



MINISTRY OF FINANCE  
REPUBLIC OF MACEDONIA

# QUARTERLY ECONOMIC REPORT

Q - 1 - 2009

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# ● QUARTERLY ECONOMIC REPORT

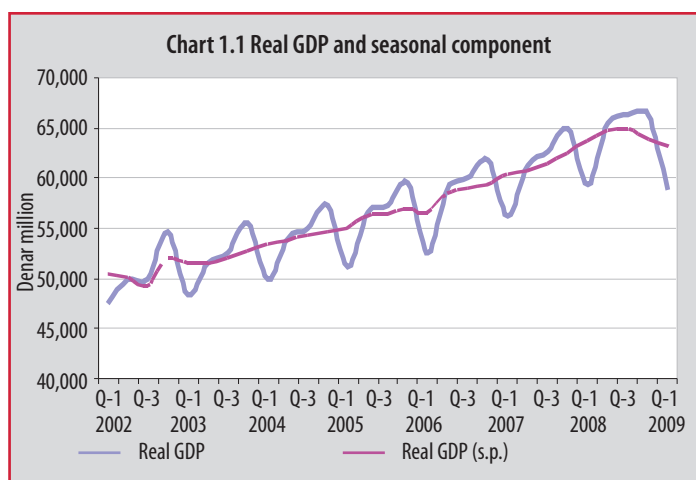
## Q-1-2009

### SUMMARY

- **Real GDP growth** in Q1 2009 was -0,9%, being the first negative growth rate on quarterly basis after 2002. Industrial production declined significantly by 10,8%.
- **Employment growth** accounted for 2.9% compared to Q1 2008, while unemployment rate (32.7%) dropped by 2.1 p.p. in relation to Q1 2008.
- **Inflation rate** was 1% (Q/Q-4), compared to 5.5% in the previous quarter.
- **Net salary** increased by 27,4% in nominal terms, mainly due to the methodological changes, and by 26.1% in real terms.
- **Budget deficit** at the end of Q1 was 0.5% of the projected GDP in 2009. Fiscal burden in Q1, measured as participation of the budget revenues in relation to nominal GDP, was 30.7%, dropping by 2.4 p.p. in relation to Q1 2008. Total public debt accounted for 26.9% of GDP at the end of Q1, which was by 1.8 p.p. lower compared to December 2008.
- **Credits to the private sector** significantly slowed down by 25.3% in relation to Q1 2008, whereby compared to Q4 2008, credit growth dropped by even 9.1 p.p. Growth of credits to the private sector, compared to nominal GDP realized in Q1 2009, was 25.2%, showing strong slowdown by 9.4 p.p. in relation to the previous quarter.
- At the end of Q1 2009, **Macedonian stock exchange index MSEI-10**, as aggregate indicator of stock exchange trends, dropped by 9.1% in relation to Q4 2008, while the drop in relation to Q1 2008 was even more significant, amounting to high 71.6%.
- **Export of goods** declined by 34.5%, while import of goods dropped by 16.7%.
- **Trade balance** reached 30.3% of quarterly GDP, still being strong deterioration at quarterly level, while BOP account deficit experienced insignificant decline and reached 23.3% of quarterly GDP, thus being the main source of risk to the external position of the country.
- **Real Denar effective exchange rate**, calculated on the basis of CPI index, continued the upward trend in Q1 2009, experiencing 1.6% appreciation compared to Q1 2008.

### 1. MACROECONOMIC TRENDS AND REAL SECTOR

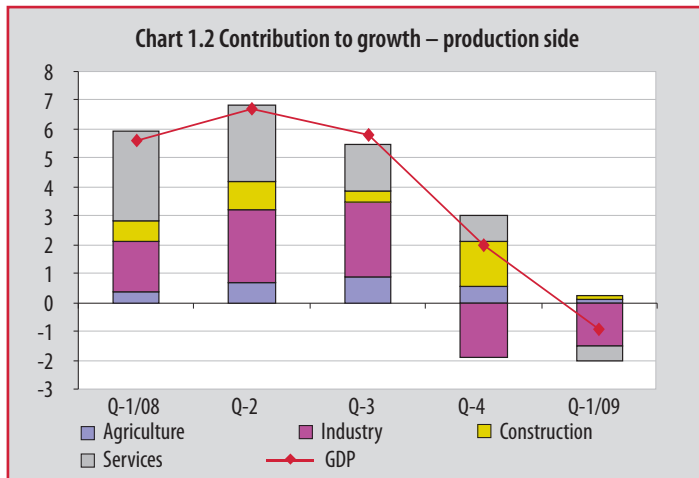
In Q1 2009, GDP in current prices was Denar 89,919 million. In terms of per capita<sup>1</sup>, it was Denar 43,871 and, compared to the same quarter in 2008, there was a nominal increase by around Denar 930. In Q1 2009, as a result of the effects of the international economic crisis on the Macedonian economy, **real GDP growth** was negative, amounting to -0.9% with regard to the same quarter in 2008, and it was the first negative growth rate at quarterly level after 2002 (Chart 1.1).



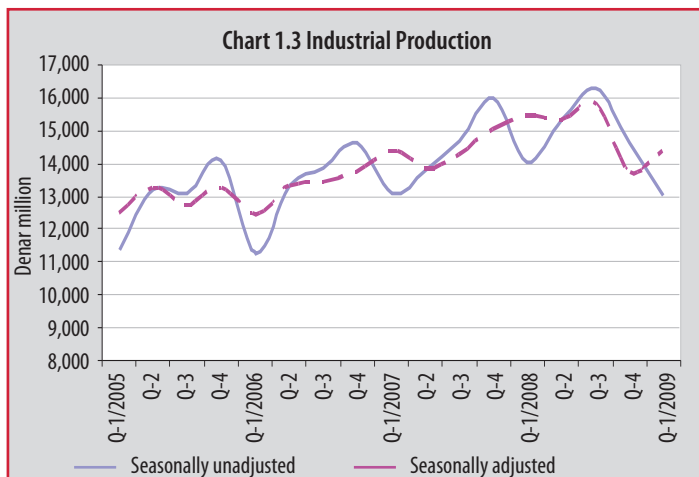
1. Evaluation of the population on 31 December 2008 according to SSO

Adjusted to the seasonal effects, in Q1 2009, GDP experienced decline by 0.9% in real terms compared to Q1 2008 and decline by 1.2% in relation to Q4 2008.

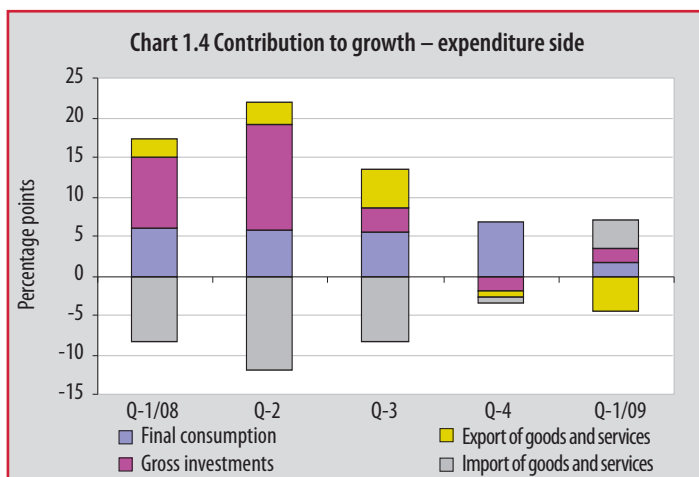
Growth in Q1 was significantly lower in the following sectors: industry (-7%), financial intermediation (-5.2%), transport and communications (-4.7%) and hotels and restaurants (-2%). On the other hand, trade, construction and agriculture were sectors realizing positive growth, at the same time preventing the GDP from deeper decline. As a whole, slowedown growth at service in Q4 2008 shifted to negative growth in Q1 2009 by 1% (Chart 1.2).



**Industrial production** dropped on annual basis by 10.8% in Q1 2009, adding to the decline registered in Q4 2008 (-7.6%). All industrial sector registered activity slowdown, however, analysed by branches having the largest share in the index, drop of industrial production in Q1 was mainly due to the realized negative growth rates at the production of base metals (-61.6%), production of clothing (-23.7%) and production of products from other non-metal minerals (-17%). In general, industry in Q1 2009 negatively contributed to the growth by 1.5 p.p., being the main reason for the GDP decline.



Observing **GDP from the expenditure side**, in Q1 2009, final consumption grew in nominal terms by 3.9%, gross investments surged by 15%, while import and export dropped by 28.5% and by 12.3% respectively. Nominal share of final consumption in growth was 1.7 p.p., being by 5.1 p.p. less compared to the previous quarter; share of gross investments was 1.8 p.p., which was better performance in relation to Q4 2008, when it was negative, while share of trade balance was negative, -2.8 p.p, and it deteriorated in relation to Q4 2008, when it was -1.6 p.p.

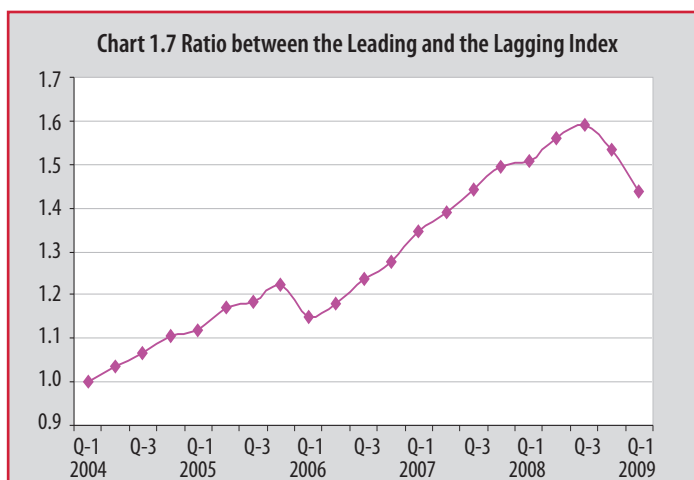
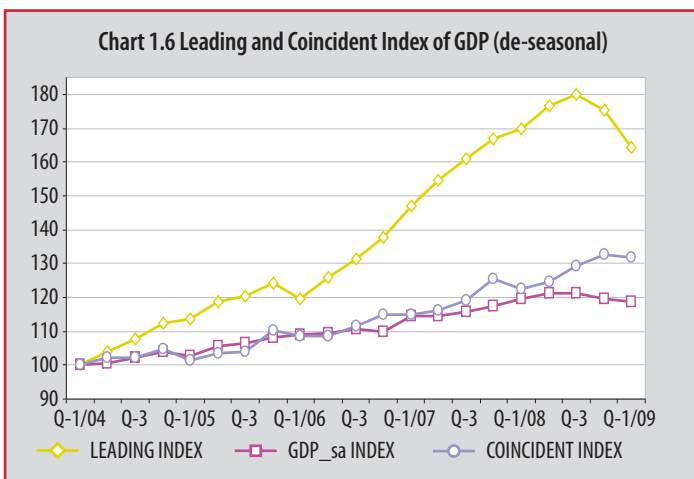
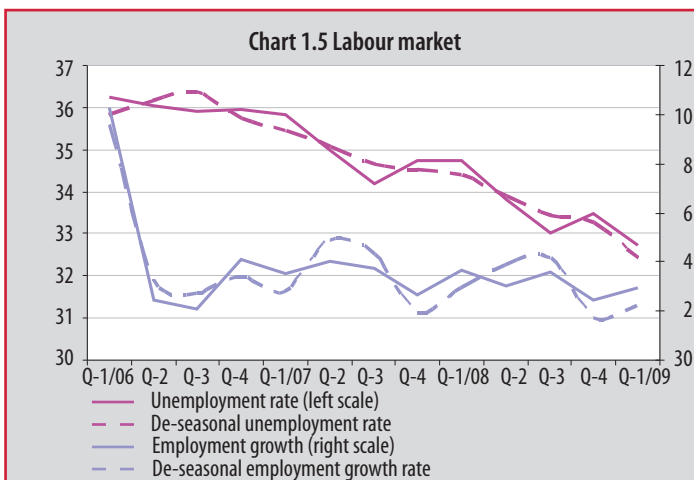


In Q1 2009, **employment growth** accounted for 2.9% compared to the same quarter in 2008, and employment rate increased to 37.8% (by 1.1 p.p.). Number of unemployed persons declined by high 6% and most of them (around 90%) were absorbed by the employment growth, while the remaining moved to inactive population, causing for labour force to decline by 0.2%. Such developments led to decline of the **unemployment rate** by 2.1 p.p. (to 32.7%), while the active population dropped by 56.2% of the working-able population (by 0.1 p.p). In fact, working positions on net basis were created by the private sector, where the number of employee increased by 7.6%, while in the other parts of the

economy, employment declined by 8.2%. If seasonal effects are excluded, unemployment rate registered no significant changes. De-seasoned unemployment rate was 32.4% in Q1 2009, pointing out that unemployment in Macedonia is more of a structural rather than fractional character.

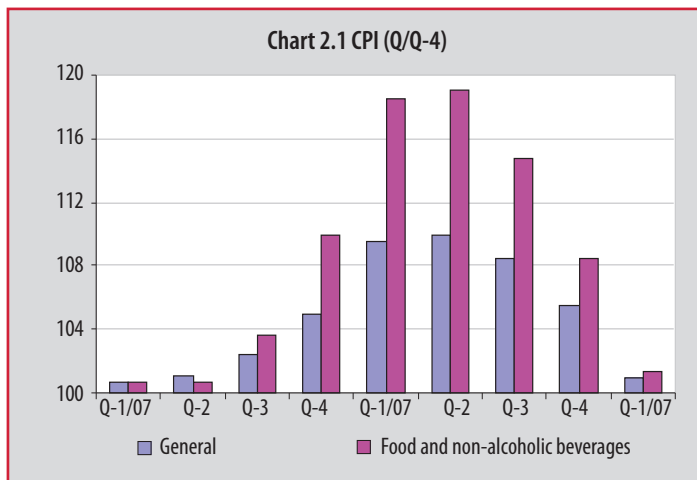
**Leading composite index, MakLead,** declined by 10.8 index points in Q1 2009 on quarterly basis, following the decline by 4.9 index points in the previous quarter. Compared to the same quarter last year, **leading composite index** was lower by 5.4 index points. Such trends registered at MakLead index suggested that economic activity would still register negative growth rates, i.e. possible positive trends could be expected at the end of the current year. In Q1 2009, leading diffusion index registered positive trends at 31.3% of the components of the composite index, being the same performance as in the previous quarter, however, twice lower compared to the same quarter in 2008.

**Ratio between leading and lagging index** in Q1 2009 dropped to 1.44, i.e. it returned to the level in Q3 2007, when this ratio was stagnant. The ratio showed that leading index was by 44% higher than the lagging index. Ratio between the leading and the lagging index was constantly increasing throughout the whole observation period. More intensive increase at this indicator was evident starting 2006, which can be taken as turning point in the economy. Q4 2008 could be taken as another turning point, when the ratio started declining, the intensity of which increased in Q1 2009.

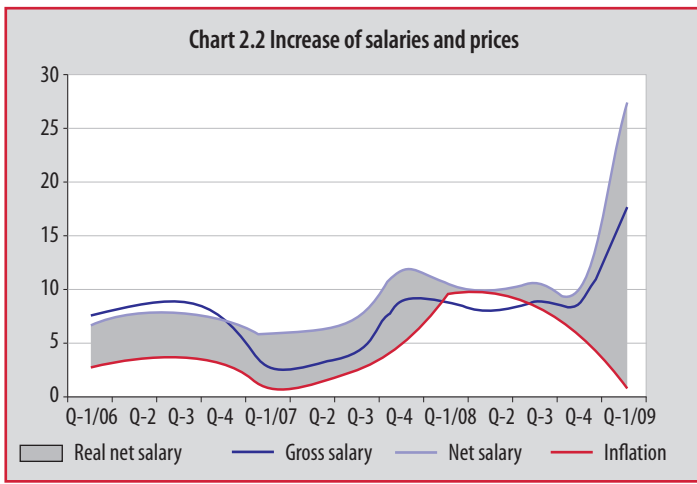


## 2. PRICES, COSTS AND PRODUCTIVITY

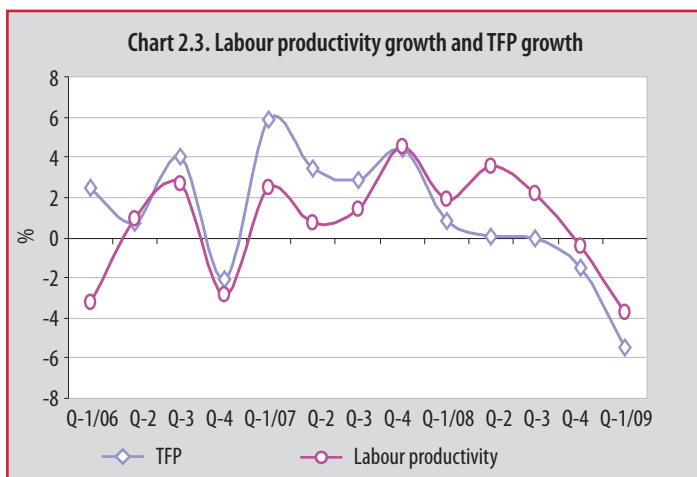
In Q4 2008, **inflation rate**, measured according to CPI, was 1% (Q/Q-4) compared to 5.5% in the previous quarter. Highest price increase by 7.4% was registered in the Housing category, mostly due to the increase of electricity price by 13.1%. Significant downward trend was registered at the growth rate of food costs (1.2% in Q1 2008), accounting for 42.4% in the total increase of consumer prices. Relatively high increase of prices on annual basis was registered at the Hotels and Restaurants category by 5.1% and the Tobacco and Beverages category by 4.5%. High price decline by 9.2% was recorded in the transport sector, as a result of the high drop of oil price on the global stock markets (by approximately 20% compared to the previous quarter). Price decline (by 9.1%) was also recorded at the administrative services, while costs in the Culture and Entertainment category were lower by 1.7%, due to the lower education prices. Mild increase of prices was registered at the Hygiene and Health category (2.1%) and Clothing and Footwear category (1.6%).



and Entertainment category were lower by 1.7%, due to the lower education prices. Mild increase of prices was registered at the Hygiene and Health category (2.1%) and Clothing and Footwear category (1.6%). **Core inflation** (which includes the effect of food and energy) also experienced downward trend in Q1 2009, amounting to 1.5%, compared to 2.3% in the previous quarter. In fact, core inflation is expected to continue the downward trend, and there is risk for oil price increase at the global stock markets in the second half of the current year to instigate certain increase of general price level.



In Q1 2009, **retail prices** remained unchanged compared to the same quarter previous year. Highest price increase was registered at the Beverages category (8.8%), while prices dropped the most at the agricultural products (4.9%) and industrial-non-alimentary products (3%). Value of the consumer basket of food and beverages for a four-member household, calculated on the basis of retail prices, increased by 5.5% compared to the previous quarter, accounting for 65.1% of the average net salary in Q1 2009.



Average **net salary** in Q1 2009, compared to same quarter previous year, was higher by 27.4%. Such increase was largely due to the methodological changes, i.e. starting January 2009, net salary includes food and travel allowances. Average **gross salary** experienced slower growth compared to the net salary, by 17.5%, as a result of the reduced rates of social contributions and the two-fold increase of personal tax exemption. Low level of inflation caused for real growth of net and gross salary not to differentiate a lot from the nominal growth, amounting to 26.1% and 16.3% respectively (see shaded field in Chart 2.2).

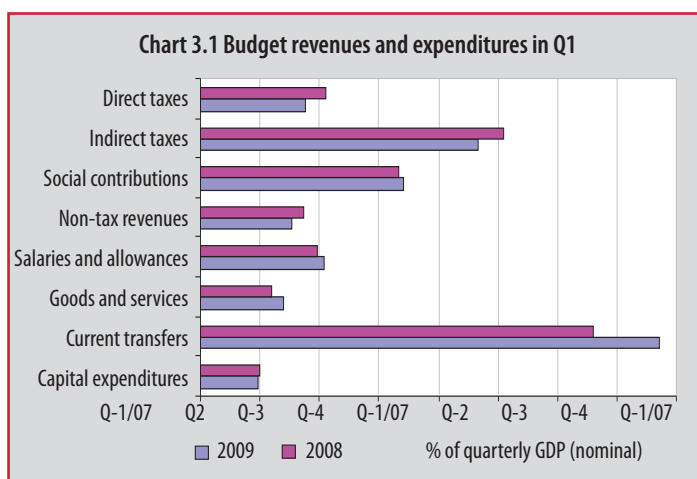
Drop in the economic activity, accompanied

by employment growth, led to decline of **productivity** by 3.7% in Q1 2009. Highest decline of productivity was registered in the civil engineering sector (by 18.6%) as a result of the high employment growth (by 25%) in conditions of relatively low construction growth (1.7%). Services sector experienced productivity decline by 5.6%, taking into account that employment growth (by 5.4%) was not followed by production growth. Unlike services, there were opposite trends in the agriculture, where productivity grew by 2.2%. Industry registered decline in both the production and the employment, whereby the higher drop in the production caused for productivity decline by 3.8%. **Total factor productivity** (TFP) registered higher decline than labour productivity, i.e. -5.5% in Q1 2009 (see Chart 2.3). TFP decline was due to the increase in investments, in particular physical capital, the real growth rate of which was around 7%.

### 3. FISCAL SECTOR

Decline in the economic activity in the Republic of Macedonia was reflected in the fiscal sphere. Lower performance of budget revenues (91% performance) in Q1 2009, accompanied by relatively higher budget expenditure, led to **central government budget deficit**<sup>2</sup> in the amount of Denar 1.9 billion or 0.5% of the projected GDP. Still, expansive fiscal policy did not jeopardize the fiscal sustainability of the country, as well as the monetary stability, taking into account that the issue of treasury bills was sterilized with the purchase of central bank bill by NBRM.

Total **budget revenues** were higher by 5.6% compared to the same quarter 2008. Slowdown in the personal consumption and import decline, followed by tax reforms undertaken to mitigate the consequences from the economic crisis, resulted in lower collection at all types of tax revenues. **VAT revenues**, accounting for 47.2% of the total tax revenues, were lower by 7.7% in Q1 2009 compared to the same quarter 2008. Regarding the structure of gross VAT revenues, there was slight increase in the turnover in the country in line with the increased trade sales, while realized VAT revenues on the basis of import dropped by 18.6%. Performance of projected revenues



on the basis of VAT in Q1 2009 accounted for 88.6%. Excise revenues were lower by 5.1% on annual basis, while import decline caused for lower collection of customs duties (by 1.2%). With respect to direct taxes, significant decline of around 30% was expectedly registered at the profit tax, taking into account that starting January 2009, only profit distributed for dividend was taxed. Personal income tax revenues were lower by 2.2%, due to the high decline of revenues on the basis of capital gain and the tax collected on this basis (-65%). Collection of social contributions was higher by 4.2%, and collection of all types of social contributions increased. In Q1 2009, non-tax revenues, accounting for 13.3% of the total budget revenues, were lower by 8.6% on annual basis.

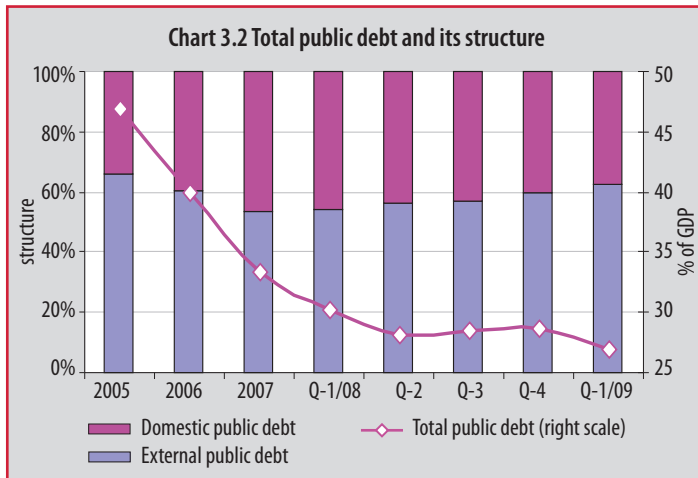
Total **budget expenditures** in Q1 2009 were higher by 15.1% compared to the same quarter previous year. **Current expenditures**, accounting for 92.2% of the total expenditures, increased by 16.6%. Unlike them, **capital expenditures** were lower by 0.3% on annual basis, although in 2009 it is planned for these expenditures to be higher by 46% compared to the one realized the previous year, i.e. around 7% of the projected GDP in 2009. Execution of capital expenditures, as of March inclusive, accounted for 9% of the projected ones for this year. Regarding capital expenditures, transfers were higher by 19.1% on annual basis, whereby the category Other Transfers (66% growth), including the transfers to the local government, contributed the most to this increase. Expenditures for goods and services increased by 18.7%, while

2. It covers central government budget and budgets of the Funds



expenditures related to salaries and allowances were higher by 6.7%. Interest-related expenditures surged by 19.8%, whereby foreign debt interest-related expenditures increased by 30.5%.

In the coming period, budget revenues are expected to be realized with slower dynamics than in the previous period, as a result of the decline of the economic activity and the measures to overcome such trends. In fact, decline in the import, profit and productivity will reflect on tax revenues as well. On the other hand, public investments are expected to intensify in the coming period so as to instigate the economic growth. Hence, projected deficit of 2.8% of GDP in 2009 seems feasible.



**Fiscal burden**, measured as participation of the budget revenues<sup>3</sup> in relation to nominal GDP, was 30.7% in Q1 2009, dropping by 2.4 p.p. in relation to Q1 2008. Total budget expenditures accounted for 37% of GDP, which was by 4.2 p.p. lower compared to Q1 2008.

**Total public debt<sup>4</sup>** amounted to 26.9% of GDP in Q1 2009, being a drop by 1.8 p.p. in relation to December 2008. Such decline was due to the high decline of the domestic public debt (by 12%), while external public debt was higher by only 0.6% in relation to December 2008. Thus, share of domestic public debt dropped by 37.2% (Chart

3.2). Such trends point out that additional borrowing, which is inevitable for conducting more expansive fiscal policy in conditions of slowed down economic growth, whether externally or internally, would not jeopardize the fiscal sustainability, whereby coordination with the monetary policy is indispensable. Sound fiscal policy is one of the Maastricht Criteria, having the limits set at budget deficit of 3% of GDP and central government debt of 60% of GDP.

**General government debt**, which does not include the debt of NBRM and the public enterprises, increased to 22.3% at the end of Q1 2009, i.e. it increased by 1 p.p. in relation to December 2008. Such phenomenon was a result of the increase of central government debt (by 17.7%) through the issue of continuous government securities. On the other hand, NBRM debt experienced decline, leading to increase of the share of general government debt in the total public debt by 8.5 p.p. (to 82.7%).

#### 4. MONETARY-FINANCIAL TRENDS<sup>5</sup>

At the end of Q1 2009, **primary money** dropped by 10.2% in relation to the previous quarter, experiencing an increase by 6.4% on annual level. In Q1 2009, **M1 monetary aggregate** decreased by 13.5% compared to Q4 2008, while on annual basis, the increase was 5.2%, mainly as a result of the increase of deposit money by 11.8%. In Q1, broader monetary aggregates **M2 and M4** dropped in relation to the previous quarter (-2.2% and -2.4% respectively), due to the decline of long-term deposits by 7.3% in the same quarter, while growth of M2 registered further slowdown on annual basis (4% in Q1 2009 and 7.1% in Q4 2008).

**Credits to the private sector** in Q1 2009 experienced significantly lower growth by 25.3% in relation to Q1 2008, whereby in relation to Q4, the credit growth dropped by even 9.1 p.p. as a result of the restrictive

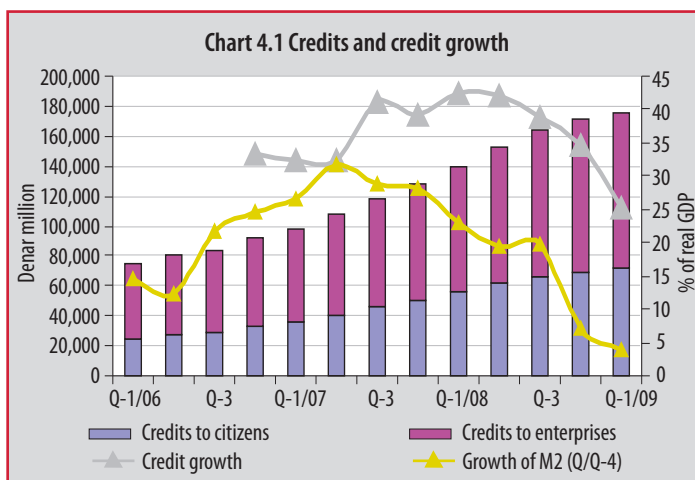
3. Includes tax revenues, social contributions and part of non-tax revenues

4. According to GFS Methodology

5. Starting Q1 2009, analyses are made on the basis of the data harmonized with the new accounting plan for the banks, in force from January 2009



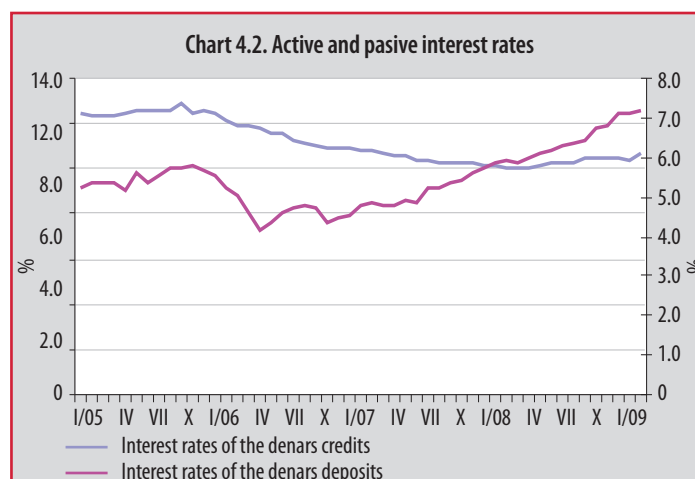
measures of the monetary policy undertaken. Strong growth slowdown was registered at credits to enterprises by 9.3 p.p. (from 33% in Q4 2008 to 23.6% in Q1 2009), leading to the conclusion that banks continued to consistently apply the policy enforced by NBRM, which in the second half of the previous year was aimed at preventing the spillover of the global financial crisis to the Macedonian banking system, safeguard of bank liquidity and the monetary stability in the country. Trend regarding credits to households was similar to the trend in corporate crediting, the growth of which continued to significantly slow down by 9.6 p.p. (27.6% in Q1 2009 in relation to 37.2% in Q4 2008). Growth of credits to the private sector, compared to nominal GDP realized in Q1 2009, was 25.2%, showing strong slowdown of 9.4 p.p. in relation to the previous quarter (Chart 4.1).



Total **deposit potential**<sup>6</sup> of the private sector registered an upward trend, while the growth dynamics continued to slow down (7.7% in Q1 2009 compared to 12.4% in the previous quarter). In Q1 2009, deposits of households increased by 12.6% in relation to Q1 2008, being a decline by 2 p.p. in relation to Q4 2008. Deposits of enterprises experienced strong decline by 11.9% in relation to Q1 2008 compared to 7.5% growth realized in Q4 2008.

**Interest on central bank bills** in Q1 2009 was kept on the same level as in Q4 2008, i.e. at 7%. For comparison purposes, in the first quarter 2009, European Central Bank revised downward the reference interest rate, which amounted to 1.5% at the end of the quarter, being a cumulative decline by 2.5 p.p. compared to Q1 2008. Specific features of the Macedonian economy make NBRM conduct the monetary policy in a direction opposite to the one of the leading central banks, such as ECB, FED and the Bank of England, which drastically reduced the interest rates as resction to the global financial crisis. In fact, global economic crisis, which affected the Macedonian economy in the last quarter in 2008 as well, imposed the risk of deepening the external imbalance and led to serious pressure on the exchange rate stability, thus making the room for loosening the monetary policy exceptionally limited.

**Average weighted interest rate** on Denar credits amounted to 9.9% at the end of Q1 2009, registering an increase of 0.2 p.p. annually, and an increase of 0.1 p.p compared to the previous quarter. Interest rates on deposits continuously grew, thus at the end of Q1 2009, interest on credit balance on Denar deposits increased by 1 p.p. in relation to Q1 2008 and amounted to 6.6%, which was by 0.1 p.p. higer compared to Q4 2008. Current monetary policy of increased reference interest rate and the other restrictive measures leave no room for reducing the interest rates of the banks in the coming period.



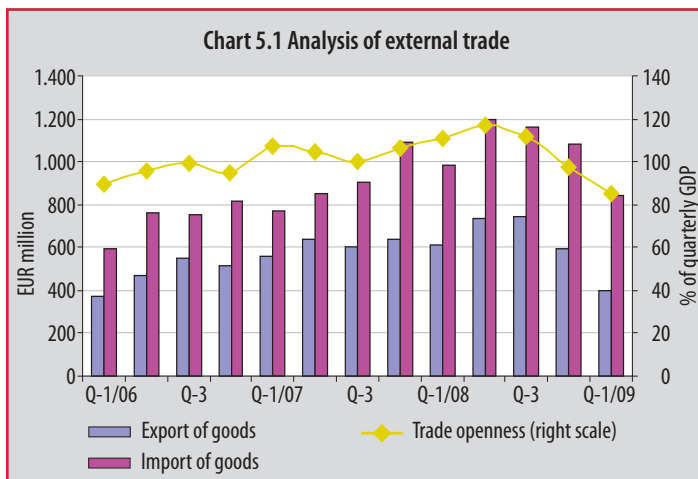
At the end of Q1 2009, **Macedonian stock exchange index** MSEI-10, as aggregate indicator of stock exchange trends, dropped by 9.1% in relation to Q4 2008, while the drop in relation to Q1 2008 was even more significant, amounting to high 71.6%. Further decline of stock exchange activity in Q1 2009 was mainly due to the global economic developments and weakening of the capital market worldwide as a result of the

6. Deposits include calculated interest

uncertainty and increased risks caused by the global financial crisis. Absence of large institutional investors in trading with securities on the Macedonian capital market affected even more the low stock exchange turnover.

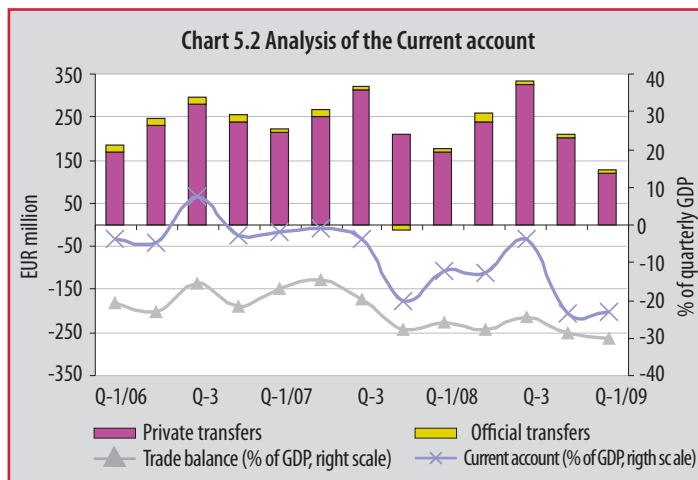
### 5. EXTERNAL SECTOR AND BALANCE OF PAYMENTS

Downward trend of both the export and the import of goods, which started in the last quarter in 2008, also continued in Q1 2009. Thereby, what is characteristic is the the export of goods declined faster in relation to

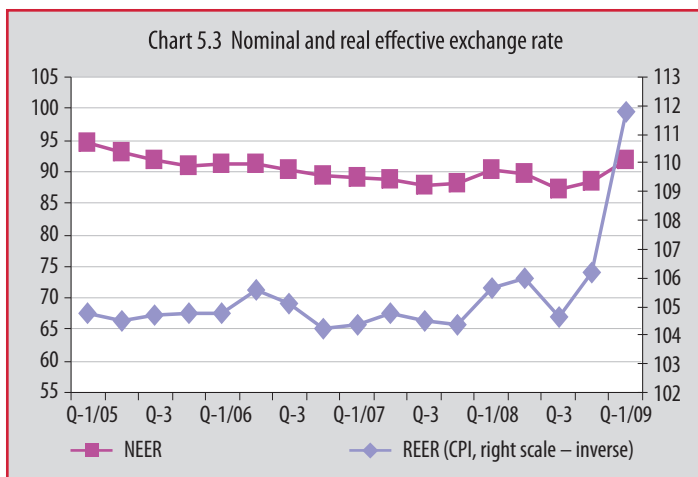


to the import, and such negative tendency did not contribute to eliminating the external trade risks. Slower decline of the import is a distinctive evidence of the high import dependence of Macedonia and the slow adjustment of the import of consumption goods.

In Q1 2009, **export of goods, expressed in euros**, dropped by 34.5% compared to the same quarter 2008, while **import of goods**, also expressed in euros, declined by 16.7% in relation to Q1 2008. In Q1 2009, negative growth rate was realized at almost each group of products according to SMTK. Thereby, highest decline was recorded at the categories raw materials (-55.2%), mineral oils and lubricants (-37%), animal and plant oil (-35.6%) and products classified according to the material (-25.7%). During the analyzed period, only the machines and transportation devices category experienced positive growth (15%). Largest disadvantage was the strong decline of the import of inouts used by the export-oriented sectors, i.e. the part of the so called import component of the export, having negative effects on the recovery of their overall production.



**Trade openness of the Republic of Macedonia** was 85% in Q1 2009, continuing the downward trend in relation to the previous quarters, and reducing the rate of openness to the levels before 2007. This was mainly due to the decline in the overall volume of the external trade by 22% in relation to the same quarter previous year.

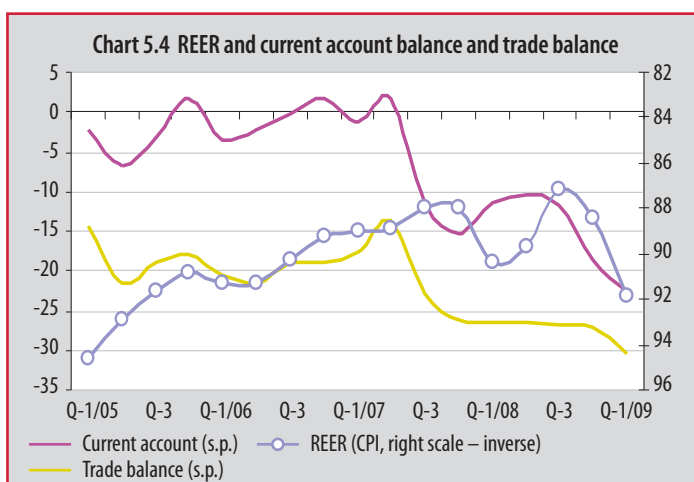


In Q1 2009, **trading volume with the EU** accounted for 53% of the total trade of the Republic of Macedonia, and in relation to Q4 2008, it remained at almost the same level. Serbia remained to be the second most significant trading partner to Macedonia, whereby the trading volume in Q1 2009

accounted for 11.4% of the total trade and it dropped by 3 p.p. in relation to the previous quarter. In Q1 2009, 62.4% of the Macedonian export was realized on the markets in Germany, Serbia, Greece and Italy.

As a result of the faster decline of the export in relation to the import, **trade deficit** in Q1 2009 reached 30.3% of quarterly GDP, further registering strong deterioration on quarterly basis. Upward trend of the **net current transfers**, which commenced in the third and the fourth quarter in 2008, was interrupted in Q1 2009, when they experienced sharp decline of even 26.3% in relation to Q1 2008, and thereby the decline was fully due to the reduced private transfers that are the dominant component and driving force of the current transfers (92%).

Following the historically largest deepening of the **current account deficit** in the last quarter 2008, in Q1 2009, it registered almost insignificant drop and reached - 23.3% of quarterly GDP, while the two-fold deepening compared to the same quarter previous year was due to the large trade deficit and the low net current transfers. At the moment, its financing is the main sources of risk to the external position fo the country.



Nominal Denar/EUR exchange rate remains as intermediary target of the monetary policy. In Q1 2009, **nominal Denar effective exchnage rate** strongly appreciated compared to the previous quarters, experiencing 5.8% increase on annual basis. **Real Denar effective exchange rate**, calculated on the basis of CPI index, continued the upward trend in Q1 2009, experiencing 1.6% appreciation compared to Q1 2008 (Chart 5.3). REER, calculated on the basis of price index of producers of industrial products, registered further depreciation of 0.3% in relation to the same quarter previous year, while compared to the previous period the same year, it interrupted the downward trends that commenced in Q3 2008 and experienced appreciation by 1.2% compared to Q4 2008, pointing out to certain worsening of the export competitiveness of the Macedonian economy.

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