National Bank of the Republic of Macedonia

MONETARY POLICY AND RESEARCH DEPARTMENT

Recent Macroeconomic Indicators
Review of the Current Situation

February 2017

Recent Macroeconomic Indicators

Review of the Current Situation - Implications for the Monetary Policy

The review of the current situation aims to give an overview of the recent macroeconomic data (November 2016 - January 2017) and to make a comparison with the latest macroeconomic projections (October 2016). This will determine the extent to which the current situation in the economy corresponds to the expected movements of the variables in the previous round of forecasts. The review focuses on the changes in external assumptions and performances of domestic variables and the effect of these changes on the environment for monetary policy conduct.

In the period between forecasts, there were no major revisions of the expectations about the global economic environment, i.e. the pace of recovery is expected to gradually strengthen. Risks remain mostly downward, and are mainly related to the uncertainty around the future measures and policies of developed countries for increased protectionism, possible financial market volatility caused by the possible tightening of the financial conditions globally, as well as the increased geopolitical risks. The gradual economic recovery in the euro area as our key economic partner continues. Initial estimates for the GDP growth rate in the last quarter of 2016 show a minimal acceleration of the quarterly growth to 0.4% (1.8% on an annual basis). Economic growth is expected to continue in early 2017, according to the preliminary results of the surveys of the corporate sector and households. The labor market continues registering favorable shifts, when unemployment rate reduced to 9.6% in December, hitting a record low since May 2009. In terms of inflation, the data for January 2017 show a significant acceleration in the annual rate to 1.8% (from 1.1% in December 2016), which is the highest rate since February 2013. This acceleration is mostly due to the effects of energy prices, while core inflation rate remained unchanged (0.9% on an annual basis).

Observed from a viewpoint of the individual external environment indicators for the Macedonian economy, the assessments regarding the foreign effective demand are minimally higher than those in the October cycle. Thus, the expected growth rate of foreign demand in 2016 and 2017 is minimally higher compared to the October forecast, as a result of the improved performances and estimates for the future growth in the region. In contrast, the estimate for 2018 has been adjusted slightly downward. October estimates for gradual acceleration in the price growth in 2017 and 2018 still apply to the **foreign effective inflation**. The latest estimations for the prices of **primary commodities** mainly refer to their recovery in 2017 and 2018, amid divergent directions of revisions of individual products. Thus, **world oil prices** expect twice higher growth in 2017 compared to the October estimates and a slight decline in 2018 contrary to previously expected growth. The decline in **metal prices** in 2016 is similar to the forecast, and in 2017, significantly faster growth of the copper price and the same growth rate of the nickel price compared to previous expectations is expected. The revisions in prices for 2018 are small, i.e. they are expected to continue stabilizing. Furthermore, as for **prices of wheat and maize**, the latest estimates for 2017 point to a moderately stronger growth compared with the previous estimates. Expectations for 2018 for the growth of the price of wheat are almost the same as those from October, and the price of corn is now expecting lower growth compared with the previous estimates. However, one should bear in mind that the expectations for the prices of these commodities are extremely volatile, which creates uncertainty about the assessment of their future dynamics and effects on the domestic economy, especially in the long-term. **EURIBOR** expectations for 2017 are similar as in the October forecasts, while minimal upward correction was made for 2018. Moreover, it is still expected that over the forecast horizon, the interest rate will be negative in accordance with the ECB's stimulating monetary policy.

The comparison of the latest macroeconomic indicators with their forecast dynamics from October indicates certain deviations in the individual segments of the economy. The estimated GDP data for the third quarter confirm the economy growth, which is slightly higher than expected in October. The available high-frequency data indicate divergent movements, but seen as a whole, the situation in the economy in the last quarter of the year would be slightly less favorable compared to the third quarter. **Speaking for the entire 2016, past performances and the currently available high-frequency indicators point to growth of the economy, and the growth rate is close to the expected growth of 2.3% in line with the October forecast.** When it comes to changes in consumer prices, in January, upward adjustments were made regarding the expected movement for 2017 in the input assumptions. In the absence of data on the movement of prices in the domestic economy in January 2017, this shift in the input assumptions indicates the existence of potential upward risks to the inflation forecast for 2017.

The foreign reserves at the end of January 2017 indicate a decline in foreign reserves (adjusted for the price and exchange rate differentials and price changes of securities). According to the analysis of change factors, the reduction of reserves is mostly due to changes in the category "other", which are also temporary, and substantially smaller negative contribution was made by the reduction of the banks' foreign currency deposits with the NBRM and transactions on behalf of the government. Currency exchange market data as of January point to net inflows from private transfers which are close to the forecasted for the first quarter of 2017. However, the assessment period is very short to make reliable conclusions. The latest available data on the balance of payments as of November 2016 indicate current account deficit close to the October forecast for the entire year, amid higher net inflows in the financial account than expected. The data from the foreign trade statistics as of December indicate that the trade deficit in 2016 is lower than projected, which is mainly due to the weaker import pressures. The analysis of foreign reserves adequacy indicators shows that they continue to hover in a safe zone.

As for the monetary sector developments, final data as of December show a significant acceleration in the monthly growth of total deposits (of 4.3%), after the solid growth in the previous month of 1.2%, suggesting further stabilization of the expectations of domestic economic agents and depletion of the effects of non-economic factors. Analyzed by sector, the growth of total deposits in December to a greater extent results from corporate deposits, and household deposits make positive, but smaller contribution to the growth. On an annual basis, total deposits in December grew by 6.0%, which is above the forecasted growth of 2.6% for the fourth quarter of 2016. Analyzing the credit market, in December, total loans registered a monthly growth of 2.9%, which is an acceleration compared to the rise of 0.2% in the previous month. The growth almost entirely stems from the higher level of loans granted to enterprises, amid a small contribution of loans to households. On an annual basis, total loans grew by 1.0%, which is above the October forecast of 0.5% for the fourth quarter. If we exclude the regulatory effect, the annual credit growth rate is 6.5% and is above the forecasted annual growth of 5.6% for the fourth quarter of 2016. Performances in lending activity correspond to the results of the latest Bank Lending Survey, according to which, in the fourth quarter, easing of the lending terms in both sectors is evident, amid a simultaneous increase in credit demand.

In December, the Budget of the Republic of Macedonia registered a deficit of Denar 2,441 million, most of which was funded through the use of the government funds which are in the form of deposits with the NBRM. For the entire 2016, the budget deficit totaled Denar 16,070 million or 2.7% of GDP. The Budget deficit accounts for 69.5% of the forecasted for 2016, according to the Budget Revision[1] and was mostly financed by external government borrowing (Eurobond issue on the international financial markets) and through the new net issuance of government securities on the domestic market. Some of the inflows were in the form of deposits on the government account with the NBRM.

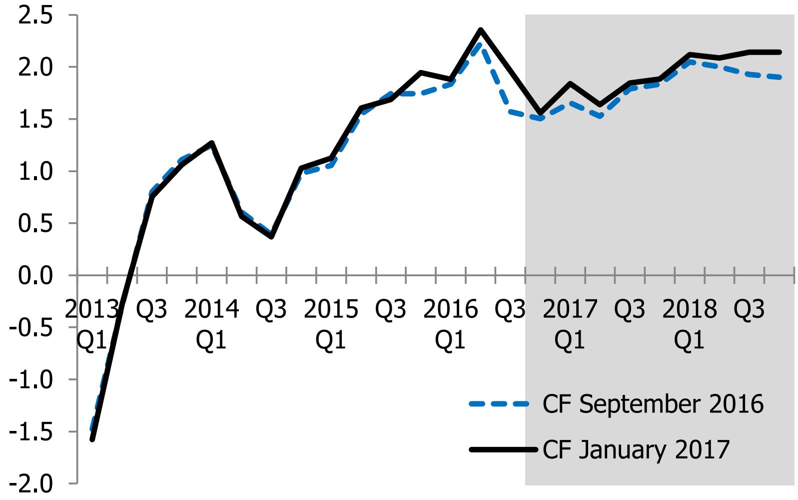
[1] Refers to the Budget Revision for 2016 of 30 August 2016.

The latest macroeconomic indicators and assessments indicate certain deviations compared to the forecast dynamics in individual segments in the economy, but the perceptions about the environment for conducting monetary policy and about the risks highlighted in the October forecasts are mainly unchanged. Foreign reserves (adjusted for price and exchange rate differentials and price changes of securities) decreased in January 2017, while the foreign reserves adequacy indicators are constantly moving in the safe zone. As for the economic activity, past performances and available shift indicators in the last quarter of the year point to growth of the economy in 2016 at a rate close to the forecasted within the October forecasts. In terms of inflation, the upward correction of the expected movement of external assumptions indicates potential upward risks to the inflation forecast for 2017. Within the monetary sector, the December data indicate higher performance in relation to the October forecasts, in both total deposits and lending activity. These performances suggest further stabilization of the expectations and depletion of the effects of non-economic factors. The performance of total deposits at the end of the year represents a solid foundation and creates conditions for support of lending in the period ahead.

				2015						2016																2017
	2012	2013	2014	Jan.	Q1	Q2	Q3	Q4	2015	Jan.	Feb.	Mar.	Q1	Apr.	May	Jun.	Q2	Jul.	Aug.	Sep.	Q3	Oct.	Nov	Dec	Q4	2016	Jan.
I. Real sector indicators																											
Gross domestic product (real growth rate, y-o-y) /2	**-0.5**	**2.9**	**3.6**		**4.2**	**0.8**	**4.5**	**6.0**					**2.6**														
Industrial production /3																											
y-o-y	-2.8	3.2	4.8	1.1	1.5	0.1	5.7	11.7	4.9	8.0	15.2	8.9	10.7	3.6	5.3	-4.4	1.3	5.1	5.2		5.0						
cumulative average	-2.8	3.2	4.8	1.1	1.5	0.8	2.5	4.9	4.9	8.0	11.7	10.7	10.7	8.7	8.0	5.6	5.6	5.6	5.5		5.4						
Inflation /4																											
CPI Inflation (y-o-y) /5	4.7	1.4	-0.5	-1.5	-0.9	0.3	-0.2	-0.4	-0.3	0.1	0.0	-0.4	-0.1	-0.7	-0.7	-0.7	-0.7	-0.3	-0.3	0.2	-0.1	0.2	-0.2	-0.2	-0.1		
CPI Inflation (cumulative average)	3.3	2.8	-0.3	-1.5	-0.9	-0.3	-0.3	-0.3	-0.3	0.1	0.1	-0.1	-0.1	-0.2	-0.3	-0.4	-0.4	-0.4	-0.4	-0.3	-0.3	-0.3	-0.2	-0.2	-0.2		
Core inflation (cumulative average)	2.1	3.0	0.6	-1.1	-0.4	0.1	0.3	0.5	0.5	1.6	1.6	1.7	1.7	1.6	1.6	1.6	1.6	1.5	1.5	1.5	1.5	1.5	1.4	1.4	1.4		
Core inflation (y-o-y)	2.1	3.0	0.6	-1.1	-0.4	0.7	0.7	1.0	0.5	1.6	1.6	1.8	1.7	1.6	1.2	1.5	1.5	1.2	1.2	1.4	1.3	1.4	1.2	1.0	1.2		
Labor force																											
Unemployment rate	31.0	29.0	28.0		27.3	26.8	25.5	24.6	26.1				24.5														
II. Fiscal Indicators																											
(Central Budget and Budgets of Funds)																											
Total budget revenues	138,115	140,248	145,929	10,527	37,779	40352.0	39,314	43,762	161,207	12,918	12,926	14,739	40,583	14,813	13,346	13,263	41,422	14,981	13,625		43,807						
Total budget expenditures	155,840	159,505	168,063	12,732	44,080	43572.0	43,667	49,313	180,632	14,606	15,695	15,917	46,218	14,309	14,529	13,891	42,729	16,991	14,485		45,953						
Overall balance (cash)	-17,725	-19,257	-22,134	-2,205	-6,301	-3220.0	-4,353	-5,551	-19,425	-1,688	-2,769	-1,178	-5,635	504	-1,183	-628	-1,307	-2,010	-860		-2,146						
Overall balance (in % of GDP) /1	-3.8	-3.8	-4.2	-0.4	-1.1	-0.6	-0.8	-1.0	-3.5	-0.3	-0.5	-0.2	-1.0	0.1	-0.2	-0.1	-0.2	-0.3	-0.1		-0.4						
III. Financial indicators /6																											
Broad money (M4), y-o-y growth rate	**4.4**	**5.3**	**10.5**	**11.1**	**8.8**	**9.2**	**6.2**	**6.8**	**6.8**	**4.5**	**5.4**	**6.2**	**6.2**	**3.8**	**3.7**	**2.5**	**2.5**	**3.6**	**4.5**	**4.0**	**4.0**	**3.9**	**4.6**	**6.1**	**6.1**	**6.1**	
Total credits, y-o-y growth rate	**5.4**	**6.4**	**10.0**	**9.2**	**9.2**	**9.0**	**8.8**	**9.5**	**9.5**	**8.6**	**8.7**	**8.4**	**8.4**	**7.5**	**6.4**	**3.5**	**3.5**	**3.0**	**2.9**	**2.5**	**2.5**	**1.8**	**1.3**	**1.0**	**1.0**	**1.0**	
Total credits - households	6.5	10.2	11.8	11.5	12.1	12.4	12.8	12.9	12.9	12.6	12.8	13.0	13.0	12.8	12.2	8.8	8.8	8.1	7.8	7.3	7.3	7.5	7.3	7.0	7.0	7.0	
Total credits - enterprises	4.5	3.8	8.6	7.5	7.1	6.7	6.0	7.1	7.1	5.5	5.8	5.1	5.1	3.7	2.0	-0.5	-0.5	-0.8	-0.9	-1.2	-1.2	-2.7	-3.3	-3.7	-3.7	-3.7	
Total deposits (incl. demand deposits), y-o-y growth rate	**4.9**	**6.1**	**10.4**	**10.6**	**8.4**	**8.9**	**5.7**	**6.5**	**6.5**	**4.3**	**5.3**	**6.2**	**6.2**	**3.1**	**3.7**	**2.3**	**2.3**	**3.5**	**4.5**	**4.0**	**4.0**	**4.0**	**4.4**	**5.7**	**5.7**	**5.7**	
Total deposits - households	7.2	6.7	8.9	8.4	8.1	6.2	5.0	4.1	4.1	3.6	3.5	3.1	3.1	0.9	-0.4	0.2	0.2	0.2	1.0	1.2	1.2	1.8	1.8	2.5	2.5	2.5	
Total deposits - enterprises	-1.6	3.1	15.7	17.4	9.0	17.8	7.1	13.0	13.0	6.4	11.8	16.0	16.0	9.2	14.5	5.6	5.6	11.8	11.7	11.3	11.3	9.6	11.8	13.4	13.4	13.4	
Interest rates /7																											
Interst rates of CBBills	3.73	3.25	3.25	3.25	3.25	3.25	3.25	3.25	3.25	3.25	3.25	3.25	3.25	3.25	4.00	4.00	4.00	4.00	4.00	4.00	4.00	4.00	4.00	3.75	3.75	3.75	3.50
Lending rates																											
denar rates (aggregated, incl. denar and denar with f/x clause)	8.5	8.0	7.5	7.4	7.3	7.1	7.0	6.9	7.1	6.8	6.7	6.7	6.7	6.7	6.6	6.6	6.6	6.6	6.6	6.6	6.6	6.5	6.5	6.4	6.5	6.6	
f/x rates	7.0	6.5	6.3	6.1	6.0	5.9	5.8	5.8	5.9	5.7	5.7	5.6	5.6	5.5	5.5	5.5	5.5	5.4	5.4	5.4	5.4	5.3	5.3	5.2	5.2	5.4	
Deposit rates																											
denar rates (aggregated, incl. denar and denar with f/x clause)	5.1	4.4	3.7	3.3	3.2	3.0	2.7	2.6	2.9	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	2.5	
f/x rates	2.2	1.8	1.4	1.5	1.5	1.3	1.2	1.1	1.3	1.1	1.1	1.1	1.1	1.1	1.1	1.0	1.1	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	1.0	
IV. External sector indicators																											
Current account balance (millions of EUR)	**-240.0**	**-134.1**	**-43.2**	**33.3**	**-61.7**	**-97.2**	**114.4**	**-142.4**	**-187.0**	**18.1**	**-16.7**	**-45.1**	**-43.7**	**-91.8**	**-76.5**	**-36.1**	**-204.4**	**65.8**	**28.4**	**21.3**	**115.5**	**-2.7**	**-50.4**				
Current account balance (% of GDP)	*-1.6*	*-1.6*	-0.5	*0.4*	-0.7	-1.1	1.3	-1.6	-2.1	0.2	-0.2	-0.5	-0.5	-1.0	-0.8	-0.4	-2.1	0.7	0.3	0.2	1.2	0.0	-0.5				
Trade balance (millions of EUR) /8	**-1,946.7**	**-1,748.1**	**-1757.9**	**-73.7**	**-378.1**	**-446.5**	**-362.3**	**-538.7**	**-1725.7**	**-65.8**	**-131.6**	**-175.8**	**-373.2**	**-160.8**	**-175.7**	**-164.9**	**-501.5**	**-112.5**	**-156.0**	**-122.9**	**-391.4**	**-146.0**	**-174.0**	**-191.3**	**-511.3**	**-1777.4**	
Trade balance (% og GDP)	*-25.7*	*-21.6*	-20.7	*-0.8*	-4.2	-4.9	-4.0	-5.9	-19.0	-0.7	-1.4	-1.8	-3.9	-1.7	-1.8	-1.7	-5.2	-1.2	-1.6	-1.3	-4.1	-1.5	-1.8	-2.0	-5.3	-18.5	
import (millions of EUR)	-5,070.6	-4,983.3	-5504.5	-365.5	-1308.1	-1481.7	-1394.0	-1593.2	-5776.9	-354.1	-477.5	-525.0	-1356.6	-529.4	-531.2	-497.2	-1557.7	-516.6	-509.5	-513.9	-1540.0	-533.8	-526.1	-592.6	-1652.4	-6106.7	
export (millions of EUR)	3,124.0	3,235.2	3746.6	291.8	929.9	1035.2	1031.7	1054.4	4051.2	288.3	345.9	349.2	983.3	368.5	355.4	332.3	1056.2	404.1	353.5	391.0	1148.6	387.8	352.1	401.2	1141.1	4329.3	
rate of growth of import (y-o-y)	0.3	-1.7	10.5	-3.0	5.4	8.2	-0.7	6.9	4.9	-3.1	16.8	-1.6	3.7	6.3	13.1	-3.3	5.1	2.1	19.0	11.7	10.5	-0.2	0.9	10.4	3.72	5.71	
rate of growth of export (y-o-y)	-2.8	3.6	15.8	23.8	13.9	9.9	4.5	5.4	8.1	-1.2	15.7	3.0	5.7	24.8	-1.0	-12.8	2.0	16.4	11.4	6.4	11.3	5.2	-2.2	23.2	8.2	6.9	
Foreign Direct Investment (millions of EUR)	**131.1**	**229.4**	**197.4**	**43.0**	**78.5**	**60.8**	**-7.7**	**71.1**	**202.8**	**24.7**	**49.7**	**42.7**	**117.1**	**25.9**	**27.9**	**-17.5**	**36.4**	**5.3**	**42.7**	**-35.9**	**12.1**	**9.9**	**32.5**				
External debt																											
Gross external debt (in milllions of EUR)	5171.7	5219.7	5992.3		6320.7	6416.2	6326.8	6290.5	6290.5				6813.4				6880.3				7503.9						
public sector	2162.1	2172.4	2846.8		3019.1	3054.2	3035.5	2933.7	2933.7				3279.4				3283.1				3891.1						
public sector/GDP (in %)	28.5	26.7	33.4		33.3	33.7	33.5	32.4	32.4				34.1				34.2				40.5						
private sector	3009.5	3047.4	3145.5		3301.6	3362.0	3291.3	3356.9	3356.9				3534.0				3597.3				3612.8						
Gross external debt/GDP (in %)	68.2	64.0	70.3		69.8	70.8	69.8	69.4	69.4				70.9				71.6				78.1						
Gross official reserves (millions of EUR) /9	**2,193.3**	**1,993.0**	**2,436.5**	**2,483.7**						**2,246.9**	**2,253.4**	**2,266.3**		**2,193.8**	**2,164.4**	**2,158.8**		**2,588.2**	**2,676.6**	**2,698.9**		**2,728.8**	**2,551.2**	**2,613.2**			**2556.8**

/1 While calculating the relative indicators, the annual GDP from the official announcement of SSO is used. For 2015, the projected level from the NBRM projections from October 2015 is used.
/2 Preliminary data for 2014. Estimated data for 2015.
/3 The changes of Index of industrial production are according to base year 2010=100.
/4 CPI calculated according to COICOP.
/5 Inflation on annual basis corresponds to end-year inflation (December current year/December previous year)
/6 The calculations are based on the New Methodology for compiling standard forms of the monetary balance sheets and surveys and the new accounting plan (in force since 01.01.2009).
/7 As of January 2015 data for active and passive interest rates are compiled according to the new methodology of NBRM.
/8 Trade balance according to foreign trade statistics (on c.i.f. base).
/ 9The data from 2008 include accrued interest. The latest available data on gross official reserves are preliminary data.

Foreign effective demand
(annual changes in %)



Source: "Consensus Forecast" and NBRM calculations.

According to the latest assessments, the foreign effective demand for 2016 and for 2017 is slightly higher than the October forecast, while expectations for 2018 are minimally revised downwards.

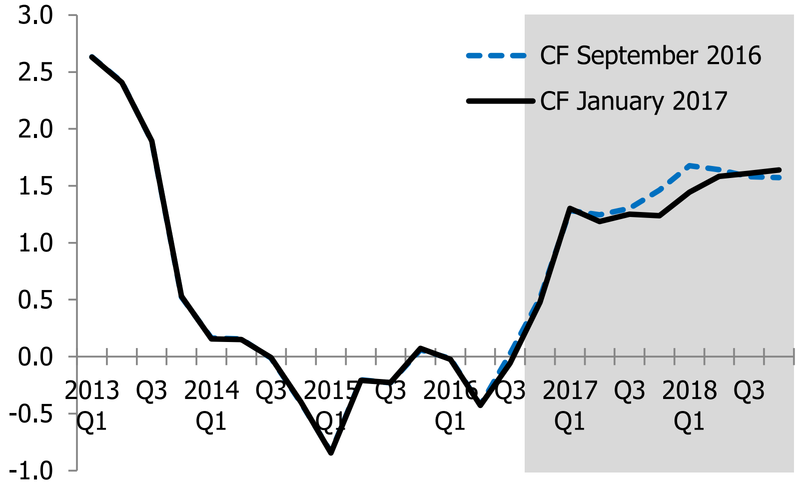
Thus, the estimated growth of foreign demand in 2016 is 1.9%, compared to 1.8% in October...

...amid minimal upward revision of the forecast for growth in 2017 (from 1.7% to 1.8%)...

...which is mainly due to the improved economic performance and expectations in the region (Bulgaria, Greece and Serbia), amid downward revision of economic growth in Germany in 2016 and 2017.

The minimal downward revision of the foreign effective demand for 2018 to 1.9% from 2.0% in October is due to expectations for lower growth of the economies of Greece and Serbia than forecasted.

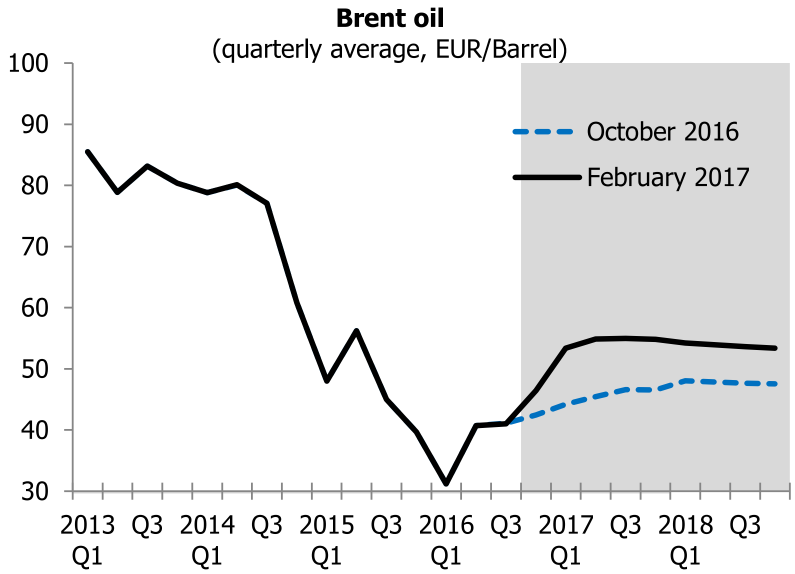
Foreign effective inflation
(annual rates in %)



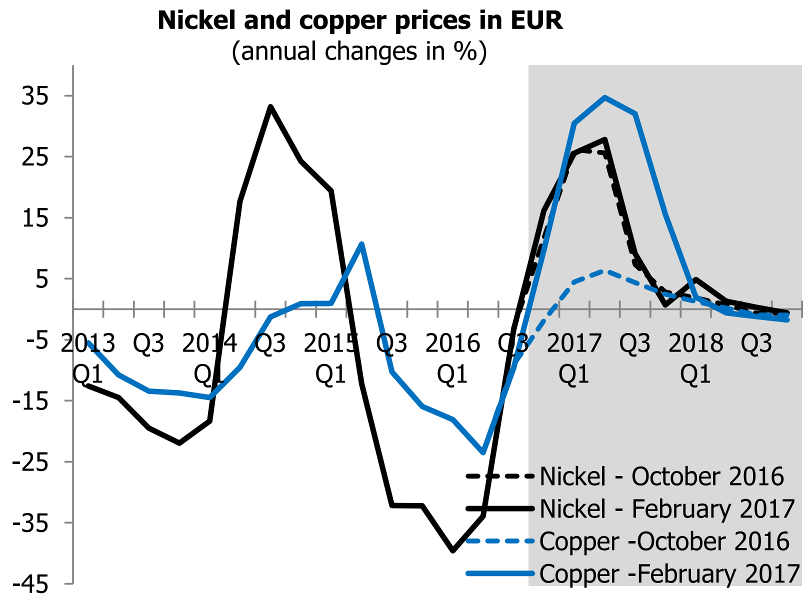
Source: "Consensus Forecast" and NBRM calculations.

The October forecasts for foreign effective inflation remained unchanged...

...i.e. the foreign effective inflation is expected to increase from 0% in 2016, to 1.3% and 1.6% in 2017 and 2018, respectively.



Source: "Consensus Forecast" and NBRM calculations.



Source: "Consensus Forecast" and NBRM calculations.

In 2017, oil price was considerably revised upward[2]...

...and the current expectations are that growth will be more than twice higher than the October forecast...

...as a result of the agreement between the OPEC countries and some non-OPEC countries for reduction of the global oil production in order to contribute to the upward movement of prices[3].

On the other hand, given the higher price level in 2017, for 2018, slight decline in oil price on world markets is forecasted, compared to the growth expected in October.

The fall in metal prices in 2016 is similar to the forecasted in October.

In 2017, in turn, the price of copper was considerably revised upward, while expectations for the price of nickel are the same to the October forecasts.

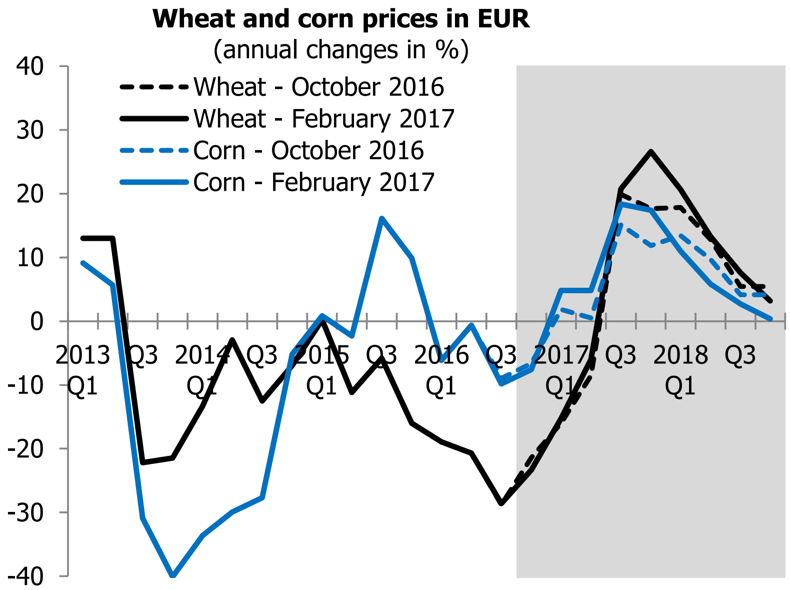
Thus, for 2017, the price of copper is expected to register double-digit growth, which is different from the moderate growth expected in October...

...largely due to the drop in global inventories of copper, possible interruptions in supply facilities and expectations for higher demand in the US and China.

In 2018, changes in the forecasts of metal prices are small, whereby their stabilization is further expected.

[2] For the analysis of prices of oil, metals and primary food products, various reports of the IMF, World Bank, FAO, OPEC, the ECB and the specialized international economic portals are used.

[3] Agreement was reached on 30 November 2016 in Vienna, requiring the production to be cut by 1.2 million barrels a day, starting from 1 January 2017. An additional meeting between the OPEC and non-OPEC countries was held on 10 December, where, for the first time since 2001, it was agreed oil production also to be cut by the non-OPEC countries, which should amount to 558 thousand barrels, in addition to cuts that were promised by the OPEC member countries. This agreement will be implemented during the first six months of the year with a possibility of extension for another six months.



Source: "Consensus Forecast" and NBRM calculations.

For 2017, stock prices of wheat expressed in dollars were revised downward, while maize prices remained unchanged.

Thus, the price of wheat is now forecasted to register slightly sharper decline than the October forecast...

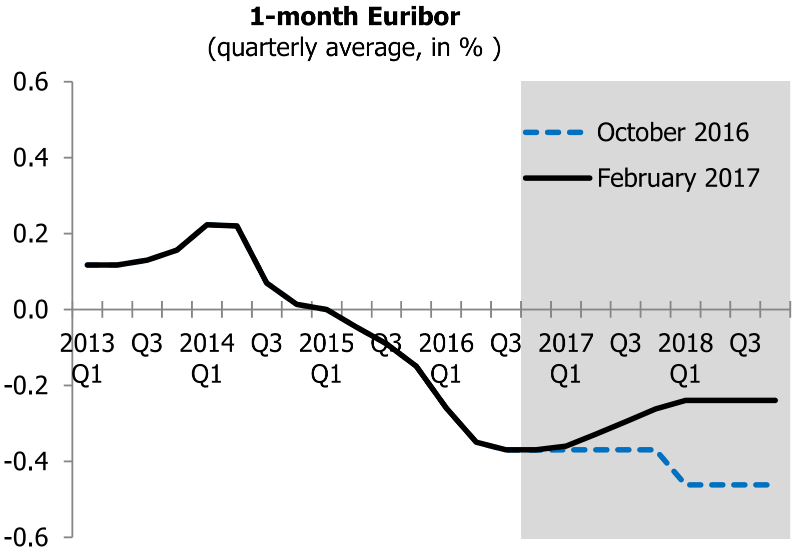
...mostly due to the improved production prospects in Argentina, Australia and Brazil and expectations for higher level of inventories worldwide.

Contrary to the movements in dollar prices, prices of wheat and maize in euros were revised upward...

...which is explained by expectations for greater appreciation of the exchange rate of the US dollar against the euro in 2017.

On the other hand, the revisions of prices of primary food products in 2018 expressed in both dollars and euros are small and in a divergent direction...

...i.e. slightly higher growth of the price of wheat and smaller growth of the price of maize is expected compared to the October forecasts.



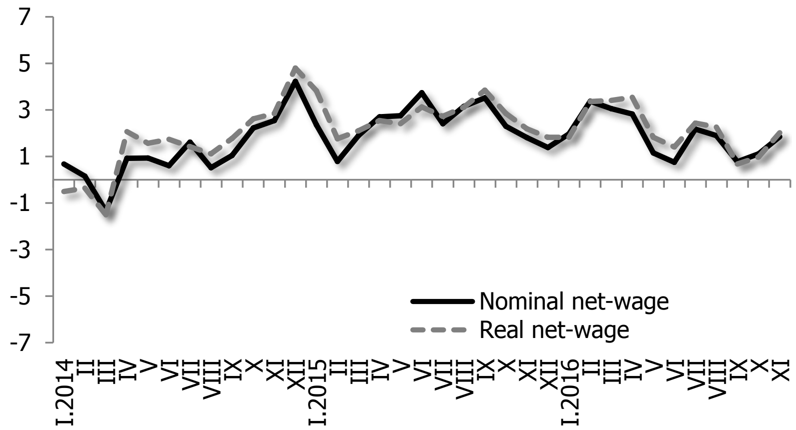
Source: "Consensus Forecast" and NBRM calculations.

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

...whereby similar average level of -0.31% (-0.37% in October) is forecasted, amid a continuation of the Quantitative Easing Program of the ECB by the end of the year, but amid a reduction of its volume.

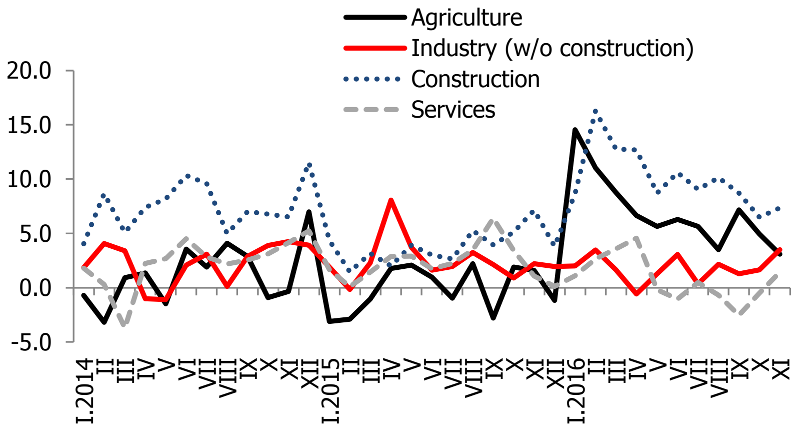
On the other hand, current expectations include the possibility of reduction of the monetary stimulus of the ECB in 2018, prompting an upward revision of the one-month Euribor to -0.24%, versus -0.46% in October.

Average net-wage
(annual changes, in %)



Source: SSO.

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



Source: SSO.

In November 2016, the average net wage in the Republic of Macedonia registered a nominal annual growth of 1.8%, which is a growth acceleration of 0.7 p.p. compared to the previous month.

Upward movement in wages is characteristic of most of the activities, amid higher growth recorded in mining, construction, administrative and auxiliary services, and in arts, entertainment and recreation. In November, lower wages were paid only in a few services[4].

Amid small decrease in the consumer prices in November the **real wages** increased by 2%.

Performances in wages in the first two months of the last quarter are mainly close to the expected movements for the quarter within the October forecast.

The currently available data for the fourth quarter indicate divergent movements. Namely, analyzed through the high-frequency indicators, the situation in the individual economic sectors in the fourth quarter is assessed as less favorable compared to the previous quarter.

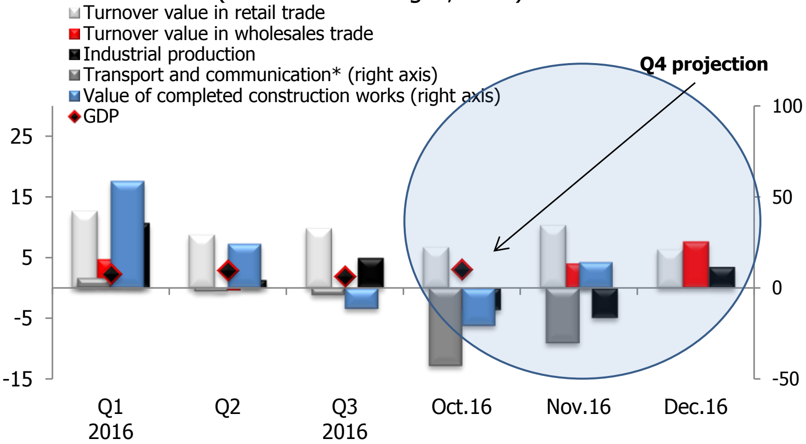
Thus, in the last quarter of the year, the **industrial output** declined by 1.8% which was mainly due to the decline in the manufacturing industry. Decline was also recorded in mining, while the energy sector registered a growth.

Within the manufacturing industry, the decline reflects less favorable developments in traditional industries (production of food products, beverages, clothing[5], and metals and fabricated metal products). The fall in production, to some extent, was mitigated by the increased production of non-metallic mineral products, machinery and equipment, as

[4] Within the services sector, lower wages were paid in November in: financial activities and insurance activities, information and communications, real estate activities, and in education.
[5] The fall in the production of clothing and beverages is due to the high base effect of the previous year.

Economic activities

(real annual changes, in %)



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

well as motor vehicles, trailers and semi-trailers.

However, seen dynamically, after the fall in October and November, in **December**, there was a moderate growth of the industrial output reflecting the higher production in the manufacturing industry (related in part to the depletion of the base effect in some traditional industries), and the higher energy production. Also, cumulatively, for the entire 2016 the industrial output is higher by 3.4%. These trends are in accordance with surveys conducted in the last quarter which did not indicate significant, structural problems associated with the operation in the industrial sector.

After the fall in October, in November, the value of completed construction works increased as a result of the increased activity in the field of civil engineering. However, seen cumulatively for the first two months of the fourth quarter, the **activity in the construction sector** declined[6].

In the period October-November, the unfavorable trends were registered in **rail traffic** amid sharp decline in passenger rail traffic[7].

On the other hand, total **trade** continued to grow in the fourth quarter, at a similar pace as in the previous quarter, which was mostly due to the higher turnover in retail trade, and wholesale trade also made a positive contribution.

According to available data for the period October-November, the **catering services** continued registering favorable trends (annual growth in the number of tourists, overnight stays and turnover).

Despite indications of less favorable developments in the economic sectors, the

[6] The decline is due to the high base effect of the previous year when record high investments were registered in road infrastructure.
[7] The relatively high decline in rail traffic is associated with the high base effect of last year, when in the second half of the year, the demand for this type of service increased as a result of the refugee crisis.

aggregate demand indicators mainly point to growth of the economic activity in the fourth quarter of 2016.

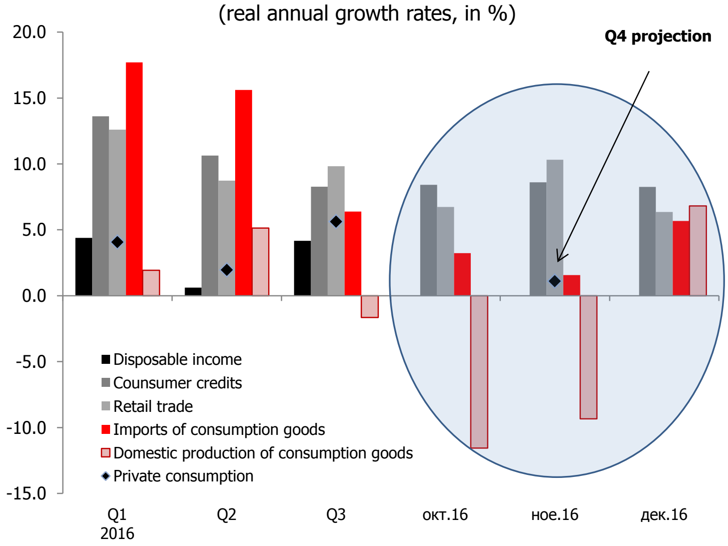
Most of the high frequency data point to growth of private consumption also in the fourth quarter...

...amid favorable performances in the main disposable income components (wages, pensions, social government transfers), as well as solid growth of household lending.

The growth of household consumption is indicated also by the growth in imports of consumer goods and higher turnover in retail trade (although the growth is slower compared to the previous quarter).

Analyzing the indicative private consumption categories, a decline was noticed in private transfers and domestic production of consumer goods.

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



Source: SSO and NBRM calculations.

Available short-term indicators of **investment activity** provide divergent directions regarding the movement of gross capital formation in the fourth quarter of 2016.

Thus, in the last quarter of the year, there was an increase in foreign direct investment[8], imports of investment goods and domestic production of capital goods, and at the same time the growth of long-term lending to the corporate sector continued.

However, all these categories registered a growth deceleration compared to the previous quarter.

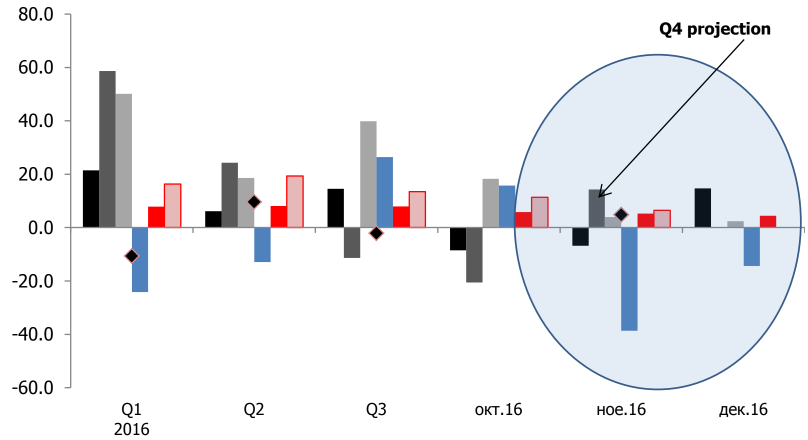
Also, in the period October-November, the value of completed construction works declined...

...and during the fourth quarter, lower government capital investments were registered.

Inventories, as a component of gross

[8] The data on foreign direct investment refers to the period October-November 2016.

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



Imports od capital goods
Completed construction works
Domestic production of capital goods
Government investments
Long term credits to enterprises
Final product stocks
Gross investment

Source: SSO and NBRM calculations.

investments, can be expected to increase in the fourth quarter, amid upward movement in the index of inventories of finished products in the industry, registered in the period October-November.

In the fourth quarter of 2016, nominal data on **foreign trade** show slight narrowing of the trade deficit...

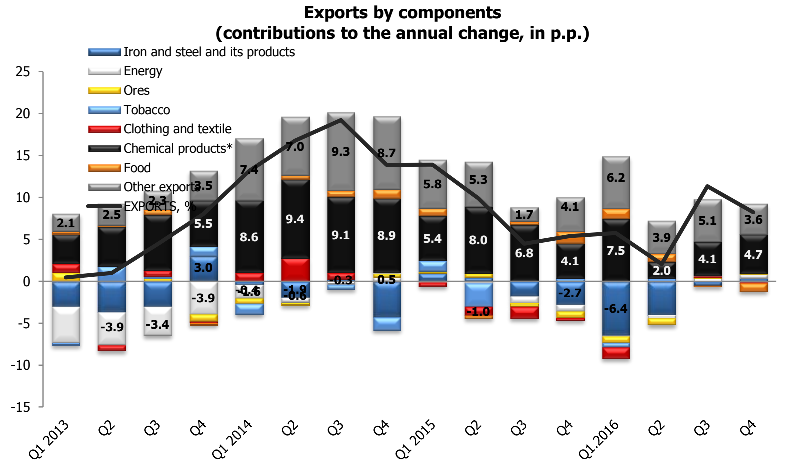
... given the higher increase in exports compared to imports of goods and services.

In the fourth quarter, the budget performances point to higher **public spending**...

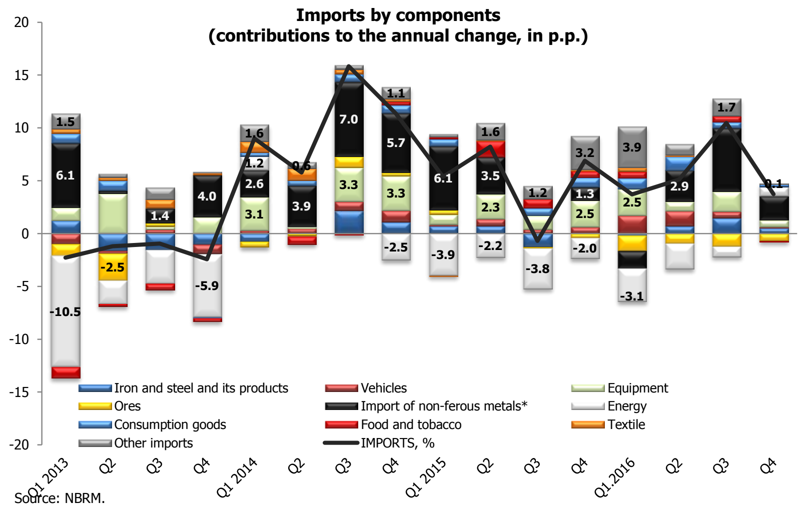
...given strong growth of the expenditures on goods and services...

...and higher wage expenses for the employees in the public sector and health care transfers[9].

[9] Most of these assets refer to expenditures on goods and services.



Source: NBRM.
** The following data depict the overall exports of one major export capacity in the free industrial zone.*



Source: NBRM.
** The following data depict the overall imports of one major export capacity in the free industrial zone.*

In the fourth quarter of 2016, the foreign trade deficit narrowed by 5.1% annually, amid solid annual growth of export component and more moderate growth in import activity.

Such performances are better than the forecast for the fourth quarter in October, which expected a slight widening of the trade deficit on an annual basis.

Exports of goods during the fourth quarter of 2016 registered an annual growth of 8.2%, largely due to the performance in the new export-oriented facilities in the economy, but also in other export components with the exception of food and clothing and textiles.

In the fourth quarter of 2016, the export performances are at the level expected with the October forecast. Other exports registered upward deviations (better performances in part of the new export-oriented facilities), as well as the export of energy and tobacco. On the other hand, there was a downward deviation in the exports of one part of the new export-oriented facilities, and the export of food and clothing and textiles.

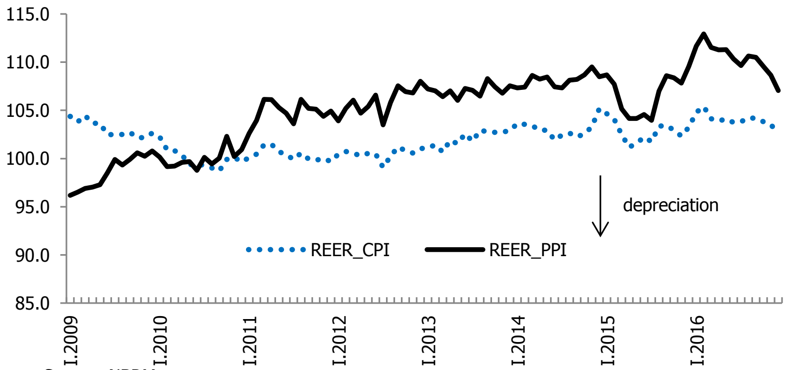
Imports of goods in the fourth quarter of 2016 registered a modest annual growth, primarily due to the growth of imports of raw materials in part of the new export-oriented facilities, but also to the growth of the imports of energy, equipment and machinery, and iron and steel...

...amid a slight decline in the imports of ores, textiles and food.

Imports of goods in the fourth quarter of 2016 indicates performance lower than forecasted. Considering the individual components, the performance was lower in almost all categories except in energy imports, while imports of consumer goods and other imports are within the October forecast.

The analysis for the entire 2016 indicates a slightly lower trade balance compared with expectations in the October forecast. The export performances are within the forecast, amid better performance in other exports (due to the new facilities in the economy) and weaker performance of part of the new export-oriented facilities, as well as food and textiles. At the same time, imports throughout 2016 was lower than forecasted, mostly as a result of the lower imports of iron and steel.

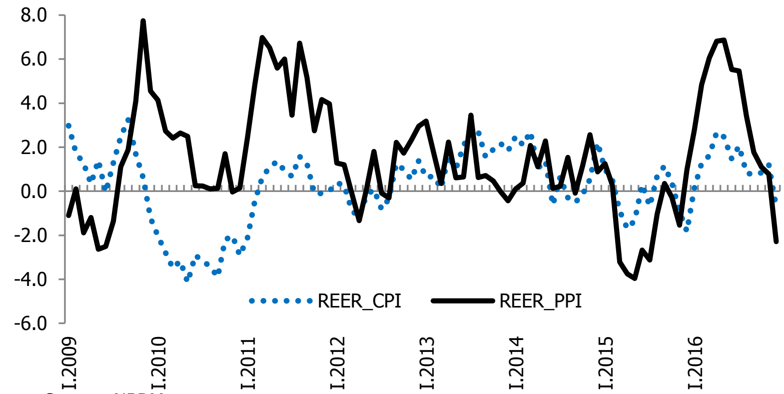
REER
(2010=100)



Source: NBRM.

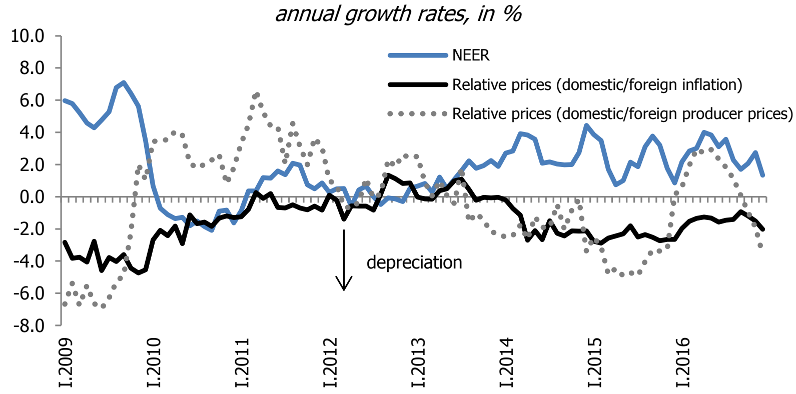
In December 2016, **indicators of price competitiveness of the domestic economy, analyzed on an annual basis, entered the zone of depreciation for the first time since late 2015.** The REER index deflated by consumer prices have depreciated by 0.7% and the REER index deflated by producer prices have registered a more pronounced depreciation of 2.3%.

REER
annual changes, in %



Source: NBRM.

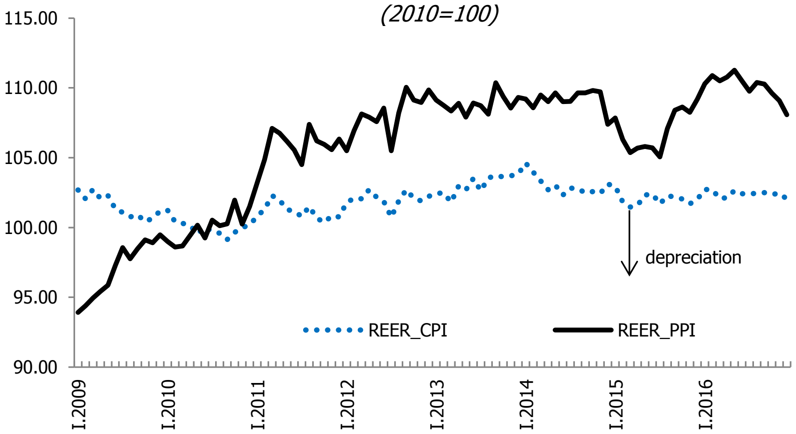
NEER and relative prices
annual growth rates, in %



Source: NBRM.

These developments are mostly due to the reduction of the relative producer prices of 3.6%, and the reduction of the relative consumer prices of 2%. Simultaneously, the NEER appreciated by 1.3% annually, mostly as a result of the depreciation of the British pound and the Turkish lira, amid a simultaneous appreciation of the Russian ruble.

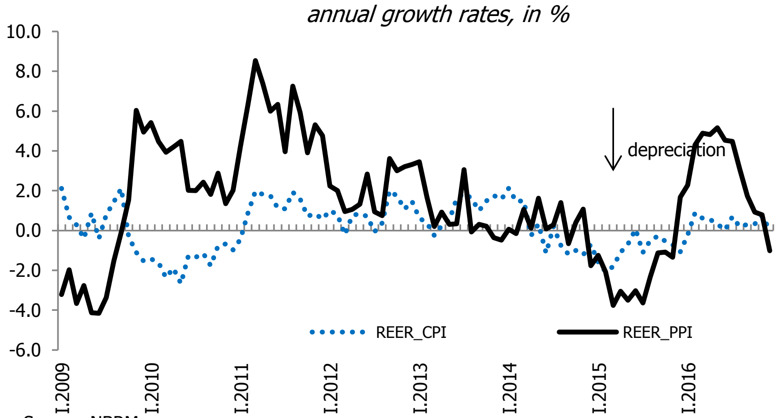
REER, excluding primary commodities
(2010=100)



Source: NBRM.

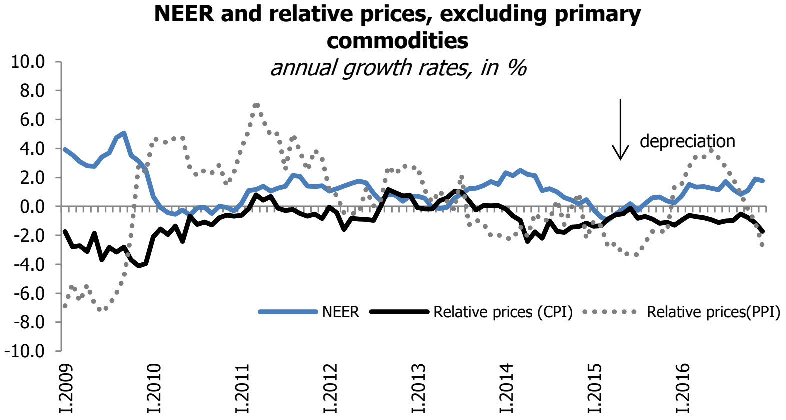
The analysis of **REER indices, as measured using weights based on the foreign trade without primary commodities**[10] **indicates that** in December the REER index deflated by consumer prices registered no change, while the REER deflated by producer prices depreciated by 1%.

REER, excluding primary commodities
annual growth rates, in %



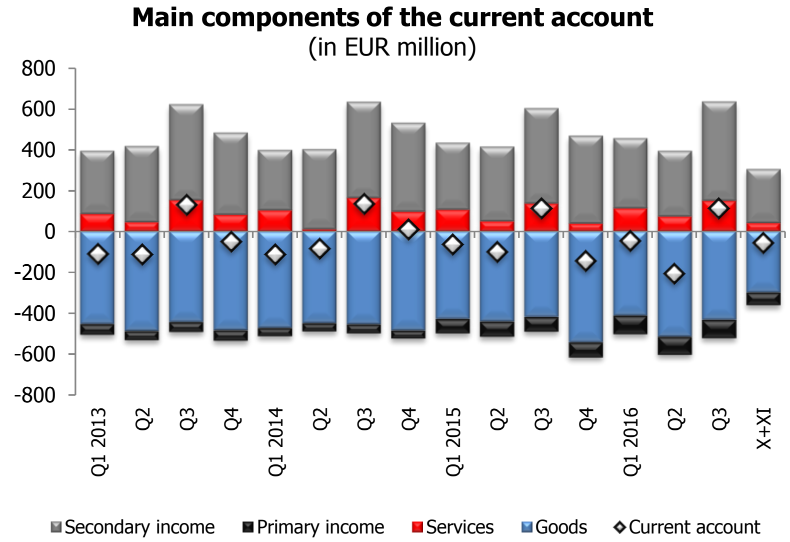
Source: NBRM.

[10] Primary commodities not included in the calculation are: oil and oil derivatives, iron and steel, ores and imported raw materials for the new industrial facilities in the free economic zones.



Source: NBRM.

On an annual basis, the relative consumer prices and the relative producer prices decreased by 1.7% and 2.7%, respectively. The NEER has appreciated by 1.8% on an annual basis.

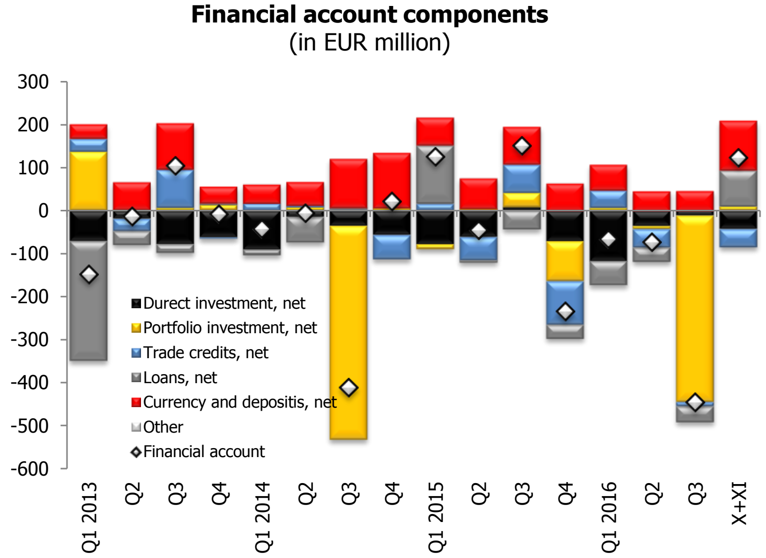


Source: NBRM.

In the period October - November 2016, the balance of payments current account registered a deficit of Euro 53.2 million (or 0.6% of GDP), which is a smaller deficit than planned for the last quarter, according to the October forecast.

Analyzing individual components, the favorable performance is mostly due to the improved trade balance, while the secondary income surplus is lower than forecasted. The other two components do not deviate significantly from the expectations according to the October forecast.

Analyzed on cumulative basis, the current account deficit for the entire 2016 is expected to be close to the October forecast.

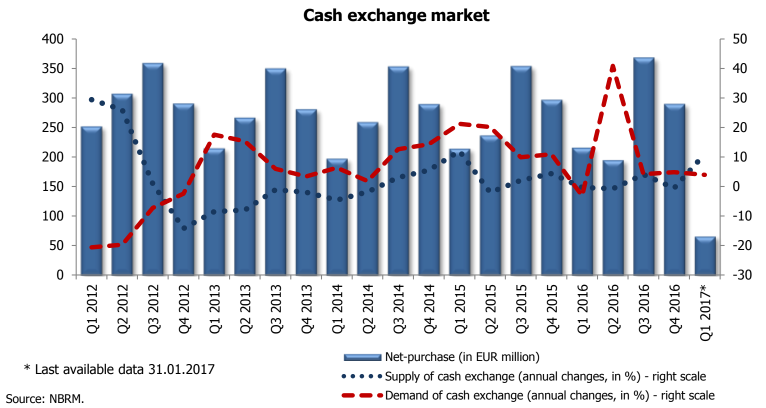


Source: NBRM.

During October and November 2016, the financial account registered net outflows of Euro 123.9 million (or 1.3% of GDP), which is the expected direction of the developments in the fourth quarter according to the October forecast, which is largely associated with the regular maturity of greater amount of external government debt[11]. The latest available data provide an indication of registering lower net outflows in the financial account than forecasted.

These deviations mainly derive from the lower net outflows in long-term loans than forecasted. On the other hand, the category "currency and deposits" registered higher net outflows, as a result of the performance of depository institutions.

On a cumulative basis, the net inflows in the financial account are expected to be higher than forecasted for 2016 as a whole.



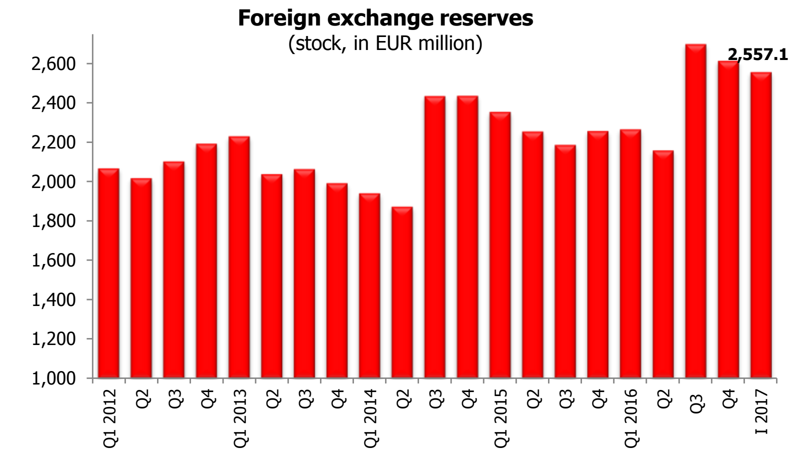
* Last available data 31.01.2017

Source: NBRM.

Recent data on currency exchange operations as of January 2017 indicate annual increase in both the supply of and demand for foreign currency.

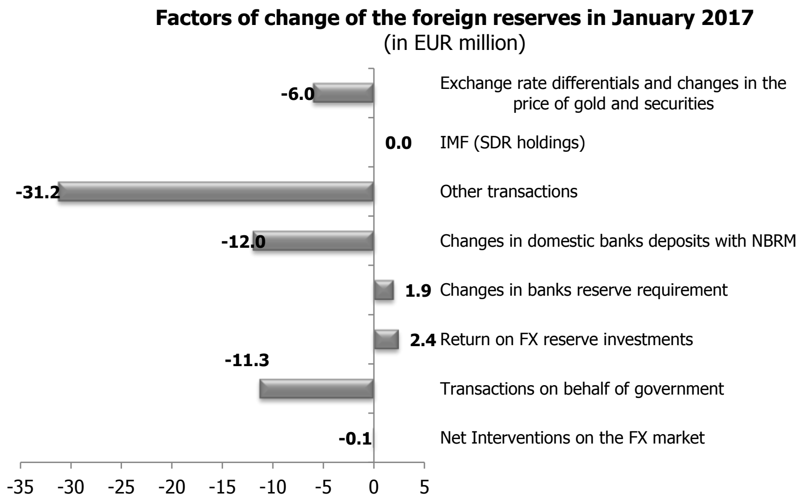
The net purchase on the currency exchange market in this period amounted to Euro 66 million, which is annual growth of 14.4% and is close to the forecast, according to the October forecasts.

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

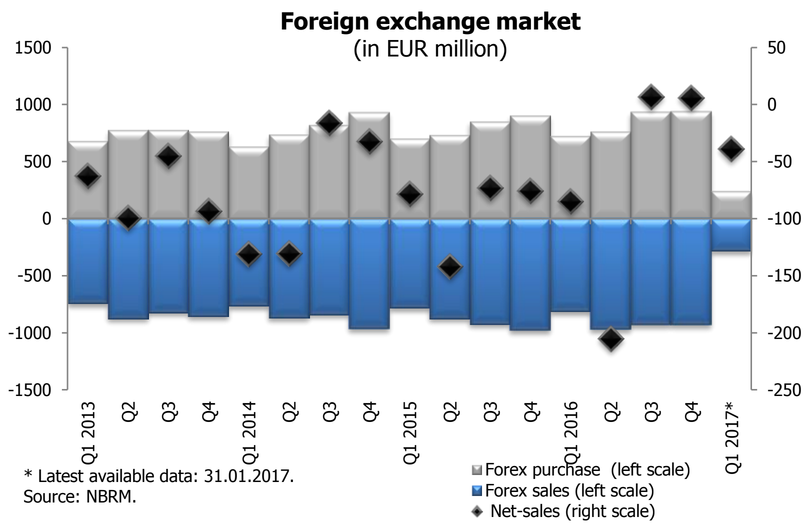


Source: NBRM.

As of 31 January 2017, the gross foreign reserves stood at Euro 2,557.1 million, down by Euro 56.3 million compared to the level of the end of 2016. The reduction in foreign reserves primarily results from changes in the category "other" and is temporary. Additionally, the reduction of the foreign currency deposits of domestic banks with the NBRM, transactions on behalf of the government and negative price changes of securities contributed to the decline in foreign reserves.

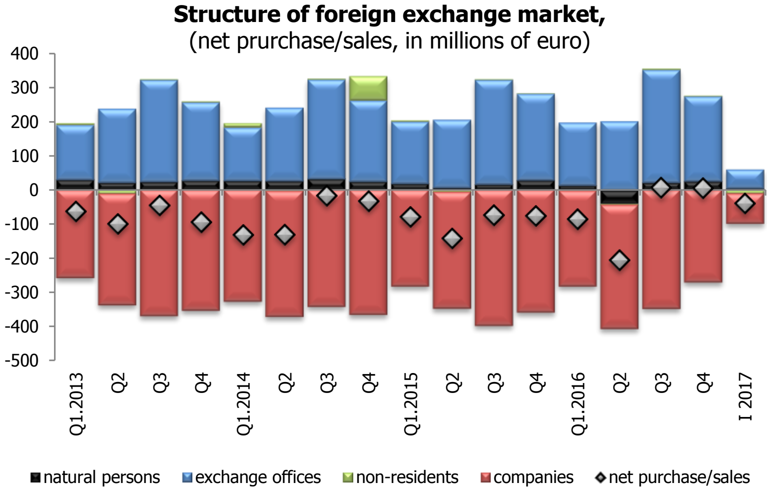


Source: NBRM.



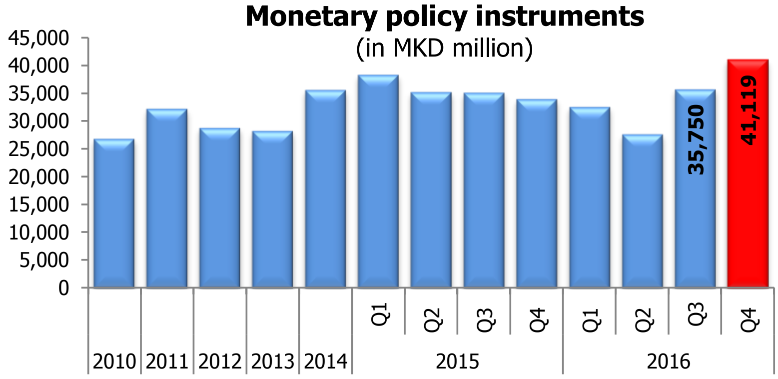
* Latest available data: 31.01.2017.
Source: NBRM.

In January 2017, the foreign exchange market of banks reported a net sale of Euro 38.8 million, by Euro 13 million higher compared to the same period last year. This annual change is a result of the faster increase in the demand for relative to the supply of foreign currency (of 13.4% and 9.2%, respectively).



Source: NBRM

Sector-by-sector analysis shows that these deviations mostly arise from the higher net sales in companies, and to a lesser extent, the higher net sales of non-residents.



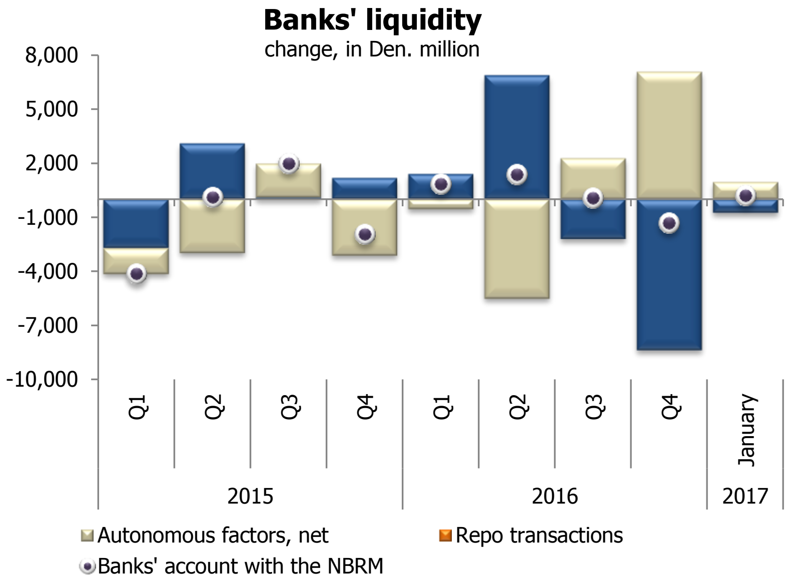
Source: NBRM.

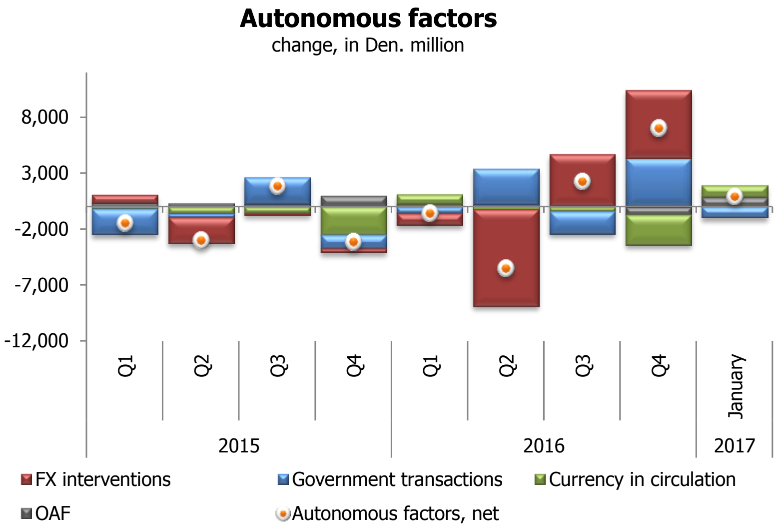
The stock of the monetary instruments at the end of December was higher compared to the end of the third quarter. The liquidity withdrawn from the banking system through the monetary instruments was within expectations according to the October forecast.

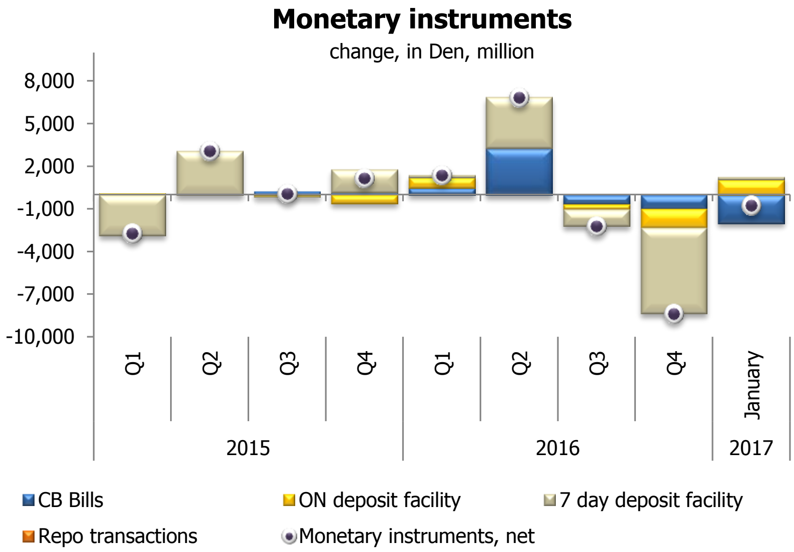
Data as of December indicate a decline in the net foreign assets of the NBRM in relation to the end of the third quarter, but significantly lower than forecasted for the fourth quarter, according to the October forecast. On the other hand, total government deposits registered a decrease which is lower than expected for the last quarter. This shift was mostly due to the achievement of lower budget expenditures and, consequently, lower budget deficit compared to the Budget Revision[12].

In December, the reserve money were higher compared to the end of the third quarter, but the growth was lower than forecasted for the last quarter. The growth is entirely due to the increase in currency in circulation, while total liquid assets of banks decreased (versus expectations for growth in both categories according to the October forecast).

[12] In 2016, 93.9% of the planned budget expenditures and 69.5% of the planned budget deficit for 2016 were realized.



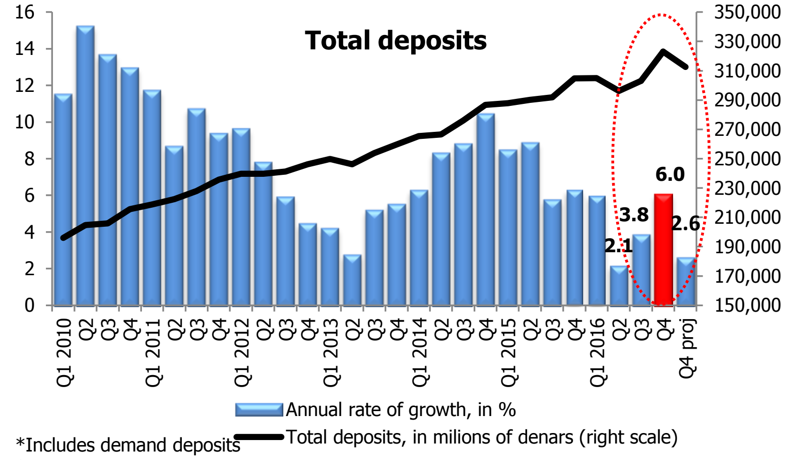




According to operational liquidity data, in January, the liquidity of the banking system registered a moderate monthly increase. Amid growth of liquidity under the influence of autonomous factors (mostly as a result of the seasonal decline in currency in circulation) and relatively high liquidity position in the system, in January, part of the excess liquidity was withdrawn by increasing the amount of CB bills[13].

Total deposits in December

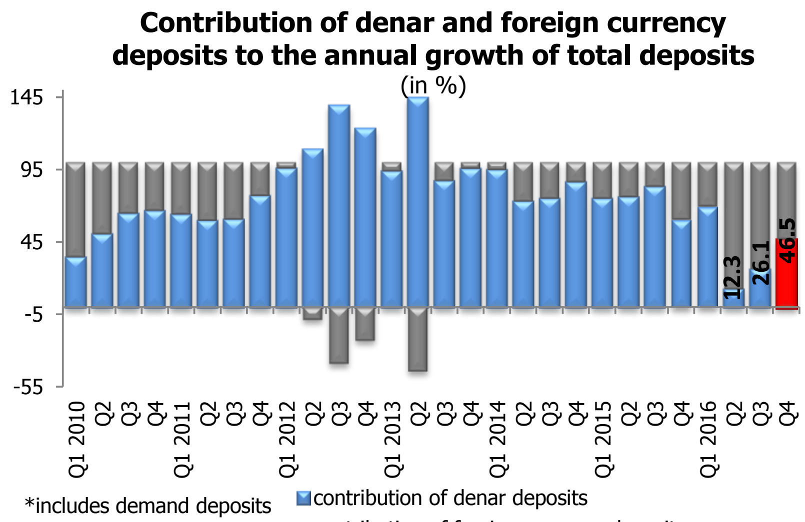
[13] At the regular meeting of the NBRM's Operational Monetary Policy Committee, held on 10 January 2017, the Committee decided to increase the supply of CB bills at the 11 January auction from Denar 23,000 million to Denar 25,000 million. At the same meeting, the Committee decided to cut CB bill interest rate from 3.75% to 3.5%, i.e. by 0.25 percentage points.



*Includes demand deposits
Source: NBRM.

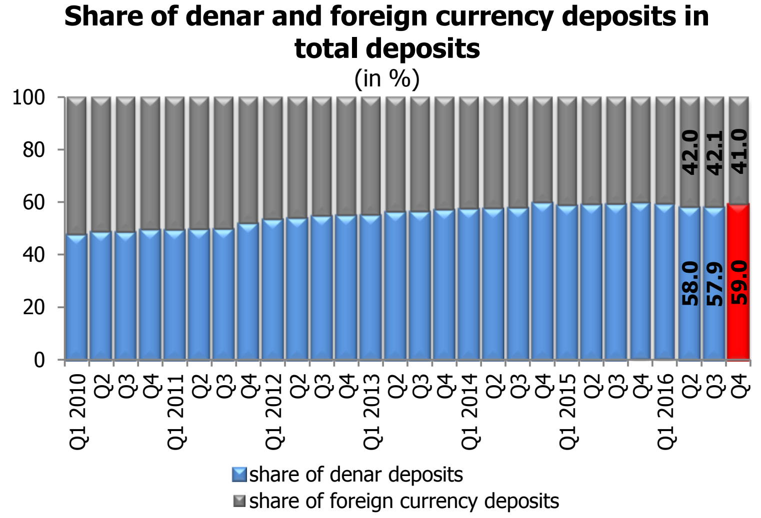
registered a significant monthly increase, which followed after the relatively moderate growth in the previous two months. Analyzed by sector, the largest contribution to the monthly growth (of 4.3%) of total deposits in December was made by the corporate deposits (55.8%), and positive, but moderately lower contribution was made by the household deposits. Analyzing by currency, the largest contribution to the monthly growth of total deposits was made by local currency deposits (80.6%), with a moderate contribution being also made by foreign currency deposits.

In December, the annual growth rate of total deposits equaled 6.0%, which is above the projected growth of 2.6% for the last quarter of 2016. Seen dynamically, the deposit base increases for the second consecutive quarter and is a clear signal for further stabilization of the expectations and depletion of the effects of non-economic factors.



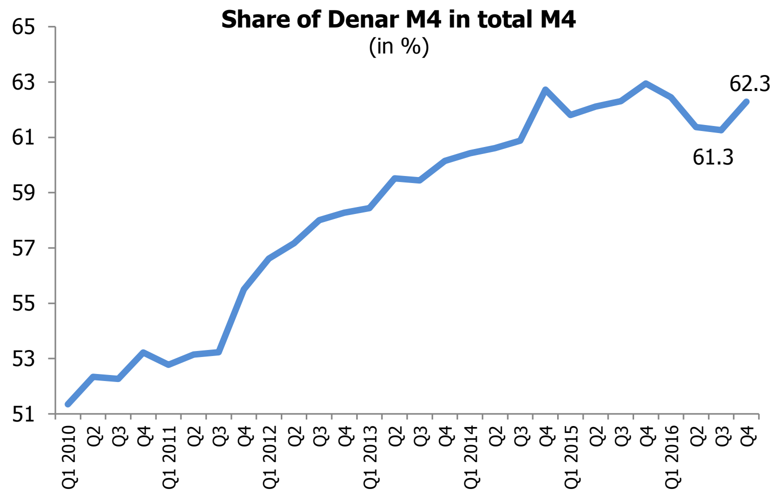
*includes demand deposits
Source: NBRM.

Similar to the previous months, the contribution of the growth of foreign currency relative to the growth of denar deposits to the annual growth of deposits in December is relatively larger. However, seen dynamically, in the second half of 2016, the contribution of foreign currency deposits to the annual growth of total deposits registered a constant monthly decline.



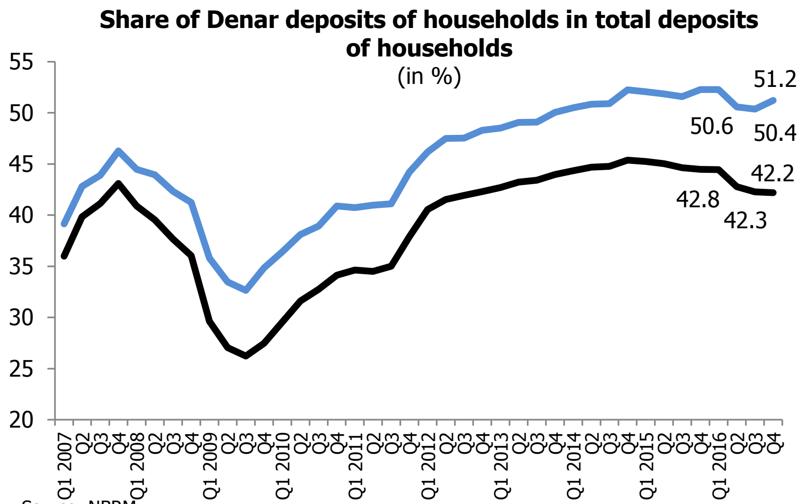
*includes denar deposits with FX clause. Source: NBRM.

Analyzing the currency structure of total deposits, in December, the share of denar and foreign currency deposits is stable, similar to the previous months. Denar deposits dominated in the banks' deposit base.

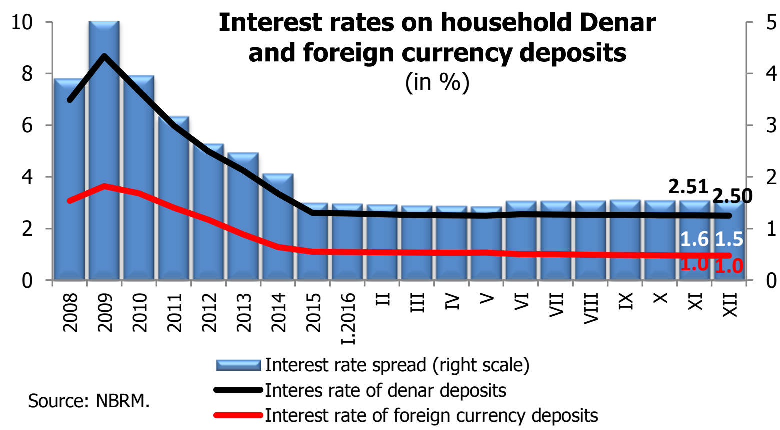


Source: NBRM.

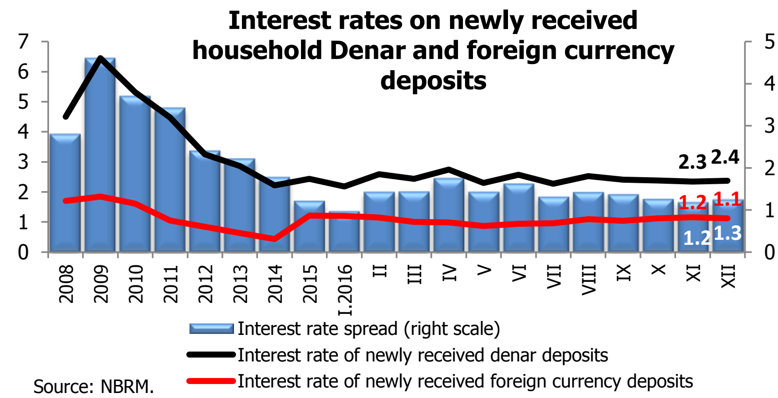
Total household deposits, in December, recorded the highest monthly growth (2.4%), which is a common dynamics for the end of the year. Analyzing by currency, in December, Denar deposits are the generator of the monthly growth of household deposits, while foreign currency deposits make small positive contribution.



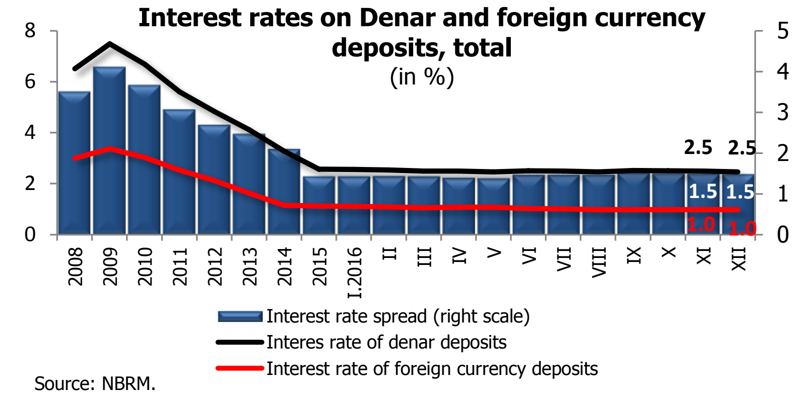
Source: NBRM.



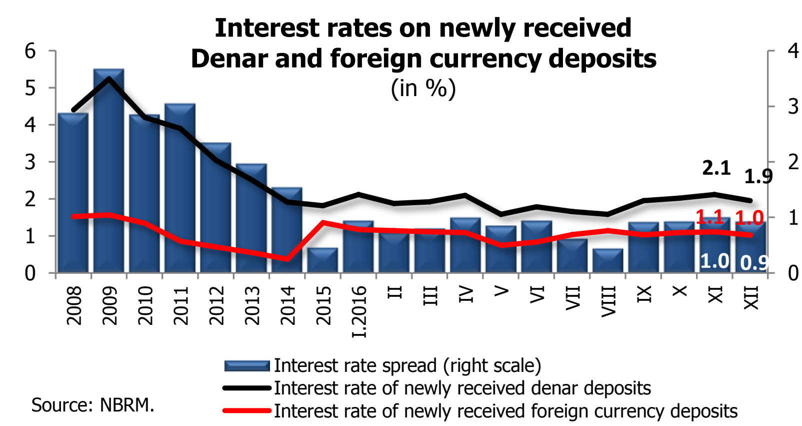
Source: NBRM



In December, interest rates on household deposits registered slight changes. The interest rate on Denar household deposits in December registered a slight shift downwards, while the interest rate on foreign currency deposits was unchanged for the seventh consecutive month. As a result of these performances, the interest rate spread between the Denar and foreign currency deposit interest rate registered a slight narrowing. Interest spread of new household deposits has widened, amid a slight increase in the interest rate on Denar deposits, amid simultaneous decrease in the interest rate on foreign currency deposits.

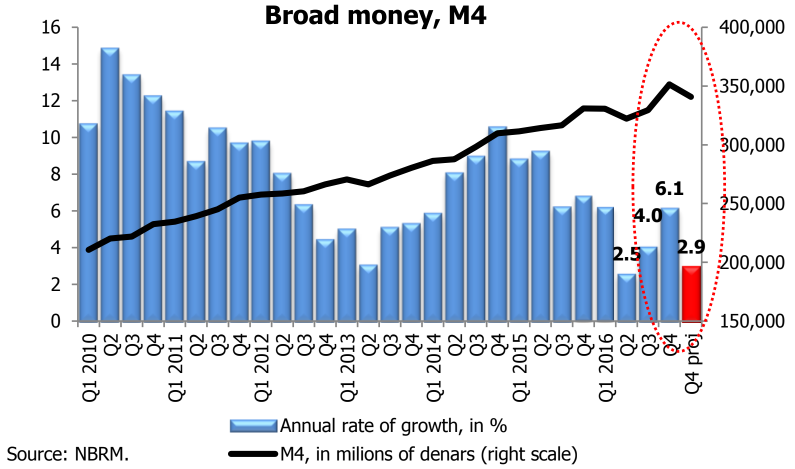


Source: NBRM



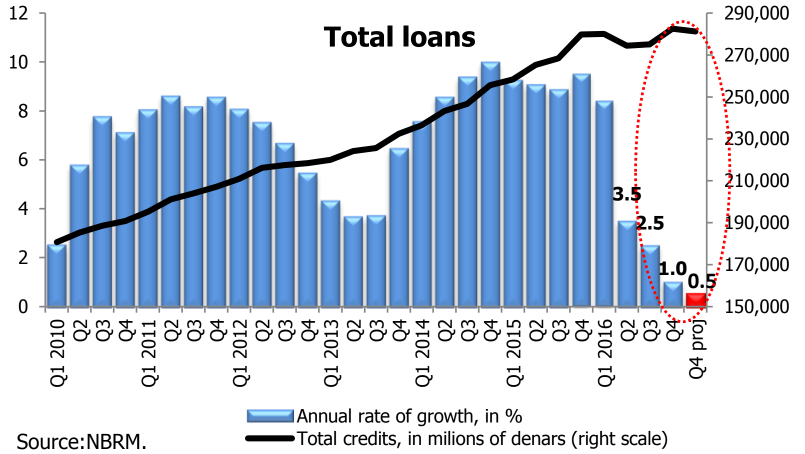
In December, interest rates on total deposits registered no changes compared to the previous month. Regarding the newly accepted deposits, in December, interest rates on Denar and foreign currency deposits registered a moderate decrease, leading to a slight narrowing of the interest spread. One should bear in mind that variable movements are characteristic of the interest rates on new deposits[14].

[14] Volatility of interest rate on newly accepted deposits results from the fact that they derive from the volume of newly received deposits (which can vary from month to month) and their interest rate.



Source: NBRM.

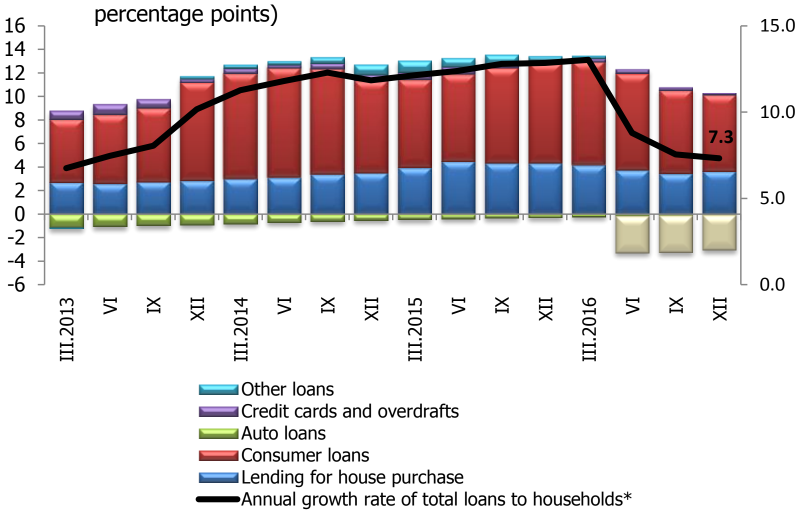
Broad money M4 registered a monthly increase (of 4.6%) in December. The increase in the money supply is mainly explained by the widening of the deposit base, amid solid growth of currency in circulation, which is a common seasonal movement in this period. **On annual basis, the broad money increased by 6.1%, which is above the growth of 2.9% forecasted for the fourth third quarter of 2016.**



Source:NBRM.

Total loans in December recorded the highest monthly increase since the beginning of the year. Analyzed by sector, the increase in total lending on a monthly basis (2.9%) almost entirely stems from the growth of corporate loans, amid small contribution of loans to households. The results of the Lending Survey regarding the banks' expectations for the first quarter of 2017 suggest a further easing of overall credit terms in both sectors, amid moderate net increase in demand in both sectors.

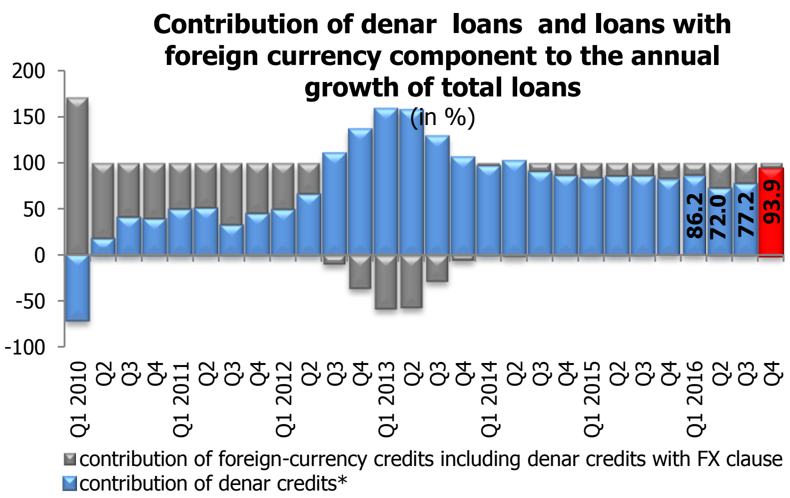
Loans of banks and savings houses extended to households
(contribution to the annual change of loans to households*, in percentage points)



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

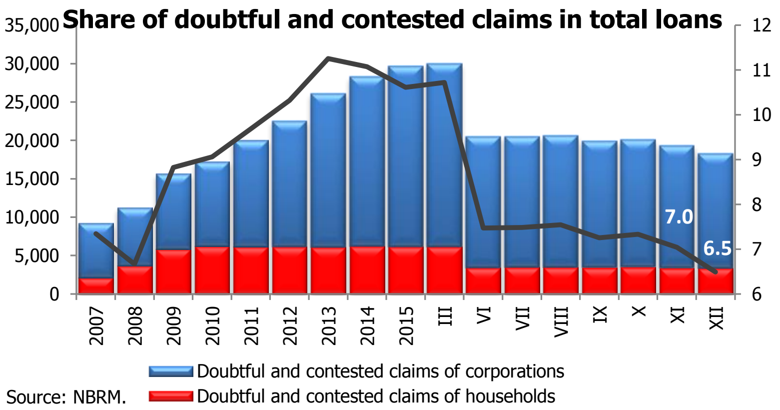
The annual growth rate of total loans at the end of December was 1.0%. If we exclude the regulatory effect, the annual rate is 6.5% and is above the forecasted annual growth of 5.6% for the fourth quarter of 2016.

Analyzing by currency, the annual rise in the total loans mostly arises from the



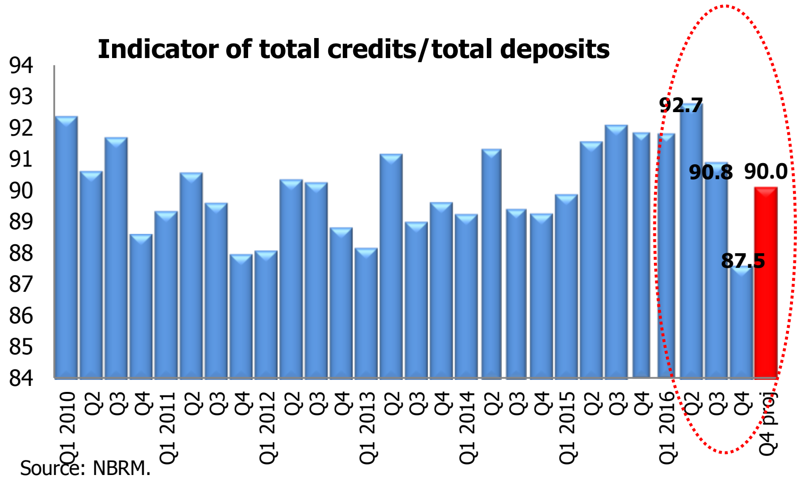
* does not include Denar credits with FX clause. Source:NBRM.

growth of denar loans[15] and denar loans with FX clause, while the contribution of foreign currency loans decreased.



Source: NBRM.

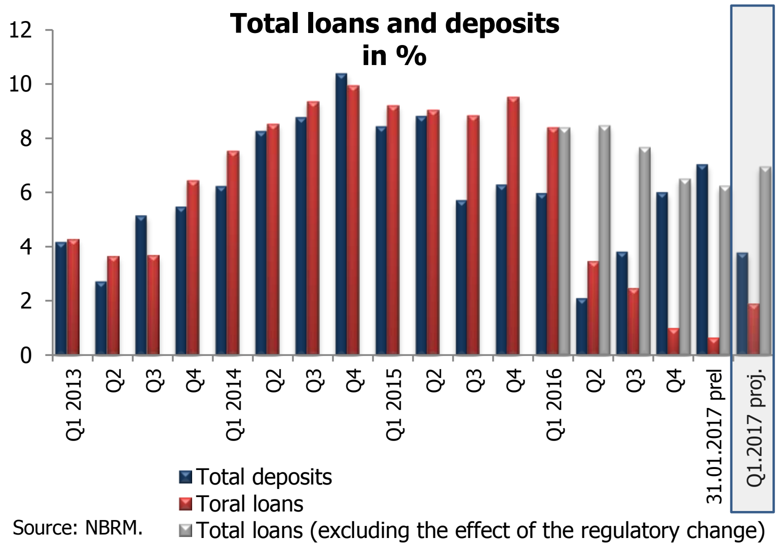
In December, the share of doubtful and contested claims in total loans decreased compared to the previous month, from 7% to 6.5%.



Source: NBRM.

Utilization of the deposit potential for lending to the private sector as measured by the loan-to-deposit ratio was 87.5% in December, which is lower compared to the expectations of the October forecast. Compared to the previous month, the indicator decreased by 1.2 percentage points. Excluding the effect of regulatory write-off, the share of loans to deposits is 92.3% (94.5% according to the October forecast).

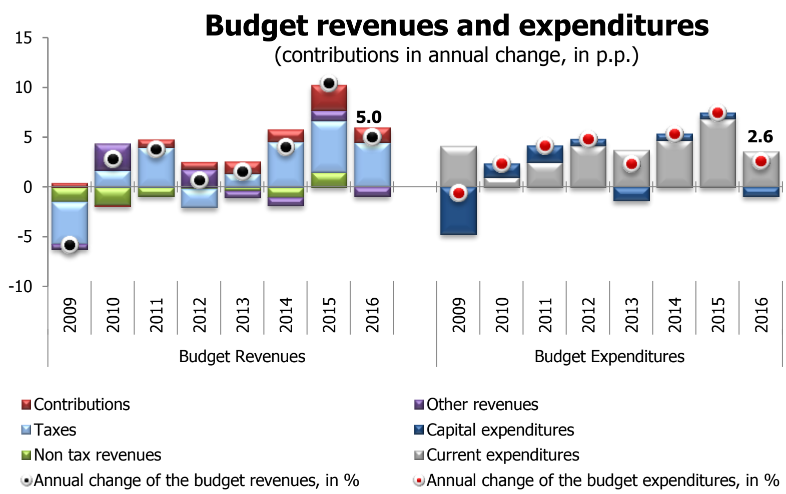
[15] Includes denar loans without FX clause, accrued interest and doubtful and contested claims.



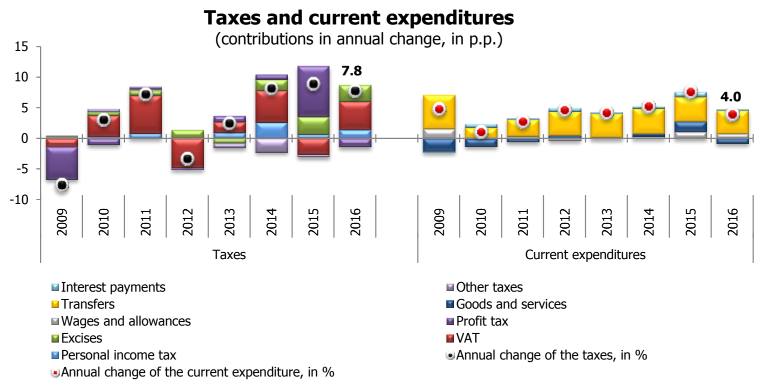
Source: NBRM.

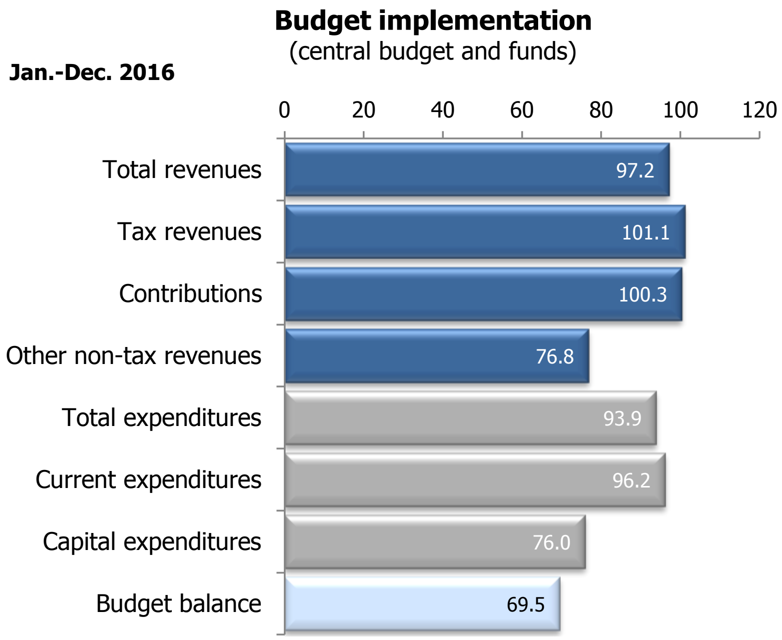
Preliminary ten-day data for January 2017 show a monthly decline in total deposits of 0.7%, compared to the monthly accelerated growth in the last quarter of 2016. This pace of total deposits is common for the beginning of the year when the deposit growth registered a slowdown or reduction. The fall in the total deposits in January entirely stems from the lower corporate deposits, while household deposits registered continuous moderate growth, from June 2016 onwards. Analyzed by currency, the reduction of total deposits is due to the decline in the savings in domestic currency, amid growth of foreign currency deposits. Analyzing the currency structure of household savings, in January, there was a reduction of local currency deposits, amid stronger growth of foreign currency deposits. These movements from currency aspect in household deposits are not uncommon for the first month of the year and are recorded in the previous two years. **On an annual basis, total deposits in January grew up by 7%, which is above the October forecast for the first quarter of 2017 (3.8%).**

In terms of lending activity, preliminary data as of January show a monthly drop of 1.6%, after the significant increase in the previous month (of 2.9%). The reduction of total loans, similar to the previous two years in the first month, entirely stems from the lower level of corporate loans, amid moderate growth of household lending. **In January, total loans increased by 0.7% annually, whereby the growth is lower than forecasted for the first quarter of 2017 (1.9%). Excluding the effect of regulatory changes, lending as of January was higher by 6.3% annually, close to the forecasted growth of 7% for the first quarter of 2017, according to the October forecast.**



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





Source: Ministry of Finance and NBRM's calculations.

Total revenues in the Budget of the Republic of Macedonia (central budget and budgets of funds) in 2016 increased by 5.0%, on an annual basis. Improved performances mostly stem from higher realization in taxes, and positive, but smaller contribution to the growth was made by contributions. On the other hand, the inflows in other revenues make moderate negative contribution to the annual growth.

The total tax revenues in the Budget of RM in 2016 increased by 7.8%, whereby analyzed by individual tax category, the largest contribution to the annual growth was made by inflows from VAT, and moderately lower, but positive contribution was also made by inflows from excise duties and inflows based on personal income tax. Inflows of income tax are lower on an annual basis.

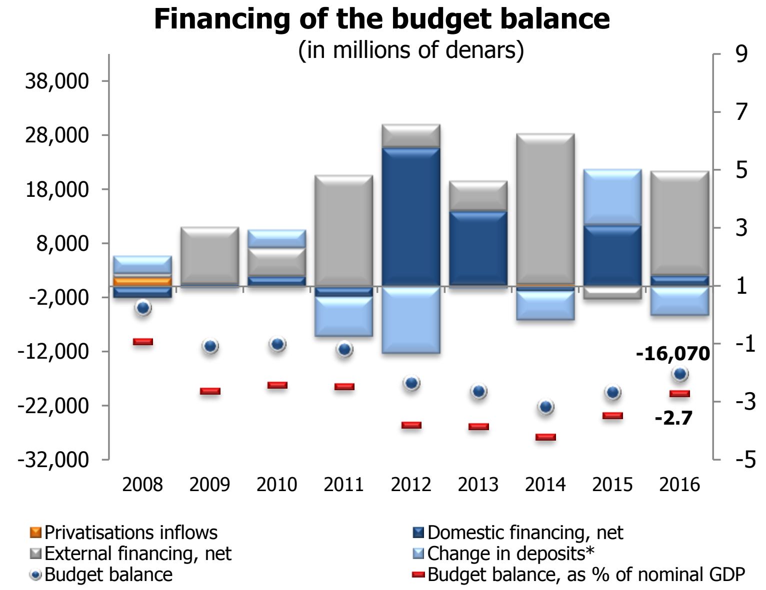
The performance of budget expenditures in 2016 increased by 2.6% on annual basis, which is entirely due to the contribution of the current costs, while capital expenditures make a negative contribution to the annual growth.

In 2016, the realized budget revenues constituted 97.2% of the revenues projected for 2016, respectively, under the Budget Revision[16]. Analyzed by category, total taxes registered performance of 101.1%, while the performance of contributions was 100.3%, compared to the Budget Revision. On the other hand, the performance of other non-tax revenues in the Budget[17] was 76,8%, compared to the Revision.

Analyzing budget expenditures, in 2016, 93.9% of the planned expenditures for 2016 were realized, which is mostly due to higher performance in the current costs (from 96.2% of the annual plan), while the realization of capital expenditure is lower (76.0% of the annual plan).

The budget deficit in 2016 accounts for 69.5% of that planned for 2016.

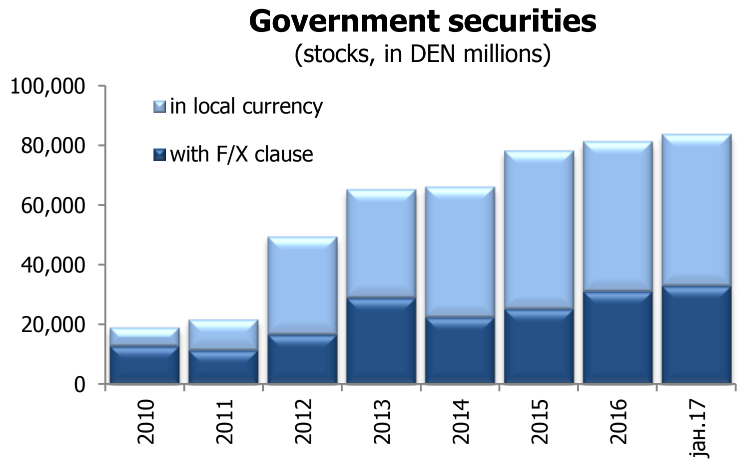
[16] The comparison is made with the Budget Revision for 2016 of August 2016.
[17] Other non-tax revenues include non-tax revenues, capital revenues, donations from abroad and revenues of recovered loans.



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

In 2016, the Budget of the Republic of Macedonia registered a deficit of Denar 16,070 million, which is 2.7% of the nominal GDP[18].

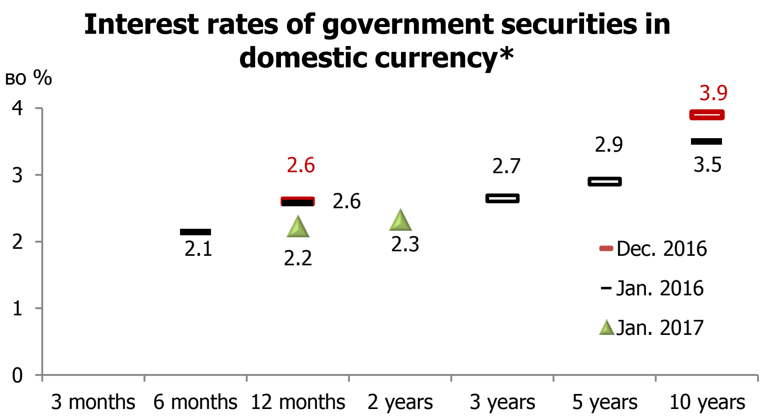
The budget deficit during this period was mainly financed through government borrowing on the foreign capital market and to a lesser extent through new net issuance of government securities on the domestic market. Some of the inflows were in the form of deposits on the government account with the NBRM.



Source: NBRM.

At the end of January 2017, the stock of government securities on the domestic market was Denar 83,815 million, which is higher by Denar 2,445 million, compared to the end of 2016.

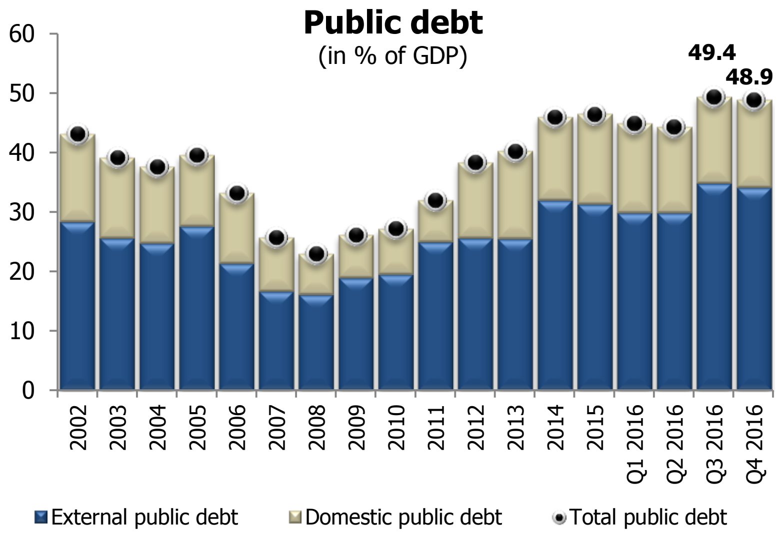
[18] The analysis of nominal GDP for 2016 uses the NBRM October projections.



* interest rates for 3y and 5y government bonds are from auctions held in September 2015 and November 2014, respectively.
Source: Ministry of Finance.

Interest rates on government securities in January[19] 2017 decreased compared with the previous month.

Compared to the same period last year, interest rates in January of the current year are also lower.



Source: NBRM's calculations based on data from the Ministry of Finance.

At the end of 2016, total public debt[20] equaled 48.9% of GDP[21], which is a quarterly decrease of 0.5 percentage points. The change largely stems from the reduction in external debt (of 0.7 p.p.), from 34.8% to 34.1% of GDP, while domestic debt increased slightly from 14.6% to 14.8% of GDP. The total government debt reduced from 40.9% to 40.0% of GDP, while the debt of public companies increased from 8.4% to 8.9% of GDP.

[19] At the auctions of government securities in January, there was an offer of 12-month treasury bills without FX clause, 2-year bonds without FX clause and with FX clause and 15-year government bonds with FX clause.
[20] The public debt is defined under the Law on Public Debt (Official Gazette of the Republic of Macedonia No. 165/14) according to which it is the sum of the government debt and the debt of public enterprises established by the state or municipalities, municipalities within the city of Skopje and the city of Skopje, and companies that are entirely or predominantly owned by the state or by the municipalities, the municipalities within the city of Skopje and the city of Skopje, for which the Government has issued a state guarantee.
[21] The analysis of nominal GDP for 2016 uses the NBRM October projections.

Annex 2

Timeline of the changes in the setup of the monetary instruments of the NBRM and selected supervisory decisions adopted in the period 2013 - 2016

January 2013

- A Decision amending the Decision on the reserve requirement (adopted in November 2012) came into force, allowing reduction of the reserve requirement base of banks for the amount of new loans to net exporters and domestic producers of electricity, as well as for the investments in debt securities in domestic currency without a currency clause, issued by the aforementioned companies. This decision fully exempts the banks from allocating reserve requirement for liabilities based on debt securities issued in local currency with an original maturity of at least two years. The Decision will apply throughout 2014, after which, depending on the results, the need for further application will be reconsidered.

- A Decision on reducing CB bill interest rate was adopted to cut the policy rate from 3.75% to 3.5%. At the same time, the interest rate on seven-day deposit facility and on overnight deposit facility was cut from 2% to 1.75% and from 1.0% to 0.75%, respectively.

March 2013

- A Decision on credit risk management was adopted, which applies from 1 December 2013.

July 2013

- A Decision on reducing CB bill interest rate was adopted to cut the policy rate from 3.5% to 3.25%. At the same time, the interest rate on seven-day deposit facility was cut from 1.75% to 1.5%.

- A Decision amending the Decision on reserve requirement was adopted, which reduces the reserve requirement rate for banks' liabilities in domestic currency from 10% to 8% and increases the reserve requirement rate for liabilities in foreign currency from 13% of 15%. In addition, the amendments stipulate a reserve requirement rate of 0% for banks' liabilities to nonresident financial companies with contractual maturity of over one year, as well as for all liabilities to nonresidents with contractual maturity of over two years. A rate of 13% still applies to short-term liabilities to nonresident financial companies in foreign currency with contractual maturity of up to one year. To maintain the reserve requirement in denars and in euros relatively stable, the amendments increase the reserve requirement in euros that is fulfilled in denars from 23% to 30%.

October 2013

- A Decision amending the Decision on banks' liquidity risk was adopted. This decision reduces the proportion of time deposits assumed to outflow from banks, from 80% to 60%, and applies from 1 December 2013. This amendment makes more room for long-term bank lending to the real sector.

November 2013

- A Decision amending the Decision on reserve requirement was adopted, which exempts the NBRM from paying reserve requirement remuneration (previously, this remuneration equaled 1% for denar reserve requirement and 0.1% for euro reserve requirement). The Decision is being applied since 1 January 2014.

- A Decision on CB bills was adopted, which introduces a methodology for determining the potential demand for CB bills. In accordance with the established mechanism, if there is a higher demand than the potential across the overall banking system, banks that bid higher amounts of their own liquidity potential will be required to place this difference in seven-day deposits.

February 2014

- A Decision on reducing interest rate on seven-day deposit facility from 1.5% to 1.25% was adopted.

April 2014

- A Decision amending the Decision on the methodology for determining the capital adequacy was adopted, introducing two amendments in the current decision that are expected to contribute positively to the credit support of the commercial banks to the corporate sector. Namely, with this Decision (and in accordance with the amendments to the new EU Regulation no. 575/2013 on prudential requirements for credit institutions and investment companies), performance guarantees or warranties that guarantee completion of works, stand out as items with low-intermediate risk, and therefore take lower conversion factor (20%), instead of 50% as it has been so far. That would mean that in the calculation of capital adequacy, smaller part of these off-balance sheet items would be treated as balance sheet items, which could affect the improvement of capital adequacy and encourage lending to the corporate sector. There is another innovation motivated by the international practice of establishing funds by low-risk entities (central governments or multilateral development banks) whose main goal is funding development projects. These projects are mostly funded through one or more commercial banks, which also contribute funds by dividing the exposure into a defined ratio between the bank and the fund or by providing guarantees or other similar instruments used by the fund (warranty provider) to guarantee coverage of part of the credit risk in the event of default by the debtor. In order to cover these cases, this decision also introduces a more favorable regulatory treatment of the funds established by one or several central governments, multilateral development banks or public institutions. These funds will take 0% risk weight, and the requirement will be that the funding is executed by payment in stakes, i.e. on-balance sheet and off-balance sheet activities to be covered by the fund's equity.

September 2014

- In order to further channel banks' excess liquidity to the non-financial sector, in September the NBRM revised the mechanism for transfer of the demand for CB bills, which is above the banks' potential into another instrument, i.e. seven-day standing deposit facility. According to these changes, for the seven-day standing deposit facility that banks are obliged to allocate if on the

CB bills auctions they demand an amount higher than the potential[22], an interest rate of 0% is determined. For the other assets that banks will voluntarily place into a seven-day standing deposit facility the regular interest rate will apply.

September 2014

- The National Bank of the Republic of Macedonia Council adopted the Decision amending the Decision on the reserve requirement, which extends the application of the non-standard measure for reduction of the base for the reserve requirement of commercial banks for the amount of new loans extended to net exporters and domestic producers of electricity. The main objective of the Decision is to provide further support to the two systemically important sectors of the economy. The current implementation of this measure has generated positive effects on the dynamics of lending and thus the overall economic growth, contributing to a reduction of the cost of funding of companies from both sectors, although with lower intensity than the potential. In such circumstances, and given the data that indicate some uncertainty about the pace of lending to the corporate sector in the next period, this Decision envisages continued application of this non-standard measure until 31 December 2015.

October 2014

- A Decision on reducing the interest rate on overnight deposit facility from 0.75% to 0.5% and on seven-day deposit facility from 1.25% to 1% was adopted.

March 2015

- A Decision on reducing the interest rate on overnight deposit facility from 0.5% to 0.25% and on seven-day deposit facility from 1% to 0.5% was adopted.

- The National Bank Council adopted the Decision amending the Decision on CB bills, which introduces a new manner of establishing the bids of banks at the auctions of CB bills. According to the Decision, the amount of supply of individual bank is calculated by applying its appropriate percentage share in the total supply of treasury bills, reduced by the amount of past due CB bills of the Macedonian Bank for Development Promotion AD Skopje. In order to ensure operational efficiency in conducting auctions of this type and greater transparency toward banks, before the auction the NBRM shall inform the banks on the maximum offer that can be submitted by each bank. This opportunity for setting the supply of banks is expected to stabilize the demand at the level of the amount offered, which eliminates the need for calculation of potential demand and subsequently it repeals the obligation for mandatory seven-day deposits for banks when demand at the auction exceeds the potential demand.

April 2015

- A new Decision on the credit of last resort which, besides the current possibility of approving credit of last resort to banks against a collateral of debt securities, foreign currencies and banks' claims on the National Bank, introduces the possibility of extending this credit also against pledging banks' claims on customers. This modality of the credit of last resort is planned to be

[22] For the method of determining the potential demand for CB bills see the Decision on CB bills, Official Gazette of the Republic of Macedonia No. 166/13).

activated if the bank does not have debt securities and foreign currencies. The Decision specifies the types of claims that are acceptable for the National Bank as collateral for the credit of last resort.

June 2015

- The National Bank Council adopted preventive measures for managing capital flows of the Republic of Macedonia to the Republic of Greece. Preventive measures pertain to restriction of capital outflows from residents of the Republic of Macedonia (natural persons and legal entities) to Greek entities based on newly concluded capital transactions, but not to a restriction of the outflows based on incoming payments for capital transactions already concluded. These measures limit capital outflows only to the Republic of Greece and to entities from the Republic of Greece (such as outflows for founding of a company, investing in securities, investing in documents for units in investment funds, investing in investment gold, financial credits, long-term loans, etc.) but not to block or in any way to impede current and future commercial operations with entities from the Republic of Greece. Current transactions remain free. Also, in order to maintain the security of foreign investors regarding the exercising of their rights to their property in the Republic of Macedonia, outflows based on realized dividends have not been restricted either. Furthermore, in order to secure the funds that domestic banks have in the banks in the Republic of Greece, Macedonian banks are required to withdraw all loans and deposits from banks based in the Republic of Greece and their branches and subsidiaries in the Republic of Greece or abroad, regardless of the agreed maturity. However, in order to allow smooth functioning of payment operations for the transactions that are not prohibited, an exception to this requirement has been made for the funds on the current (correspondent) accounts with those banks. Existing prudential and supervisory measures and limits for banks to investments in securities including Greek securities are supplemented by explicit ban on all residents to invest in Greek securities. Those are temporary protective measures, introduced to prevent the threat of any significant outflows of capital from the Republic of Macedonia to the Republic of Greece to cause significant disturbance to the equilibrium in the balance of payments and undermine the stability of the financial system.

August 2015

- The National Bank Council adopted the Decision on amending the Decision on reserve requirements that reduces the reserve requirement rate for the bank liabilities to natural persons in domestic currency with contractual maturity of over one year from 8% to 0%, with these liabilities obtaining the same treatment as the liabilities with maturity over two years, for which rate of 0% since 2012 has been applied. Having in mind that the amendment releases the banks from the reserve requirement for the natural persons' denar deposits with maturity exceeding one year, this measure is expected to have adequate influence toward larger supply of denar savings products with stimulative interest rates.

- The National Bank Council adopted the Decision on amending the Decision on CB bills that envisages adjustment of the mechanism of participation at the CB bills auction of the National Bank, where the main criterion will be the individual share of the banks in the total liabilities in domestic currency without currency clause of the banking system. With these amendments, the National Bank continues to support the natural persons' savings in domestic currency and on a longer run, which creates room for the banks for active credit support to the private sector.

December 2015

- The Council adopted the Decision amending the Decision on the methodology for determining the capital adequacy, introducing measures to slow the growth of long-term consumer loans. The measure increases capital requirements for banks on long-term consumer loans with maturity equal to or longer than eight years. Thus, the risk weight for claims on consumer loans with a contractual maturity equal to or longer than eight years, increases from 75% i.e. 100% to 150%. To avoid major shocks in the market of consumer lending, yet the growth rates to be reduced to a moderate level, this measure is aimed only at newly approved long-term consumer loans, i.e. loans with maturity equal or longer than 8 years approved after 1 January 2016. At the same time, this decision introduces higher capital requirement (risk weight of 75%) for the increase of overdrafts and credit cards in relation to 31 December 2015. The aim of this decision is to prevent the possibility of changeover to this type of borrowing as a result of the measure to decelerate consumer loans. Also, this Decision facilitates the access of legal entities. Namely, the capital requirement for guarantees issued by banks is reduced, which guarantees payment based on a certain business relationship of the client and banks' claims backed by commercial property that meets certain conditions. This way allows banks to allocate lower amount of capital for credit and guarantee operations with legal entities, including small and medium enterprises, which can cause reduction in the cost of banks and therewith, of clients for this type of operation.

- The National Bank Council adopted the Decision on amending the Decision on credit risk management, which requires starting from 1 January 2016, and by June 30 2016 to write-off all claims that have been fully booked for more than two years, and where the bank has identified and fully covered the credit risk of default at least two years before. According to the existing regulations, banks are required to fully reserve claims where the client defaulted at least 1 up to 5 years if there is a specific collateral, and the new measure requires from banks to write them off two years after their full provisioning. In addition, banks will still be allowed and required to take actions to collect these claims, although they are written off. The measure does not incur additional costs for banks since claims which are fully provisioned are written off, at least two years before.

- The National Bank Council decided to extend the application of the non-standard measure to reduce reserve requirement base in denars of commercial banks for the amount of newly approved loans to net exporters and domestic producers of electricity for two more years, untill the end of 2017.

- On 29 December 2015, the Decision on introducing special protective measures adopted by the National Bank Council on 28 June 2015 due to the debt crisis in Greece at that time, ceased being valid. The measures were adopted to protect against any disruptions in the balance of payments or the stability of the financial system of the Republic of Macedonia due to any significant capital outflows from Macedonia to Greece. They were temporary for a period of up to six months, with a possible extension of their application. The protective measures served their purpose and prevented major capital outflows from the Republic of Macedonia, yet not disturbing the business of domestic companies with Greek companies. They delivered equilibrium in the balance of payments and stability of the domestic banking system. The situation in Greece has been stabilizing for quite some time. The lenders continued to financially support Greece, which, in turn, pledged to apply economic and social reforms, and austerity measures. Therefore, after the expiry of six-month validity period of the protective measures on 28 December 2015, since 29 December 2015, this decision is no longer in use.

May 2016

- At the regular meeting of the NBRM's Operational Monetary Policy Committee held on 3 May 2016, it was decided the interest rate on CB bills to be increased by 0.75 percentage points, from 3.25% to 4%. The decision to tighten the monetary policy is a reaction to the increased demand for foreign currency and pressures on banks' deposit base, which were entirely due to the deteriorating expectations of economic agents, caused by the unstable political situation in the country. Thus, the change in the interest rate is a response to the action of factors of non-economic nature.

- The National Bank Council adopted the Decision on reserve requirement, which increased the reserve requirement rate for banks' liabilities in domestic currency with FX clause. The measure has been aimed at further encouraging the process of denarization of deposits in the domestic banking system. Given the negligible market share of these liabilities in the banks' balance sheets, the changes are exclusively for further maintenance of low propensity of the economic agents for placing this type of deposits in domestic commercial banks.

- In order to maintain and increase deposits in the domestic banking system, the National Bank Council reviewed and improved the terms for placing foreign currency deposits of domestic banks at the National Bank and adopted the Decision on foreign currency deposit with the National Bank of the Republic of Macedonia. Accordingly, starting from 13 May 2016, the banks can place foreign currency deposits at the central bank at higher interest rates compared to current negative interest rates prevailing in the international financial markets. It is expected that this measure will contribute to reduce the cost of domestic banks, which would accordingly contribute to higher interest rates on the deposits of their clients, domestic legal and natural persons.

October 2016

- In the regular meeting held on 25 October 2016, the NBRM's Operational Monetary Policy Committee decided not to offer additional foreign currency deposits that banks would place in the NBRM.

December 2016

- At the regular meeting of the NBRM's Operational Monetary Policy Committee, held on 13 December 2016, the Committee decided to cut CB bill interest rate by 0.25 percentage points, to 3.75%, and to increase the supply of CB bills at the 14 December auction from Denar 22,000 million to Denar 23,000 million.

- The National Bank Council adopted the Decision on amending the Decision on the methodology for determining the capital adequacy. This Decision is part of the compliance process of the domestic regulations with the reforms of the international capital standard Bazel 3, as well as with the provisions of the European Regulation 575/2013 on prudential requirements for credit institutions and investment firms, in the part of the structure of the banks' own funds. The most significant amendments relate to the strengthening of the quality of own funds, both in terms of their structure and in terms of the criteria that should be met by certain positions in order to be a part of the banks' own funds. In this context, the own funds continue to be divided into core and additional capital, **but the new Decision changes the structure of the core capital, which is divided into regular core capital and additional core capital.** The regular core capital includes capital positions with the highest quality (equity capital and reserves) which are fully and readily available to cover risks and losses during the bank's operation. The new own funds component, the additional core capital, includes instruments which, among other things, contain a clause for their transformation into instruments of the regular core capital or for their write-off on temporary or permanent basis (reduction of the value of their principal), if the so-called critical event occurs. **The amendments to the Decision on the capital adequacy replace current restrictions in terms of size and ratio of individual elements of the own funds with the statutory prescribed minimal rates for the regular core capital, core capital and own funds,** i.e. 4.5% for the regular core capital, 6% for the core capital and 8% for the own funds of the risk-weighted assets. Thus, the greatest importance is given to the regular core capital positions (shares, reserves, retained undistributed profit), as capital positions with the highest quality.

January 2017

- At the regular meeting of the NBRM's Operational Monetary Policy Committee, held on 10 January 2017, the Committee decided to cut CB bill interest rate by 0.25 percentage points, to 3.5%, and to increase the supply of CB bills from Denar 23,000 million to Denar 25,000 million.