-----|-----|
| | 2019 | Q1 | 2020 | Q3 | Q4 | 2020 | 2021 | Q2 | Q3 | 2019 | Q1 | 2020 | Q2 | Q3 | 2020 | 2021 | Q2 | Q3 |
| Consumer price index - all items | 0.8 | 0.6 | 0.5 | 1.5 | 2.2 | 1.2 | 2.0 | 2.8 | 3.5 | 0.8 | 0.6 | 0.5 | 1.5 | 2.2 | 1.2 | 2.0 | 2.8 | 3.5 |
| Food | 1.9 | 0.5 | 2.9 | 3.3 | 3.6 | 2.6 | 2.1 | 1.5 | 3.6 | 0.7 | 0.2 | 1.0 | 1.2 | 1.3 | 0.9 | 0.7 | 0.6 | 1.3 |
| Energy | -1.1 | 0.7 | -6.3 | -0.5 | 0.6 | -1.4 | 3.1 | 9.9 | 6.0 | -0.2 | 0.1 | -0.8 | -0.1 | 0.1 | -0.2 | 0.4 | 1.3 | 0.8 |
| Electricity | 0.0 | 0.0 | 0.0 | 4.9 | 7.4 | 3.1 | 7.4 | 7.4 | 2.4 | 0.0 | 0.0 | 0.0 | 0.4 | 0.5 | 0.2 | 0.5 | 0.5 | 0.2 |
| Heat energy | -4.3 | -6.4 | -6.4 | -2.2 | 0.0 | -3.8 | 0.0 | 0.0 | -2.7 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Fuels and lubricants | -3.2 | 3.4 | -22.8 | -11.8 | -12.9 | -11.3 | -3.5 | 25.3 | 20.0 | -0.1 | 0.1 | -0.8 | -0.4 | -0.5 | -0.4 | -0.1 | 0.7 | 0.6 |
| Food and energy (volatile prices) | 1.0 | 0.6 | 0.4 | 2.3 | 2.8 | 1.5 | 2.3 | 3.6 | 4.2 | 0.5 | 0.3 | 0.2 | 1.1 | 1.4 | 0.7 | 1.1 | 1.8 | 2.1 |
| Core inflation calculated by the NBRM (total index - food and energy (categories 01.1, 04.5, 07.2.2)) | 0.5 | 0.7 | 0.5 | 0.8 | 1.6 | 0.9 | 1.6 | 2.0 | 2.9 | 0.3 | 0.4 | 0.3 | 0.4 | 0.8 | 0.5 | 0.8 | 1.0 | 1.5 |
| Overall index excluding energy, liquid fuels and lubricants and unprocessed food (SSO) | 0.8 | 1.7 | 1.7 | 1.6 | 2.1 | 1.8 | 1.9 | 2.2 | 2.9 | | | | | | | | | |
| Overall index excluding energy, liquid fuels and lubricants, unprocessed food, tobacco and alcoholic beverages (SSO) | 0.5 | 1.4 | 1.5 | 1.4 | 1.7 | 1.5 | 1.5 | 2.1 | 2.8 | | | | | | | | | |

Source: State Statistical Office and NBRM calculations.

In the third quarter of 2021, **food prices** registered an annual growth of 3.6% (1.5% in the previous quarter). This acceleration of the food prices growth is mainly explained by the higher prices of vegetables, which may be partly related to the lower supply due to unfavorable summer conditions. Analyzing the structure, the annual food prices growth mainly arises from the vegetable prices, as well as the prices of oil and fat and the prices of bread and cereals, caused by the surge in oil and cereal prices on world markets. In the third quarter of 2021, foreign effective food prices also grew at a slightly faster pace, amid moderate acceleration of the growth of sales prices of domestic food producers²⁵. In the third quarter, **energy prices** continued to grow, slower though, primarily due to the exhaustion of the transmitted effect of the regulatory increase in the domestic price of electricity in August 2020²⁶, with a small contribution of the reduction of the price of central heating²⁷. On the other hand, the annual growth of oil derivative prices continued in line with the upward movements in oil price on the world markets.

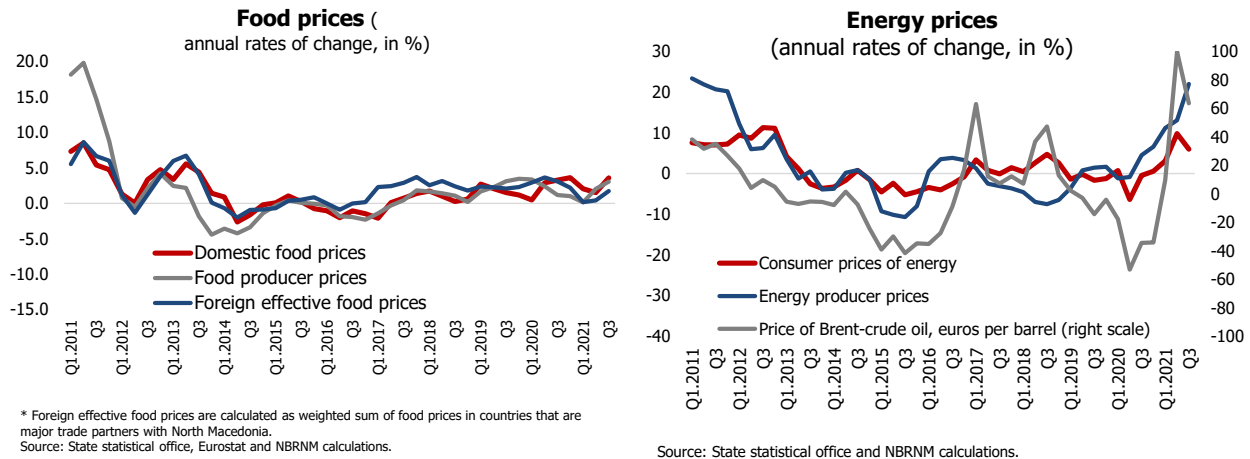
²³ The increase was caused by the amendments to the Law on Tobacco and Tobacco Products which require all packs of cigarettes to have 20 cigarettes by November 2020 (previously there were packs of 19 cigarettes), which together with the increased excise charged per cigarette rose producer costs. Additionally, the annual growth of tobacco price reflects the increase in cigarette prices in July 2021, in line with the annual scheduled increase in cigarette excise duties by Denar 0.20 per piece as of 1 July 2023.

²⁴ The energy category includes electricity, gas, liquid and solid fuels for heating and central heating.

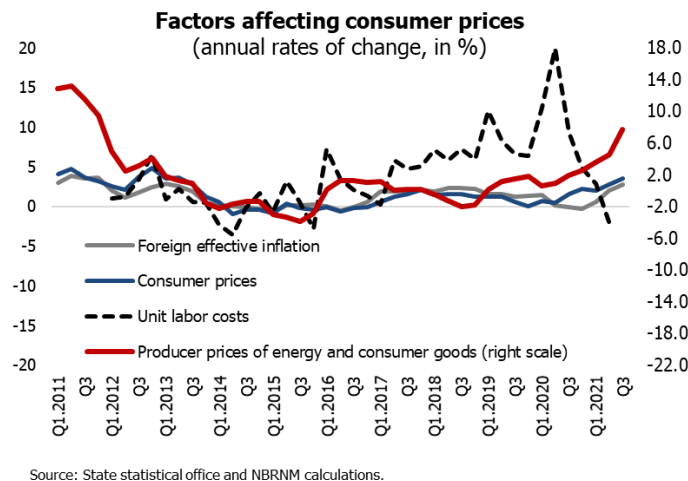
²⁵ The analysis of sales prices of domestic food producers and foreign effective food prices refers to the first two months of the third quarter.

²⁶ On 29.07.2021, the Energy Regulatory Commission adopted a decision to reduce heating price by 4%, i.e. as of 1 August, the heating tariff for households and educational institutions will be Denar 1.8498/ kWh, while for other consumers this tariff will be Denar 2.5898/kWh.

²⁷ On 29.07.2021, the Energy Regulatory Commission adopted a decision to reduce heating price by 4%, i.e. as of 1 August, the heating tariff for households and educational institutions will be Denar 1.8498/ kWh, while for other consumers this tariff will be Denar 2.5898/kWh.



Producer prices of industrial products continued to increase at a faster pace of 9.8% on an annual basis in the third quarter (6.2% in the previous quarter) mainly due to higher metal prices on world stock markets. Also, **producer prices of energy and consumer goods**, as an aggregate category, registered an annual growth of 7.7% (4.5% in the previous quarter)²⁸. **Foreign effective inflation**²⁹, as an indicator of imported inflation, accelerated in the third quarter to 2.8% (2.0% in the previous quarter). On the other hand, after years of continuous growth, in the second quarter of 2021, **unit labor costs** registered an annual decline of 2% (growth of 2.8% in the previous quarter). Given the estimates for a moderately positive output gap³⁰ in the domestic economy, the movement of these factors is not expected to create serious and long-term upward pressures on domestic prices of final products in the future.



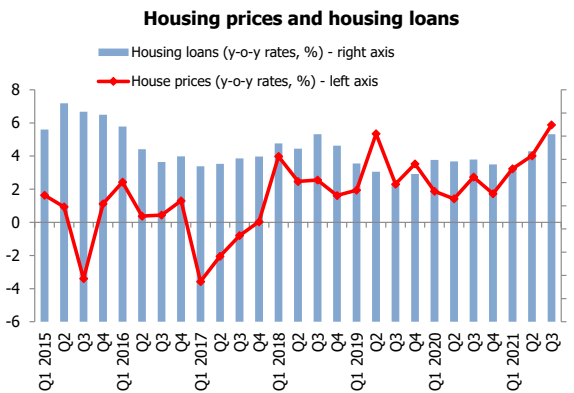
²⁸ The analysis of producer prices of industrial products and producer prices of energy and consumer goods refers to the first two months of the third quarter of 2021.

²⁹ 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 2010-2012. The calculation of this indicator includes Bulgaria, Germany, Greece, France, Italy, Austria, Slovenia, Croatia and Serbia.

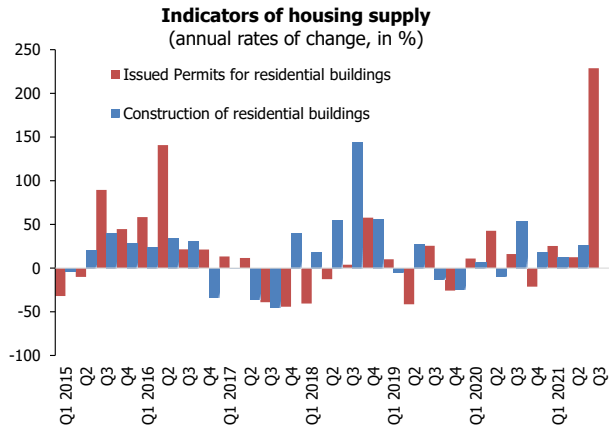
³⁰ The National Bank assessments show that domestic output is above potential (moderate positive output gap) in the period 2021-2023.



In the third quarter of 2021, apartment prices as measured by the Hedonic index³¹ increased annually by 5.9%, which is a moderate acceleration, compared to the previous quarter (4%). Observing the supply, the value of residential buildings increased rapidly in the second quarter of 2021, while the available data on the value of issued building permits in the third quarter of 2021 indicate a significant increase³², on an annual basis. Analyzing housing demand, it is still supported by loans, given the accelerated growth of housing loans³³.



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 future price movement, most of the domestic and international institutions expect moderate acceleration of the inflation rate in the current year and gradual stabilization in the next two years. Compared to previous forecasts, they are slightly higher, primarily due to supply-side factors and continued pressure from primary commodity prices, amid expectations for further recovery of economic activity, both globally and in the domestic economy. Similar are the expectations of the economic analysts expressed in the **Inflation and Real GDP Expectations Survey**³⁴ conducted in September, according to which, they expect moderate inflation acceleration to 2.8% in 2021, followed by a moderate slow down to 2.5% in 2022 and 2.3% in 2023. Compared to the expectations expressed in the survey conducted in June, they are slightly higher (in June, inflation was expected to be 2.3% in 2021 and 2.1% and 2% in the next two years).

³¹ 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 arising from the size of the apartment, the location, the floor, whether the apartment has central heating and whether the apartment is new.

³² The analysis refers to the first month of the third quarter of 2021.

³³ Available data for the first two months of the quarter.

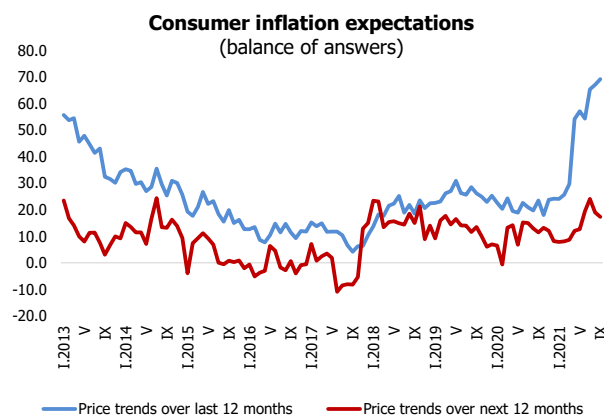
³⁴ In October 2017, the National Bank modified its Inflation Expectations Survey. The new Inflation and Real GDP Expectations Survey is conducted on a sample of economic analysts, extending the Survey subject in line with the practice of the European Central Bank (ECB).

Forecasts and expectations for the inflation rate

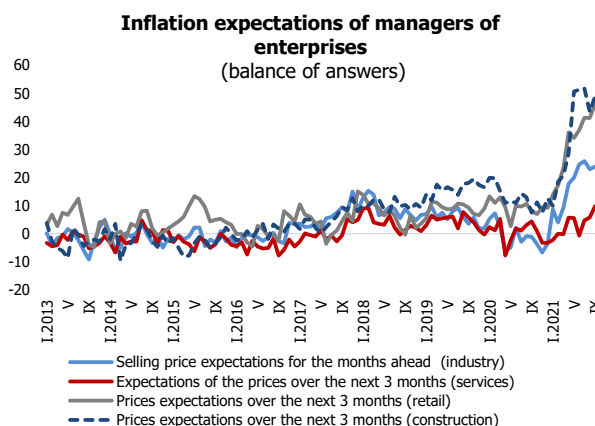
| | 2021 | 2022 | 2023 |
|---------------------|------|------|------|
| Economic analysts | 2.8 | 2.5 | 2.3 |
| IMF | 3.1 | 2.2 | 1.5 |
| Consensus Forecast | 2.3 | 2.0 | / |
| Ministry of Finance | 3.0 | 2.4 | 2.0 |
| NBRNM | 3.1 | 2.4 | 2.0 |

Source: Inflation and real GDP growth expectations survey, September 2021; IMF World Economic Outlook, October 2021; Consensus Forecast, September 2021; Ministry of Finance, Fiscal Strategy 2022-2024, May 2021; and NBRNM, October 2021.

Similar are the short-term expectations of consumers and corporate executives for the price movements expressed in surveys in the third quarter of 2021. Thus, according to the **consumer expectations for price changes in the next 12 months**³⁵, those who expect an increase in prices in the next 12 months exceed those who expect them to reduce or remain unchanged. Analyzing the expectations in the **corporate sector**³⁶, this quarter the executives of construction and retail trade companies expect an increase in prices of their products in the next three months as well. The executives of industrial and service businesses also expect prices to increase, but moderately.



Source: European Commission.



Source: European Commission.

1.6. Balance of payments

In the second quarter of 2021, current account deficit remained almost identical to the level of the same period last year, amid further recovery of the export sector and functioning of production chains that include part of domestic export capacity. However, the balance of goods tended to widen the current account deficit, due to the faster growth of imports than exports. Primary income deficit acted in the same direction, which on an annual basis increased in line with the estimates for more favorable performance of the foreign capital companies for this year. On the other hand, given the gradual opening of the economy and relaxation of the restrictive measures, there was an increase in inflows from exchange operations, with a favorable effect on the secondary income balance. In this quarter, services balance also registered positive movements. Within the financial account, the second quarter registered net inflows, which mostly result from net inflows from direct investments, and less

³⁵ European Commission's Consumer Survey as of September 2021.

³⁶ European Commission's business tendency surveys in industry, retail trade, construction and services sector as of September 2021.



from loans. Changes in the balance of payments enabled growth of foreign reserves in the second quarter, thus keeping them in the safe zone.

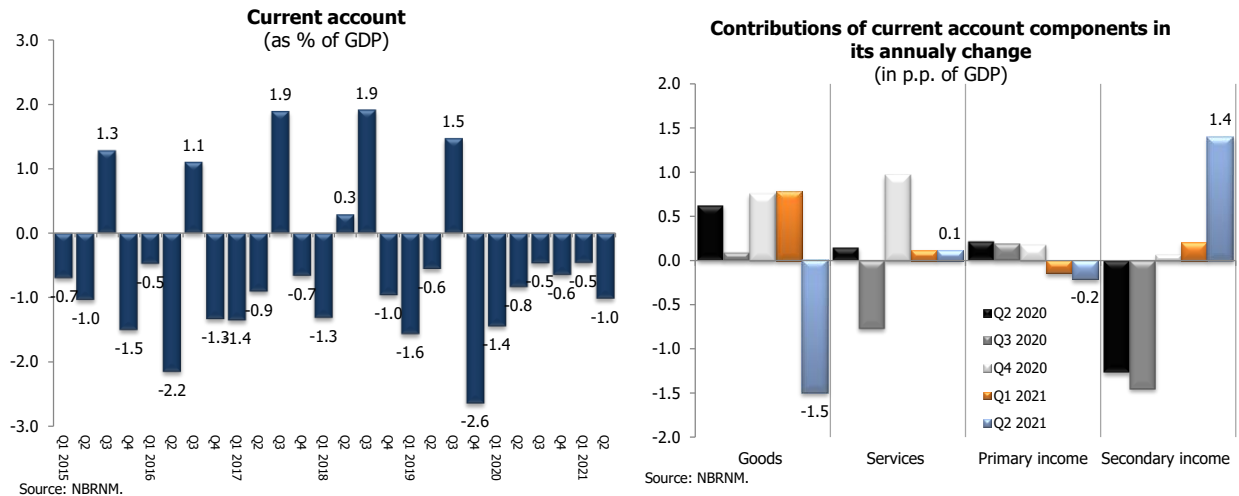
| | 2020 | | | | | | 2021 | | | 2020 | | | | | | 2021 | | |
|---|---------------------|--------|--------|--------|---------------|----------------|--------|--------|----------------|----------|------|------|------|-------------|--------------|------|------|-------------|
| | q1 | q2 | q3 | q4 | I-VI | I-XII | q1 | q2 | I-VI | q1 | q2 | q3 | q4 | I-VI | I-XII | q1 | q2 | I-VI |
| | In millions of euro | | | | | | | | | % of GDP | | | | | | | | |
| I. Current account | -155.7 | -90.0 | -50.6 | -69.9 | -245.7 | -366.2 | -54.7 | -120.0 | -174.7 | -1.4 | -0.8 | -0.5 | -0.6 | -2.3 | -3.4 | -0.5 | -1.0 | -1.5 |
| Goods and services | -382.4 | -246.7 | -321.2 | -427.9 | -629.1 | -1378.2 | -311.8 | -433.1 | -744.9 | -3.6 | -2.3 | -3.0 | -4.0 | -5.8 | -12.8 | -2.6 | -3.7 | -6.3 |
| Credit | 1515.0 | 1175.1 | 1718.8 | 1855.4 | 2690.1 | 6264.2 | 1798.9 | 1903.8 | 3702.7 | 14.1 | 10.9 | 16.0 | 17.2 | 25.0 | 58.2 | 15.2 | 16.1 | 31.3 |
| Debit | 1897.4 | 1421.8 | 2039.9 | 2283.3 | 3319.2 | 7642.4 | 2110.7 | 2337.0 | 4447.7 | 17.6 | 13.2 | 18.9 | 21.2 | 30.8 | 71.0 | 17.9 | 19.8 | 37.6 |
| Goods | -545.2 | -351.9 | -402.0 | -505.5 | -897.1 | -1804.6 | -505.2 | -563.0 | -1068.1 | -5.1 | -3.3 | -3.7 | -4.7 | -8.3 | -16.8 | -4.3 | -4.8 | -9.0 |
| Services | 162.9 | 105.2 | 80.9 | 77.6 | 268.0 | 426.5 | 193.4 | 129.8 | 323.2 | 1.5 | 1.0 | 0.8 | 0.7 | 2.5 | 4.0 | 1.6 | 1.1 | 2.7 |
| Primary income | -100.7 | -99.4 | -104.7 | -106.7 | -200.1 | -411.5 | -127.2 | -133.7 | -261.0 | -0.9 | -0.9 | -1.0 | -1.0 | -1.9 | -3.8 | -1.1 | -1.1 | -2.2 |
| Secondary income | 327.3 | 256.1 | 375.2 | 464.8 | 583.4 | 1423.4 | 384.3 | 446.9 | 831.2 | 3.0 | 2.4 | 3.5 | 4.3 | 5.4 | 13.2 | 3.3 | 3.8 | 7.0 |
| II. Capital account | 0.3 | 4.3 | 1.8 | 4.8 | 4.6 | 11.2 | -3.7 | 2.8 | -0.9 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.1 | 0.0 | 0.0 | 0.0 |
| Net lending (+) / net borrowing (-) (balance from current and capital account) | -155.4 | -85.7 | -48.8 | -65.1 | -241.1 | -355.0 | -58.4 | -117.2 | -175.6 | -1.4 | -0.8 | -0.5 | -0.6 | -2.2 | -3.3 | -0.5 | -1.0 | -1.5 |
| III. Financial account | 79.0 | -672.7 | 118.7 | 31.3 | -593.7 | -443.7 | -639.3 | -163.7 | -803.0 | 0.7 | -6.2 | 1.1 | 0.3 | -5.5 | -4.1 | -5.4 | -1.4 | -6.8 |
| Direct investment | -123.2 | 8.6 | 8.2 | -48.3 | -114.6 | -154.7 | 13.9 | -204.0 | -190.1 | -1.1 | 0.1 | 0.1 | -0.4 | -1.1 | -1.4 | 0.1 | -1.7 | -1.6 |
| Portfolio investment | 31.6 | -632.5 | 77.5 | 239.5 | -600.9 | -283.8 | -636.9 | 8.6 | -628.3 | 0.3 | -5.9 | 0.7 | 2.2 | -5.6 | -2.6 | -5.4 | 0.1 | -5.3 |
| Currency and deposits | 71.8 | 130.5 | 175.6 | 111.0 | 202.4 | 489.0 | 27.6 | 120.2 | 147.8 | 0.7 | 1.2 | 1.6 | 1.0 | 1.9 | 4.5 | 0.2 | 1.0 | 1.3 |
| Loans | 113.0 | -166.7 | -80.8 | -134.2 | -53.7 | -268.7 | -18.5 | -145.4 | -163.9 | 1.0 | -1.5 | -0.8 | -1.2 | -0.5 | -2.5 | -0.2 | -1.2 | -1.4 |
| Trade credit and advances | -14.1 | -12.8 | -61.2 | -135.4 | -27.0 | -223.6 | -26.4 | 56.9 | 30.5 | -0.1 | -0.1 | -0.6 | -1.3 | -0.3 | -2.1 | -0.2 | 0.5 | 0.3 |
| Other accounts receivable/payable | 0.0 | 0.1 | -0.2 | -1.1 | 0.1 | -1.2 | 1.1 | 0.0 | 1.2 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Special drawing rights (Net incurrence of liabilities) | 0.0 | -0.1 | 0.0 | 0.0 | -0.1 | -0.1 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| IV. Net errors and omissions | -14.9 | 17.0 | 13.7 | 10.1 | 2.1 | 25.9 | 30.6 | 48.1 | 78.7 | -0.1 | 0.2 | 0.1 | 0.1 | 0.0 | 0.2 | 0.3 | 0.4 | 0.7 |
| V. Reserve assets | -249.3 | 604.0 | -153.8 | -86.3 | 354.7 | 114.6 | 611.5 | 94.5 | 706.1 | -2.3 | 5.6 | -1.4 | -0.8 | 3.3 | 1.1 | 5.2 | 0.8 | 6.0 |

Source: NBRNM.

1.6.1. Current account

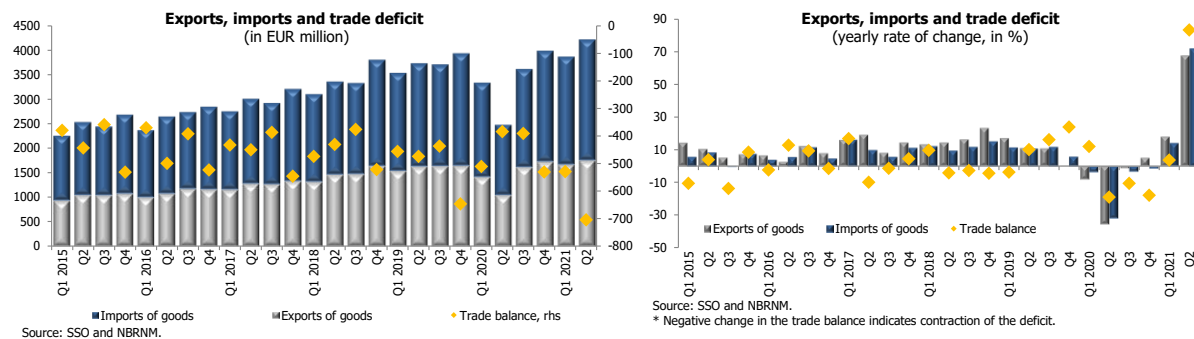
In the second quarter of 2021, current account deficit was Euro 120 million or 1.0% of GDP³⁷. The analysis on an annual basis indicates a slightly higher current account deficit (by 0.2 percentage points of GDP), which largely stems from the balance of goods, as well as the balance of primary income. The faster import to export growth contributed to a higher deficit in the balance of goods amid further recovery of the total foreign trade, amid expansion of both non-energy and energy balance. The widening of non-energy balance deficit is largely due to higher raw material imports for industry, while higher prices and higher volume of imports deteriorated the energy balance. The primary income also had an adverse effect on current account balance amid estimate of a larger amount of newly created profit compared to last year, and thus a larger deficit in investment income. The secondary income balance acted in the opposite direction in conditions of growth of private transfers (higher net inflows from exchange operations) and higher government transfers as well as a slight improvement in the services balance mainly due to increased surplus in telecommunications, computer and information services as well as in other business services.

³⁷ The calculations use the nominal GDP forecast (from October 2021).



Annex: Foreign trade in goods and movement of the Nominal and the Real Effective Exchange Rate (NEER and REER)³⁸

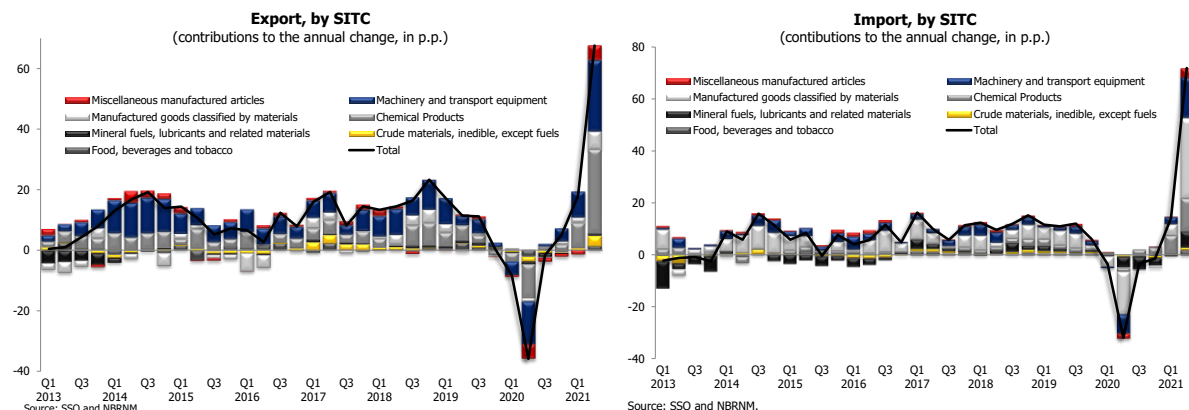
In the second quarter of 2021, foreign trade amounted to Euro 4,200.6 million or 35.5% of GDP, which is an upsurge of Euro 1,731.1 million or 12.6 percentage points of GDP compared to the second quarter of the previous year, when the adverse effect of the pandemic on foreign trade was the strongest, mostly due to strict restrictions and temporary cessation of production chains. The high growth of foreign trade was due to the simultaneous increase of both exports and imports of goods on an annual basis.



The export component in the second quarter grew by 67.6% annually, which is mostly a reflection of the low base effect. In the second quarter of 2020, strict containment measures were introduced almost globally, which caused disruption in supply chains, closure of some production facilities and decline in exports. Analyzing change factors, intensification of exports of foreign automotive companies explains nearly three quarters of annual export growth, which is expected given that this export segment was most affected by the pandemic in the same period last year. The growth was concentrated in the category of chemical substances and products, and machinery and equipment, and to a lesser extent in the export of furniture, all categories that include products of automotive companies. Additionally, the growth of metal prices on world stock markets created favorable conditions for growth of exports of the metal processing industry and ore exports in this quarter. A positive signal is the export recovery in all categories compared to the same period last year. **Import of goods also**

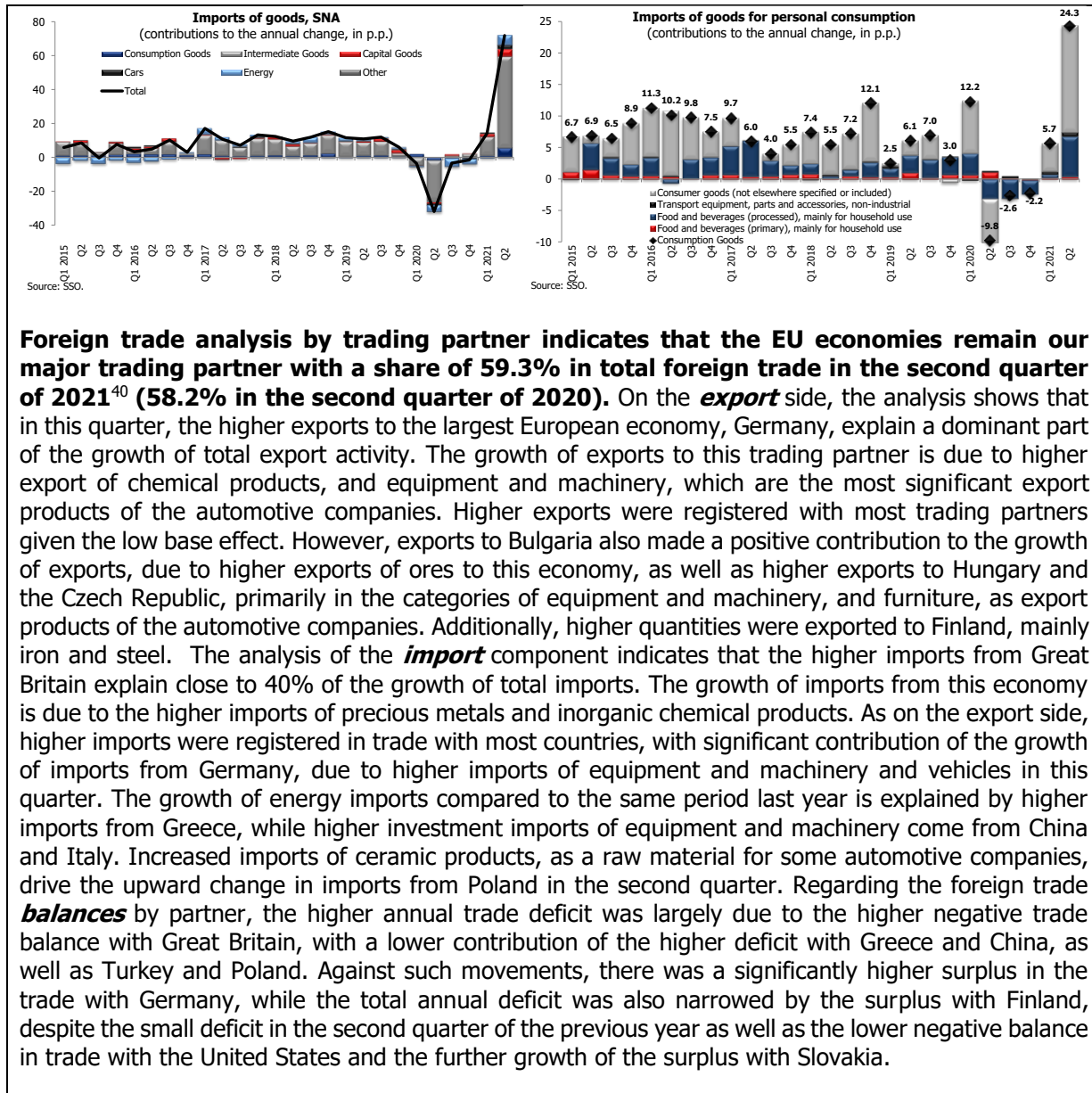
³⁸ According to the Foreign Trade Methodology, data on export of goods are published on an f.o.b. basis, and on import of goods, on a c.i.f. basis.

registered an intensive growth of 71.9% in the second quarter. Here, the low base effect is again the driving factor that explains the highest annual growth of imports so far, as well as the significant upward movement of stock market prices of primary products in this period, especially noticeable in energy, metals and some food products. The highest contribution to the growth of imports was made by the import of non-ferrous metals, followed by the import of equipment and machinery and chemical products, all raw materials relevant for the production and export of the automotive sector. Higher imports compared to the second quarter of 2020 were registered in the other import categories, with a more positive contribution of energy imports, non-metallic minerals products and iron and steel. The growth of energy imports is a combination of the significant growth of energy prices on world stock markets, especially the price of crude oil, which has grown more than twice on an annual basis, as well as higher imported quantities. Namely, the movement restrictions that were most pronounced in the second quarter of 2020 significantly reduced the imported quantities of energy. **The faster growth of import than export of goods in the second quarter widened the trade deficit by 83.4% on an annual basis.** Analyzed by balance, the widening is driven simultaneously by non-energy and energy balances, with a significantly higher contribution of non-energy component. The latest available foreign trade data for July and August 2021 indicate a slower annual growth, which is due to the exhaustion of the base effect. In this period, export growth (13.1%) was more moderate than the import growth and was driven by the export of iron and steel, the export of some of the automotive facilities, as well as the export of ore. The increase in commodity prices on the world stock markets had a positive impact on the metal processing and mining sector of the economy. On the import side, the annual increase of 21.7% was largely due to higher energy imports, as a combination of significantly higher prices and higher quantities of energy imports, amid positive contribution to the import of iron and steel and inorganic chemical products, with some growth slowdown registered in the import of equipment and machinery.

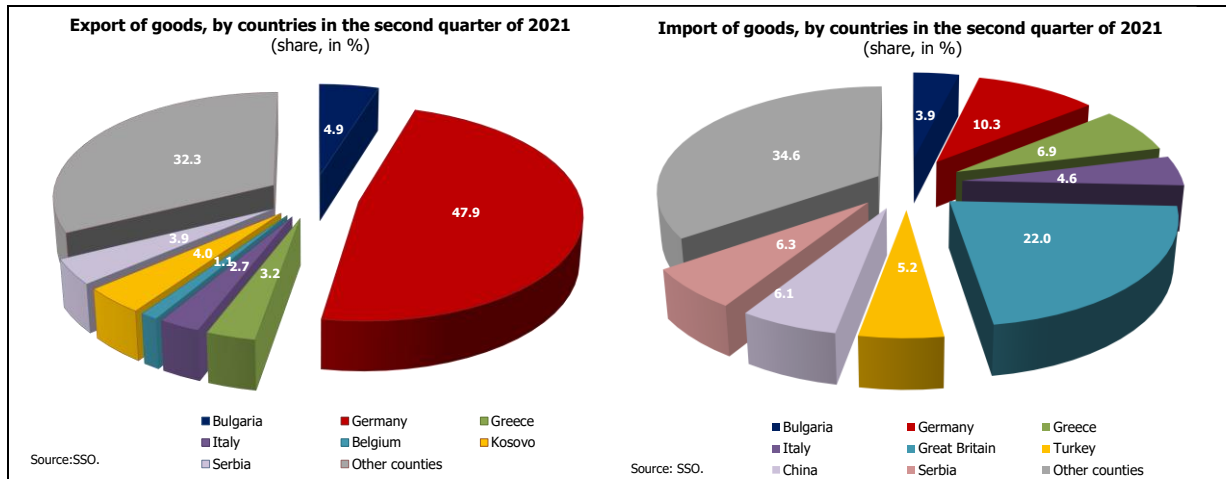


According to the analysis of imports of goods in the Broad Economic Categories - BEC, the growth of imports in the second quarter of 2021 was due to higher non-energy imports, with the highest contribution of categories within the import of intermediate goods. The analysis of import of private consumption goods³⁹ indicates more intensive growth in this component as well, due to the high growth of consumer goods (not elsewhere mentioned) and the increase in imports of processed food and beverages intended for private consumption, with significantly lower contribution of import of passenger vehicles. Analyzed dynamically, import of private consumption goods registered a high annual growth after the moderate increase in the previous quarter, but was also explained by the low base effect and so far does not indicate significant pressures on total imports.

³⁹ 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.

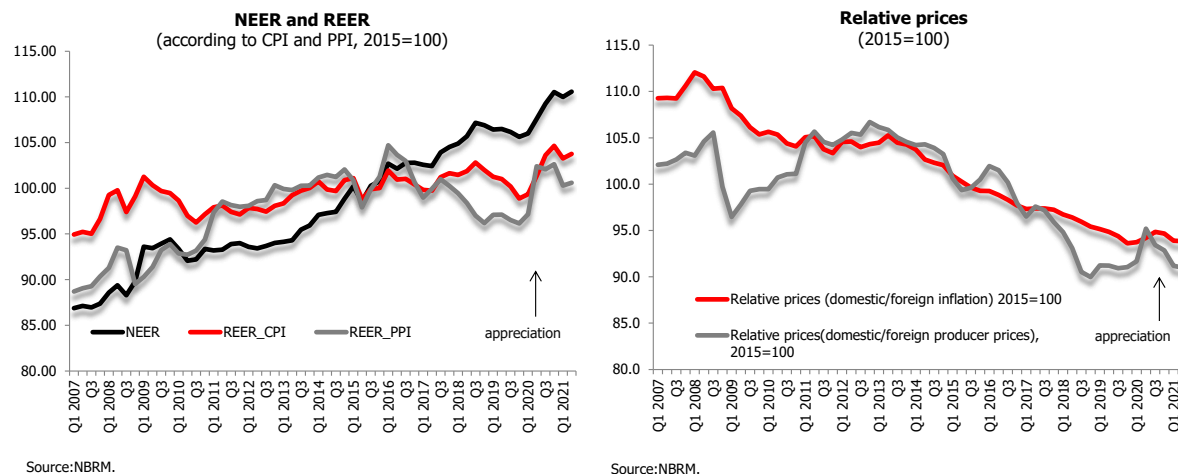


⁴⁰⁴⁰ Taking into account the Brexit, trade data with the European Union do not include trade with this partner. Indicatively, including the Great Britain, the share is 73.1% of total foreign trade, which is an increase of 3.5 percentage points compared to the same period last year.



Price competitiveness indicators of the domestic economy in the second quarter of 2021

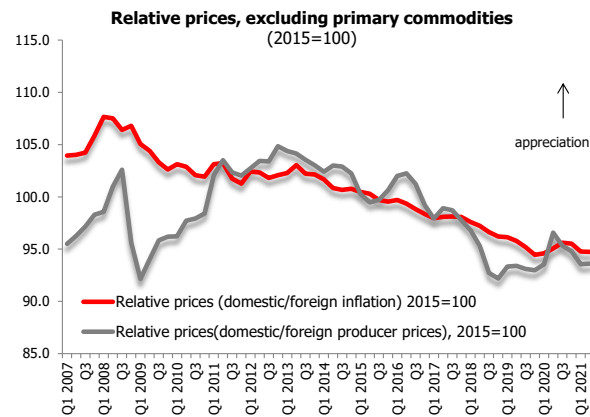
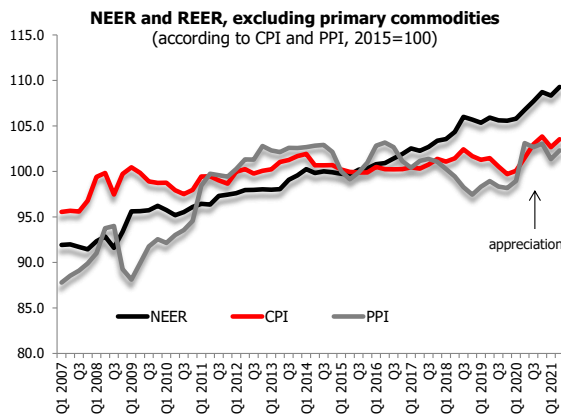
show divergent movements in various indicators on an annual basis. More specifically, the real effective exchange rate deflated by consumer prices continued to register a moderate appreciation of 2.4% compared to the same period of the previous year, while the index deflated by producer prices depreciated on an annual basis by 1.8%, for the first time after six consecutive quarters of growth. The nominal effective exchange rate appreciated by 2.8%, due to the depreciation of the Turkish lira, the Russian ruble and the US dollar against the domestic currency. The positive shifts in relative prices, i.e. the reduction of relative consumer prices by 0.4% on an annual basis and lower producer prices by 4.4% acted in the opposite direction.



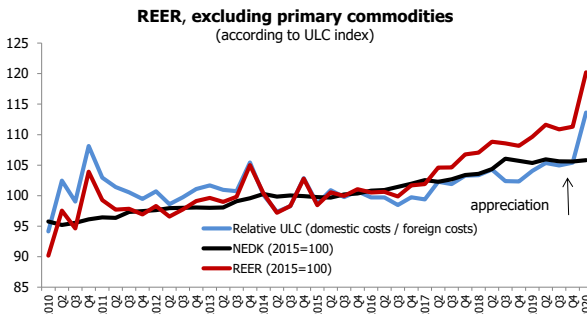
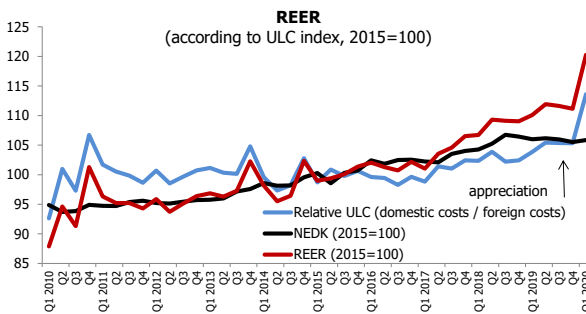
Similar trends were observed in REER indices as measured using foreign trade weights without primary commodities⁴¹. REER deflated by consumer prices appreciated by 2% on an annual basis, while REER deflated by producer prices decreased by 0.8% compared to the same period last year. Such movements were influenced by the appreciation of the nominal effective exchange rate of 2.4% on an annual basis, due to the depreciation of the Turkish lira and the US dollar against the domestic currency. On the other hand, the relative prices dropped on an annual basis by 0.4% in the consumer prices and by 3.1% in the relative producer prices.

⁴¹ Primary products not included in the calculation are: oil and oil derivatives, iron and steel, ores and imported raw materials for the foreign capital facilities. For more detailed information on the methodology for calculating the real effective exchange rate visit: http://nbrm.mk/WBStorage/Files/Statistika_REDK_Informacija_za_promenite_na_metodologijata_za_presmetuvanje_na_realno_t_efektiven_devizen_kurs_na_denarot_mak.pdf

In July-August 2021, while the REER index deflated by consumer prices registered a slight appreciation of 0.6%, the REER index deflated by producer prices depreciated by 1.9%. The movements in the index calculated by weights based on foreign trade statistics without primary commodities acted in the same direction, namely, consumer price index registered an appreciation of 1.1% on an annual basis and producer price index registered a depreciation of 0.5%.



REER indices deflated by unit labor costs indicate an annual appreciation in the second quarter of 2021. REER deflated by total foreign trade increased by 5.4% on annual basis, driven by an increase in the relative labor costs (by 2.8%) and simultaneous appreciation of the nominal effective exchange rate (by 2.6%). Additionally, the index calculated with the weights based on the foreign trade without primary commodities registered a more moderate appreciation of 3.3% on annual basis. Thereby, the shifts were mainly driven by the NEER increase (of 2.4%), amid minor increase of the relative costs (by 0.9%).

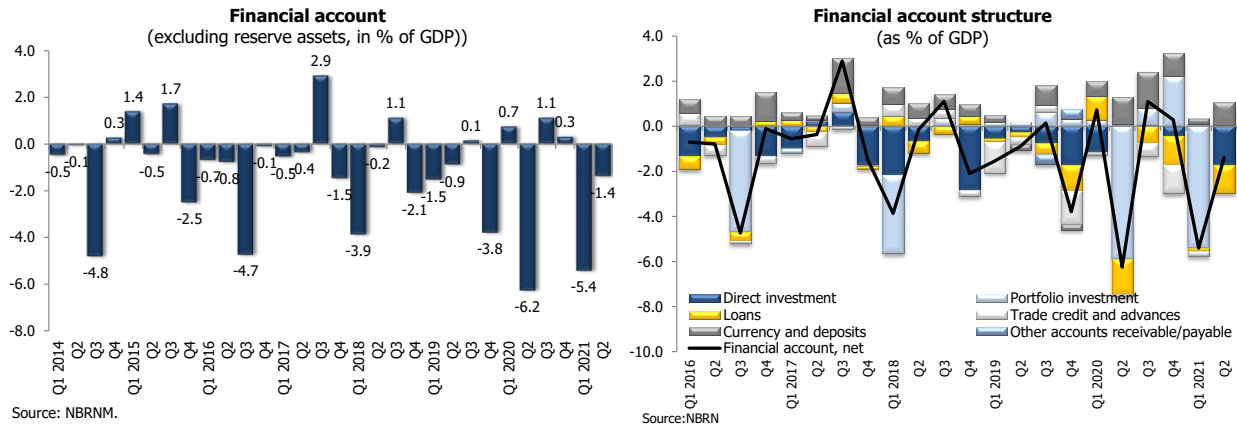


1.6.2. Financial account

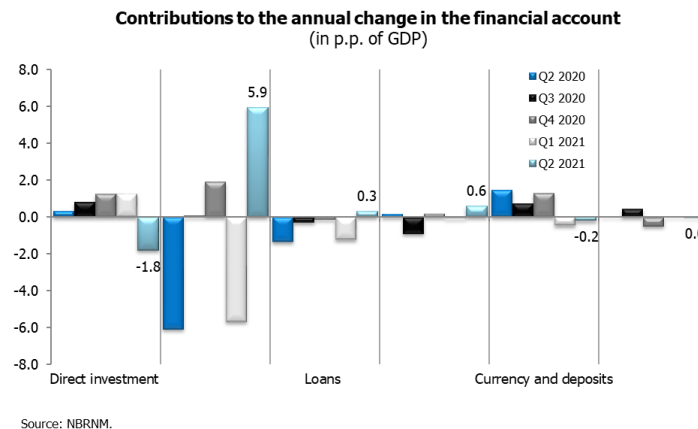
In the second quarter of 2021, the financial account of the balance of payments registered net inflows of Euro 163.7 million, or 1.4% of GDP. Such movements are mostly a result of the net inflows on the basis of foreign direct investments and loans, while the other flows registered net outflows. Within the direct investments, solid net inflows were registered in all components, whereby the inflows in debt components and reinvested profit were higher. In loans, the net inflows largely result from the performances in short-term loans as a result of the specific activities of the central bank related to the foreign reserves management, and to a lesser extent from long-term government loans (in conditions of deleveraging of the private sector). On the other hand, the category currency and deposits (amid high net



outflows in the other sectors), trade credits (deleveraging on a net basis) and portfolio investments registered net outflows.



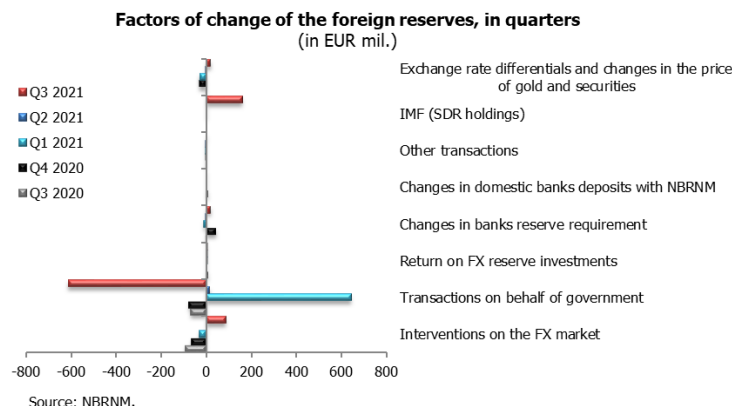
The annual analysis indicates lower net inflows in the financial account in the second quarter of 2021. However, in the second quarter of 2020, the seventh Eurobond in the amount of Euro 700 million was issued. If this one-off effect is excluded, the movements in the other financial account components are more favorable compared to the same period last year. Thus, more favorable annual movements were registered in direct investments, amid high net inflows registered in the second quarter of 2021 on the basis of debt instruments and reinvested profit, unlike the net outflows registered in the second quarter of 2020. In addition, there are lower net outflows on the basis of currency and deposits which is due to the lower net outflows in the other sectors. On the other hand, the movements on an annual basis in trade credits are less favorable, as well as the movements in financial loans, according to the lower long-term government borrowing⁴², and in conditions of higher net inflows on the basis of short-term loans.



At the end of the second quarter of 2021, the gross foreign reserves amounted to Euro 4,031.1 million, which is a quarterly increase of Euro 91.9 million. Observed through the factors of change, for the most part, the change in foreign reserves was driven by foreign reserves management and transactions on behalf of the government⁴³. The remaining flows had a moderate impact on the shifts in foreign reserves in the analyzed period.

⁴² In April 2020, the Ministry of Finance took out a loan from the IMF in the amount of Euro 176.8 million.

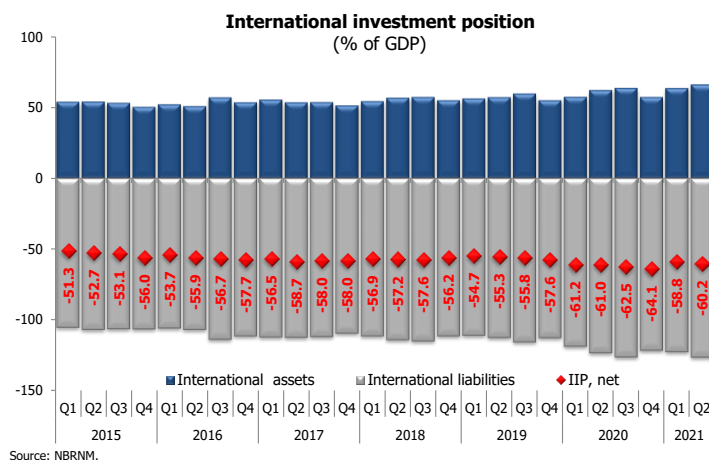
⁴³ On 1 June 2021, the European Commission disbursed the approved funds in the amount of Euro 80 million, intended for dealing with the pandemic.



At the end of the third quarter of 2021, the gross foreign reserves amounted to Euro 3,690.7 million, which is a quarterly decrease of Euro 340.3 million. Observed through the factors of change, for the most part, the change in foreign reserves stems from the transactions on behalf of the government⁴⁴. On the other hand, the IMF allocation of special drawing rights⁴⁵, as well as the National Bank's interventions on the foreign exchange market had a positive impact on the changes in foreign reserves in the analyzed period.

1.6.3. International investment position and gross external debt

At the end of the second quarter of 2021, the net debt position of the Macedonian economy to the rest of the world amounted to Euro 7,111.4 million, or 60.2% of GDP⁴⁶. Compared to the end of the first quarter of 2021, the net international investment position (net IIP) expanded by 1.4 percentage points of GDP, in conditions of higher growth of international liabilities relative to the growth of international assets. Observed by sector, the quarterly change mostly results from the growth of the net liabilities of the other sectors (growth of the net liabilities to foreign investors), and to a lesser extent from the growth of the net liabilities of the government. On the other hand, the net assets of the central bank registered a moderate increase, amid unchanged net liabilities in depository institutions.



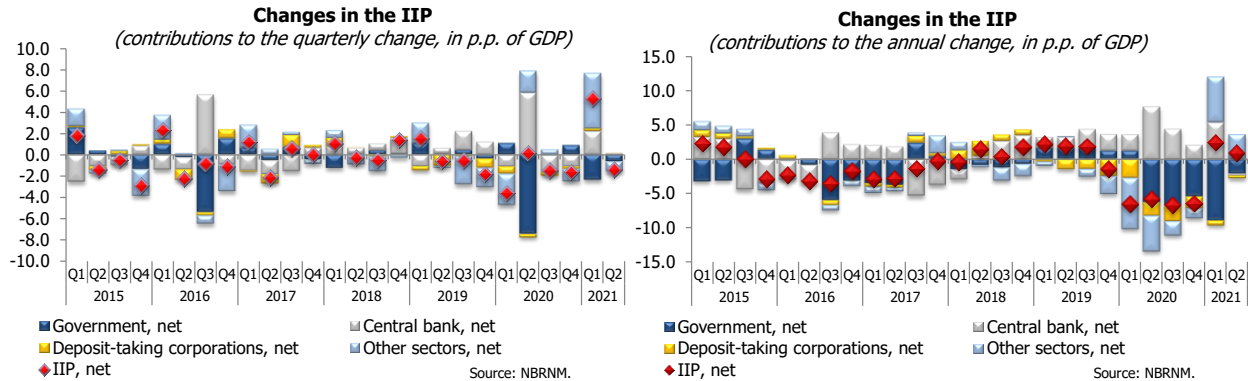
⁴⁴ On 23 July 2021, the Ministry of Finance repaid the principal and the interest for the Eurobond issued in 2014, with a nominal value of Euro 500 million.

⁴⁵ On 23 August 2021, the International Monetary Fund (IMF) allocated the Republic of North Macedonia new, about Euro 133 million special drawing rights (SDRs), or about Euro 166 million which are included in the official foreign reserves.

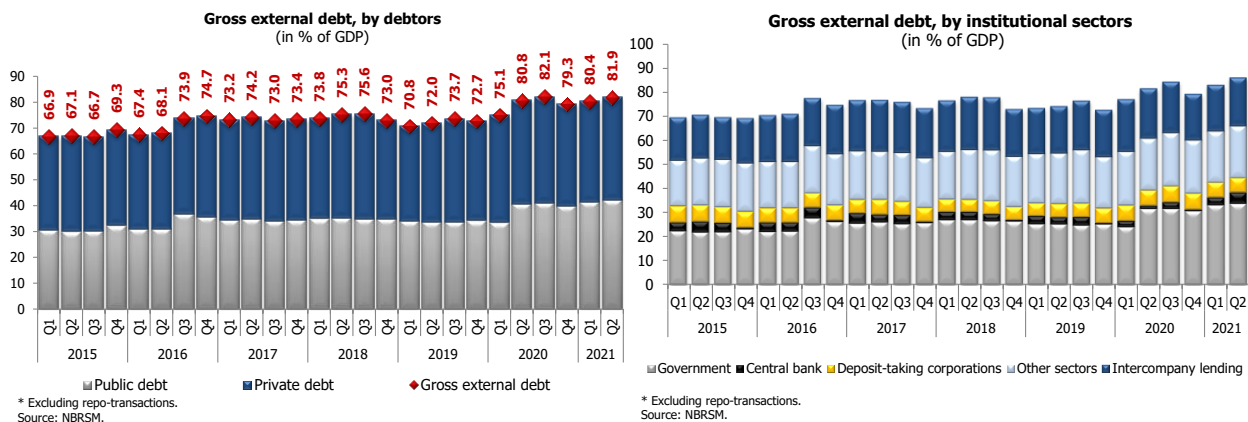
⁴⁶ The calculations use the projected amount of the nominal GDP (from October 2021).



The annual change in the negative international investment position, on the other hand, points to a narrowing of 0.9 percentage points of GDP, as a result of the higher growth of international assets relative to the growth of international liabilities (by 3.9 and 3 percentage points of GDP, respectively). Observed by sector, the annual fall is mainly due to the fall in the net liabilities in the other sectors (mainly due to the lower net liabilities in direct investments and loans, as well as the moderately higher net assets in portfolio investments). On the other hand, the net liabilities of the government increased (mostly as a result of the increased liabilities on the basis of long-term securities), as well as the net liabilities in depository institutions (lower net assets in currency and deposits), and a decrease is also registered in the net assets of the central bank.



At the end of the second quarter of 2021, the level of the gross external debt was Euro 10,158.8 million, or 85.9% of GDP, which is an increase of 3.0 percentage points of GDP, compared to the previous quarter. *By excluding the effect of the specific activities for managing the foreign reserves of the National Bank⁴⁷, the gross external debt registers a quarterly growth of 1.5 percentage points of GDP.* Observed in relative indicators, this shift in the level of the gross external debt results from the higher growth of the private than the growth of the public external debt. The change in the private debt mainly results from the increase in the intercompany debt, while the quarterly increase in the public debt is mostly due to the external government borrowing in the form of long-term loans.

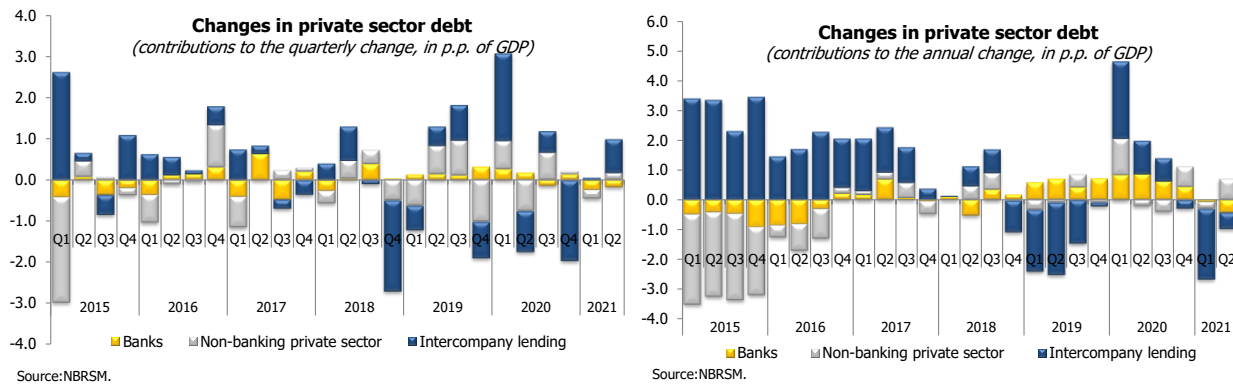


The annual change in the gross external debt indicates an increase of 1.2 percentage points of GDP, registered in circumstances of growth in the public debt, amid a slight decline in the private debt (of 1.4 and 0.3 percentage points of GDP, respectively). The annual change in the public debt is mostly due to the higher government debt in the pandemic period, on the basis of debt securities and long-term loans.

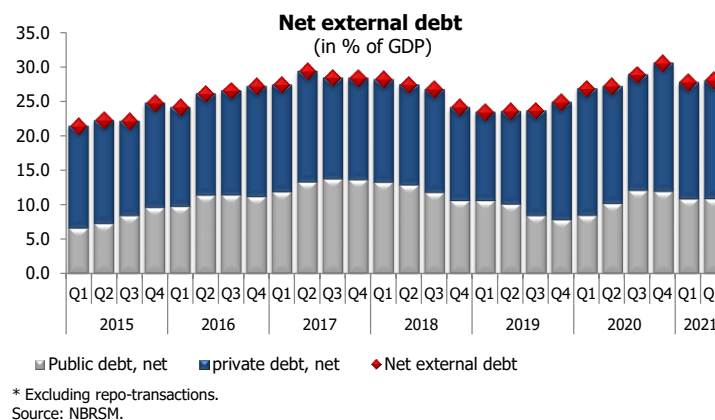
⁴⁷ The specific foreign reserves management activities of the central bank include repo agreements and other foreign reserves management operations.



On the other hand, the fall in the private debt is mostly due to the reduced intercompany debt and the banking sector debt, in circumstances of growth in the non-banking sector debt on the basis of short-term trade credits and advances.



As of 30.6.2021, the net external debt equaled Euro 3,320.4 million, or 28.1% of GDP, which is a quarterly growth of 0.3 percentage points of GDP, amid stable net debt of the public sector and moderate growth of the private sector.



External debt ratios of the national economy remain in the safe zone. Gross external debt to GDP ratio still classifies our economy in the group of highly indebted countries, while all other solvency and liquidity ratios are generally stable and point to low indebtedness of the country.



| Indicators for external indebtedness | 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 | 1.92 | 130.64 | 81.09 | 13.69 | 1.72 | 0.98 | 22.93 |
| 31.12.2020 | 1.92 | 122.97 | 78.27 | 13.69 | 1.93 | 1.11 | 20.38 |
| 31.03.2021 | 2.32 | 131.50 | 84.36 | 17.38 | 1.93 | 1.18 | 21.53 |
| 30.06.2021 | 2.32 | 134.02 | 85.98 | 17.38 | 1.89 | 1.18 | 22.04 |
| Moderate indebtedness criterion* | 12 - 20% | 165 - 275% | 30 - 50% | 18 - 30% | 1.00 | | |

*The moderate indebtedness criterion is according to the World bank's methodology of calculating indebtedness indicators, which implies 3-year moving averages of GDP and exports of goods and services in the calculation of the indicators.

In compliance with "External debt statistics: Guide for compilers and users," published by the IMF.

*According

to the "Greenspan-Guidotti rule", a country should maintain full coverage of short-term debt at remaining maturity with gross foreign reserves.

Short-term debt at remaining maturity is calculated by addition of the long-term external debt (original maturity), with final contractually scheduled payment of less than a year, to the short-term debt (original maturity).

Source: NBRNM.

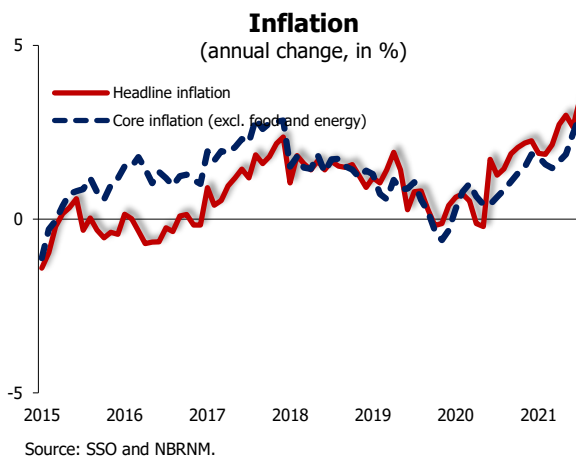
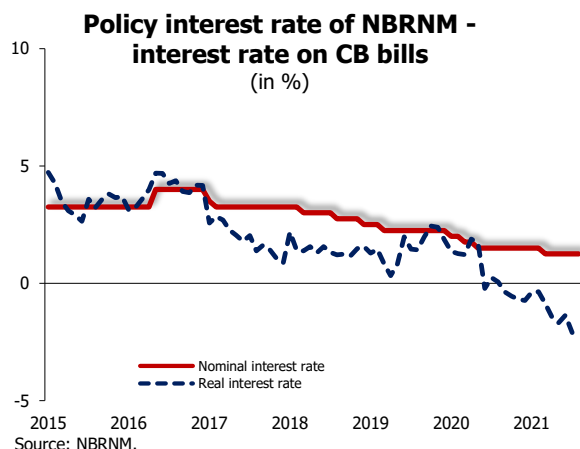
II. Monetary policy⁴⁸

During the third quarter of the year, the National Bank maintained the policy rate at a historic low of 1.25%, continuing with the relaxed character of the monetary policy. Such monetary stance aims to contribute to supporting credit flows in the economy and increasing liquidity in the banking system, in order to mitigate the effects of the pandemic on the domestic economy, which still lasts. Foreign reserves in the third quarter are still at an appropriate level and are maintained in the safe zone. The trend of solid growth rates of total deposits and total loans continued also during the third quarter of the year. Inflation in the period July-August was above the expectations, under the influence of factors on the supply side, amid pronounced uncertainty in the movement of the world prices of primary products in the period ahead. In conditions of uncertainty arising from the further course of the pandemic, the National Bank will continue to carefully monitor the indicators and potential risks of the domestic and external environment, in order to adequately adjust the monetary policy setup.

⁴⁸ For more information on the new monetary measures, see the National Bank website: https://www.nbrm.mk/content/MPI%20publikacii/Hronologija_na_promenite_vo_postavenosta_na_monetarnite_instrumenti_na_Na_rodната%20banka.pdf

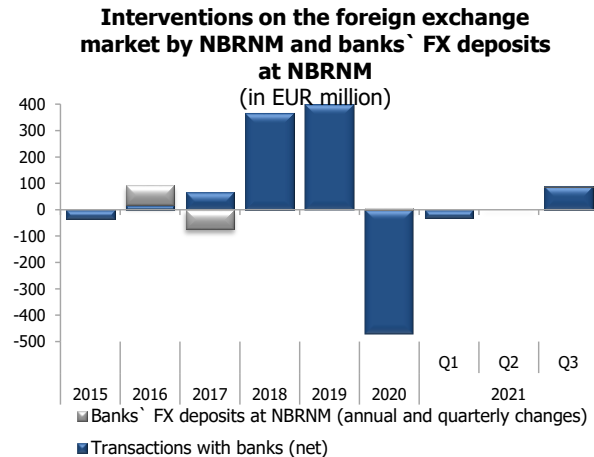


In the third quarter of the year, the National Bank did not change the monetary policy position, and the policy rate remained at the historically lowest level of 1.25%. Given the already performed monetary relaxation at the beginning of the year, the monetary stance was assessed as appropriate to the current economic and financial conditions. The current decline in the key interest rate, as well as the significant reduction of the offered amount of CB bills, contributed to increasing liquidity of the banking system, easing financial conditions and supporting credit flows in the economy.

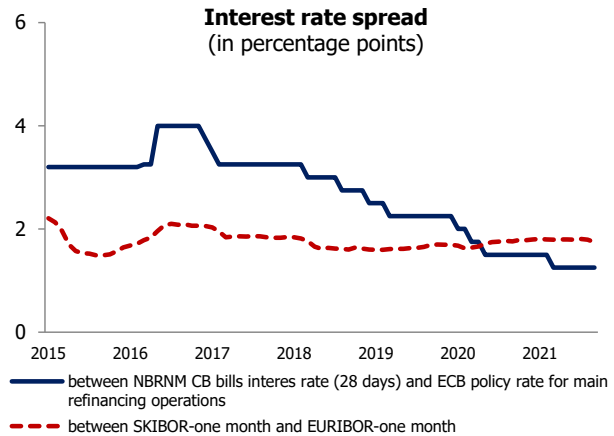


The comparison of the latest macroeconomic indicators of the domestic economy⁴⁹ with their forecasted dynamics of the April forecasting round, showed that they are generally within the expectations. After the annual fall in the previous four quarters, which is related to the occurrence of the COVID-19 pandemic, the gross domestic product in the second quarter of 2021 registered a real growth of 13.1% on an annual basis, in line with the expectations, which entirely results from the positive contribution of domestic demand, amid a negative contribution of net exports. The high frequency data for the third quarter of 2021 are partial and insufficient to have an overall view of the situation. Analyzing inflation, in the period July - August, the annual price growth averaged 3.5%. Inflation performances are slightly higher than expected, amid pronounced uncertainty in the movement of world prices of primary commodities in the period ahead. The price growth is mostly caused by factors on the supply side, such as the increased import prices of certain products that are driven by the world markets (oil and oil derivatives), with an additional impact of the increases of administrative and regulatory nature (electricity and tobacco prices), as well as the higher prices in restaurants and hotels, which is also partially related to the measures for prevention of the spreading of COVID-19. Regarding the foreign reserves, the latest data show that they are maintained at an appropriate level and in a safe zone. In the third quarter, the greatest effect on the change in the foreign reserves was that of the purchase of foreign currency made by the National Bank in accordance with the favorable developments in the foreign exchange market, the repayment of the Eurobond issued in 2014 and the allocation of Euro 160 million from the special drawing rights by the IMF. In terms of the movements in total deposits and total loans, the data as of August point to their further solid annual growth, with slightly stronger dynamics relative to the April forecast.

⁴⁹It refers to the available information during the third quarter of 2021 that was taken into account when making the decisions on the monetary stance in that period.



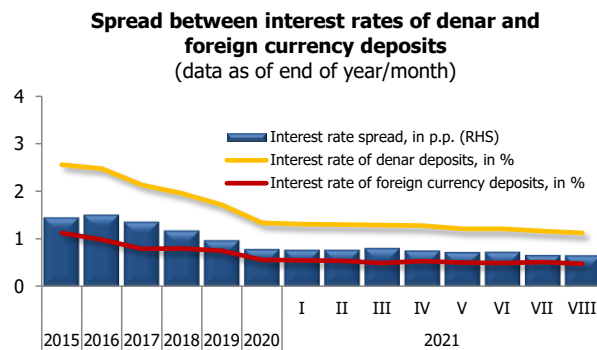
Source: NBRNM.



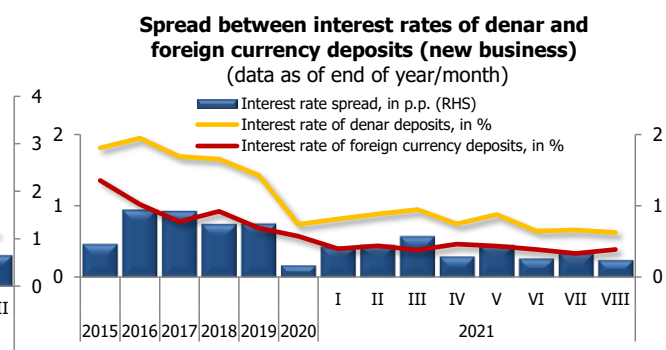
Source: NBRNM and ECB.

In the third quarter of 2021, the ECB continued to implement relaxed monetary policy in order to maintain favorable financial conditions. Amid unchanged policy rates of the ECB and of the National Bank, the spread between these two interest rates in the third quarter remained at the same level. Regarding the indicative market interest rates of 1m EURIBOR and 1m SKIBOR, the spread between them registered a slight narrowing at the end of the third quarter, which results from the reduction of 1m SKIBOR, amid unchanged 1m EURIBOR, compared to the previous quarter.

In the domestic economy, in the interest rates on total deposits (in denars and in foreign currency), the interest rate spread in August remained relatively stable and equaled 0.7 percentage points, amid minimal decline in the interest rate on denar deposits of 0.1 percentage point and unchanged interest rate on foreign currency deposits. In total newly accepted⁵⁰ deposits, the interest rate spread in August remained stable and equaled 0.2 percentage points, in conditions of unchanged denar and foreign currency interest rates.



Source: NBRNM.



Source: NBRNM.

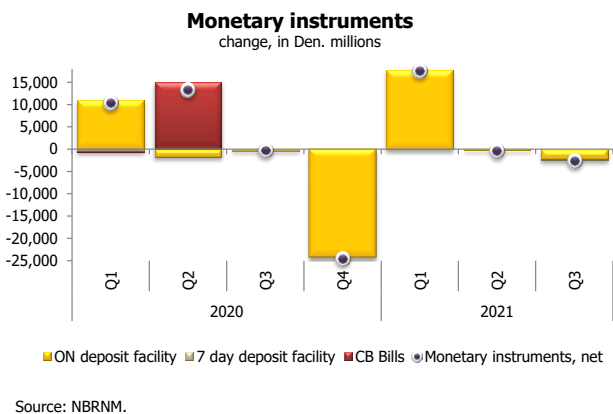
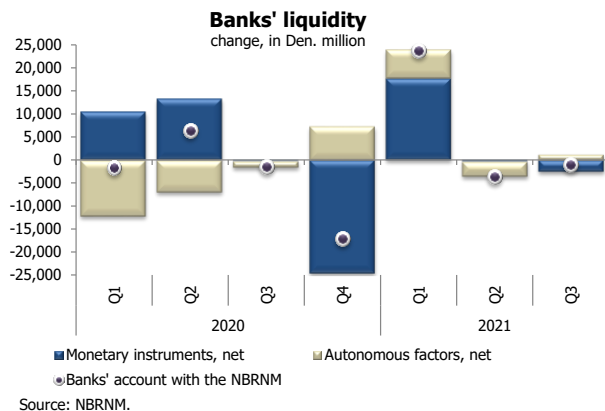
2.1. Bank liquidity

In the third quarter of 2021, the banks' denar liquidity decreased, which entirely results from the change in the monetary instruments, i.e. from the higher amount of banks' funds placed in deposits with

⁵⁰ Regarding the interest rates on newly approved loans, one should have in mind that they are characterized with variable movements. Volatility of interest rate 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.

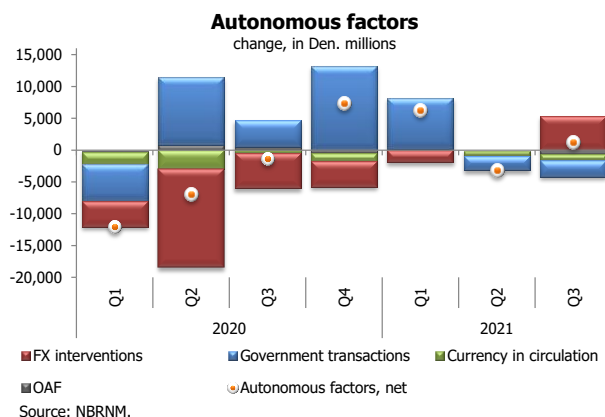


the National Bank. The autonomous factors, net, contributed to creating liquidity in the banking system, as a result of the foreign currency interventions of the National Bank.



Regarding the monetary instruments, the banks' deposit facilities with the National Bank in the third quarter contributed to withdrawing liquidity (by Denar 2,523 million), amid an increase in the stock of the overnight deposit facility (by Denar 2,210 million) and in the 7-day deposit facilities (by Denar 313 million). At the end of the third quarter, the stock of the main instrument - the CB bills of the NBRNM was Denar 10,000 million and registered no changes compared to the end of the previous quarter. During the third quarter of the year, the banks' interest in placing their foreign assets in a foreign currency deposit with the National Bank also increased, whereby the stock of the foreign currency deposit was higher by Denar 184 million. This instrument, which was activated in the second half of 2020 amid increased uncertainty on the international markets, gives the banks in the country a chance to place part of their foreign assets in short-term and safe instruments of the central bank.

The autonomous factors, net, in the third quarter created liquidity in the amount of Denar 1,252 million. Such change is entirely a result of the National Bank interventions on the foreign exchange market, amid an increase in currency in circulation, while government transactions acted towards withdrawing liquidity from the banking system.



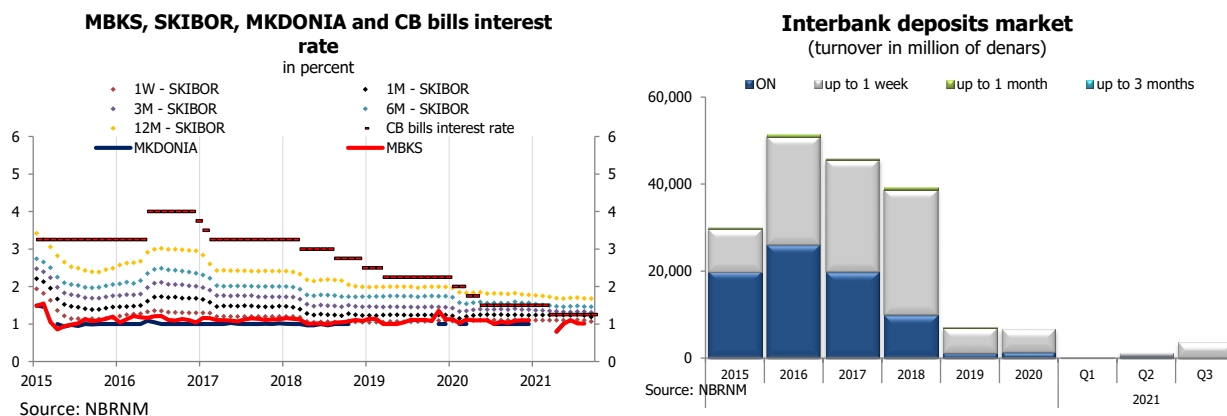
In the third quarter of the year, the banks continued to have more allocated funds on the accounts with the National Bank than the determined amount of the reserve requirement in denars, on average by about 10%.

III. Financial market developments

The interest rate on the interbank deposit market in the third quarter remained at a low and stable level and averaged 1%. In conditions of unchanged key interest rate of the National Bank, almost all SKIBOR quotations remained stable, with the exception of the one-month quotations which registered a small downward shift. In the primary government securities market, the new issues were mainly in longer maturities and in domestic currency, while on the secondary market, there was mostly trading with government bonds, and to a lesser extent with treasury bills. On the Macedonian Stock Exchange, the stock exchange turnover increased by 65.5%, amid growth of the value of the MBI-10 of 7.9%, which is in line with the movements of the regional stock exchange indices. In the international financial markets, the volatility indices of the bond and stock markets, i.e. the MOVE and VIX indices on a daily basis, on average, registered an upward change, which indicates a slight increase in the uncertainty on the global markets. The downward correction of the yields on Macedonian Eurobonds amid a simultaneous more moderate reduction also of the yields of German government bonds, contributed to narrowing the spreads between these two bonds.

3.1. Interbank market for uncollateralized deposits

In the third quarter of the year, the average interest rate on the interbank deposit market (MBKS) remained stable and amounted to 1%, in conditions of an unchanged key interest rate of the National Bank (1.25%). In conditions of maintenance of the banks' liquidity at a high level, the trading on the interbank deposit market remained at a low level and amounted to Denar 3,610 million (Denar 1,256 million in the previous quarter), mostly as a result of transactions with maturity up to 7 days and to a small extent of overnight transactions. On a quarterly basis, almost all average SKIBOR quotations remained stable, with the exception of the one-month quotations, which registered a small downward shift.

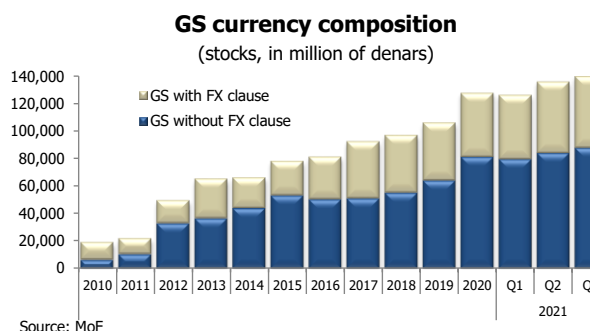
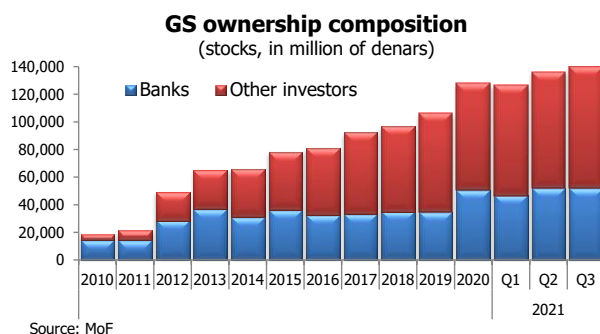
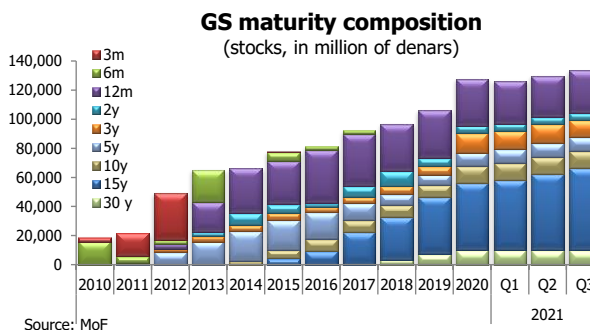
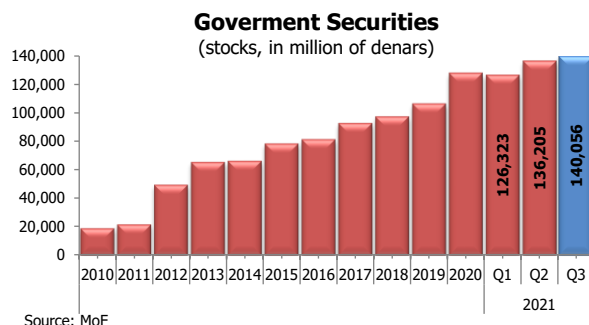


3.2. Government securities market

The stock of the issued government securities on the primary market in the third quarter of the year increased by Denar 3,852 million on a quarterly basis and reached Denar 140,056 million. From structural point of view, the growth is mostly a result of the fifteen-year government bonds, amid smaller growth of the twelve-month treasury bills. Government bonds remain dominant category (with a share of

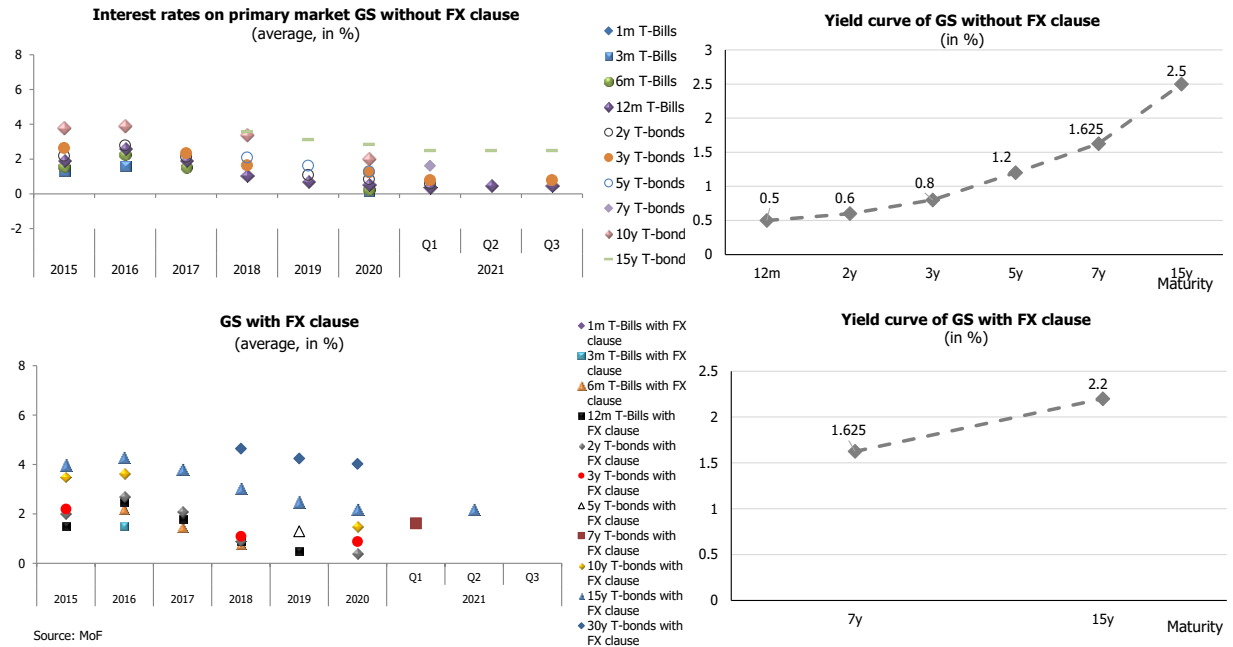


79.1%) in the stock of total government securities issued on the primary market. Observing maturity, the third quarter registered a quarterly growth of the share of the fifteen-year government bonds, from 38.6% to 40.3%, at the expense of the reduced share of other government securities. Such performances are still in line with the guidelines from the strategy of the Ministry of Finance for issuing government bonds with longer maturities, in order to reduce the debt refinancing risk.⁵¹ In terms of currency structure, government securities without currency clause maintained their dominant share, making up 62.6% of total government securities (61.5% in the previous quarter). Moreover, the banks in this quarter reduced the share in the ownership structure of the government securities from 38.2% to 37%, while the other investors increased the share. Within the other investors (63%), dominant holders of government securities are still the pension funds (with a share of 43.5%).

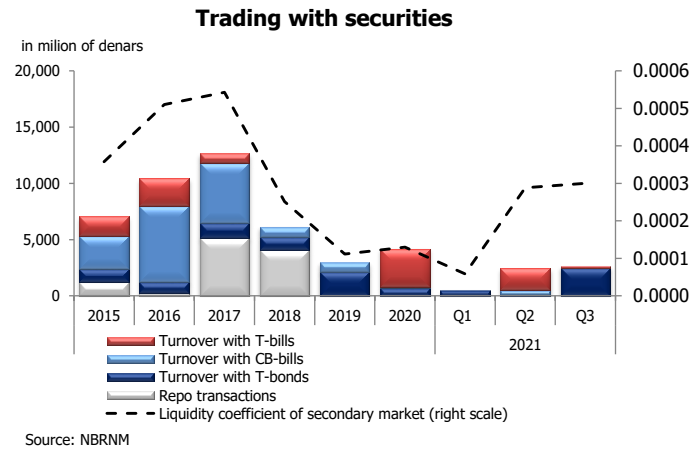


Interest rates on government securities also during the third quarter of 2021 were determined by the Ministry of Finance and registered no changes compared to the previous quarter. Thus, on the primary market, there was an issuance of twelve-month treasury bills without currency clause at an interest rate of 0.5%, three-year government bonds without currency clause at an interest rate of 0.8% as well as fifteen-year government bonds without currency clause at an interest rate of 2.5%.

⁵¹ Fiscal Strategy of the Republic of North Macedonia for 2022-2024 (with prospects until 2026), Ministry of Finance, May 2021.



Trading with securities on the secondary market in the third quarter of the year was similar to the previous quarter and amounted to Denar 2,651 million, which still indicates a relatively low level of liquidity on the secondary government securities market (measured by the liquidity ratio⁵²). Moreover, transactions with government bonds were mostly concluded on this market segment, and to a lesser extent there were also transactions with treasury bills. Observing maturity, there were transactions with residual maturity from 3 to 6 months, up to 1 year, 1 to 2 years, 2 to 3 years, 5 to 10 years and 10 to 15 years (with an average yield to maturity of 0.4%, 0.3%, 0.6%, 0.8%, 1.6% and 1.9%, respectively).

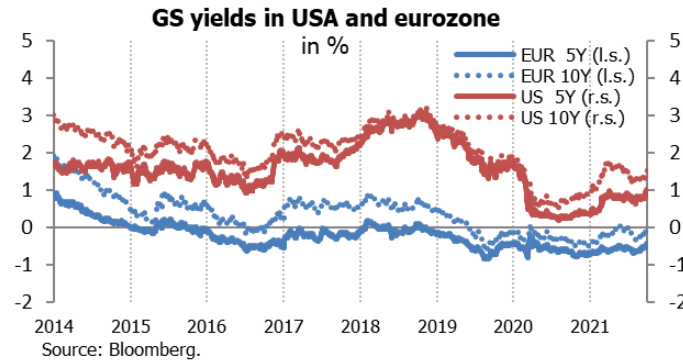


In the third quarter of 2021, on the financial markets in the euro area, the yields of the 10-year government securities⁵³ averaged around -0.2% (0% in the previous quarter), while the yields of the US 10-year government bonds⁵⁴ amounted to 1.3% (1.6% in the previous quarter of the year).

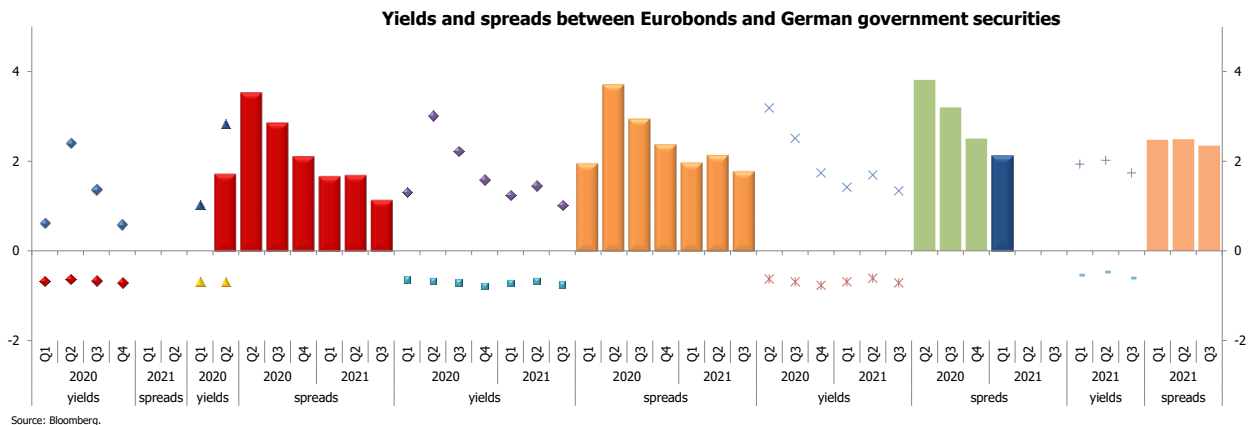
⁵² The liquidity ratio on the secondary market is the correlation between the average daily turnover and the stock of government securities.

⁵³ Those are generic government bonds derived from the yield curves of government bonds of Germany and France.

⁵⁴ Those are generic yields derived from the yield curve of government bonds of the United States.



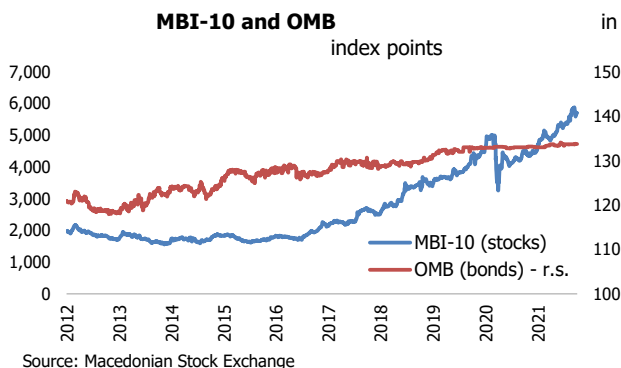
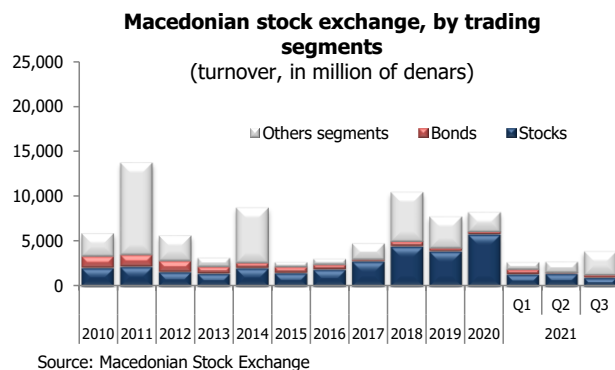
Also, the yields on Macedonian Eurobonds⁵⁵ in the third quarter of the year on average registered a decline, amid a simultaneous reduction of the yields of German government bonds, which led to a narrowing of the spreads between these two bonds, which averaged 1.1 percentage points, 1.8 percentage points, 2.1 percentage points and 2.3 percentage points, respectively.



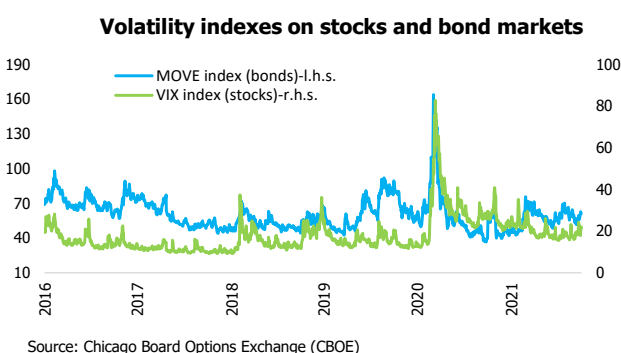
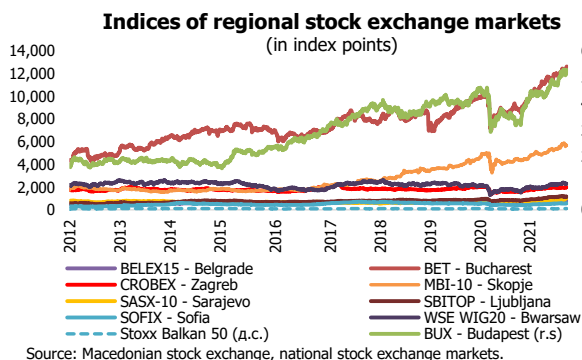
3.3. Stock markets

On the Macedonian Stock Exchange, the value of the stock exchange index MBI-10 increased by 7.9% in the third quarter of 2021 (9% in the previous quarter) and reached 5,697 index points. The stock market turnover registered a quarterly growth of 65.5%, almost entirely reflecting the increased turnover from block trades, and to a small extent from bond trading. The bond index value (OMB) remained stable at 134 index points during the quarter.

⁵⁵ It refers to the Macedonian Eurobonds issued in July 2016, in January 2018, in June 2020 and March 2021. Eurobonds are issued in the nominal amount of Euro 450 million, Euro 500 million, Euro 700 million and Euro 700 million, respectively, with a maturity of 7, 7, 6 and 7 years, respectively, and annual interest rates of 5.625%, 2.75%, 3.675% and 1.625%, respectively. In July 2021, the Macedonian Eurobond which was issued in July 2014 in a nominal amount of Euro 500 million, with a maturity of 7 years and an annual interest rate of 3.975%, fell due and it was repaid in full.



In the third quarter of 2021, the growth of stock exchange indices in the region continued with an overall average growth of 7% (growth of 8.5% in the previous quarter). The Bosnian and Hungarian indices registered a significant upward movement, while other stock market indices in the region grew more moderately. Volatility indices on the bond and stock markets⁵⁶, i.e. the MOVE and VIX indices on a daily basis registered an average growth of about 3%, which indicates a slight increase of global market uncertainty.



IV. Monetary and credit aggregates⁵⁷

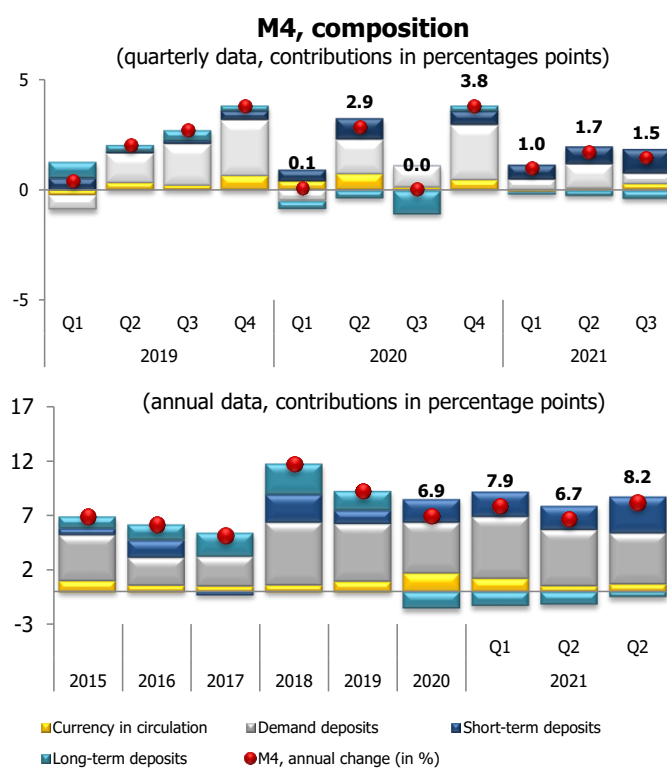
In the third quarter of 2021, the broad money M4 registered a further growth with similar dynamics as in the previous period. Structurally speaking, the increase is mostly due to short-term deposits, and to a lesser extent to cash in circulation and demand deposits. In line with the favorable developments in the banks' deposit base, the solid growth of lending to the private sector continued, with somewhat more moderate dynamics compared to the previous quarter. The results of the Lending Survey for the third quarter indicate an increase in credit demand by enterprises and households, amid simultaneous net tightening of credit standards for both sectors.

⁵⁶ 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 the indices indicates a decrease in volatility.

⁵⁷ Monetary aggregates, and total deposits and loans data since August 2020 do not include data on a small bank whose founding and operating license was revoked and which went into bankruptcy in August 2020.

4.1. Monetary aggregates

The broad money M4 in the third quarter of 2021 registered a quarterly growth of 1.5%⁵⁸, which is a similar growth as in the previous quarter (1.7%). Analyzing the money supply structure, the growth mostly results from short-term deposits (positive contribution of 1.1 percentage points), and to a lesser extent from currency in circulation and demand deposits (a positive contribution of 0.3 percentage points and 0.5 percentage points, respectively), with a small adverse contribution of long-term deposits (0.4 percentage points). Regarding the currency structure, denar deposits (excluding demand deposits) continued to have a negative contribution of 0.6 percentage points in the quarterly growth of the broad money M4, with a positive contribution of foreign currency deposits (1.3 percentage points). Accordingly, the share of foreign currency deposits in M4 at the end of the third quarter registered an inconsiderable increase to 37.2% (36.5% at the end of the previous quarter). Annually, at the end of the third quarter the growth of M4 accelerated compared to the previous quarter and at the end of September reached 8.2% (6.7% at the end of the previous quarter).



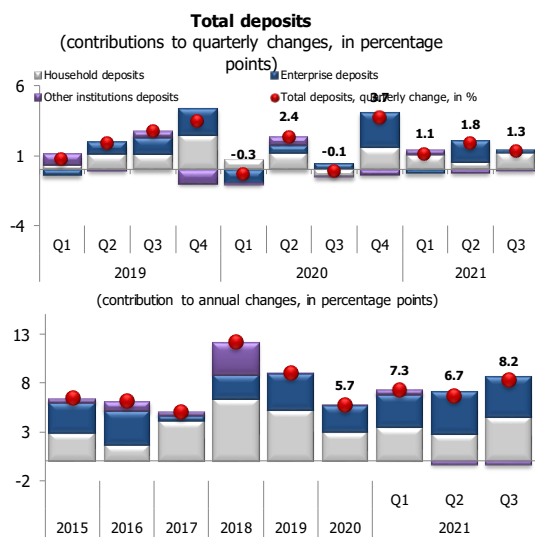
Total financial system deposits⁵⁹ in the third quarter of 2021 increased by 1.3% on a quarterly basis (a quarterly growth of 1.8% in the previous quarter). Analyzing by sector, the deposit increase is primarily due to the growth of household deposits amid growth of corporate deposits, with minor decrease in other sectors' deposits. Observing the currency, growth was registered in both foreign currency deposits and denar deposits (demand deposits included). Analyzing the maturity structure, the growth entirely

⁵⁸ The increase in deposits in part is also a result of one-time factors, such as the significant amount of government subsidies paid in agriculture and the payment of dividends by a large bank.

⁵⁹ 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.nspk.



reflects short-term deposits, amid fall in long-term deposits. On an annual basis, the growth of total deposits equaled 8.2% at the end of September (6.7% at the end of the previous quarter).



| Total deposits | | | | | | | |
|--|------|------|------|------|------|------|------|
| | 2020 | | | | 2021 | | |
| | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 |
| quarterly change, in % | | | | | | | |
| Total deposits | -0.3 | 2.4 | -0.1 | 3.7 | 1.1 | 1.8 | 1.3 |
| contributions to quarterly growth, p.p. | | | | | | | |
| Deposit money | -0.5 | 1.7 | 1.1 | 2.7 | 0.5 | 1.2 | 0.5 |
| Denar deposits | -0.7 | -0.4 | -1.4 | -0.4 | -0.2 | -0.7 | -0.6 |
| FX deposits | 0.9 | 1.0 | 0.3 | 1.4 | 0.8 | 1.3 | 1.4 |
| Short-term deposits | 0.6 | 1.0 | 0.0 | 0.7 | 0.7 | 0.9 | 1.2 |
| Long-term deposits | -0.4 | -0.4 | -1.2 | 0.3 | -0.1 | -0.3 | -0.4 |
| Households | 0.7 | 1.2 | -0.5 | 1.6 | 1.1 | 0.5 | 1.2 |
| Enterprises | -0.9 | 0.6 | 0.5 | 2.5 | -0.3 | 1.5 | 0.2 |
| Other institutions deposits | -0.1 | 0.6 | -0.1 | -0.4 | 0.3 | -0.2 | -0.1 |

Source: NBRNM.

In the third quarter of the year, the growth of household deposits continued at an accelerated pace compared to the previous quarter (a quarterly growth of 1.8%, compared to 0.8% in the previous quarter). Analyzed by currency, the increase was mostly due to foreign currency deposits, amid a smaller contribution of denar deposits (demand deposits included). Analyzing the maturity structure, short-term deposits increased, amid further decline in long-term deposits. The annual increase in total household deposits was 6.9% at the end of September (4.2% at the end of the previous quarter).

Corporate deposits in the third quarter registered a moderate quarterly increase of 0.8% (after the growth of 5.6% in the second quarter). Analyzing the currency structure, the growth is a result of the increase in foreign currency deposits, amid a decline in denar deposits (demand deposits included). From a maturity perspective, growth was observed in short-term deposits, with a decline in long-term deposits. Annually, at the end of September, corporate deposits increased by 15.6% (16.7% at the end of the previous quarter).

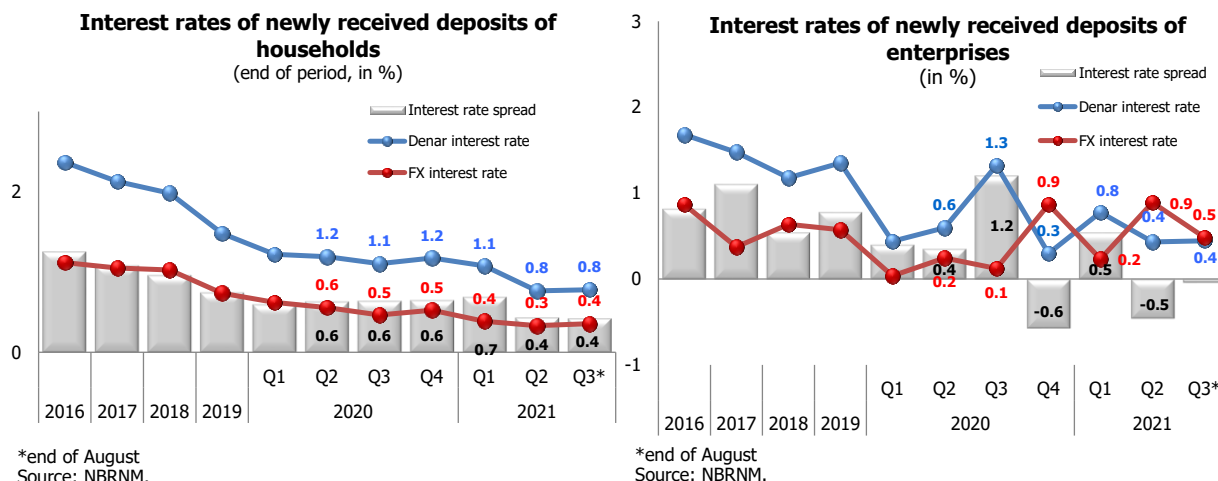
| Household deposits | | | | | | | |
|--|------|------|------|------|------|------|------|
| | 2020 | | | | 2021 | | |
| | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 |
| quarterly change, in % | | | | | | | |
| Total household deposits | 1.1 | 1.8 | -0.7 | 2.4 | 1.7 | 0.8 | 1.8 |
| contribution to quarterly change of total deposits, in p.p. | | | | | | | |
| Deposit money | 0.7 | 1.5 | 0.5 | 2.0 | 0.6 | 0.5 | 0.9 |
| Denar deposits | -0.2 | -0.9 | -1.7 | -0.1 | 0.1 | -0.6 | -0.4 |
| FX deposits | 0.6 | 1.2 | 0.5 | 0.6 | 1.0 | 0.9 | 1.3 |
| Short-term deposits | 0.5 | 0.8 | 0.7 | 0.5 | 1.1 | 1.0 | 1.3 |
| Long-term deposits | -0.1 | -0.4 | -1.9 | -0.1 | -0.1 | -0.7 | -0.4 |

Source: NBRNM.

| Enterprise deposits | | | | | | | |
|--|------|------|------|------|------|------|------|
| | 2020 | | | | 2021 | | |
| | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 |
| quarterly change, in % | | | | | | | |
| Total enterprise deposits | -3.4 | 2.2 | 1.8 | 9.5 | -0.9 | 5.6 | 0.8 |
| contribution to quarterly change of total deposits, in p.p. | | | | | | | |
| Deposit money | -3.9 | 2.0 | 2.8 | 6.7 | -0.3 | 3.1 | -0.4 |
| Denar deposits | -1.4 | -0.4 | -1.0 | -0.7 | -0.3 | -0.4 | -0.8 |
| FX deposits | 2.0 | 0.6 | -0.1 | 3.6 | -0.3 | 2.9 | 2.1 |
| Short-term deposits | 1.5 | 0.2 | -1.1 | 1.8 | -0.7 | 1.3 | 1.6 |
| Long-term deposits | -1.0 | 0.1 | 0.1 | 1.0 | 0.1 | 1.2 | -0.4 |

Source: NBRNM.

The analysis of the returns⁶⁰ on the new savings shows that in August, the interest rates on the newly accepted⁶¹ denar and foreign currency deposits of the households were 0.8% and 0.4%, respectively (0.8% and 0.3%, respectively in June). In such conditions, the interest rate spread between the new denar and foreign currency savings of households in August remained stable at 0.4 percentage points. Interest rates on newly accepted denar and foreign currency corporate deposits in August amounted to 0.4% and 0.5% respectively (0.4% and 0.9%, respectively in June). With such shifts, the interest rate spread between newly accepted denar and foreign currency corporate deposits at the end of August, was insignificant. Regarding the total accepted deposits (denar and foreign currency), the interest rates on household and corporate deposits in August registered a minor fall to 0.7% and 1.1%, respectively (0.8% and 1.2%, respectively in June).



4.2. Lending activity

Banks' lending activity in the third quarter of the year continued to grow, but at a more moderate pace compared to the previous quarter (from 2.6% to 1.1% growth, on a quarterly basis). Analyzing credit standards, according to the results of the Lending Survey, the third quarter witnessed net tightening of credit standards for both corporate and household sectors. However, the largest percentage of banks still indicates unchanged credit standards for both sectors. There was also an upward movement of total credit demand by corporations and households. For the fourth quarter of 2021, banks expect a net increase in the total demand for loans by both sectors, amid net tightening of credit standards for the corporate sector and slight net easing of credit standards for the households.

⁶⁰ 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:

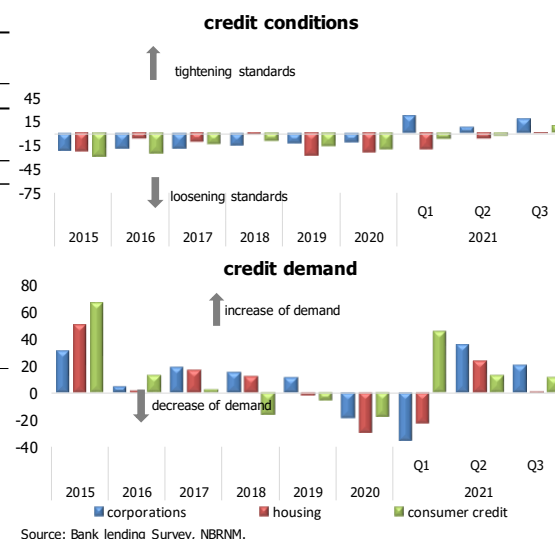
http://www.nbrm.mk/monetarna_statistika_i_statistika_na_kamatni_stapki.nspix.

⁶¹Note that the interest rates on the newly accepted deposits are volatile. Volatility of interest rate on newly accepted deposits results from the fact that they are driven by the volume of newly accepted deposits (which can vary from month to month) and their interest rate.

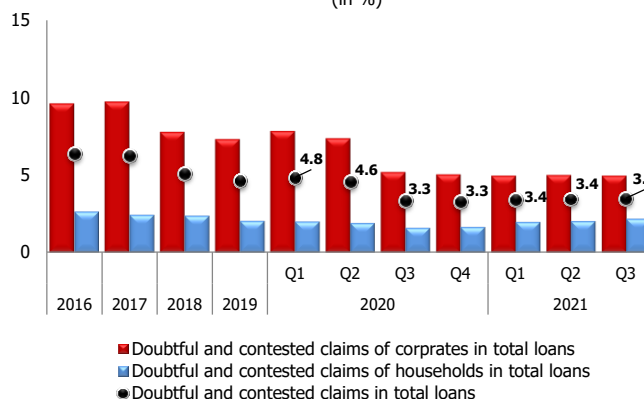
**Total credits of private sector**

| | 2020 | | | | 2021 | | |
|--|-------------------------------|------|------|-----|------|-----|------|
| | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 |
| | quarterly change, in % | | | | | | |
| Total credits of private sector | 0.7 | 2.6 | 0.03 | 1.3 | 1.2 | 2.6 | 1.1 |
| Contribution in quarterly change of total credits (in p.p.) | | | | | | | |
| Denar credits | 0.5 | 1.7 | -0.1 | 0.6 | 0.7 | 1.8 | 0.7 |
| Foreign currency credits | 0.2 | 0.9 | 0.1 | 0.6 | 0.5 | 0.8 | 0.4 |
| Short-term credits | 0.1 | -0.4 | -1.2 | 0.4 | 0.5 | 0.6 | -0.4 |
| Long-term credits | 0.3 | 2.7 | 2.2 | 1.0 | 0.5 | 1.9 | 1.5 |
| Households | 0.8 | 1.1 | 1.4 | 0.7 | 0.8 | 1.4 | 0.9 |
| Corporations | -0.1 | 1.5 | -1.4 | 0.5 | 0.4 | 1.1 | 0.3 |

Source: NBRNM.



The analysis of sectoral structure of loans to the private sector indicates an increase in lending to both sectors, with a larger contribution of household loans. Analyzing the currency, the growth primarily arises from denar loans, as well as foreign currency loans⁶². Analyzing maturity structure, the quarterly growth of total loans primarily stems from the accelerated growth of long-term loans, amid fall in short-term loans. Additionally, the share of doubtful and disputed claims in total loans slightly increased compared to the end of the second quarter and in September amounted to 3.5%.

Share of doubtful and contested claims in total loans (in %)

Source: NBRNM.

Annually, total loans at the end of the third quarter increased by 6.3%, which is higher compared to the end of the previous quarter (5.1%). Loan growth is primarily due to the rise of household loans, amid positive contribution of corporate loans. Loan/deposit ratio remained relatively stable and equaled 81.1% at the end of September (81.2% at the end of June).

Household loans continued increasing in the third quarter of 2021. The quarterly growth of 1.7% (2.8% in the second quarter) largely stems from the increase in housing and consumer loans, with a negative contribution of other loans, while credit cards and overdrafts do not have a major contribution to growth. The results of the Lending Survey for the third quarter in the household sector indicate a net increase in the demand for consumer and housing loans, with a slight net easing of the credit standards for housing loans and net tightening of the credit standards for consumer loans. Analyzing the currency,

⁶² Foreign currency loan data also include denar loans with currency clause.

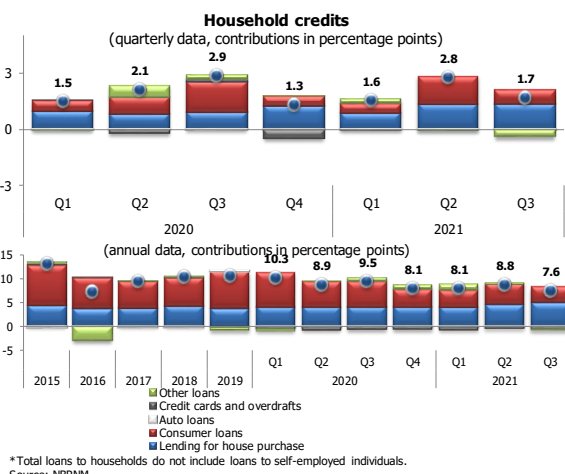


the growth of household loans primarily arises from the positive contribution of denar loans, amid smaller growth of foreign currency loans. Analyzing the maturity structure, the growth continued to be driven mostly by long-term loans, amid insignificant contribution of short-term loans. Annually, at the end of September, total loans to households increased by 7.5% (8.7% in June).

Total credits of households

| | 2020 | | | | 2021 | | |
|---|------|------|------|------|------|-----|-----|
| | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 |
| quarterly change, in % | | | | | | | |
| Total credits of households | 1.5 | 2.1 | 2.8 | 1.3 | 1.6 | 2.8 | 1.7 |
| Contribution in quarterly change of household credits (in p.p.) | | | | | | | |
| Denar credits | 0.9 | 1.6 | 2.5 | 0.6 | 1.0 | 1.3 | 1.0 |
| Foreign currency credits | 0.6 | 0.5 | 0.3 | 0.7 | 0.5 | 1.4 | 0.6 |
| Short-term credits | 0.01 | -0.4 | 0.03 | -0.1 | 0.2 | 0.1 | 0.0 |
| Long-term credits | 1.5 | 1.9 | 2.6 | 1.3 | 1.1 | 2.7 | 1.6 |

Source: NBRNM.



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

In the third quarter of 2021, the quarterly growth of total loans granted to the corporate sector slowed down to 0.6% (2.3% in the second quarter). The results of the Lending Survey for the third quarter indicate a net increase in the corporate loan demand, amid net tightening of credit standards. Analyzing the currency, the growth of total corporate loans is a result of the almost equal increase in denar and foreign currency loans (including loans with foreign currency clause). The analysis of maturity structure shows that the quarterly growth is due to the increase in long-term loans, amid fall in short-term loans. Annually, the increase in total corporate loans accelerated and at the end of September they were by 4.8% higher (1.2% at the end of June).

Total credits of corporations

| | 2020 | | | | 2021 | | |
|---|------|------|------|-----|------|-----|------|
| | Q1 | Q2 | Q3 | Q4 | Q1 | Q2 | Q3 |
| quarterly change, in % | | | | | | | |
| Total credits of corporations | -0.2 | 3.2 | -2.9 | 1.0 | 0.8 | 2.3 | 0.6 |
| Contribution in quarterly change of corporation credits (in p.p.) | | | | | | | |
| Denar credits | 0.0 | 1.8 | -2.8 | 0.5 | 0.2 | 2.3 | 0.3 |
| Foreign currency credits | -0.2 | 1.3 | -0.1 | 0.6 | 0.6 | 0.1 | 0.2 |
| Short-term credits | 0.1 | -0.4 | -2.2 | 0.9 | 0.9 | 1.1 | -0.7 |
| Long-term credits | -0.9 | 3.7 | 1.9 | 0.4 | -0.1 | 1.1 | 1.5 |

Source: NBRNM.

According to the data on interest rates⁶³ on newly approved loans⁶⁴ in August, interest rates on denar loans to households decreased from 5.1% to 4.7%, while interest rates on foreign currency loans did not change compared to the previous quarter and amounted to 3.6%. In such conditions, the interest rate spread between the new denar and foreign currency lending to households narrowed quarterly from 1.5 percentage points to 1.1 percentage points. The interest rates on newly approved denar and foreign currency corporate loans in August equaled 3.6% and 2.5%, respectively (3.4% for each type, respectively, in the previous quarter), thus the interest rate spread between the new denar and foreign currency corporate lending expanded to 1.1 percentage points. Regarding total loans granted to the private sector,

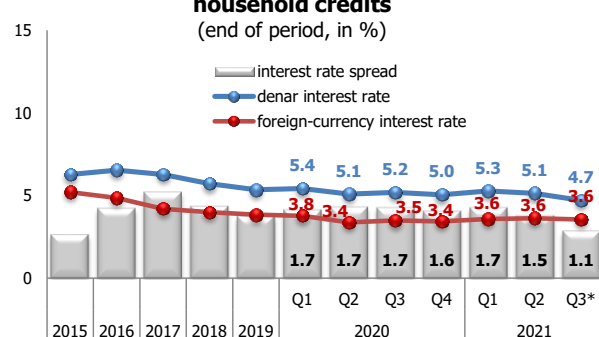
⁶³ Data on interest rates are in accordance with the methodological changes of the National Bank from June 2018. For more information on the methodological changes visit: http://www.nbrm.mk/monetarna_statistika_i_statistika_na_kamatni_stapki.nspix.

⁶⁴ Note that the interest rates on newly approved loans are volatile. Volatility of interest rate on newly approved loans results from the fact that they are driven by the volume of newly approved loans (which can vary from month to month) and their interest rate.



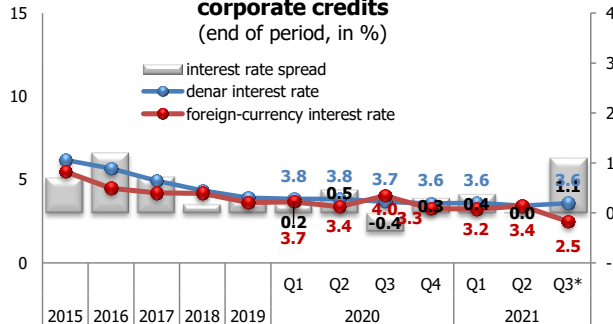
at the end of August, the interest rates on household and corporate loans did not change compared to the previous quarter, and equaled 5.3% and 3.6%, respectively.

Interest rate of total newly granted household credits
(end of period, in %)



*End of August.
Source: NBRNM.

Interest rate of total newly granted corporate credits
(end of period, in %)



*End of August.
Source: NBRNM.

V. Public finance

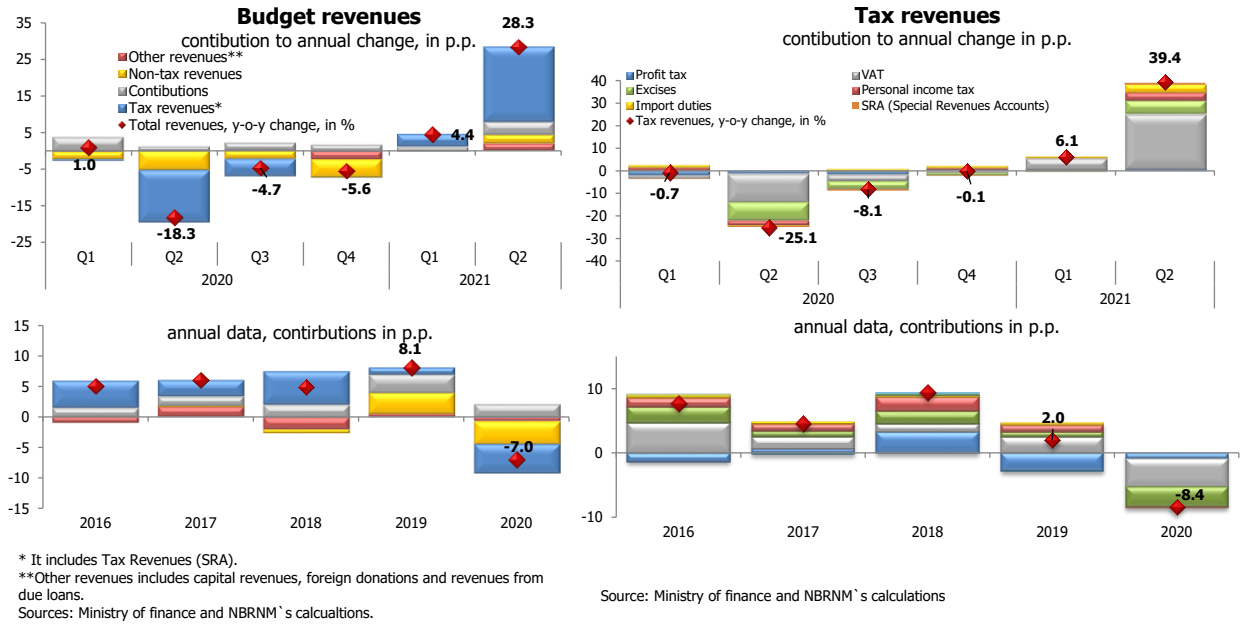
Amid economic recovery, in the second quarter of 2021, budget revenues recorded high annual growth, in part due to the low base effect when the economy registered a significant contraction with an adverse effect on budget revenues. Additionally, the growth of budget expenditures is significantly more moderate. Against such background, the budget deficit equaled 1.2% of GDP. Budget deficit amounted to Denar 24,202 million or 3.3% of GDP in the first eight months of 2021, constituting 52.4% of the forecast budget deficit for 2021. In this period, the budget deficit was mostly financed through net government borrowing on the foreign market, and less through net borrowing on the domestic market, with part of the funds retained on the deposit account with the National Bank. Thus, total public debt reached 62.5% of GDP at the end of the second quarter of 2021, which is by 2.3 percentage points more compared to the end of 2020.

In the second quarter of 2021, total revenues in the Budget of the Republic of North Macedonia⁶⁵ increased by 28.3%, on an annual basis (4.4% in the previous quarter). The annual growth of budget revenues is partly a result of the low base effect due to the adverse shock to the domestic economy from the rapid spread of COVID-19 and strict measures to prevent its spread. With the start of economic recovery, the second quarter witnessed an annual increase in all categories of budget revenues, mostly due to the growth of taxes⁶⁶, with a positive effect of the contributions, non-tax revenues and other revenues⁶⁷. Taxes, as the most significant revenue item, registered an annual growth of 39.4% in the second quarter of 2021 (with a positive contribution of 20.6 percentage points in the growth of total revenues). Contributions continued to increase at a faster rate compared to the previous period, registering an annual growth of 9% (a positive contribution of 3.5 percentage points), while non-tax revenues and other revenues were higher by 40.8% and 65.5%, respectively, on an annual basis (with a positive contribution of 2.4 percentage points and 1.9 percentage points, respectively).

⁶⁵Central budget and budgets of funds.

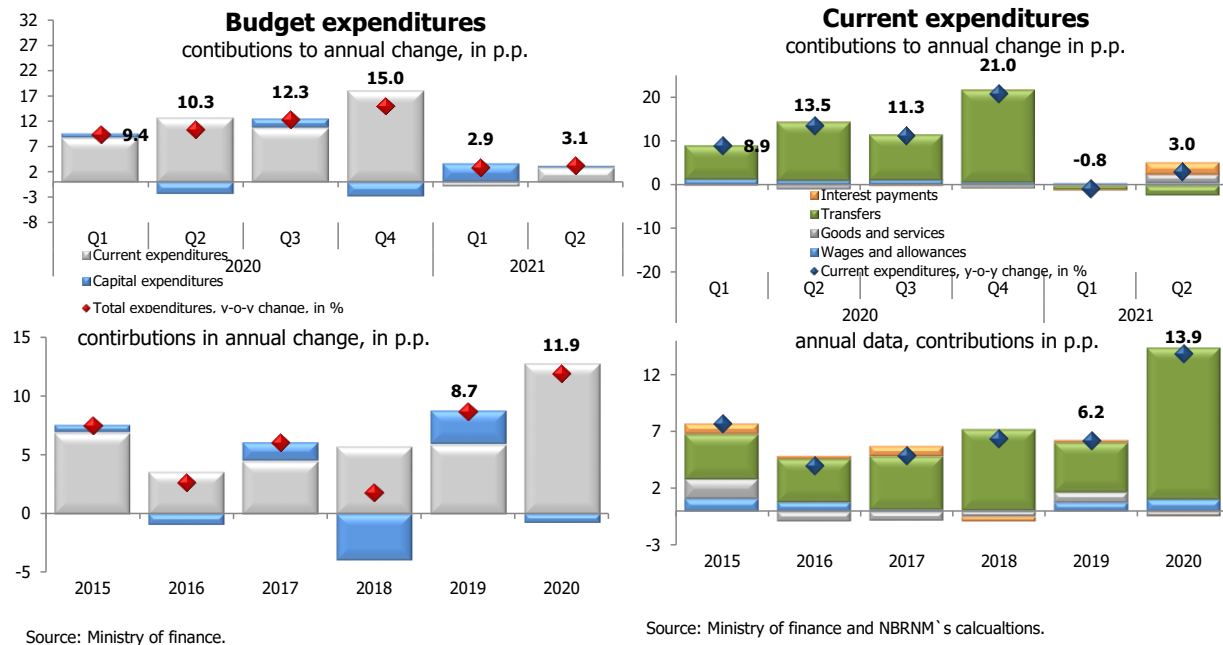
⁶⁶ It also includes own revenue accounts (SSP).

⁶⁷ Other revenues include capital revenues, donations from abroad and revenues from recovered loans.



Source: Ministry of finance and NBRNM's calculations

The growth of total tax revenues of 39.4% in the second quarter of 2021 stems primarily from the higher revenues from indirect taxes (positive contribution of 33.7 percentage points), as well as from direct taxes (positive contribution of 4.5 percentage points). Analyzing indirect taxes, higher growth was registered in VAT revenues (with a positive contribution of 24.1 percentage points), with lower contribution by excises and import duties revenues (positive contribution of 5.9 percentage points and 3.7 percentage points).

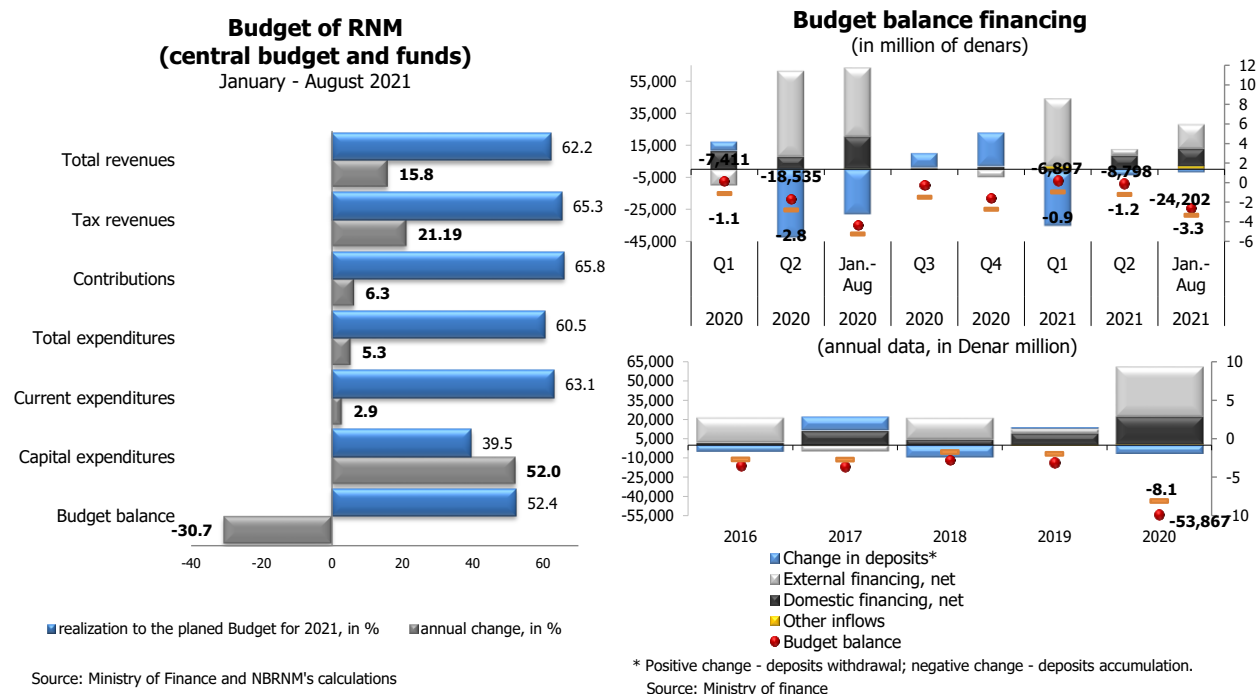


Source: Ministry of finance and NBRNM's calculations.

The growth of total budget expenditures in the second quarter of 2021 was 3.1% on an annual basis (2.9% in the previous quarter), which is mostly due to higher current expenditures (contribution of 2.9 percentage points), and less to capital expenditures (contribution of 0.3 percentage points). The increase in current expenditures by 3% (a decline of 0.8% in the previous quarter) is mainly due to the



increase in the categories of interest payments⁶⁸ and goods and services (positive contributions of 2.8 percentage points and 2 percentage points, respectively), with a decline of the category of transfers⁶⁹ (negative contribution of 2.2 percentage points)



In the second quarter of 2021, the budget deficit was Denar 8,798 million or 1.2% of GDP, which is lower compared to the same period last year (deficit of 2.8% of GDP⁷⁰). The deficit was mainly financed by net government borrowing on the domestic market, coupled with net borrowing on the foreign market, while in this period, the government accumulated funds on the deposit account with the National Bank.

⁶⁸ It is mostly a result of the payment of interest on the Eurobond issued in June 2020.

⁶⁹ The category of transfers refers to pension costs, social security costs, health care costs and other transfers (mainly subsidies). The decrease in transfers in the second quarter of 2021 is mostly related to the higher base effect, when wage subsidies were paid to companies affected by the corona crisis (mostly in June).

⁷⁰ The analysis of nominal GDP for 2021 uses the NBRM October forecasts.


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

| | 2021 | | | | | 2021 | | | | | |
|--------------------------------|------------------|-------------------------|---------------|---------------|----------------|---|---|---|---|---|---|
| | Budget for 2021 | Revised Budget for 2021 | Q1 | Q2 | Jan.-Aug. 2021 | Q1 | | Q2 | | January-August | |
| | in denar million | | | | | Annual changes, period in Q1 2021, in % | Contributions in annual changes, period in Q1 2021, in p.p. | Annual changes, period in Q1 2021, in % | Contributions in annual changes, period in Q1 2021, in p.p. | Annual changes, period in Q1 2021, in % | Contributions in annual changes, period in Q1 2021, in p.p. |
| TOTAL REVENUES | 212,630 | 222,542 | 48,545 | 52,522 | 138,444 | 4.4 | 4.4 | 28.3 | 28.3 | 15.8 | 15.8 |
| Tax revenues and contributions | 186,282 | 193,068 | 44,304 | 47,244 | 125,931 | 5.0 | 4.6 | 26.4 | 24.1 | 15.3 | 14.0 |
| Taxes* | 117,982 | 123,873 | 28,004 | 29,817 | 80,382 | 6.1 | 3.4 | 39.4 | 20.6 | 21.1 | 11.7 |
| Contributions | 68,300 | 69,195 | 16,300 | 17,427 | 45,549 | 3.3 | 1.1 | 9.0 | 3.5 | 6.3 | 2.3 |
| Non-tax revenues | 16,954 | 17,586 | 3,298 | 3,319 | 8,900 | -0.9 | -0.1 | 40.8 | 2.4 | 24.6 | 1.5 |
| Capital revenues | 3,187 | 3,187 | 194 | 238 | 671 | -48.7 | -0.4 | 73.7 | 0.2 | -31.1 | -0.3 |
| Foreign donations | 6,207 | 8,701 | 749 | 1,721 | 2,942 | 24.0 | 0.3 | 64.4 | 1.6 | 36.6 | 0.7 |
| TOTAL EXPENDITURES | 247,568 | 268,772 | 55,444 | 61,320 | 162,646 | 2.9 | 2.9 | 3.1 | 3.1 | 5.3 | 5.3 |
| Current expenditures | 223,513 | 238,968 | 51,463 | 58,740 | 150,872 | -0.8 | -0.8 | 3.0 | 2.9 | 2.9 | 2.7 |
| Capital expenditures | 24,055 | 29,804 | 3,981 | 2,580 | 11,774 | 98.0 | 3.7 | 6.7 | 0.3 | 52.0 | 2.6 |
| BUDGET DEFICIT/SURPLUS | -34,938 | -46,230 | -6,899 | -8,798 | -24,202 | | | | | | |
| Financing | 34,938 | 46,230 | 6,899 | 8,798 | 24,202 | | | | | | |
| Inflow | 78,291 | 89,583 | 12,014 | 12,167 | 64,335 | | | | | | |
| Other inflows | 800 | 2,300 | 2,003 | 188 | 2,243 | | | | | | |
| Foreign loans | 53,042 | 63,731 | 43,062 | 5,965 | 49,427 | | | | | | |
| Deposits | 1,312 | 403 | -33,898 | -3,880 | -1,940 | | | | | | |
| Treasury bills | 23,129 | 23,129 | 834 | 9,894 | 14,592 | | | | | | |
| Sale of shares | 8 | 20 | 13 | 0 | 13 | | | | | | |
| Outflow | 43,353 | 43,353 | 5,115 | 3,369 | 40,133 | | | | | | |
| Repayment of principal | 43,353 | 43,353 | 3,266 | 3,369 | 38,284 | | | | | | |
| External debt | 37,234 | 37,234 | 917 | 1,927 | 34,313 | | | | | | |
| Domestic debt | 6,119 | 6,119 | 2,349 | 1,442 | 3,971 | | | | | | |
| Other outflows | | | 1,849 | 0 | 1,849 | | | | | | |

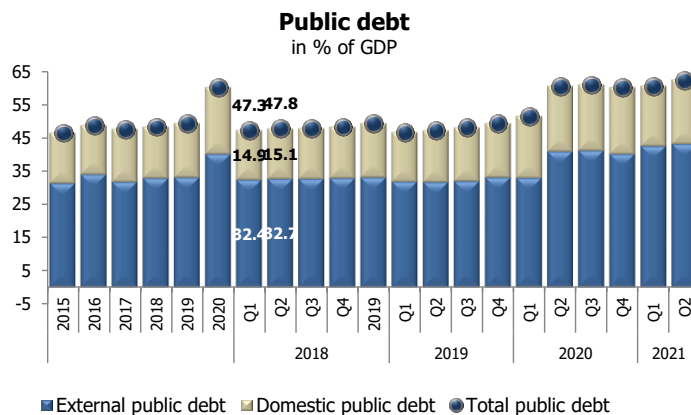
* Includes Special Revenues Accounts (SRA)

Source: Ministry of Finance and NBRNM calculations.

In the period January-August 2021, total budget revenues increased by 15.8% on annual basis. The considerable increase in budget revenues is partly due to the low base effect, reflecting the deteriorating economy due to the health crisis caused by COVID-19 and the significantly reduced budget inflows, which was most pronounced in the period April-May. The increase in budget revenues is largely due to higher performance in taxes, contributions, non-tax revenues and foreign donations (positive contribution of 11.7 percentage points, 2.3 percentage points, 1.5 percentage points and 0.7 percentage points, respectively), while capital revenues registered a slight decrease (negative contribution of 0.3 percentage points). Furthermore, budget expenditures were higher by 5.3% on an annual basis, given the growth in both current and capital expenditures (positive contributions of 2.7 percentage points and 2.6 percentage points, respectively). In the first eight months of 2021, budget deficit amounted to Denar 24,202 million or 3.3% of GDP, making up 52.4% of the deficit forecast⁷¹ for 2021. In this period, the budget deficit was mostly financed through net government borrowing on the foreign market⁷², and less through net borrowing on the domestic market, with part of the funds retained on the deposit account with the National Bank.

⁷¹ Budget Revision for 2021 was adopted on 28 July 2021 (Official Gazette of the Republic of North Macedonia No. 171 of 28.7.2018).

⁷² Government borrowing on the foreign market is mostly due to the eighth Eurobond issued in early March in the amount of Euro 700 million and withdrawal of the second tranche of the EU macrofinance support in early June in the amount of Euro 80 million (out of Euro 160 million EU microfinance support to fight corona crisis).



Source: MoF and NBRNM calculations.

At the end of the second quarter of 2021, total public debt⁷³ equaled 62.5% of GDP, which is an increase of 2.3 percentage points of GDP compared to the end of 2020. This change was mainly driven by the external public debt (the Eurobond issued) which increased by 3 percentage points of GDP and equaled 43.2% of GDP at the end of the quarter, despite the decrease in the internal public debt of 0.7 percentage points of GDP (to 19.3% of GDP). Analyzing the debt structure, total government debt⁷⁴ was 54.2% of GDP, which is an increase of 3 percentage points, compared to the end of 2020, while public sector debt (guaranteed and non-guaranteed)⁷⁵ was 8.3% of GDP, which is a decrease of 0.7 percentage points. At the end of the first quarter of 2021, compared to the same period of 2020, total public debt increased by 1.9 percentage points of GDP.

VI. Macroeconomic forecasts and risks

The latest available indicators for the domestic economy, together with the built-in external and domestic assumptions for the next period do not indicate major changes in the economic dynamics compared to the April forecasts. The domestic economic recovery is as expected, despite the uncertainty associated with the pandemic crisis and the emergence of a new wave of pandemics during the third quarter of 2021. Growth forecasts keep the previous assumptions for improvement of the external environment, amid assessments for more pronounced foreign demand recovery and more favorable price conjuncture in metals, which will have a stimulating effect on the domestic export segment. On the other hand, unfavorable external factors, which have become particularly pronounced recently, are the disruptions of the global supply chains, transport and logistics, which affect the regular production process worldwide, especially in the automotive sector and the food industry. However, such unfavorable trends and their effects on the economy are assessed as temporary, while expectations for their stabilization during 2022 are maintained. But if this assumption does not materialize, it could have a negative impact on the current economic

⁷³ 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 public debt 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.

⁷⁴ Government debt is defined as a sum of debts of the central government, the public funds and the municipalities.

⁷⁵ 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).

outlook. In terms of the domestic environment, it is still expected that the acceleration immunization will have a positive effect on the trust and behavior of economic agents, which will contribute to improving economic conditions, with expectations for gradual stabilization of the epidemiological situation and gradual depletion of the negative effects of the health crisis in the forecast horizon. The assessments for further introduction of public and private investments and for inflow of foreign investments remained the same, amid stable environment. In accordance with these assumptions for the external and domestic economic context, and with achievements close to the expected, the October forecasts keep the forecasts for economic growth of 3.9% in 2021 and with the same dynamics in 2022. Such growth trajectory implies expectations for economic rebound to the pre-pandemic level in 2022. The growth of the economy will continue in 2023 and 2024, with the same expected rate of 4%, as in April. Analyzing the GDP structure, the economic growth in the coming period is still expected to be entirely due to domestic demand, and would make a higher positive contribution to growth, compared to net exports, which would have a more pronounced negative contribution. The higher performances during the year and the upward corrections in the external input assumptions for energy and food prices led to a moderate upward revision of the inflation rate for 2021, which is now estimated to be 3.1% (2.2% in the previous forecast). However, import pressures related to higher global energy and food prices and the mismatch between supply and demand are generally assessed as temporary and are expected to be gradually exhausted in the second half of next year. Hence, in 2022, it is expected that the inflation rate will decrease and will average 2.4%, which is a slightly higher level compared to the April estimate (2%). Furthermore, for 2023-2024, inflation is expected to stabilize and move around the historical average of 2%. Estimates of external sector movements point to certain widening of the current account deficit in 2021 to 3.8% of GDP, amid unfavorable price pressures on energy imports and pronounced risks from the disrupted functioning of global supply chains. For 2022, the forecasts envisage certain stabilization of stock market volatility and gradual stabilization of supply chains during the year, which would accordingly lead to maintaining the current account deficit at 3.8% of GDP. For 2023-2024, there are expectations for more pronounced exhaustion of the negative effects of COVID-19 and the pandemic risks and further reduction of the current account deficit to an average level of 2% of GDP. Throughout the forecast horizon, foreign reserves are expected to remain appropriate.

6.1. Assumptions in the external environment forecast⁷⁶

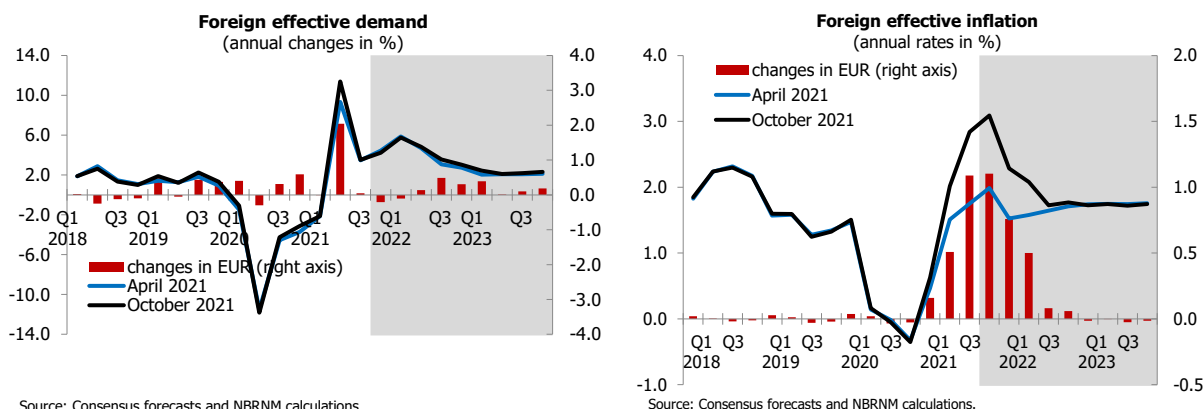
The latest estimates relating to the foreign effective demand⁷⁷ were revised upwards in the entire forecast horizon. Namely, it is now expected the foreign effective demand to be 4.1% and 4.3% in 2021 and 2022, respectively (3.6% and 4.1%, respectively in April). The upward revision for 2021 reflects the expectations for higher economic growth in almost all our major trading partners, mostly Italy, Serbia, Greece and Bulgaria, while for 2022 it is largely due to the expectations for

⁷⁶ Historical data on foreign demand, foreign inflation, exchange rate of the US dollar/euro and EURIBOR are sourced from Eurostat, while the World Bank statistics is a source of the data on prices of oil, food and metals. The forecasts of foreign demand, foreign inflation, foreign exchange rate of the US dollar and EURIBOR are based on the Consensus Forecast, while the forecasts of the prices of oil, food and metals are based on the forecasts of market analysts. The analysis uses various reports of the IMF, the World Bank, ECB, FAO, OPEC and specialized economic portals.

⁷⁷ Foreign effective demand is calculated as the weighted sum of GDP indices of the major trading partners of the Republic of North Macedonia. The calculation of this index includes Germany, Greece, Italy, the Netherlands, Belgium, Spain, Serbia, Croatia, Slovenia and Bulgaria.

greater economic activity in Germany.⁷⁸ As for 2023, further positive growth rates are expected, estimating that the increase in the foreign demand will decelerate and equal 2.3%.

Regarding foreign effective inflation,⁷⁹ upward corrections for 2021 and 2022 were also made compared to April forecast, with now expecting to equal 2.2% and 2%, respectively (compared to 1.4% and 1.6% in 2021 and 2022, respectively, in April). The correction made is due to the assessment for higher inflation in almost all our import partners, with the largest positive contribution in 2021 being made by Germany, Serbia and Croatia⁸⁰, and Germany and Croatia in 2022. Growth is expected to slow down in 2023, with foreign inflation estimated at 1.7%.



According to the latest forecasts for the movement of the euro/US dollar exchange rate in 2021 and 2022, an upward revision was made compared to April. The current forecasts envisage smaller depreciation of the US dollar against the euro of 4.5% in 2021, compared to 5.6% in April and a small appreciation of 0.3% in 2022, instead of a depreciation in April (of 1.0%). This shift mostly reflects the larger uncertainty about the impact of the new corona virus variants on the global economic growth, as well as the investors' expectations for gradual tightening of the monetary policy in the USA. For 2023, the US dollar is expected to depreciate against the euro, and the decline will be 0.9%.

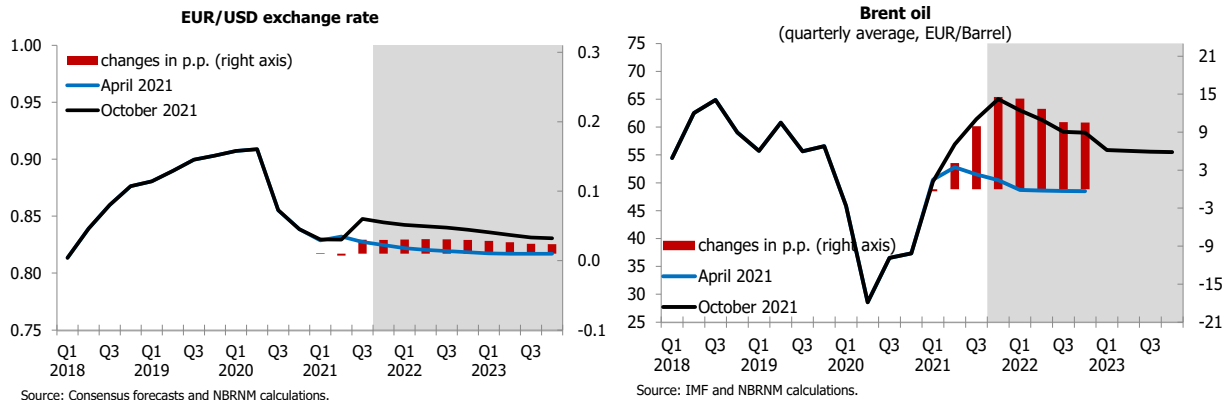
The new oil price estimates have been revised upwards, compared to the April forecast, especially for 2021. Namely, in 2021 the currently expected growth equals 57.6% (instead of a growth of 38.5% in April), while in 2022 a small growth of 3.8% is expected, compared to the projected fall of 5.3% in April. The upward revision largely reflects the expectations for strong growth in oil demand, extension of OPEC + measures to limit oil production⁸¹ and reduced inventory levels as a result of the stagnation of investments in new production facilities during 2020. In 2023 the estimates indicate downward movement of the prices, and the decrease is expected to equal 8.2%.

⁷⁸Forecasted growth in Germany of 3.3% in 2021 and 4.5% in 2022 (3.4% and 3.9% for 2021 and 2022, respectively in April).

⁷⁹ The foreign effective inflation is calculated as 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 calculation of this indicator includes Bulgaria, Germany, Greece, France, Italy, Austria, Slovenia, Croatia and Serbia. Inflation in Croatia and Serbia has been adjusted for the changes in the exchange rate.

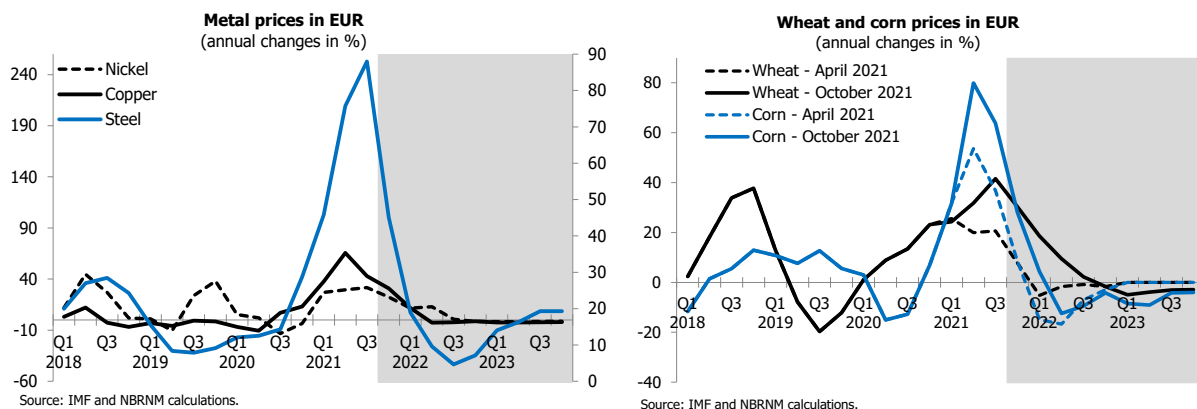
⁸⁰ Inflation in Serbia and Croatia was adjusted for the changes in the exchange rate.

⁸¹On 4.10.2021 OPEC+ countries made a decision to extend the measure which was adopted in July, for a gradual monthly increase in oil production by 400 barrels per day, also in November 2021.

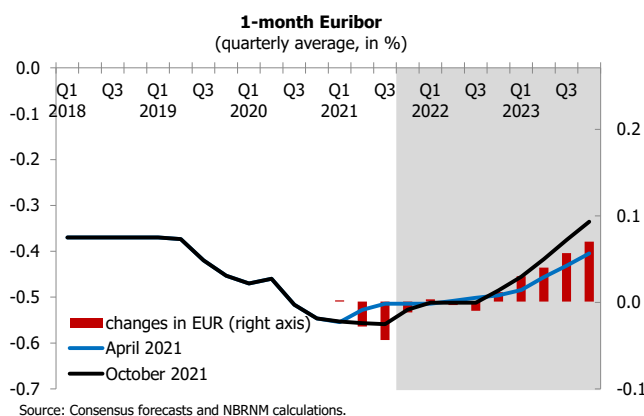


In 2021, the metal prices have mainly been revised upwards compared to April forecasts, while for 2022 divergent movements are being registered. Namely, significant growth in the copper and nickel prices in 2021 is currently expected, compared to the April forecasts, while for 2022 they are expected to grow, compared to the anticipated slight decline. The upward adjustment in the copper prices is due to disrupted production in Chile and growth in demand in China as a result of the government measures to support the economy and employment. Regarding nickel, the correction is a result of the expectations for further solid demand by the industrial sectors, especially in the production of electric vehicles, as well as the low level of inventories. In the case of steel, the corrections are in a different direction, with a larger increase in prices in 2021 and a larger decline in 2022 being expected compared to the April forecast. The upward correction in 2021 is a reflection of the high demand for steel, during the more significant global economic movement after the pandemic year, while for 2022 the downward correction is due to the gradual stabilization of prices in anticipation of more moderate growth in demand. In 2023, stabilization of metal prices and their reduction compared to the previous year is expected, with a more significant drop in the price of steel.

The estimates for the prices of primary food products for 2021 and 2022 have been revised upwards, which is larger for this year. Namely, currently a significant growth in food prices is expected in the current year, than forecasted in April, while moderate growth is expected in the following year, instead of the slight decline in the wheat prices and less slight decline in the corn prices. The upward revision in wheat prices is largely due to expectations for lower levels of global stocks (mainly in Canada, Russia and the United States), amid rising demand for wheat. The upward correction in corn is due to higher demand expectations, driven by demand for food in Brazil, Canada and China, and industrial demand in Brazil and the United States. For 2023, a small decline in stock exchange food prices is expected.



Regarding the interest rate of the one-month EURIBOR, the forecasts are almost unchanged compared to April, still expecting it to move in the negative zone for the entire forecasting horizon. Namely, it is now expected that the one-month EURIBOR would average -0.55% in 2021 (-0.53% in April) and -0.51% (-0.5% in April) in 2022. The unchanged ratings reflect expectations that the ECB will continue its accommodative monetary policy to support the economic recovery following the pandemic, amid further uncertainty surrounding the future development of the pandemic and an assessment of temporary inflationary pressures in the euro area. For 2023, the EURIBOR interest rate is expected to remain in the negative zone and will be -0.4%, on average.



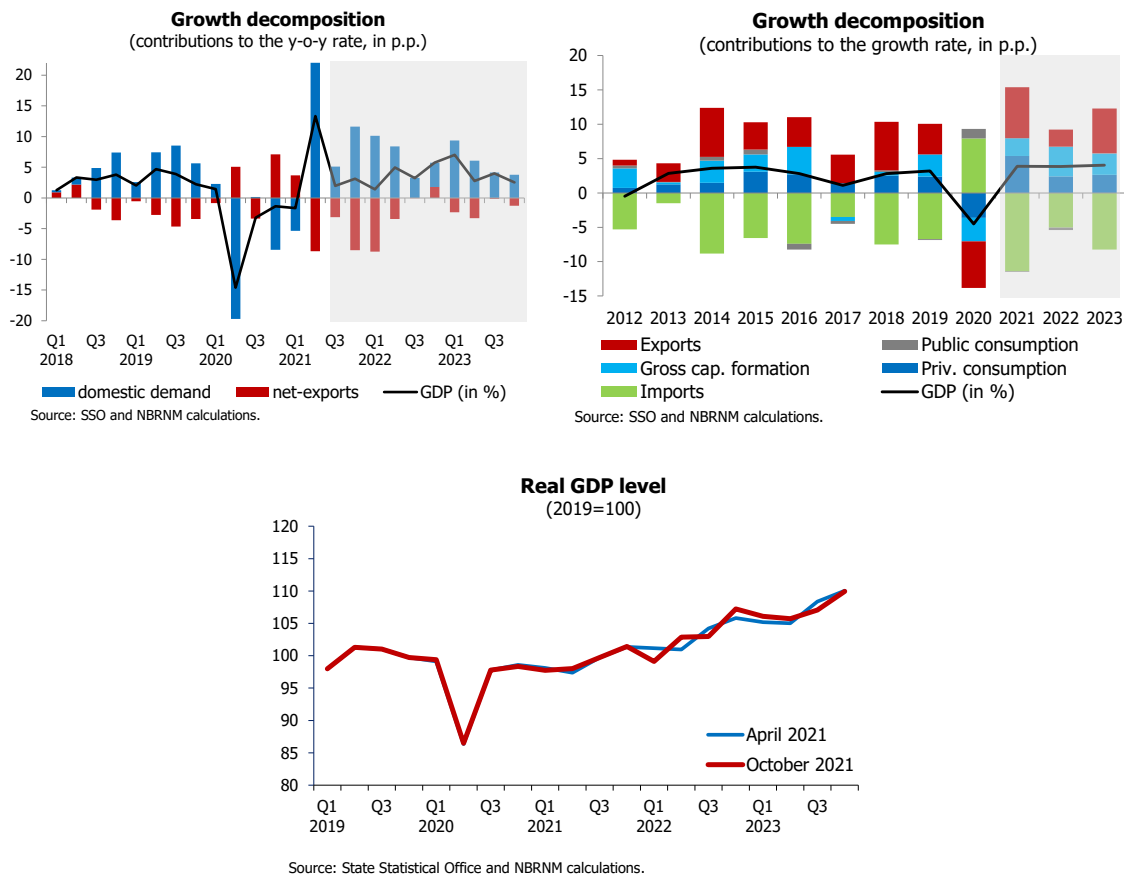
6.2. Forecast and effects on monetary policy

The basic macroeconomic scenario for the Macedonian economy is similar to the April forecast, without major changes in growth perceptions, but with further downward risks, especially in the external environment. Notwithstanding the above, the forecasts still indicate favorable external position of the economy and foreign reserves, which in the next period will be at an appropriate level. At the same time, with further moderate recovery of the economy this year, projected growth path for the next period and at the same time significant growth of world prices of energy and other primary products in 2021, greater pressures on the import side are expected, especially in the current year, whose scope, however, could not jeopardize the external balance. Hence, it is predicted that the current account deficit will expand by 2021, followed by a path of its gradual narrowing, and the main sources of funding will be inflows of foreign direct investment and public sector borrowing. From the aspect of the relevant foreign interest rate, as an important exogenous determinant of the domestic monetary policy stance, no significant changes have been made in this forecast. Thus, it is still expected that the interest rate of the one month EURIBOR will be in the negative zone over the entire forecast horizon, according to the expectations for maintaining the stimulating character of the ECB monetary policy. The risks of achieving the basic macroeconomic scenario are assessed as significantly low, and mainly similar to those in the April forecast horizon. The main downside risks are again related to the course of the pandemic, including the possibility of the emergence of new transmissible variants of the corona virus, which would lead to the introduction of stricter restrictive measures and more pronounced disruptions in trade flows and discrepancies between supply and demand, reducing the pace of immunization due to the growing hesitation of the population about vaccines, as well as problems with the distribution of vaccines globally. Also, the possible faster tightening of global financial conditions could adversely affect countries that depend on external financing or have increased public debt. A new downside risk to economic growth is the global energy crisis, which

*if prolonged could lead to a reduction in global industrial activity, but also to demand, which would slow down the economic recovery. Other global risks, which are influenced by geopolitical, information, security, social and climatic factors, are presented in this cycle, as well. **On the other hand, a positive risk is the possible intensification of the vaccination process globally, which through the trust channel would have favorable effects on consumption and investment in the private sector, as well as possible faster productivity growth, driven by the trend of automation and job transformation that started during the pandemic.** Domestic positive risks remain as a possibility for more pronounced positive effects of our country's membership in NATO, as well as possible start of the negotiation process for full EU membership, and a new positive risk for growth projections is the realization of the latest development and investment plans of the Government⁸² in the medium term, which would support investment projects in the public and private sectors and increase the growth and competitiveness of the economy in the medium term.*

After the reduction of economic activity in 2020, in the first half of 2021 the domestic economy returned to the growth zone, which is partly due to the low comparison base from the previous year, when the effect of restrictive measures was strongest, but also the positive impact from the beginning of the process of massive immunization on the confidence and optimism of economic entities. Thereby, the recovery of the economic activity as a whole resulted from the positive contribution of the domestic demand. The growth of this component is mostly explained by the higher private consumption, supported by the strong growth of disposable income, in conditions of adequate adjustment of the behavior of the subjects to the epidemiological situation and lower comparative basis from the previous period. There are similar effects with the investment demand, which has also increased, probably due to the reduction of investment uncertainty and restraint with the calming of the epidemiological situation. Simultaneously, slight increase was registered also in the public consumption. On the other hand, the net export had negative contribution to the growth, given registered high growth rates and export and import. The available high-frequency data and ratings point to continued economic recovery in the third quarter, although the annual growth rate will be more moderate compared to the previous quarter, partly due to the comparison basis, as well as due to the new rise in the number of infected with COVID-19 in summer period and the introduction of additional virus protection measures, which impose obligatory vaccination certificates for entry into facilities and in the presence of group events. Assuming further stable development of the pandemic and absence of stricter restrictive measures, in the last quarter of the year a slight acceleration of the growth of economic activity is expected, resulting from the recovery of investment activity, as well as further growth of private consumption, in conditions of faster growth of foreign demand, positive expected effects of vaccination on the mobility of the immunized population, greater confidence among consumers and investors, growth of disposable income and further favorable financial conditions. **Consequently, for the entire 2021, the domestic economy is expected to grow by 3.9%, with the same growth rate being forecasted for 2022.** Such a projected GDP path will allow to compensate the economic losses from the corona crisis and overcoming the pre-pandemic level of 2019 during 2022. Furthermore, with the gradual exhaustion of the negative shock from the health crisis, in **2023 - 2024 it is estimated that GDP growth will reach 4%.** By structure, it is expected that domestic demand will have a high positive contribution to the entire forecast horizon, as opposed to the contribution of net exports, which will be negative.

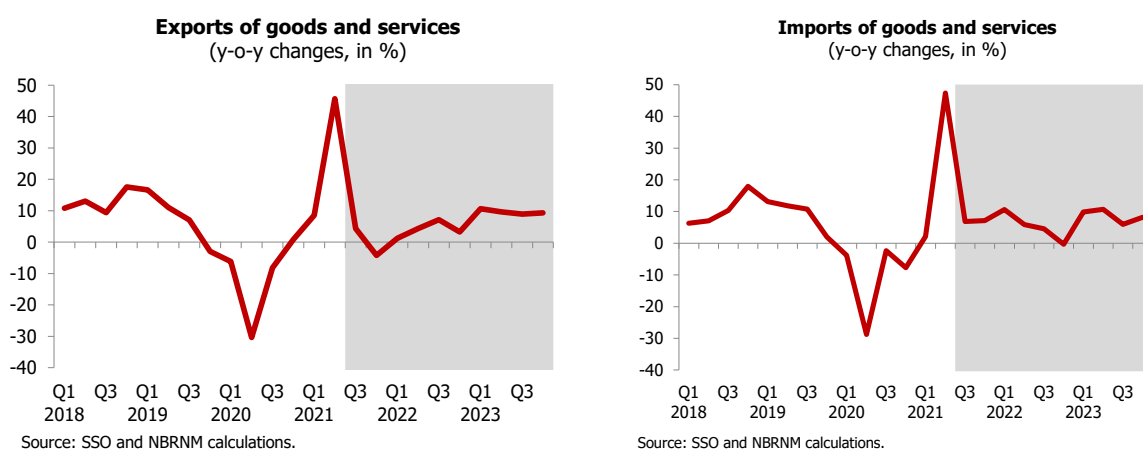
⁸²In accordance with the Plan for accelerated economic growth for 2022 - 2026.



From the aspect of the expenditure side of GDP, most of the components are expected to grow in the positive zone in the forecast horizon. Thus, in accordance with the achievements and estimates so far, recovery of real exports of goods and services from the pandemic crisis is expected for 2021, which in part reflects the low comparison base from last year, but in part reflects the strong growth of foreign demand, after the last year drop, the revitalization and intensified export activity of the capacities of the automotive industry in the technological-industrial development zones and the improved export achievements of the companies from the traditional export sector, primarily as a result of the extremely favorable conjuncture in the export metal prices. Hence, with the projected double-digit growth, it is estimated that real exports would be the component with the highest single positive contribution to GDP growth for this year. Furthermore, given the high level already reached in 2021, a certain slowdown in real export growth is expected in 2022, which would intensify again in 2023. Thus, on a collective basis, exports would continue to be the most important individual factor of overall economic growth in the coming period. The positive export expectations in the part of the new industrial facilities and the traditional segment, will support the envisaged growth, stimulated by the further growth of the foreign demand, the increase in the export orders and the mostly favorable movements in the stock exchange metal prices. However, some uncertainty about the dynamics of future export activity arises from the possible prolonged disruptions in the global supply and transport chains, which could adversely affect the export demand for domestic products.

Observed within the domestic demand, for 2021 it is estimated that the largest positive contribution to the growth will be made by the household consumption, while in the next two years, the gross investment would have a greater effect on the growth. The estimates for high growth of private consumption in 2021, in addition to the low comparative basis, are largely supported by the strong growth of disposable income,

especially driven by the pronounced recovery of private transfers in conditions of facilitated international traveling of the population, and has an impact and enhanced optimism with the implementation of the immunization process and changes in consumer behavior. Thus, it is expected that private consumption will fully recover and exceed the pre-crisis level in the current year. Furthermore, for the period 2022 - 2023, further growth of private consumption is predicted, but more moderate, similar to the pre-crisis period, in conditions of gradual exhaustion of the negative effects of the pandemic on consumer decisions. In doing so, private consumption will be supported by positive developments in all major sources of funding. Thus, solid growth of the wage amount is expected, having in mind increased activity in the economy and further solid growth of employment. Regarding other components of the disposable income, the amount of pensions is expected to increase, in line with the legal harmonization with the price growth and further increase in the number of pension beneficiaries, with increased inflows based on private transfers also being anticipated. At the same time, the constant solid growth of the credit activity of the domestic banks in this segment is expected to contribute to support the household consumption in the future period.

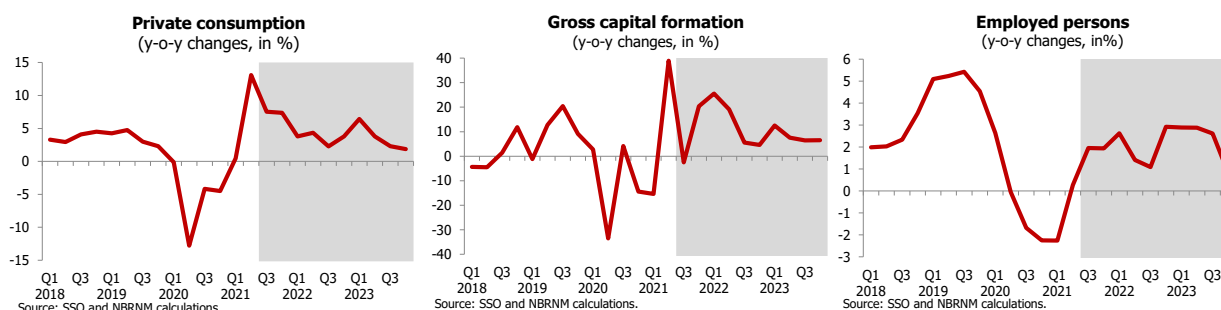


After the negative shock and the low level in 2020, for 2021 a solid recovery of **gross investments** and their positive contribution to the growth is predicted, in conditions of growth of the foreign demand back in the positive zone, further realization of the public investments and support of the private investments through favorable credit lines, strong export growth, higher inflows of foreign direct investment and gradual return of confidence and reduction of risk aversion of private entities due to the pandemic. Estimation for gradual stabilization of the epidemiological situation in the country and abroad and the more predictable environment would have a positive impact on investment inclination in the coming period, because of which the effect of the gross investment in 2022 - 2023 on domestic demand would become bigger and would be the main driver of its growth. Hence, more pronounced growth of investment activity is expected, especially in 2022, which is based on the expectations for accelerated growth of foreign demand, continuation of construction works related to public investments in road infrastructure, new state investments related to NATO membership, higher investments of private entities in the residential and energy sector and higher growth of foreign direct investments. It is also expected that favorable financial conditions and increased corporate lending by banks will have an additional stimulating effect on the overall investment cycle in the country.

According to the latest medium-term fiscal plan, after the significant budget stimulus in 2020 to deal with the acute phase of the pandemic, a moderate reduction of real **public consumption** is expected for the period 2021 - 2023⁸³ on a cumulative basis, and on average, it will have negative contribution to the expected GDP growth.

⁸³ The public consumption forecasts are based on the available data from the Budget Revision for 2021 from July 2021 and the Fiscal Strategy 2022-2024 (with a prospect until 2026) from May 2021.

The real import of goods and services would increase significantly in 2021, mainly due to stronger export demand, as well as pronounced recovery of the main components of domestic demand - private consumption and gross investments. Given the stronger expected recovery of imports from exports, it is estimated that net exports will negatively affect the overall economic growth for this year. Furthermore, it is predicted that the import demand to increase in the next period, although the growth will be more moderate, given downward movement of rates for 2022 and upward movement for 2023, which is in line with the projected dynamics of real exports and private and investment consumption. Thereby, it is expected that net exports will have a negative contribution to GDP growth in 2022 and 2023, which, however, will gradually narrow by the end of the forecast horizon.



The latest credit market forecasts indicate moderate acceleration in the credit activity in 2021 and gradual stabilization of the growth rates in the next three years. Namely, it is expected that the solid growth of loans in the first three quarters, supported by the measures taken by the National Bank to mitigate the adverse effects on the economy caused by the COVID-19 pandemic, will continue until the end of the year. Thus, it is currently estimated that at the end of 2021 the growth rate of loans will be 7.1% (4.7% at the end of 2020). In the period ahead, gradual stabilization of the lending activity is expected, at an average growth rate of 6.9% in the period 2022 - 2023 and 7.8% in 2024, in circumstances of growth in the domestic economy, stabilization of the expectations and increased demand for loans by households and the corporate sector. Credit growth will continue to be supported by the solid deposit growth as the main source of financing. In accordance with the estimates for stabilization of the environment, intensification of the economic activity and further growth of the propensity to save in banks, annual deposit growth of 7.1% is expected by the end of 2021 (5.7% in 2020). The solid growth of total deposits will continue also in the coming period, amid a forecasted average rate of annual growth of 7.5% in the period 2022 - 2023 and 8% in 2024.

It is expected that the current account deficit in 2021 will moderately expand by 0.4 percentage points of GDP on an annual basis, reaching a level of 3.8% of GDP, mostly due to the deteriorated expectations for the trade balance, and a small contribution to the change is also expected from the higher deficit in primary income. Regarding the foreign trade, a more pronounced upward adjustment on the import side is forecasted, in part caused by price factors, which, despite the high growth in exports, would expand the trade deficit. There are also additional import pressures during 2021 due to the recovery of the domestic demand and of the export activity. On the other hand, a significant recovery in the surplus of the secondary income is expected, caused by private transfers which in 2021 would exceed the pre-pandemic level. Also, positive shifts are forecasted in the surplus in the trade in services, due to the expectations for better export performances in this category, especially in the category other services (mainly telecommunication, computer and investment services). **For the next 2022, no change in the current account deficit is forecasted (3.8% of GDP).** The gradual stabilization and the recovery of the value chains, supported by the falling risks from the pandemic in conditions of increased vaccination would contribute to stabilization of the balance of goods and services in the following year, due to the maintenance of the higher level of the energy deficit, while in the non-energy deficit, a significant narrowing is expected. Also, a certain narrowing of the primary income deficit is expected. The surplus in services



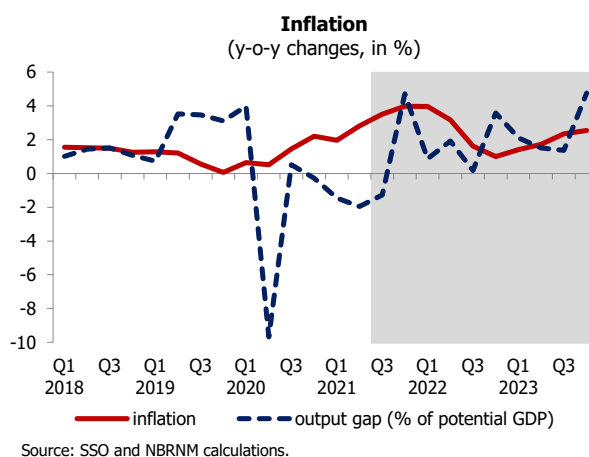
would continue to grow, and once the pre-pandemic level is reached, certain stabilization of the current transfers as a share in GDP is also envisaged. **The current account deficit in the period 2021 - 2022 will mostly be financed through long-term government borrowing, as well as by the foreign direct investments.** Amid expansion of the trade balance, part of the financing will be also through trade credits. On the other hand, it is expected that the net outflows in the category currency and deposits will continue, but at a more moderate pace, in conditions of gradual stabilization of the expectations and the confidence. **For the period 2023 - 2024, a further improvement of the current account is envisaged, whereby the average deficit would be 2% of GDP,** in conditions of a gradual exhaustion of the risks from the pandemic, stabilization of the situation globally, with both the value chains and with the temporary price pressures especially on the energy side, which would cause a more significant improvement in the balance of goods and services. It is envisaged that the borrowing of the public sector and the further growth of the foreign direct investments will be primary sources of financing of the current account deficit, which would also enable an additional increase in the foreign reserves. **Throughout the forecast horizon, foreign reserves are expected to remain appropriate.**

Balance of payments forecast (% of GDP)

| | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | 2024 |
|-------------------------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|-------------|
| Current account | -1.0 | -0.1 | -3.3 | -3.4 | -3.8 | -3.8 | -2.4 | -1.6 |
| Balance of goods and services | -14.1 | -12.7 | -14.4 | -12.8 | -16.2 | -16.2 | -13.7 | -12.5 |
| Trade balance, net | -17.8 | -16.2 | -17.4 | -16.8 | -20.4 | -20.8 | -18.3 | -17.3 |
| Services, net | 3.7 | 3.5 | 3.0 | 4.0 | 4.2 | 4.6 | 4.6 | 4.8 |
| Primary income, net | -4.0 | -4.2 | -4.6 | -3.8 | -4.0 | -3.8 | -4.4 | -4.4 |
| Secondary income, net | 17.0 | 16.8 | 15.7 | 13.2 | 16.4 | 16.2 | 15.6 | 15.4 |
| Private sector | 15.9 | 15.8 | 15.4 | 12.2 | 15.4 | 15.5 | 15.0 | 14.8 |
| Capital account, net | 0.2 | 0.1 | 0.1 | 0.1 | 0.0 | 0.0 | 0.0 | 0.0 |
| Financial account, net | 0.5 | -5.0 | -6.1 | -4.1 | -4.5 | -4.0 | -3.7 | -2.6 |
| Direct investment, net | -1.8 | -5.6 | -3.2 | -1.4 | -3.0 | -3.2 | -3.4 | -3.4 |
| Portfolio investment, net | 0.2 | -3.0 | 1.3 | -2.6 | -1.3 | 0.3 | -0.2 | 0.3 |
| Other investment, net | 2.1 | 3.6 | -4.2 | 0.0 | -0.2 | -1.0 | -0.1 | 0.5 |

Source: NBRNM

For 2021, a temporary and moderate acceleration in the inflation rate in the domestic economy is expected, which will be mainly conditioned by the faster growth of import prices, while no significant inflationary pressures are expected through the domestic demand channel. Thus, after the price growth of 1.2% in the previous year, **for 2021 it is estimated that inflation will reach 3.1%,** amid upward movements in all its components. Moreover, the largest contribution to the faster growth of domestic prices is expected from the energy component, which is associated with the substantial increase in the global energy prices in world markets this year, as opposed to their decline last year. Also, an acceleration is expected in both food and core inflation, which is in line with the forecasts for growth of the world food prices, when disturbances on the supply side still exist, as well as for a gradual recovery of the domestic economy from the pandemic crisis. **Following the temporary acceleration in 2021, under the influence of the factors on the supply side, during 2022, prices would decrease, whereby the inflation rate would average 2.4%.** This downward movement in inflation largely results from the expected slowdown in the growth of the prices of the energy and core component, and amid embedded assumptions for a more moderate growth of energy prices in world markets. On the other hand, with the stabilization of the global markets of primary products and the reduction of the pressures from import on domestic prices, **it is envisaged that inflation will decrease in 2023** and will again reduce to the historical average of 2%, stopping at that level also in 2024. The main risks in terms of the inflation forecast relate to the extremely high volatility of the prices of primary products in world markets, which is especially associated with the uncertain character of the global energy crisis, as well as with the possible further adverse effects of the corona-crisis on their supply and demand. Additional risk also includes the possible more pronounced transfer of the growth of the prices of raw materials and of the costs for energy and transport on the final prices of products and services, in case of a more significant reduction of the profit margins of business agents.



6.3. Comparison with the previous forecast

Compared to the April forecasting round, in the latest macroeconomic forecasts no changes were made in the expectations for GDP and its structure, but certain changes were made in the assessments for the inflation and in the balance of payments. Thus, the economic growth forecast in the period 2021 - 2023 is the same as in April, amid performances close to the forecasted rate, on average, for the first half of 2021 and unchanged assessments for the period ahead. Inflation has been revised upwards for the period 2021 - 2022, due to the higher performances in all components in the first three quarters of the current year and the higher input assumptions than the April assessments, while the assessment for 2023 has remained unchanged. The upward adjustments of the expectations for the prices of primary products, especially energy prices, as well as the recovery of the domestic and export demand conditioned faster growth of imports than expected and slightly higher average current account deficit in the period 2021 - 2023, compared with the April forecast.

Forecast of selected macroeconomic variables

| | 2021 forecast | | 2022 forecast | | 2023 forecast |
|--|---------------|-------------|---------------|-------------|---------------|
| | Apr. | Oct. | Apr. | Oct. | Oct. |
| GDP, % | 3.9 | 3.9 | 3.9 | 3.9 | 4.0 |
| Private consumption | 3.8 | 7.0 | 3.5 | 3.5 | 3.6 |
| Gross capital formation | 8.6 | 7.3 | 10.1 | 12.6 | 8.2 |
| Public consumption | -1.1 | -1.1 | -1.6 | -2.0 | 0.5 |
| Exports of goods and services | 10.2 | 11.4 | 4.1 | 3.9 | 9.7 |
| Imports of goods and services | 10.3 | 13.7 | 4.9 | 5.2 | 8.7 |
| Inflation | 2.2 | 3.1 | 2.0 | 2.4 | 2.0 |
| Current account deficit, % of GDP | -2.9 | -3.8 | -2.3 | -3.8 | -2.4 |

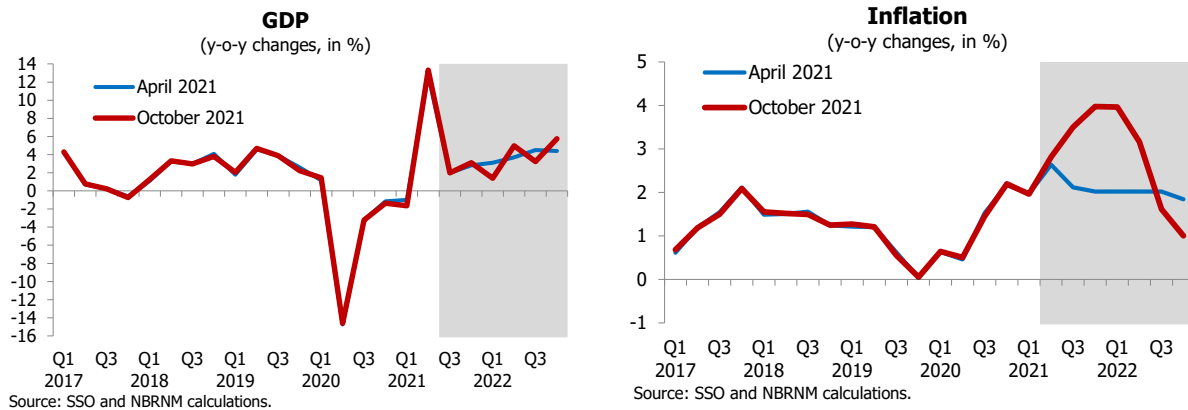
Source: NBRNM.



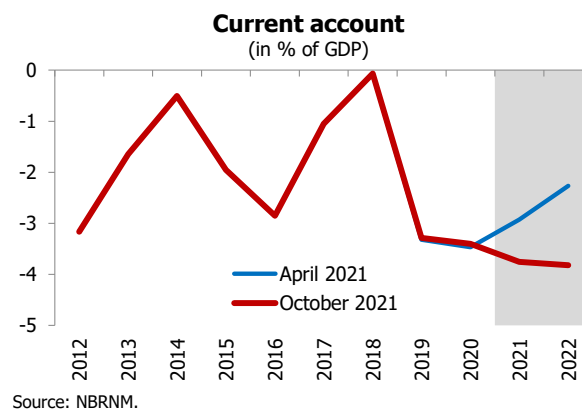
In the October macroeconomic forecasts, it is envisaged that the forecasted GDP growth rates will be the same as in April, i.e. recovery of the economy is expected during 2021 and 2022 with growth rates of 3.9% and further growth of 4% in 2023. The unchangeability in the assessments is based on the performances for the total economic activity in the first half of 2021, which are close to the forecasts, as well as on the expectations for further smooth continuation of the immunization process, increased confidence of the private sector, stronger lending to the private sector than previously expected and upward revision of the foreign effective demand, as opposed to the prolonged uncertainty arising from the pandemic and certain adverse effects on the domestic facilities of the disturbances in the global value chains, especially in the automotive industry, which were previously assessed as temporary without significant negative effects on the domestic economy. Besides the unchanged dynamics, no changes in terms of the GDP structure were made either, but only in the intensity of the changes. Thus, it is still expected that domestic demand will be the main driver of the GDP growth in the period 2021 - 2022, whereby its contribution would be larger compared with April. Moreover, for 2021, a larger upward adjustment in the annual growth rate of the household consumption was made, amid assessments for faster growth in the second half of the year, in conditions of intensified vaccination of the population, reduction of the restrictive measures and the greater mobility, as well as assessments for higher growth relative to the April expectations in the disposable income, amid faster growth of wages and inflows of private transfers, as well as of lending. A positive contribution is also expected from gross investments, but slightly weaker than the April forecasts, due to the weaker performances in the first half of the year, while public consumption would register the same fall rate as in the April forecasts.

In terms of net external demand, for 2021, a greater negative contribution compared with the previous forecast is expected, amid a larger upward adjustment in the real import than the export of goods and services. Moreover, the two components of the international trade were also subject to a significant upward adjustment relative to April. In conditions of an upward revision of the foreign demand and a more favorable price conjuncture in metals, the strong upward adjustment in exports results from the current better performances, but also the more favorable expectations by the end of the year and in the new export-oriented companies and in the metal industry. In accordance with the more favorable assessments in the exports, but also the domestic demand, a significant upward revision was also made in the growth rate of the real import of goods and services.

According to the assumption for continuation of the immunization process in the next year and therefore, further increase in the confidence of the private sector, as well as further growth in lending, also for 2022 it is expected a stronger recovery of the domestic demand and consequently, its larger positive contribution to the GDP growth, compared to the April forecasts. Moreover, the assessment that the growth will mostly result from the increased investment activity is again maintained, currently expecting a higher growth rate of gross investments, in conditions of expectations for higher foreign direct investments, intensification of the already started projects and expectations for the start of new longer-term investment projects, related to the residential and the energy sectors and to the membership in NATO. Private consumption would register the same growth rate as in April, but with a slightly smaller positive contribution, while public consumption would register a slightly larger negative contribution, amid unchanged assessments for growth of the nominal public consumption. Regarding the external sector, also in this round of forecasts, a more moderate growth in the two components of the foreign trade in 2022 is expected. Moreover, in conditions of expectations for prolonged effects of the disturbance in the global value chains, but also the higher base from 2021 in accordance with the upward revisions, small downward revisions were made in the growth of the real export, and consequently, of the real import of goods and services. Moreover, it is expected that net exports will make a larger negative contribution to the GDP growth, compared to the April assessment, as a reflection of the smaller downward revision in imports than exports, in conditions of stronger import pressures from domestic demand.



The inflation rate forecast for 2021 has been revised upwards, and it is now expected to be 3.1%, versus the expectations of 2.2% in April. In conditions of similar performances according to the April forecast in the first half of the year, the upward correction in the annual inflation rate stems from the stronger pace of growth registered in the third quarter than expected and the higher expectations for the last quarter, caused by factors on the supply side. Amid an upward adjustment relative to April in the foreign effective inflation and the import prices of energy and cereals, an upward revision was made in all three components of inflation. For 2022, as in April, the inflation rate is expected to slow down, but it will be slightly higher and will equal 2.4%, compared to the April forecasts of 2%. Observing individual components, such upward adjustment largely results from the higher transmission effect, but also from the higher expected growth in energy prices and core inflation, while the growth in the food component is similar to the April forecasts. The higher growth of the energy component is mainly related to the expected small growth of world oil price, instead of the expected fall in April. A smaller upward adjustment was made in core inflation, in conditions of a higher assessed domestic demand, an upward revision of the foreign effective inflation, as well as amid expectations for a certain transmission effect of the higher domestic energy prices.



The current October forecast envisages a higher current account deficit for the period 2021 - 2023 compared to the expectations in April, i.e. an average deficit of 3.3% of GDP, compared to the deficit of 2.3% of GDP according to the April forecast. **A more pronounced change in the expectations was made in the first two years of the forecast period, while the expectations for 2023 deviate more moderately from the April forecasts.** The upward correction for 2021 is 0.8 percentage points of GDP, while the forecasted current account deficit for 2022 is now higher by 1.6 percentage points of GDP. This is due to the new risks which arise from the slow adjustment of the global economy to the increased demand, but also from the problems in the international transport of goods, which caused a



shortage of a large number of resources and products, spurring on the expectations for the prices of primary products, especially energy prices. The price growth, as well as the recovery of domestic and export demand led to higher import pressures than expected. Accordingly, the changed expectations are due to the higher trade deficit in goods (caused by the larger deepening in the non-energy and energy deficit), as well as the slightly higher deficit in primary income, in conditions of higher inflows in secondary income and better expectations for the balance of services. On the other hand, in the surplus of services, the movements are more favorable relative to the April forecast according to the improved export performance, which would continue also in the following period. Also, the secondary income forecasts in this period are more favorable, largely due to the faster recovery of this category from the negative shock in 2020. **For 2023, a slightly higher current account deficit of 0.6 percentage points of GDP compared to the April expectations is forecasted,** which is mainly explained by the same growth factors, but their impact will be gradually exhausted. **Analyzing financial flows, cumulatively observed for the period 2021 - 2023, higher net inflows than previously forecasted according to the April round are expected.** The changes result from the higher external government borrowing in this period, amid unchanged expectations for the movement in foreign direct investments.

Comparison of GDP and inflation forecasts for North Macedonia from various organisations

| Organisation | Month of publication | Real GDP growth, % | | | Inflation (average rate, %) | | |
|--|----------------------|--------------------|------|------|-----------------------------|------|------|
| | | 2021 | 2022 | 2023 | 2021 | 2022 | 2022 |
| IMF | October 2021 | 4.0 | 4.2 | 3.8 | 3.1 | 2.2 | 1.5 |
| World Bank | October 2021 | 4.6 | 3.7 | 3.4 | 2.4 | 2.0 | 1.8 |
| European Commission | May 2021 | 3.7 | 3.8 | - | 1.7 | 1.7 | - |
| EBRD | November 2021 | 4.0 | 4.0 | - | - | - | - |
| Consensus Forecast | October 2021 | 4.0 | 4.1 | - | 2.3 | 2.0 | - |
| Ministry of Finance | October 2021 | 4.1 | 4.6 | 5.2 | 3.0 | 2.4 | 2.0 |
| National Bank of the Republic of North Macedonia | October 2021 | 3.9 | 3.9 | 4.0 | 3.1 | 2.4 | 2.0 |

Source: IMF, World Economic Outlook, October 2021; World Bank, Europe and Central Asia Economic Update, Fall 2021; European Commission European Economic Forecast, Spring 2021; EBRD Regional Economic Prospects, November 2021; Consensus Forecast, October 2021; Ministry of Finance, Draft Budget for 2022, October 2021 and Fiscal Strategy 2022-2024, May 2021; and the National Bank of the Republic of North Macedonia, October 2021.

Annex: Alternative macroeconomic scenario with longer-term effects of the COVID-19 pandemic and of the impaired global value chains

Although the COVID-19 pandemic lasts for almost two years, however the uncertainty about its duration and the possible effects on the economy remain a main risk to the global growth, and in our country as well. The vaccination process gave initial positive impulse to the economies around the world, but the unequal availability and distribution by country is a main risk factor for the future growth, through occurrence and spreading of new and more contagious types, to which the current vaccines are less efficient. Hence, the **risks included in this alternative scenario refer to a possible stagnation of the immunization rate due to a distrust of the population of the vaccines, an occurrence of new more contagious types and a new increase in the number of infected persons, especially in the first half of 2022, which would lead to reintroduction of more restrictive measures. In addition, partially related to the pandemic worldwide, the risk of stronger and longer-term disturbance of the global value chains is also included, which would adversely affect demand and production and would lead to price pressures.** Consequently, the possible materialization of these new risks may lead to a slower economic recovery, amid assessments for smaller production, especially in the segment of the automotive industry, which is most affected by the bottlenecks in the international trade, as well as a more difficult recovery of the sectors with close social interaction. At the same time, it may also lead to increased risk aversion, possible tightening of the financial conditions, as well as occurrence of more lasting adverse effects on the labor market. The international mobility of the population would be limited again, and the uncertainty and restraint of economic agents would be significantly more pronounced.

Given the high uncertainty and risks, also in this round of forecasts, an adverse alternative scenario was made. **The alternative scenario again assumes adverse effects on the foreign effective demand, smaller inflows of informal remittances and foreign direct investments, more pronounced restraint of domestic economic agents in conditions of longer-term uncertainty, as well as prolonged, adverse effects on the labor market, compared with the baseline scenario for the period 2022 - 2023.** Moreover, it is expected that the adverse effects will be more pronounced in the first half of 2022, and then they will gradually decrease and will completely disappear by the end of 2023.

In order to cover this effect of the global risks⁸⁴, it is assumed smaller growth of the foreign effective demand by 1.5 and 0.5 percentage points in 2022 and 2023, respectively. The downward correction in the foreign effective demand would have the greatest direct negative effect on exports, as well as on foreign direct investments and total investment activity. **The estimated direct effect of the lower foreign demand on the overall GDP points to slower economic growth by about 0.6 percentage points, on average, for both years, relative to the growth in the baseline scenario (i.e. smaller growth by 0.7 percentage points in 2022 and by 0.5 percentage points in 2023).**

Besides the direct effect of the weaker foreign demand, it is assumed that the deteriorating prospects and the increased uncertainty due to stagnation in the process of immunization of the domestic population, possibly the occurrence of a new pandemic wave and introduction of more restrictive measures will also be reflected on the domestic demand, through greater restraint from consumption and investments (domestic and foreign), and through the labor market also on the disposable income. Thus, the alternative scenario additionally assumes stagnation of employees and real wages in 2022 and slower recovery in 2023, compared to the solid growth in both years in the baseline scenario. The weaker economic activity in the world, especially in Europe, as well as the more severe restrictions in terms of travellings, would also be reflected on the remittances from abroad, due to which it is assumed stagnation of net inflows of private

⁸⁴ The estimated effects on the global growth by the OECD (October 2021) are taken into account, as well as the estimated effects on the growth in the euro area by the ECB (September 2021), within their pessimistic alternative scenarios.



transfers in 2022 and their gradual increase in 2023, and the same assumption also refers to the level of foreign direct investments.

If all aforementioned assumptions are realized, one can expect slower recovery of the domestic economy, i.e. slower economic growth by 1.7 and 0.8 percentage points in 2022 and 2023, respectively, compared with the baseline scenario, amid a lower positive contribution from private consumption, investments and exports of goods and services, partially offset by the smaller negative contribution by imports. Hence, the smaller GDP growth in the alternative scenario will result from the smaller positive contribution of domestic demand, while net exports will make a smaller negative contribution.

The inflation rate was also subject to downward changes compared with the baseline scenario, whereby under the assumption for unchanged prices of primary products in world markets, it is estimated that inflation would be lower by 0.8 and 0.6 percentage points in 2022 and 2023, respectively, taking into account the lower expected pressures from the domestic demand side (smaller positive output gap relative to the baseline scenario).

