Revision of macroeconomic forecasts
– May 2023 –

Anita Angelovska Bezhoska
Governor

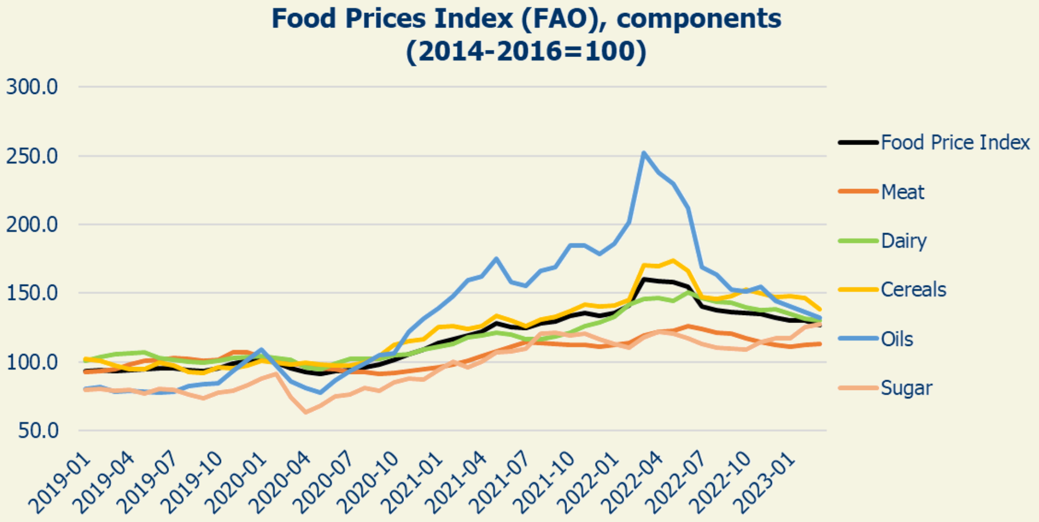
Global environment remains uncertain given the protracted geopolitical tensions

Last year, global economy faced another non-economic shock of unprecedented proportions (the war in Ukraine) with significant economic effects - commodity prices hit a record high (gas 1300%, electricity 800%), which significantly accelerated inflation and decelerated economic growth.

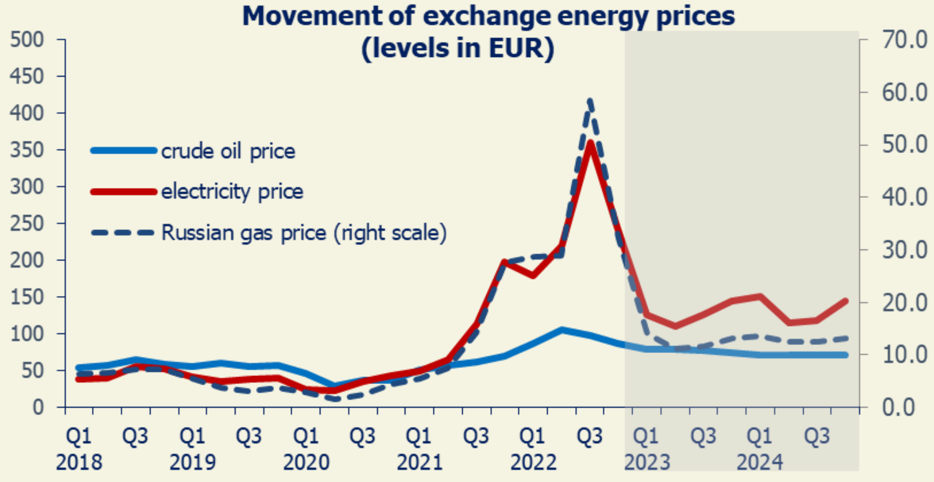
– **global inflation** almost doubled to 8.7%, and in less developed economies reached double-digit rates - in CSEE it averaged out to 13.5%

– **global economic growth** in just one year almost halved to 3.4% (in CSEE from 7.3% to 3.4%) amid rapid growth in commodity prices, supply chains disruptions as well as strong and a synchronized monetary tightening (the strongest in the last 50 years) which tightened the global financial conditions - lower global liquidity and higher interest rates with a negative impact on global financial flows (FDIs, portfolio investment and loans)

However, since the second half of last year, we have witnessed a decrease in commodities prices and easing of supply disruptions, which lowered inflationary pressures - in CSEE the peak was in November (16.1%), and since then it has been decreasing (to 13.4% in March in CSEE).



Source: FAO



Source: IMF, EEX and NBRNM calculations.

At the beginning of this year the global economy faced with new risk- financial (in)stability, as visible by collapse of several banks in the United States and tensions at European financial markets; yet the swift response of the financial regulators prevented major spillover effects on a wider scale.

According to the latest IFIs forecasts, global economic growth and global inflation are expected to slow down this year

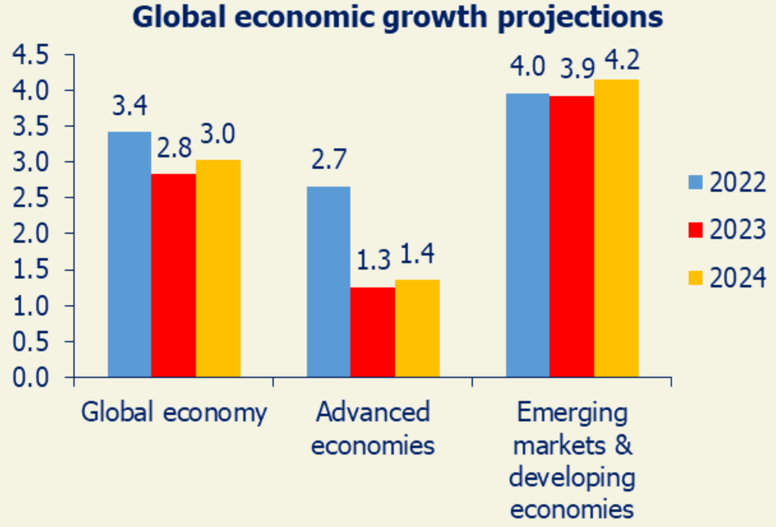
- **The IMF forecasts that global growth will slow down from 3.4% in 2022 to 2.8% in 2023, followed by moderate acceleration to 3% next year** and will remain close to that level over the medium term, which is the lowest medium-term forecast in the last few decades
- This indicates that the subsequent shocks will have **deeper and longer-term implications on the growth potential** of economies
- **Greater deceleration is expected for developed economies,** and minor for lower income economies.
- **These latest IMF growth estimates are very similar to their previous forecasts**
- On the other hand, IMF made an **upward corrections in global inflation** - it is still expected to slow down (to 7% this year and to 4.9% in 2024), but at a slower pace, primarily due to the greater persistence of core inflation. Therewith, the central banks would fully achieve inflation targets in 2025.

Risks to economic growth remain mostly downside, and to inflation mostly upside:

- New escalation of the war in Ukraine and rise in energy prices
- Stronger tightening of international financial conditions
- Stress in the financial sector
- Geo-economic fragmentation
- Weaker growth of the Chinese economy as the second largest in the world

The IMF's alternative scenario that factors in adverse effects on the global financial system, points to slower global growth of around 0.3 p.p.

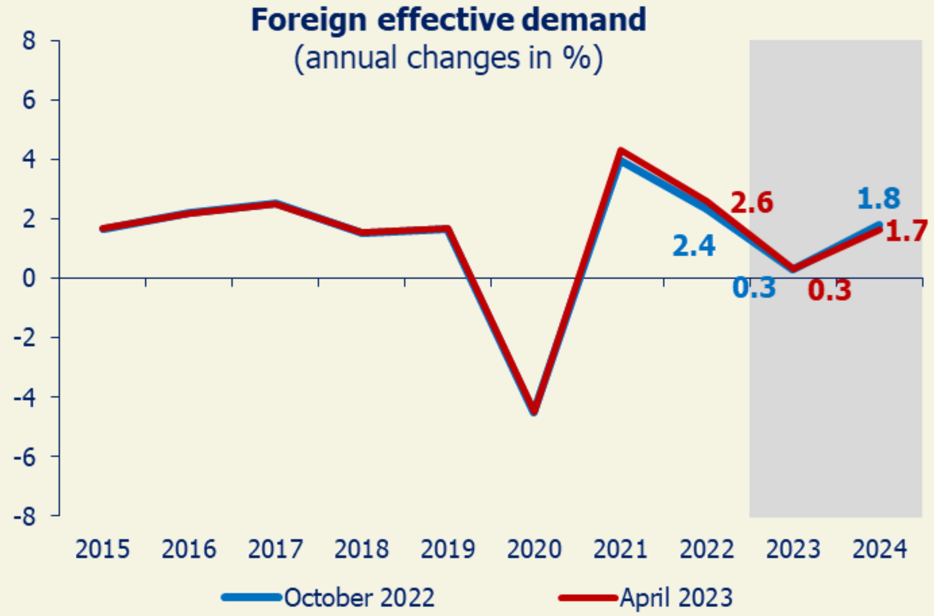
Source: IMF, WEO database.



Source: IMF World Economic Outlook, April 2023.

What does such global environment mean for our export demand?

- **Foreign demand will grow by 0.3% for 2023 and accelerate to 1.7% next year**, which is almost the same as in the October forecasts (growth of 0.3% and 1.8% in 2023 and 2024, respectively). **No significant changes since the October forecasts.**

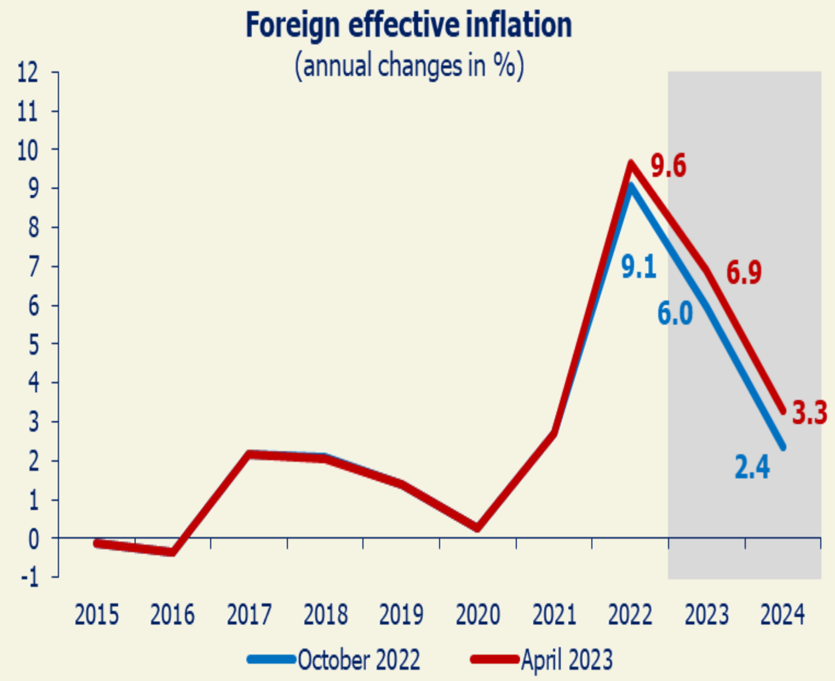


Source: Consesus Forecasts and NBRNM calculations.

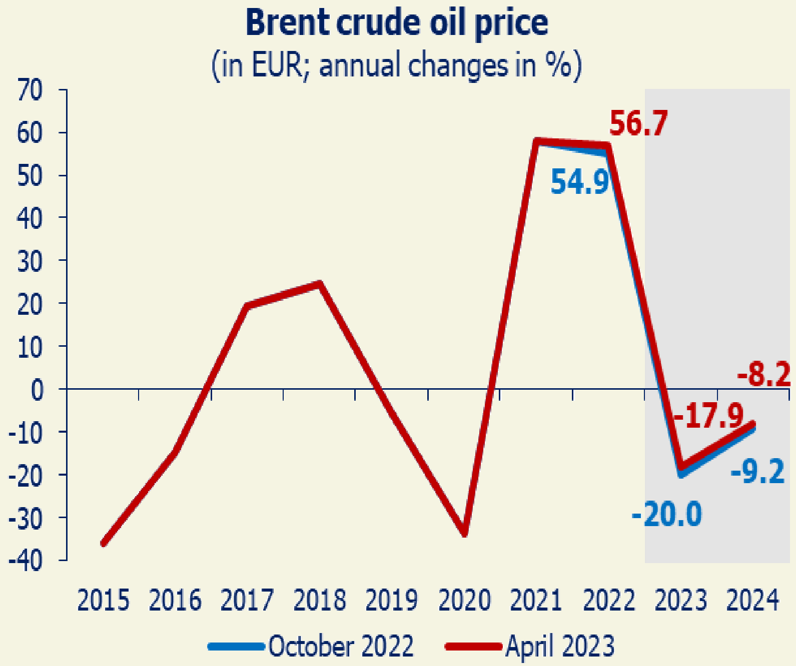
What does such global environment mean for our import and export prices?

- In general, after the unprecedented increase of **commodity prices last year, IFIs project decline in 2023 and stabilization in 2024.**

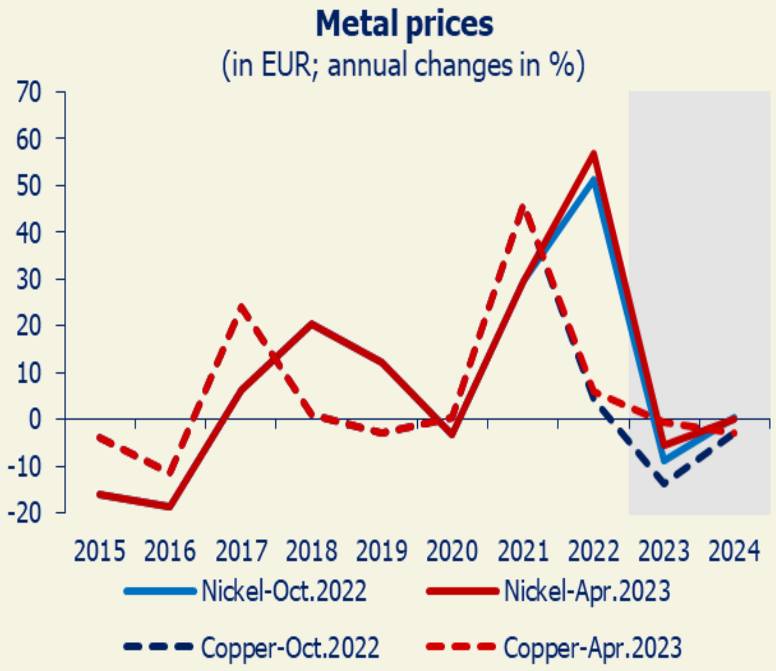
- **Compared to the October forecasts,** almost all commodity prices are revised downwards, especially of energy, which points to a *lower import pressures on inflation and trade deficit , but uncertainty remains.*



Source: Consesus Forecasts and NBRNM calculations.



Source: IMF and NBRNM calculations.



Source: IMF and NBRNM calculations.

Key assumptions for the Macedonian economy forecast

- **Continued uncertain global environment** due to the protraction of the war in Ukraine, **which poses risks to the economic growth and inflation**

- **After the strong growth last year, a significant drop in primary commodity prices is expected for 2023 and relative stabilization next year** which implies positive effect on production costs, terms of trade and trade balance.

- **Less favorable financial conditions in international markets** reflecting the more intense cycle of monetary tightening by the central banks, especially in the most developed economies

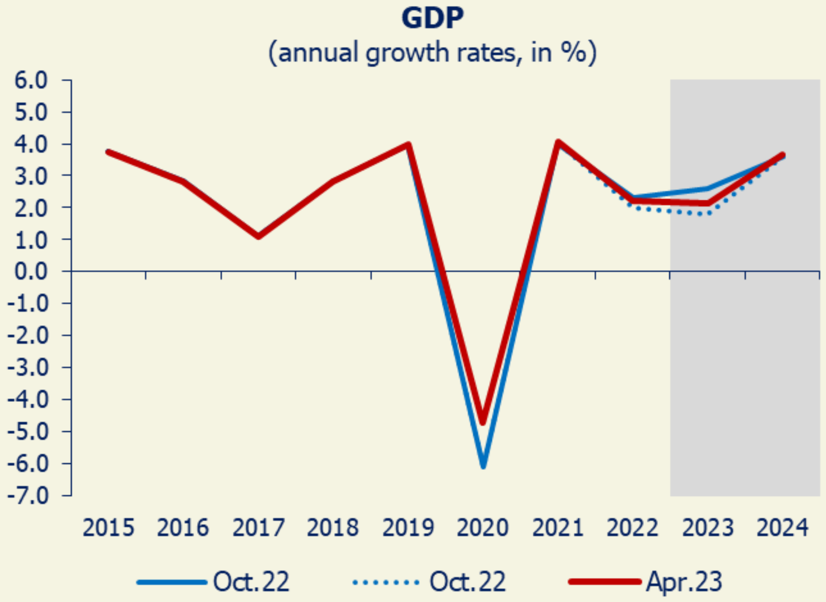
- **According to FS 2023-2025, fiscal consolidation will continue in the medium term** - the budget deficit would narrow from 4.5% of GDP in 2022 to around 3% of GDP in 2025, financed by both domestic and foreign sources

- **Intensification of public infrastructure investments**

Macroeconomic scenario for 2023 - 2025

GDP forecast

- **Last year GDP growth was 2.1%,** which was within our forecast range (2% - 2.3%), but with a visible deceleration of the growth in the second half of the year.
- Lower growth rates are also expected in the first half of this year, which will be followed by moderate acceleration in the second half leading to average growth rate for **2023 to 2.1%** - same as last year.
- The forecasted **economic growth would be lower than in the baseline scenario** but in the middle of the interval of the two scenarios from the October forecast.
- In the medium term, in line with the expected recovery of the global environment (foreign demand), it is projected to gradually accelerate to about **3.6% - 4%**. Yet, the global uncertainty and risks remain.



GDP forecast for 2023-2024

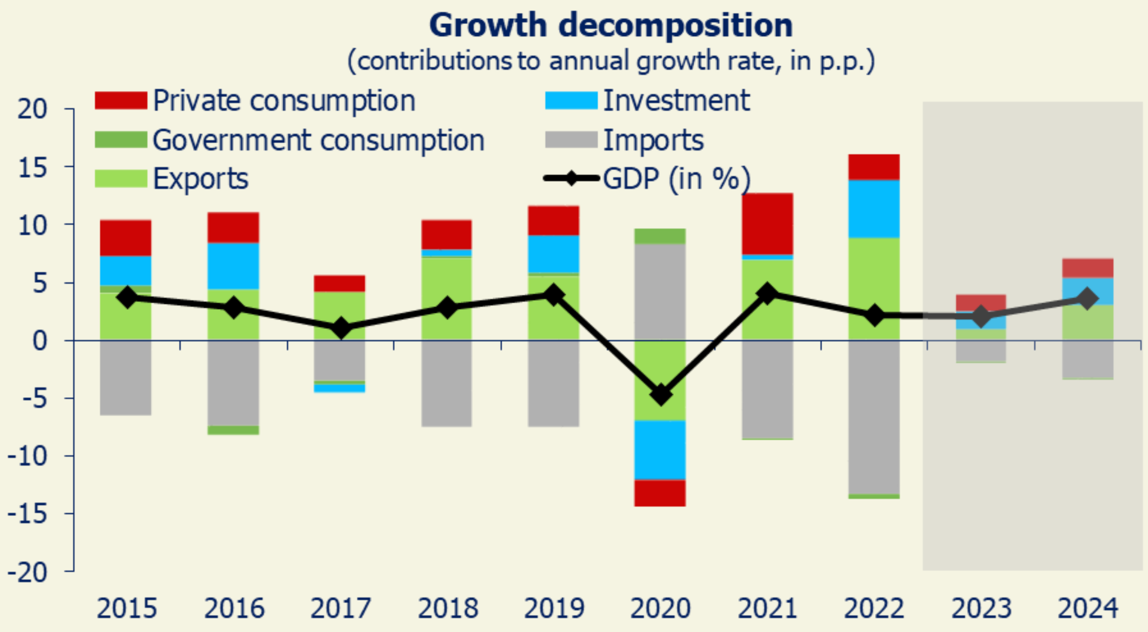
- **Analyzing the growth structure,** same as in October, domestic demand is expected to make a positive contribution and net export to make a small negative contribution.

  - **Investment** – average growth of 5.5% underpinned by public investment, private investment in the manufacturing and energy sectors, solid foreign direct investment and further, albeit more moderate, growth in corporate lending.

  - **Private consumption** – average growth of 2.2%, supported by the growth of disposable income (about 4%).

  - **Exports** – average growth of about 3%, in line with the recovery of foreign demand.

  - The growth of exports and domestic demand (which have a relatively large import component) will increase **imports** pressure (2.3%), so that net-exports will have a negative contribution.



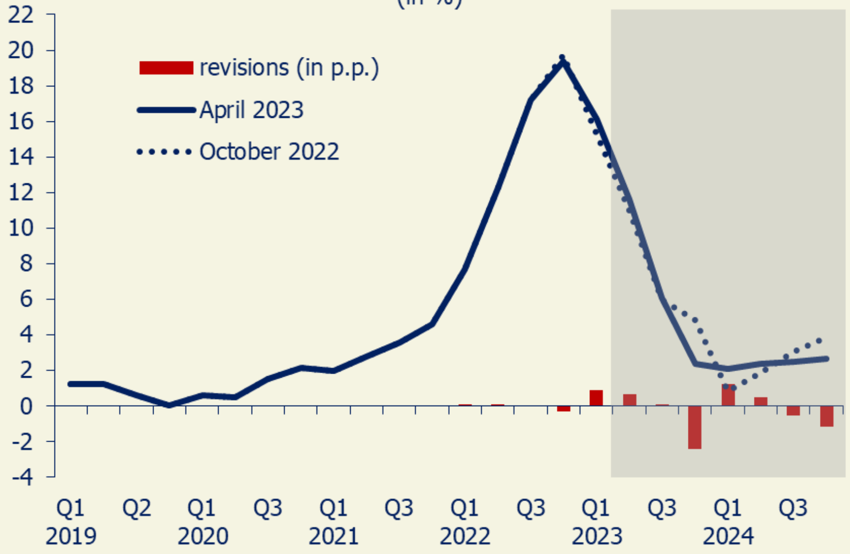
Inflation forecast

- **Last year, inflation averaged out at 14.1%**, which is fully in line with our forecast (14.2%). Also, its movements since the beginning of this year match our forecasts for 2023.

- Taking into account its movements so far, as well as the IFI forecasts for fall/stabilization of food and energy prices, tightening of monetary conditions and other measures, **inflation is forecasted to slow down to a single-digit level of 8% - 9% in 2023**, and then in the medium-term to further slowdown to below 3%, as in the October forecast.

- **In view of the geopolitical developments, risks to the inflation forecast remain**, which further underlines a need for prudent domestic policies-policies that affect the aggregate demand.

Inflation rate
(in %)



Comparison of GDP and inflation forecasts for our economy

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

Organisation	Month of publication	**Real GDP growth, %**		**Inflation (average rate, %)**	
		2023	2024	2023	2024
IMF	April 2023	1.4	3.6	9.2	3.5
World Bank	April 2023	2.4	2.7	9.1	3.0
European Commission	May 2023	2.0	3.1	7.9	3.7
EBRD	May 2023	2.0	3.0	-	-
Ministry of Finance	December 2022	2.9	4.1	7.1	2.5
National Bank of the Republic of North Macedonia	April 2023	2.1	3.6	8-9	2.4

Source: IMF, World Economic Outlook, April 2023; World Bank, Western Balkans Regular Economic Report, Spring 2023; European Commission European Economic Forecast, Spring 2023; EBRD Regional Economic Prospects, May 2023; Ministry of Finance, Revised Fiscal Strategy 2023-2025, December 2022; and the National Bank of the Republic of North Macedonia, April 2023.

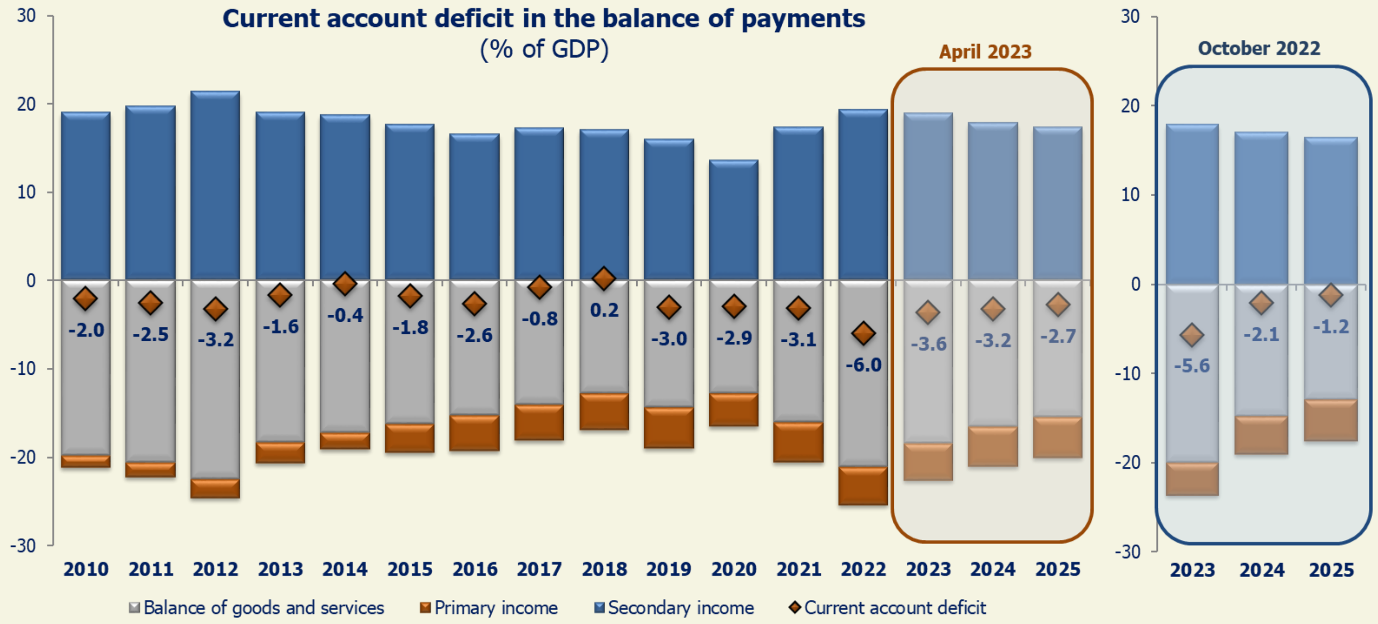
Balance of payments
- current account -

- **The energy shock, besides on inflation, also had major impact on the current account deficit,** which doubled last year (from 3% to 6% of GDP), with significant expansion of trade deficit, which was partially offset by the considerable growth of private transfers.

- **For 2023**, deficit is expected to narrow to 3.6% of GDP given the forecasts for lower commodities prices and somewhat more moderate growth of private transfers that have already hit an all-time high.

- **Compared to the October forecasts, the above still points to a more favorable external position.** The current account deficit in 2022 was lower than our forecasts (by 1.4 pp of GDP), and for this year it is estimated to be lower by 2 pp of GDP, with a positive effect on foreign reserves.

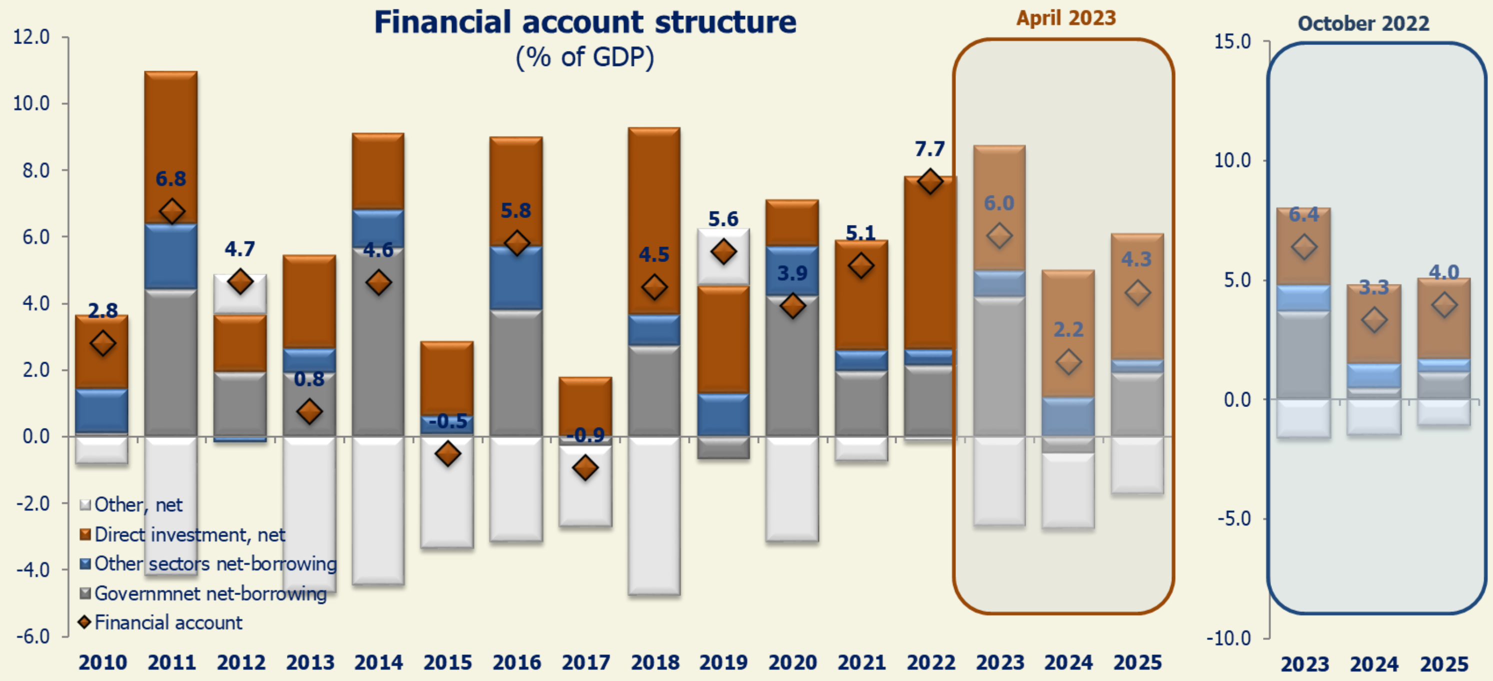
- **In the medium term**, the expected stabilization of commodities prices, coupled with global economic recovery, especially that of the EU which will improve also non-energy trade balance, would further narrow current account deficit (3% on average) and make way back towards the pre-pandemic level.



Balance of payments
- financial account -

- **Net financial inflow for the period 2023-2025 would be sufficient to fully cover the current account deficit and to ensure additional reserves accumulation.**
  - **Expectations for net financial inflows of 6% of GDP this year** and 3.3% of GDP in the medium term (2024-2025).
  - **Foreign direct investments and external borrowing** of the government are expected to be dominant financial flows, as before.

- Therefore, **foreign reserves are expected to be maintained at a level corresponding to international standards for maintaining exchange rate stability** throughout the forecast horizon.



Deposit and credit growth

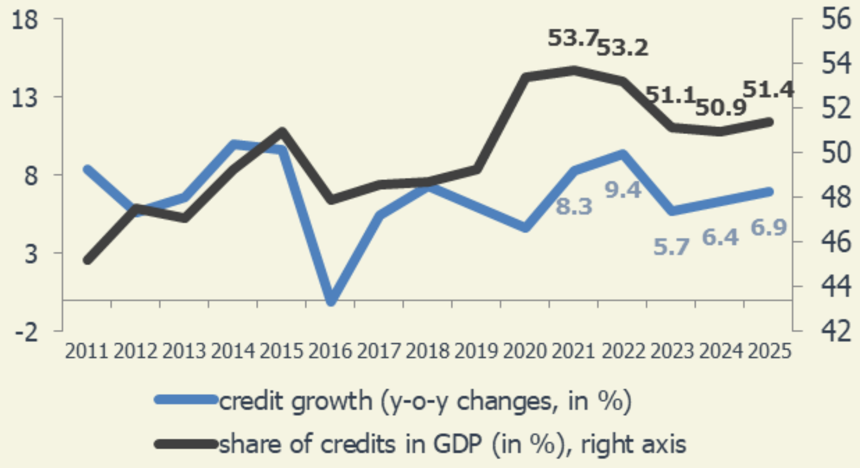
- **The banking system continued to provide solid credit support, although with somewhat more moderate dynamics** - credit growth in the first quarter of 2023 was 6.6% (8.5% according to the October forecast), with expectations for a moderate deceleration to 5.7% by the end of the year, given the monetary tightening and reduced demand.

- **An average loan growth of 6.6% is expected in the medium term, 2024 - 2025,** amidst traditionally solid liquidity of the banking system and solid capitalization (17.7% CA) which, among other things, is due to the systemic and macroprudential measures aimed to strengthen the banking sector resilience.

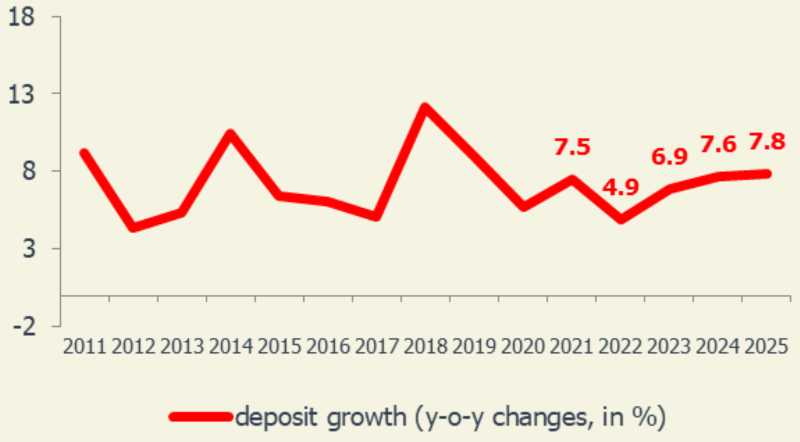
- **Deposits, as the most significant source of financing, registered an annual, stronger than expected, growth of 6.9% in the first quarter,** (4.5% according to the October forecast), given the stabilization of expectations, further increase of confidence, as well as growing returns on savings, coupled with the monetary measures taken.

  - We expect a solid deposit growth of 6.9% **by the end of 2023,** and 7.7%, on average, **in the medium term** (2024 - 2025 period).

Credit growth



Deposit growth



Summary

- **Global economy will continue to grow, but downside risks still prevail.** With the April forecasts, the IMF did not make significant changes to the global economic outlook - expectations for moderate growth slowdown to 2.8% this year, followed by a moderate acceleration to 3% in the coming year.

- With similar assumptions about the external environment and domestic factors, as in October, **the Macedonian economy is expected to grow** at a rate of 2.1% this year as well, and then in line with the global economic recovery, to accelerate moderately.

- **Inflation** is expected to continue to decelerate and to average single digits this year, same as the global inflation, and in the medium term to gravitate towards the historical average.

- Given the stabilization of commodity markets, the **external position** of the economy is better than expected, with a positive effect on foreign reserves that remain in the safe zone.

- Yet, the global environment remains uncertain and unpredictable, posing **risks** to economic growth, inflation and the external position. This brings to the fore the need for prudent domestic macroeconomic and structural policies.

- **Amid increased inflationary pressures and inflationary expectations, this year the National Bank continued with monetary tightening that began at the end of 2021, first by regulating liquidity, and then through the interest rates, elevating the policy rate to 5.75%.** Such monetary setup was also supported and strengthened by changes to the reserve requirement, aimed at increasing denar savings, as well as by systemic and macroprudential measures, such as introduction of a countercyclical capital buffer and macroprudential measures aimed at increasing the loan demand quality, which further strengthens the banking system resilience. Given the monetary strategy of a stable exchange rate of the denar against the euro, the changes in the domestic monetary policy mirror the changes in the monetary policy of the European Central Bank.

- **The National Bank performs vigilant and day-to-day monitoring of macroeconomic data and risks and as before, will deploy all necessary measures and available instruments to maintain exchange rate and medium-term inflation stability.**

THANK YOU FOR THE ATTENTION!