Republic of Macedonia
MINISTRY OF FINANCE
- Macroeconomic Policy Department -

# ANNUAL ECONOMIC REPORT OF THE REPUBLIC OF MACEDONIA FOR 2007

Skopje, June 2008

2007

## ABBREVIATIONS

| | |
|---|---|
| EARM | Employment Agency of the Republic of Macedonia |
| JSC | Joint Stock Company |
| IRJSC | Insurance and Reinsurance Joint Stock Company |
| GDP | Gross Domestic Product |
| BH | Bosnia and Herzegovina |
| TFP | Total Factor Productivity |
| VAT | Value Added Tax |
| TB | Treasury Bills |
| SSO | State Statistical Office |
| GB | Government Bonds |
| GS | Government Securities |
| EBRD | European Bank for Reconstruction and Development |
| EU | European Union |
| EFTA | European Free Trade Association |
| ECB | European Central Bank |
| ILO | International Labour Organization |
| MSEI | Macedonian Stock Exchange Index |
| IMF | International Monetary Fund |
| MoF | Ministry of Finance |
| NBRM | National Bank of the Republic of Macedonia |
| OPEC | Organization of Petroleum Exporting Countries |
| p.p. | Percentage Points |
| PIT | Personal Income Tax |
| USA | United States of America |
| FDI | Foreign Direct Investments |
| SITC | Standard International Trade Classification |
| PRO | Public Revenue Office |
| HIFRM | Health Insurance Fund of the Republic of Macedonia |
| RF | Road Fund |
| PDIFRM | Pension and Disability Insurance Fund of the Republic of Macedonia |
| CEE | Central and Eastern Europe |

# 2007

## CONTENTS

# 2007

## PREFACE

Honourable,

Global economic trends in 2007 were a result of many events that slowed-down the pace of the global expansion. A financial crisis delivering a blow to the overall financial system in the USA and threatening the other (developed) economies, a drastic increase of processed metals, energy sources and food on the world stock exchanges and depreciation of the US dollar are perhaps the most significant developments that influenced them. Besides the economic factors, trends in the global economy in 2007 were also, to a great extent, determined by a series of non-economic factors - climate changes and political instability in different parts of the world.

In the case of the Republic of Macedonia, 2007 was the most successful economic year in the past 17 years. Economic results in 2007 confirmed the success of the ambitious economic program of the Government of the Republic of Macedonia, supported by disciplined fiscal policy and consistent monetary policy. Reports by two eminent world institutions also speak in favour of the intensive reforms in the Republic of Macedonia. The first one refers to the report Doing Business 2008, published by the World

Bank and the International Financial Corporation (IFC), according to which Macedonia is ranked fourth in the world among 179 countries - top ten reformists in the field of economy in 2006/07. Such a jump was due to the progress the Republic of Macedonia made in shortening the time and reducing the costs for business start-ups, in particular to the tax reform resulting in reducing and levelling the tax rates of the personal income tax (from 15%, 18% and 24% to 10%), profit tax (from 15% to 10%) and withholding tax (from 15% to 10%), thus contributing to transparent and efficient administrative procedures, simple and easy calculation of taxes and filling tax forms.

The second recognition is obtained from Transparency International, which ranked Macedonia at the 84th position according to the corruption perceptions index. Moving up 21 positions, Macedonia has shown that it is on the right track. These two reports, as well as the positive assessments by the IMF for the policies the Government of the Republic of Macedonia implemented, are of special importance to us, being a confirmation of the so-far effort invested and an incentive for further reforms.

The 2007 Annual Economic Report includes a number of analyses and data for all economic sectors; however, I would like to point out the most significant indicators in this paper. The GDP growth rate in 2007 was 5.1%, being the highest GDP growth since Republic of Macedonia gained independence, whereby it is important that the growth realized was diversified, i.e. almost all production sectors realized growth, except agriculture which experienced a drop of 2.9%. Growth was most evident in the services sector. The average inflation rate in 2007, despite the inflationary pressures especially evident in the last quarter as a result of the increase in food and energy sources prices on the world stock markets, was low, amounting to 2.3%.

Real sector growth was reflected in the external sector as well, whereby in 2007 export was 39.8%, while import grew by 38.9%, pointing out a slight real reduction of the trade deficit. However, most important is that such positive trends had a positive impact on the social sphere. Thus, the unemployment rate determined through the Labour Force Survey (ILO definition) in the fourth quarter in 2007 accounted for 34.7%, which compared to the same period in 2006, was a drop by 1.8 percentage points. At the same time, the average wage grew by 7.9% in nominal terms and by 5.5% in real terms, which reflected on the growth of the purchasing power of the citizens, i.e. the personal consumption, having a high positive influence over GDP growth.

The 2007 Fiscal Policy was prudent as agreed under the IMF Arrangement. Thereby, in 2007, significant fiscal reforms were undertaken, i.e. a 10% flat personal income tax and profit tax was introduced with a transitional 12% rate in 2007, VAT on agricultural products was reduced from 18% to 5%, and in the second half of the year the VAT rate on pharmaceuticals and medical aids, computers and computer equipment, solar collectors and public transportation was also reduced. What is of special importance in this period is that tax revenues, despite the significant tax reforms, grew by 16% in relation to 2006, whereby the profit tax revenues exceeded the projected level by 50%. Such an increase in the tax revenues was due to many factors, the most important being the following: significantly increased economic growth, high increase in the profitability of the companies in 2006 (29.7%), administrative simplifications regarding payment of taxes, changes in the behaviour of the economic agents, i.e. a reduction of the grey economy, as well as the decisive efforts by the Public Revenue Office and the Customs Administration for better collection of tax revenues.

Achieved results presented in the 2007 Annual Economic Report were the fruits of the commitment of the Government of the Republic of Macedonia to realize the set economic reforms, as well as its ability to reach wise decisions at moments calling for fast action. One can always do better and more. Aware of the problems and future challenges, we go on.

In 2008, like so far, we continue with dedicated work to create a functional, competitive market economy, capable of dealing with the challenges on the road to the European Union and minimizing the adverse effects from the process of real convergence towards the European economy. In 2008, we continue our dedicated work to accomplish the key economic goals - further increase of the economic growth and improvement of the living standard of the citizens in the Republic of Macedonia. We have shown that we know and we can. We remain on this path, to work for a better future for the citizens in the Republic of Macedonia.

*Sincerely yours,*
*Minister of Finance*
***Trajko Slaveski Ph.D.***

# 2007

# 1. WORLD ECONOMIC TRENDS

## 1.1. World Economy in 2007

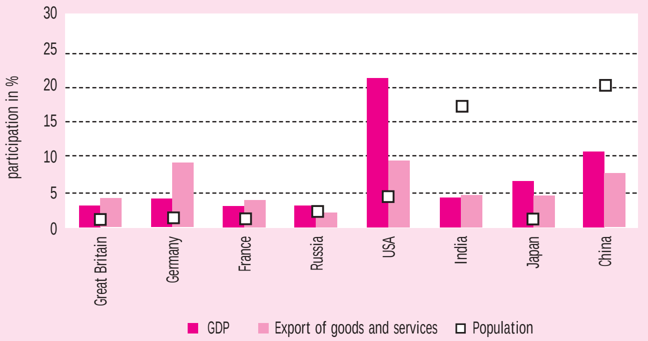
Besides the economic factors, trends in the global economy in 2007 were also, to a great extent, determined by a series of non-economic factors - climate changes and political instability in different parts of the world.

Global economic expansion in 2007 slowed down mainly due to the large financial crises, stimulated by the developments on the real estate market, especially in the USA. The economy in the USA in the last year faced financial shocks which firstly appeared on the secondary mortgage market, later on spreading into other segments. Economic growth in Western Europe also started to slow down, while economic activities in Japan were more flexible to the changes. In 2007, underdeveloped and developing countries were not exposed to significant financial turbulences and, headed by China and India (with 11.4% and 9.2% growth respectively) continued to realize higher growth rates.

The World economy in 2007 was influenced by the interaction of two important forces: financial crises that struck the developed countries and the further liberalization and convergence of the underdeveloped economies.

All in all, the **global GDP increased by 4.9%** in 2007, being significantly above the average growth of 3.9% in the past 7 years.

**Chart 1.1.** Share of selected countries in total population, GDP and export of goods and services




Source: IMF, World Economic Outlook, April 2008

The increase in prices of energy sources and food on the world stock market in 2007 stirred up inflation in many countries. Inflationary trends were especially strong at the end of the year. Thus, the **global inflation rate in 2007 accounted for 3.9%,** while food participated with 1.7 percentage points. With respect to the developing countries, a general increase in prices was more evident due to the increased economic growth and the increase of the aggregate demand, as well as due to the higher share of energy and food products in the consumer basket. In the Middle East, the annual inflation rate amounted to 10.4%, in Africa to 6.3%, and in Central and East Europe to 5.6%.

Increase in commodity processes has an adverse impact on the balance of payments of the countries - net importers of goods. In 2007, the volume of world trade grew by 6.8% on an annual basis, whereby the commodities trade grew by 6.4%, which was by 2.7 percentage points higher compared to 2006. The USA was still the largest export in 2007, participating with 9.6% in the world export, followed by Germany with 9.2%, and China being the third with 7.8% share in the total export (see Chart 1.1.).

## 1.2. Prices on world stock markets

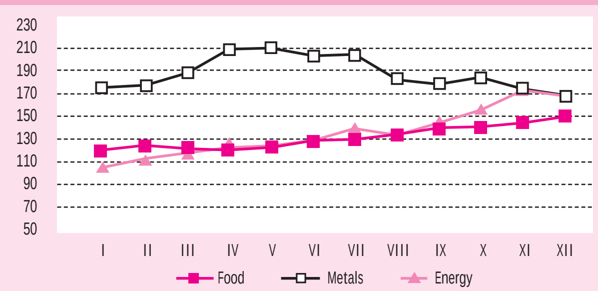
In the course of 2007, prices on world stock markets experienced a strong increase, mainly in the metals, raw materials and food products.

**The prices of metals** in 2007 increased more than the prices of any other goods in the last four years, mainly as a result of the increased demand from China. The prices of metals, for which China is the net importer, especially copper, experienced a large increase, while prices of metals for which China is net exporter, mainly aluminium and zinc, also surged, however with a slower pace. In parallel to the global narrowing of the offer of credits in August and September, prices of metals dropped by more than 10% (as a result partially of their sensitivity to acceleration of economic activity, and it could be that they were exposed to speculative pressures when the investors closed their positions so as to finance other losses in their portfolios). Prices of metals reached a peak in 2007; however, they are expected to drop by 5% in 2008 and to continue declining in 2009, since growing demand eventually will lead to a surplus in the market.

*The price of nickel* constantly grew in the first half of 2007, mainly as a result of the chronically low stocks and strong demand for non-corrosive nickel, but it experienced an unstable drop, with a 50% reduction by the end of the year. This drop was due to the increase in the stocks and the low demand for this metal. However, compared to last year, the price of nickel grew by 53%.

*The price of lead* grew throughout the whole year, experiencing a decline in the last two months in 2007. The increase was due to the suspension of the production in Australia, related to the environmental issues and the decline in export from China. The drop of the price in November and December was a result of the increase in the stocks and the expectations that the production from Australia would resume in the first quarter in 2008. However, compared to 2006, the price of lead grew by 100% in 2007.

**Chart 1.2.** Basic products price indices (2005=100)




Source: IMF

With respect to other metals, the increase in the stock market prices in comparison to 2006 was recorded at 15.7% for *gold* and 5% for *copper*.

**Prices of energy sources** on the world stock markets in 2007 also increased as a result of the continuous increase of oil prices and the search for other cheaper sources of energy. Substitutions were recorded for electricity generation, where oil is more and more substituted with coal and natural gas. Regarding transport, there are no alternative sources that could more significantly reduce oil demand.

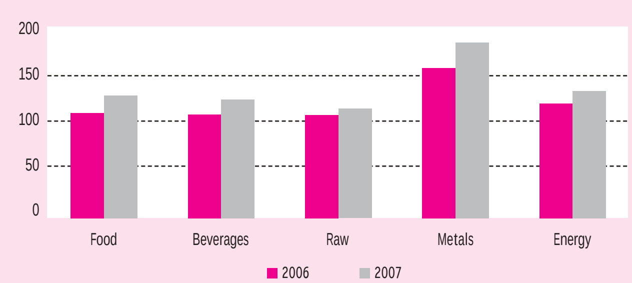
*The nominal price of oil,* measured in US dollars, beat a historical record in November, reaching almost US$ 100 per barrel on spot markets[1]. High oil prices slowed down the global oil demand. The price of crude oil continuously increased in 2007, almost twice in the period January-December in comparison to 2006, oil price by 12%. The price increase was a result of the increased demand for this energy source on the world market, reduced production by OPEC in the past period, as well as the drop in stocks and the fear of interruption in the supply due to the shortage of this energy source. In addition, the US dollar depreciation contributed to the oil price surge. The oil demand in 2007 declined in Europe and Russia, but increased everywhere else in the world, due to the rapid increase of income in the underdeveloped and the developing countries.

Since OPEC reserves are limited and production is kept at a low level, the oil price will remain high and unstable on the medium run, above the level of US$ 75 per barrel by 2009. On the long run, it is possible for prices to drop to US$ 50 per barrel, due to the increased concern for the environment and the use of alternative energy sources, which will contribute to mitigating the growing oil demand.

*The price of coal* in 2007 surged by around 80% while the price of *natural gas* remained unchanged.

The increase in the **prices of agricultural products** during 2007 was a result of the increased demand for food, especially in the developing countries, leading to a 20% increase in food prices at a global level. Compared to 2006, when food prices were at the lowest level, they grew by 75%. An increased demand for food was the result of the increased use of crops for the production of bio-fuels, a rapid increase of income in the developing countries, increased prices of fertilizers, droughts and discouraging harvests that hit the most important countries

**Chart 1.3. Basic products price indices (2005 = 100)**




Source: IMF

1) Spot markets are markets where goods are sold for ready money and delivered immediately. So, purchase agreements on these markets are executed immediately.

- food exporters. Raw materials for the production of bio-fuels played a more important role on the markets for agricultural products.

The increase in the prices of food products was most evident in the price of *cooking oil* (50%) and crops (22%), among which prices of wheat and corn surged significantly. *Soybean* prices also surged on the world stock markets, as well as the prices of *cocoa* and *coffee*, which led to a surge of beverage prices by 13%. In 2007, only the price of *sugar* dropped by 32%, as a result of improved production conditions in India, Pakistan and Thailand, and the expansion of plantations and favourable climate conditions that increased the production in Brazil.

**The prices of raw materials** on the world stock markets (wood materials and wood building materials, cotton, jute, rubber, wool, etc.) slightly increased in 2007, while the prices of fertilizers surged significantly.

### 1.3. Trends of foreign exchange rates

**The nominal effective foreign exchange rate of euro**[2], following the certain drop in 2005 from the peak reached in 2004, significantly recovered in 2006. At the beginning of 2007, the euro continued to appreciate in relation to the other currencies, mainly relying on the growing trend from the previous year. The trend of appreciation slowed down in the period of May to mid-August, when it experienced relatively narrow-ranged movement. Within the turmoil on the global financial market, the euro depreciated in August, before achieving strong appreciation during the rest of the year.

By the end of the year, the euro, in nominal terms, was by 6.3% above the level in January, and by 8.2% higher than its average level in 2006. Appreciation was the strongest in relation to the US dollar, followed by the British pound, and there was more moderate appreciation in relation to the Japanese yen, Chinese Yuan and Swiss frank.

*Appreciation of the euro against the US dollar* was the result of the changed market estimate of the cycle trends in both economic areas in favour of the Euro zone and of the trends of the interest differential. In addition, a constantly high current account deficit in the USA contributed to the weakening of the American currency. In the first months in 2007, the announcement of the quality data in the Euro zone in relation to the weaknesses in the US data led to a narrowing of the interest differential. From May to mid-August, the

2) Taking into account that the Denar exchange rate is pegged to the euro, the analysis covers the euro in relation to the other main currencies.

euro/US dollar exchange rate experienced several fluctuations, after the market participants revised their assessment of the relative cyclical scale of both economies. Following a short initial period of depreciation, as a result of the financial turbulences caused by the global liquidity crisis on the money and credit markets, the euro strongly appreciated in relation to the US dollar in the period from the end of August to the end of November. The weakening of the US dollar was probably related to the underestimation of the expectations of the market participants regarding the prospects of growth of the American economy, and less a result of the announcement of the expected results for the American labour and housing market. After the value of US$ 1.49 on 27 November 2007, by the end of the year the euro insignificantly depreciated, amounting to US$ 1.47 on 31 December 2007, an increase of 11.8% from the beginning of the year.

*In 2007, strengthening of the euro against the Japanese yen* was recorded, despite the instability on the short run. One of the main factors influencing the trends of the Japanese currency value was the change in the level of risk for the foreign investors, as well as the changes in the level of attractiveness to execute certain transactions, known as "carry trades" - selling currency with a relatively low interest rate, and buying currency with a higher interest rate. Thus, the investor tries to earn from the interest rate difference, which could be significant, depending on the level of indebtedness the investors chooses. Low Japanese interest rates and a historically low level of volatility in the exchange rate trend, combined with the favourable relation to the risk by the foreign investors, contributed to the significant increase of volume in such transactions. On 13 July, the euro reached a high value of 168.67 Japanese yen. The euro appreciation trend was interrupted by the global financial turbulences, leading to a re-assessment of the risk by foreign investors and reduction of "carry trades" transactions. From mid-August to mid-October, the euro started to strengthen in relation to the Japanese yen, although the euro/yen exchange rate trend witnessed certain turbulences. On 31 December 2007, the euro was positioned at the level of 164.93 yen or was 5.1% higher than at the beginning of the year.

*The euro also appreciated in relation to the pound sterling* in 2007 (by around 9.2%) in the period September-December. At end-December 2007, the euro was traded for 0.73 pound, its highest value since its introduction as a single currency in 1999. The pound decline was related to the market expectations for a further drop of the interest rates by the Bank of England, as reaction to the unfavourable financial and economic surrounding.

In 2007, the euro strengthened in relation to the currencies of several Asian countries. The euro appreciated more significantly in relation to Korean currency by 12.5% and Hong Kong dollar by 12.1%, and more moderately in relation to the Singapore dollar by 4.8% and Chinese Yuan by 4.6%. Relative appreciation in relation to the Chinese currency reflected, to a certain level, a greater will of the Chinese authorities to allow for a stronger appreciation of their currency in relation to the US dollar, especially at the end of the year.

The euro appreciation in relation to these currencies was partly counter-balanced with the *euro depreciation in relation to the Polish zloty by 6.2%, Canadian dollar by 5.4%, Norwegian krone by 3.4% and Czech koruna by 3.1%.*

**The real effective euro exchange rate,** based on different costs and price measurements, also appreciated in the course of 2007. In the fourth quarter in 2007, the real effective euro exchange rate, based on consumer prices, was around 5.5% above the level determined one year before.

## 1.4. Economic trends in 2007 in the developed countries

The global slowdown of economic activities and spreading of the financial crisis caused unfavourable circumstances in the developed countries and hindered conditions for the economic growth in many regions in the world.

What was characteristic for the developed economies in 2007 was the relatively lower GDP growth by 2.7% in relation to the realized 3% in 2006. In 2007, economic growth was initiated by the private consumption, which increased by 2.6%, while the growth of the gross domestic investments reached 1.7%, a drop of 2.3 percentage points compared to the previous year.

The main driving force of the growth in the developed countries, despite the slowed down economic activity, was the USA with 38% share in GDP growth. GDP growth in the USA was 2.2%. Because of the developments on the real estate market in the USA, domestic investment contracted and in 2007 dropped by 2%, reflecting on the future economic growth. Growth was underpinned by the expansive fiscal policy, resulting in a 2.5% budget deficit, an increase in the public expenditures by 1.9% and an increase in the private consumption by 2.9%.

In 2007, a positive trend of the economic growth continued in most of the Western Balkan countries. Countries within the Euro zone realized a GDP growth of 2.6% in 2007, while the GDP in Great Britain, despite the oscillations in the banking sector, grew by 3.1%.  Euro appreciation and the declined export activity (0.6% of GDP) significantly affected the growth. In the Euro zone, the driving force of the economic growth was the gross domestic investments, which grew by 4.4%, in 2007, and the public consumption, which grew by 2.2%. Average fiscal deficit in the countries in the Euro zone dropped from 1.4% in 2006 to 0.6% of GDP in 2007. Progress in these countries was also achieved in the social sphere, having in mind that the unemployment rate decreased by 7.4%, a drop of 0.8% percentage point compared to 2006.

Growth in the Euro zone countries in 2007, like in the previous years, was led by Germany, which contributed with 25.2% of the economic growth in the Euro zone.

Within the Euro zone countries, the highest rates of economic growth were seen in Slovenia, where the real GDP was higher by 6.1%, in Luxembourg by 5.4% and in Ireland by 5.3%. In addition to the highest

GDP growth in the Euro zone, Slovenia saw the highest price increase as well. The lowest inflation rate was recorded in Malta with only 0.7%. France, the Netherlands and Finland maintained inflation at a stable level and prices in these countries surged by 1.6%. The lowest unemployment rate in the Euro zone was recorded in the Netherlands, where only 3.2% of the labour force was unemployed, while it was the highest in Germany - 8.4%.

**Table 1.1.** Selected economic indicators for the developed countries

| | Real GDP growth | | | Inflation | | | Unemployment rate | | |
|---|---|---|---|---|---|---|---|---|---|
| | 2005 | 2006 | 2007 | 2005 | 2006 | 2007 | 2005 | 2006 | 2007 |
| Developed countries | 2.6 | 3.0 | 2.7 | 2.3 | 2.4 | 2.2 | 6.0 | 5.7 | 5.4 |
| Euro zone | 1.6 | 2.8 | 2.6 | 2.2 | 2.2 | 2.1 | 8.6 | 8.2 | 7.4 |
| - Germany | 0.8 | 2.9 | 2.5 | 1.9 | 1.8 | 2.3 | 9.5 | 9.8 | 8.4 |
| - Greece | 3.8 | 4.2 | 4.0 | 3.5 | 3.3 | 3.0 | 9.8 | 8.9 | 8.3 |
| - Italy | 0.6 | 1.8 | 1.5 | 2.2 | 2.2 | 2.0 | 7.7 | 9.2 | 8.3 |
| - The Netherlands | 1.5 | 3.0 | 3.5 | 1.5 | 1.7 | 1.6 | 4.7 | 3.9 | 3.2 |
| Great Britain | 1.8 | 2.9 | 3.1 | 2.0 | 2.3 | 2.3 | 4.8 | 5.4 | 5.4 |
| The USA | 3.1 | 2.9 | 2.2 | 3.4 | 3.2 | 2.9 | 5.1 | 4.6 | 4.6 |
| Japan | 1.9 | 2.4 | 2.1 | -0.3 | 0.3 | 0.3 | 4.4 | 4.1 | 3.9 |

Source: IMF, World Economic Outlook, April 2008

Further on, it is necessary to point out that in 2007 the lowest inflation rate in the developed countries of 0.3% was recorded in Japan, where consumer prices remained at approximately the same level as the previous year. In 2007, Japan had the highest budget deficit among the developed countries of 3.4% of the GDP. In addition, the unemployment rate in Japan remained to be one of the lower among the developed countries and it amounted to 3.9% in 2007. The lowest unemployment rate among the developed countries of 2.6% in 2007 was recorded in Norway.

**Box 1.1. Financial Crisis in 2007**

The financial crisis that appeared on the mortgage market in August 2007 was assessed as one of the largest financial crises in the last several decades. It hit the overall financial system in the USA and was a threat to the other (developed) economies in the world. The crisis in the USA originated from the so-called housing bubble, i.e. placing mortgage credit for unrealistically high value of the mortgage, which afterwards leads to a crisis at the moment when the credit applicant (borrower) cannot repay the credit, and the bank cannot recover the credit by calling in the mortgage. More specifically, motives for mortgage borrowing in the USA increased due to the growing prices of real estate, but the credit applicants also believed they could re-finance the mortgage credit later on, if the crediting requirements improved (mainly, if interest rate dropped). This process in the USA, which commenced in 2001, started developing in a negative path at the end of 2006, when the prices of real estate started to drop and credit applicants could no longer re-finance their credits, which reflected on the mortgage market for high-risk mortgage credits. In this period, liquidity of the whole banking system in the USA additionally declined also due to the increase of the so-called abolishment of the right to mortgage repurchase[3]. These two processes led to a significant increase of the interest rates on the mortgage credit market in the USA. Thus, credit risk on the mortgage market increased and banks started registering losses as a result of the reduced credit repayment. Such a crisis then spilled over to the secondary mortgage market, whereby large losses were also suffered by the holders of shares, based on mortgage credits (acquired through the so-called process of securitization of mortgage credits).

As a result of the increase of credit risk, banks reduced their credit activity and increased interest rates. Commercial issuers of securities also had to increase interest rates on their securities. Finally, chaos on the financial market in the USA pushed the economy into recession, since higher interest rates held back the economic activity, and credit activity of the banks dropped. Regarding the real estate market, price reduction slowed down construction activities on new real estate.

All this encouraged the Federal Reserve of the USA to reduce the discount interest rate to the historically lowest level, so as to stimulate economic activity, a process to occur in future, the effects of which will be additionally valorised.

The effect from the financial crisis, having a direct impact on the USA economy, was also felt in the other economies. Liquidity of the USA financial system shortly spilled over to the financial markets in

3) Poni{tuvawe e pravna procedura vo koja imatelot na hipoteka (zaemodavatelot) pribavuva sudski prestanok na pravoto za reotkup na hipotekata od strana na nejziniot davatel. Zaemodavatelot se steknuva so sigurnost od zaemobaratelot preku stavawe pod hipoteka nekoe sredstvo, kako ku}a, za da go obezbedi kreditot. Ako zaemobaratelot stane kreditonesposoben a zaemodavatelot se obide da stekne sopstvenost nad imotot {to bil zalo`en, Sudot mo`e da mu go dade na zaemobaratelot pravoto za reotkup na imotot ako go otplati dolgot. Koga vakvoto pravi postoi, zaemodavatelot ne mo`e da bide siguren deka uspe{no }e mo`e da go stekne imotot (vo sopstvenost) vo slu~aj na nelikvidnost na zaemobaratelot, pa zaemodavatelot bara da go poni{ti pravoto na reotkup.

the other economies, the most in the Euro zone. Most of the central banks in the economies that felt the blow undertook urgent measures to prevent complete spill over of the crisis. Thus, ECB immediately started to increase liquidity in the system through its instruments, in order to prevent an increase of the interest rates above the level defined with ECB discount frame. In addition, central banks across the world strengthened their cooperation, mostly through more intensive exchange of information and joint monitoring of the market trends, and later on through jointly coordinated steps to increase liquidity. The ECB, among other things, increased dollar liquidity in its system, whereby liquidity in euros remained unchanged; however, the goal was to improve global financing conditions. Thus, although the financial crisis in the USA spilled over to the economies in most of the developed countries in the world, it had no significant negative repercussions outside thanks to coordinated action of their central banks. Preventive actions of the ECB indirectly isolated the Republic of Macedonia from the spillover of the financial crisis and jeopardizing the circumstance for crediting and investment activity, i.e. from entering recession.

## 1.5. Economic trends in 2007 in the countries in Central and Eastern Europe (CEE)

In 2007, CEE countries, as well as the developed countries, registered a slowdown of GDP growth, in conditions of growing, but moderate, inflation rate and fiscal sustainability. Position in the economic relations of CEE countries with the rest of the world had worsened, and the average BOP current account deficit grew by 6.5% (from 6.2% to 6.6%), amounting to 6.6% of GDP.

**Table 1.2.** Selected macroeconomic indicators for selected economies

| | Real GDP growth | | | Inflation (CPI) | | | BOP current account (% of GDP) | | |
|---|---|---|---|---|---|---|---|---|---|
| | 2005 | 2006 | 2007 | 2005 | 2006 | 2007 | 2005 | 2006 | 2007 |
| Central and Eastern Europe | 6.1 | 6.6 | 5.8 | 5.1 | 5.4 | 5.6 | -4.7 | -6.2 | -6.6 |
| Bulgaria | 6.2 | 6.3 | 6.2 | 6.0 | 7.4 | 7.6 | -12.0 | -15.6 | -21.4 |
| Poland | 3.6 | 6.2 | 6.5 | 2.1 | 1.0 | 2.5 | -1.6 | -3.2 | -3.7 |
| Romania | 4.1 | 7.9 | 6.0 | 9.0 | 6.6 | 4.8 | -8.9 | -10.4 | -13.9 |
| Slovakia | 6.6 | 8.5 | 10.4 | 2.8 | 4.4 | 2.8 | -8.5 | -7.1 | -5.3 |
| Russia | 6.4 | 7.4 | 8.1 | 12.7 | 9.7 | 9.0 | 11.0 | 9.5 | 5.9 |
| Turkey | 8.4 | 6.9 | 5.0 | 8.2 | 9.6 | 8.8 | -4.7 | -6.1 | -5.7 |
| Western Balkans | | | | | | | | | |
| - Albania | 5.8 | 5.5 | 6.0 | 2.0 | 2.5 | 3.1 | -7.4 | -7.3 | -8.3 |
| - Bosnia and Herzegovina | 3.9 | 6.7 | 6.0 | 4.3 | 6.1 | 1.5 | -18.0 | -8.4 | -13.1 |
| - Croatia | 4.3 | 4.8 | 5.6 | 3.3 | 3.2 | 2.9 | -6.4 | -7.8 | -8.6 |
| - Serbia | 6.2 | 5.7 | 7.5 | 17.3 | 12.7 | 6.8 | -8.4 | -11.5 | -16.0 |
| - Macedonia | 4.1 | 4.0 | 5.1 | 0.5 | 3.2 | 2.3 | -2.7 | -0.9 | -3.1 |

Source: IMF, World Economic Outlook and European Commission (for Western Balkan countries)

The highest economic growth rate in 2007 among CEE countries was recorded in Slovakia - 10.4%, followed by Latvia, which in 2007, like in the previous year, recorded a two-digit GDP growth of 10.2%.

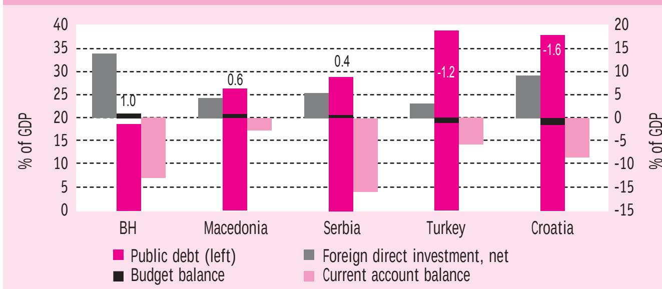
**Chart 1.4.** Basic economic indicators for CEE countries, members of EU


Source: IMF, World Economic Outlook, April 2008 and Eurostat

Latvia recorded the highest level of BOP current account deficit of 23.3% of GDP in 2007, without any consequences to the value of the national currency due to the establishment of the Currency Board. In addition, significantly worsened positions abroad after the accession to the EU and a high current account deficit of 21.4% of GDP in 2007 were registered in Bulgaria, around 6 percentage points higher compared to the previous year. The lowest current account deficit was recorded in the Czech Republic, at the same time showing a low inflation rate of 2.8%. A similar price increase was recorded in Slovakia, while the highest price increase of 2.5% was registered in Poland. Among these countries, Slovakia and Poland have the highest unemployment rates of 11.1% and 9.6%, respectively, while the lowest unemployment rates in 2007 in CEE countries were registered in Lithuania (4.3%) and Estonia (4.7%) (See Chart 1.4.).

Among the Western Balkan countries, the highest economic growth rate of 7.5% was registered in Serbia. Growth in this country was due to the increased domestic demand, caused by the high salary increase (22.1%), resulting in high increase of import of goods and services of 48.1% of GDP, while export grew by 27.4% of GDP. BOP current account deficit in Serbia amounted to 16% of GDP and, together with Bosnia and Herzegovina; Serbia experienced the highest deficit among the Western Balkan countries. High deficit in the trade of goods and services with Bosnia and Herzegovina was partially neutralized by the high inflow of foreign direct investments, which in net amount accounted for 13.7% of GDP, being the highest amount among the Western Balkan countries (see Chart 1.5.). Among these countries, the Republic of Macedonia registered the lowest current account deficit of 3% of GDP, although compared to 2006, it increased by around 2 percentage points. The Republic of Macedonia also recorded positive results in the fiscal sphere, realizing a budget surplus of 0.6% of GDP despite the tax system reforms, aimed at reducing the tax rates. Albania faces a high rate of budget deficit several years in a row, which in 2007 was estimated at 3.4% of GDP, with a relatively high

**Chart 1.5.** Selected economic indicators for the candidate countries (potencial) for EU




Source: European Commission

level of public debt. Maintenance of "tight" monetary policy in Albania contributed for the increase of consumer prices to be a moderate (3.1%), despite the shock of the offer on the primary sector at the end of the year.

Serbia recorded the highest inflation rate of 6.8% in 2007 among the Western Balkan countries, while the lowest rate of 1.5% was registered in Bosnia and Herzegovina, 4.6 percentage points lower increase of prices compared to 2006. Regarding the social sphere, Croatia has the lowest unemployment rate of 11%. Progress was registered in Macedonia and Bosnia and Herzegovina, having the highest unemployment rates of 34.4%, i.e. 42.9%, in 2007.

# 2007

## 2. MACROECONOMIC TRENDS IN THE REPUBLIC OF MACEDONIA IN 2007

### 2.1. Macroeconomic trends in 2007

Economic performance in the Republic of Macedonia in 2007 was the best so far in the period of transition, showing positive trends in almost all sectors of the economy, with the confirmation of the successful implementation of economic reforms supported by disciplined fiscal policy and consistent monetary policy.

**GDP** growth rate in 2007 was 5.1%, whereby it was important that the growth observed was diversified, i.e. all production sectors noted growth, except agriculture which showed 2.9% decline. Growth was most evident in the service sector, i.e. retail and wholesale (14%), transport and communications (12.5%), civil engineering (5.8%) and financial intermediation (5.3%).

The average **inflation rate** in 2007 was low and reached 2.3%, being within the low inflation and close to the Euro zone. However, in the last quarter in 2007, in line with the regional and global trends, the inflation rate recorded a more intensive increase (4.8% in the fourth quarter), mainly as a result of the increase in food prices.

Real sector growth was reflected in the **external sector** as well, whereby in 2007 export was 39.8%, while import grew by 38.9%, pointing out to slight real reduction of the trade deficit. Both in the real and the external sector, growth was detected in almost all segments, whereby the highest growth was achieved in the export of base metals (83.4%, mainly as a result of the increase in the demand for these products, as well as the increase in their prices on the world markets), construction materials (35%), food and beverages (24.8%), clothing (25%), production of metal products (31.5%), production of machines and devices (45.6%) etc. The decline in exports was noted only in the production of oil and oil derivatives as a result of the temporary closing of Kosovo market for the OKTA Refinery, a problem that has already been overcome by meeting the European standards on manufacturing. Positive economic trends were also underpinned by the strong increase in the import of investment products and intermediary goods of 33.5%, indicating increased production and investment activity in the country.

Regarding the **social sphere,** effects of the intensified economic activity started to be felt. Thus, the unemployment rate determined through the Labour Force Survey (ILO definition) in the fourth quarter in 2007 accounted for 34.7%, which compared to the same period in 2006, was a drop of 1.8%. The number of unemployed persons registered at the Employment Agency at the end of 2007 was 357,166 persons, which was a 2.5% decline compared to end-2006. At the same time, the average wage grew by 7.9% in nominal terms and by 5.5% in real terms in 2007, which reflected on the growth of purchasing power of the citizens, i.e. the personal consumption, having a high positive influence over GDP growth.

Positive trends in the real sector were also supported by the movements in the **monetary sphere.** In December 2007, primary money was 21.8% higher on an annual basis, at the same time having the demand for ready money and banks' liquidity increased by 10.7% and 42.5% respectively. The narrowest money supply M1 increased by 31.7% on an annual basis, whereby the deposit money (current and giro accounts) grew by 50.1%, mostly contributing to a M1 increase. Broader monetary aggregates M2 and M4, under the influence of the increase of the total deposit potential, grew by 28.3% and 29.5% respectively. In the course of 2007, there was a low, but continuous reduction of average weighted interest on credit balance of the commercial banks. On the other hand, average weighted interest on debit balance, under the influence of tightened competition in the banking sector, and as part of the policy for attracting deposits, continuously increased. The trend of gradual tightening of interest margins of the banks, and at the same time loosening the non-interest related requirements they offer, led to facilitating the access to necessary funds for the corporate sector. A high increase was registered as long-term credits to the corporate sector (funds used for investments), being significant support to the economic activity.

With regard to the achievements in the banking system, the total deposit potential of banks grew by 28.8% in December 2007 compared to December 2006, mainly as a result of the increased saving of the citizens, which participated in the growth of the deposit potential with around 72%. Higher deposit potential, coupled by the greater competition in the banking sector (entry of Societe General) and the proactive credit policy led to an annual growth rate of credit to the private sector by 39.1%. Thereby, the highest growth at an annual level was recorded as short-term credit to citizens (81.1%). Long-term credit to enterprises dominated the structure of banks' credit to the non-government sector, at the same time recording high growth of 41.5% at an annual level.

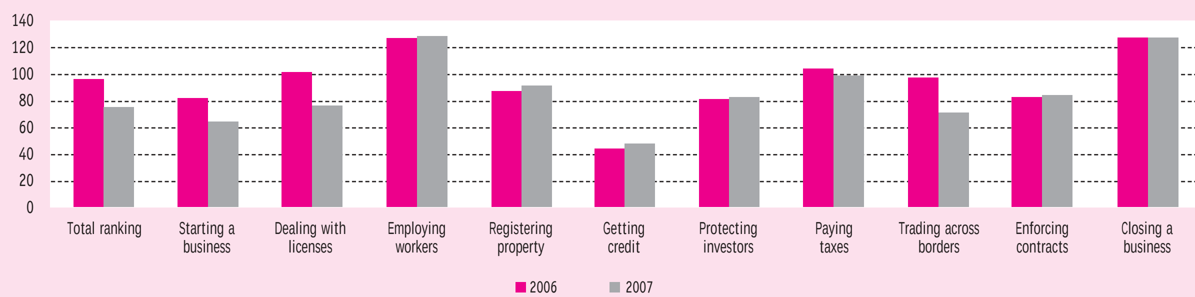
**2007 Fiscal Policy** was prudent as agreed under the IMF Arrangement. Thereby, it is important to mention that in 2007 significant fiscal reforms were undertaken, i.e. 10% flat personal income tax and profit tax was introduced with a transitional 12% rate in 2007, VAT on agricultural products was reduced from 18% to 5%, and in the second half of the year VAT rate on pharmaceuticals and medical aids, computers and computer equipment, solar collectors and public transportation was also reduced. What is of special importance in this period is that tax revenues, despite the significant tax reforms, grew by more than 13% in relation to the projections, whereby the profit tax revenues exceeded the projected level by 59%. Such increase in the tax revenues was due to many factors, the most important being the following:

significantly increased economic growth, the high increase in the profitability of the companies in 2006 (29.7%), administrative simplifications regarding payment of taxes, changes in the behaviour of the economic agents, i.e. reduction of the grey economy, as well as the decisive efforts by Public Revenue Office and the Customs Administration for better collection of tax revenues.

## 2.2. Republic of Macedonia through the prism of the international institutions

In 2007, the Republic of Macedonia saw certain progress, as observed by many reputable international institutions. Reports by these institutions depict the international perception of the Republic of Macedonia, which certainly is a strong signal to potential foreign investors.

**Chart 2.1.** Republic of Macedonia: Business Climate Indexes

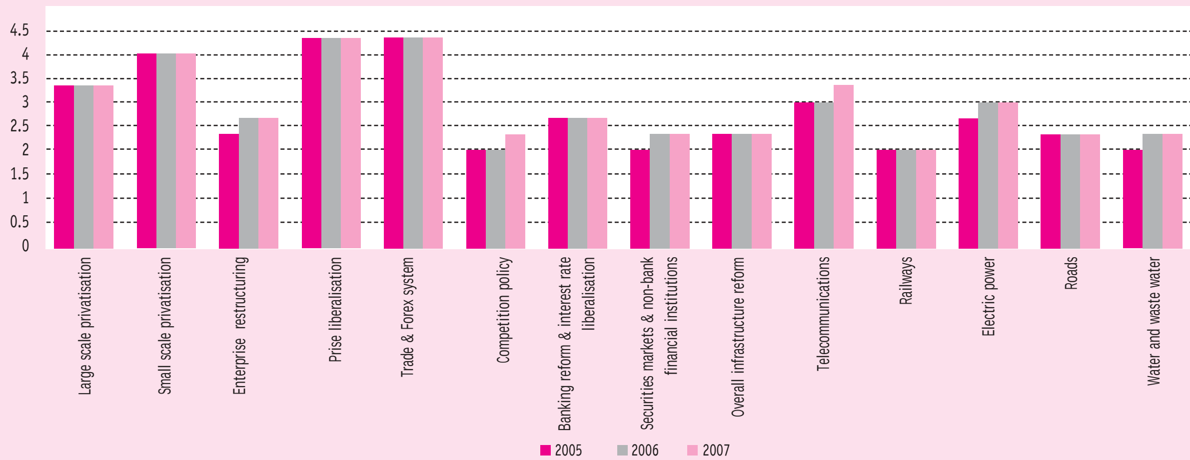



Source: Doing Business, World Bank

**The Doing Business Report** of the World Bank provides an objective assessment of the business regulations and their application in a certain country. According to the analysis of Doing Business 2008 of the World Bank, the Republic of Macedonia was ranked fourth in the world among 178 countries - top ten reformists in 2006/2007[4], as a result of the implemented reforms for improving the conditions for business start-ups, reduction of bureaucratic procedures and procedures for obtaining licences and permits, as well as the implemented tax reform that simplified the tax payment system. Ranking of countries under Doing Business was carried out on the basis of the number of on-going reforms, as well as according to the effect they have on facilitating the business conditions. Should one take into account the general rating, according to Doing Business, the Republic of Macedonia was in the 75th position in 2007, which compared to 2006, was an improvement by 19 positions (94th position in 2006). Compared to the countries in the region, the Republic of Macedonia was ranked higher than Serbia (86), Croatia

4) Ranking under the Doing Business 2008 Report covers the period April 2006 - June 2007.

**Chart 2.2.** Republic of Macedonia: Transition Index*



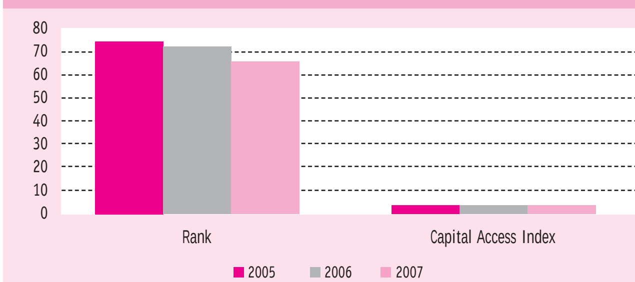

Source: EBRD

* Indicators scale is from 1 to 4+, where 1 represents small or no change from rigid central-planned economy, and 4+ represents the industrialized market economy standard.

(97), Bosnia and Herzegovina (105) and Albania (136), while Bulgaria (46), Romania (48), Slovenia (55) and Turkey (57) were ranked higher than Macedonia.

According to the **Report of the European Bank for Reconstruction and Development (EBRD),** in 2007, the Republic of Macedonia recorded the best results of the following indicators: small-scale privatization, price and trade liberalization and trading on the global foreign exchange stock market. Compared to 2006, improvement of the position of the Republic of Macedonia was also observed in the competitiveness and telecommunications policy. EBRD determines the progress in the transition process by summing up the indicators used for monitoring the reforms and the development of the countries at the beginning of the transition. Progress is measured against the standards of functional market economies, whereby it is taken into account that no "pure" market economy exists, nor single ultimate point of transition.

**Chart 2.3.** Republic of Macedonia: Capital Access Index

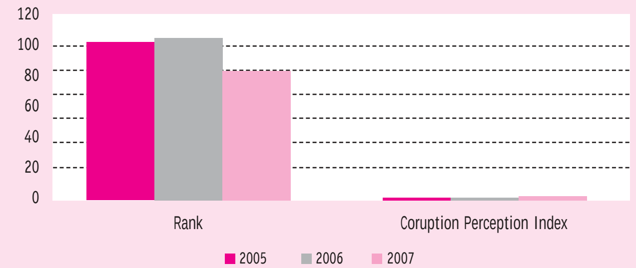



Source: Milken Institute

According to the **Milken Institute Capital Access Index,** the Republic of Macedonia was ranked in 67th position in 2007 among 122 countries, improving by 6 positions compared to last year. This index ranks the countries according to the financial infrastructure, as support to entrepreneurial activity for ensuring access to capital.

The index includes factors such as: financial and banking institutions, development of the share and bond market and alternative sources of capital. Having in mind that access to capital for the enterprises provides for implementation of innovative ideas and contributes to technological development, job creation and improvement of quality of life, capital access index should be an important indicator and, through the signals its sends, it should lead to undertaking certain measures aimed at eliminating the barriers to capital access. Among the countries in the region, Slovenia (46), Turkey (51), Bulgaria (53), Croatia (54) and Romania (58) are better ranked, while Bosnia and Herzegovina (87) lags behind the Republic of Macedonia.

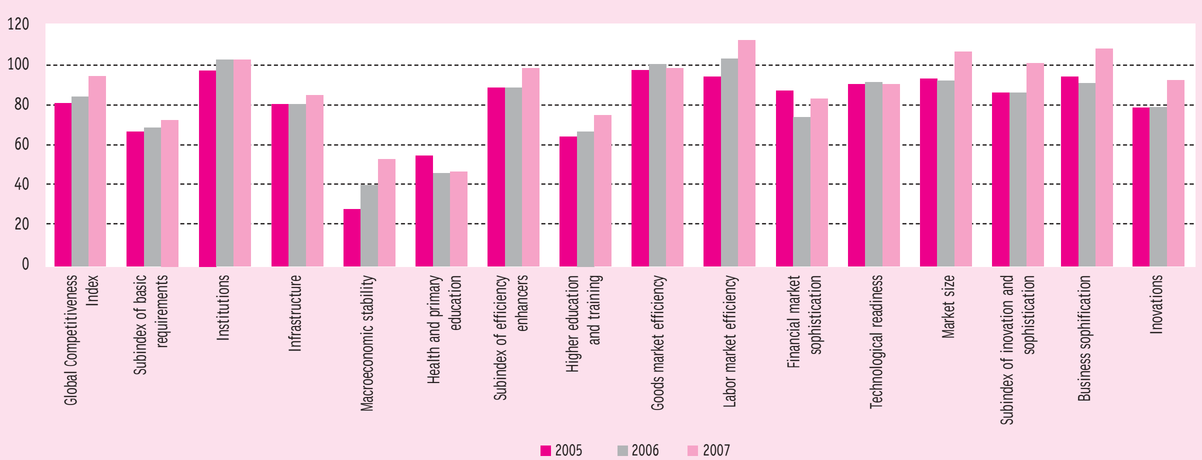
**Chart 2.4.** Republic of Macedonia: Corruption Perception Index




Source: Transparency International

In 2007, the Republic of Macedonia achieved significant progress in the fight against corruption. According to **2007 corruption perception index of Transparency International,** the Republic of Macedonia moved from 105th position in 2006 to 84th position in 2007, with 3.3 points out of 10 maximum points. The corruption perception index of Transparency International ranks the countries of the world according to "the degree to which corruption is perceived to exist among public officials and politicians". It is a composite index scheme of data related to corruption collected by experts and under business research, carried out by different, independent and important institutions. It ranges between 10 (squeaky clean) and 0 (highly corrupt). Despite the obvious progress in 2007, the Republic of Macedonia, according to the corruption perception index, still falls behind the EU member states, as well

**Chart 2.5.** Global Competitiveness Index




Source: World Economic Forum

as the countries in the region. The Republic of Macedonia is only  ranked higher than Montenegro and Albania.

**The global competitiveness index** is a comprehensive composite indicator for measuring competitiveness, set up by a number of macro and micro economic factors. Unlike last year, when the two-pillar index was used, the index in 2007 was comprised of 12 pillars. 131 countries were ranked under the global competitiveness index in 2007.

According to the competitiveness index, the Republic of Macedonia was ranked in 94th position in 2007, meaning it was in a worse position compared to the 84th position in 2006. It was due to the faster progress of the other countries. In 2007, the Republic of Macedonia was the best ranked according to the sub-index of basic requirements, and the worst ranked under the sub-index of innovations and sophistication. Health and education, together with macro economy, had the highest scores, while the lowest scores were assigned to efficiency of the labour market, business sophistication and market size. With respect to the countries in the region, the Republic of Macedonia was ranked higher than Bosnia and Herzegovina (106) and Albania (109), lagging behind Slovenia (39), Turkey (53), Croatia (57), Montenegro (82) and Serbia (91).

## 2.3. Economic cycle indicators

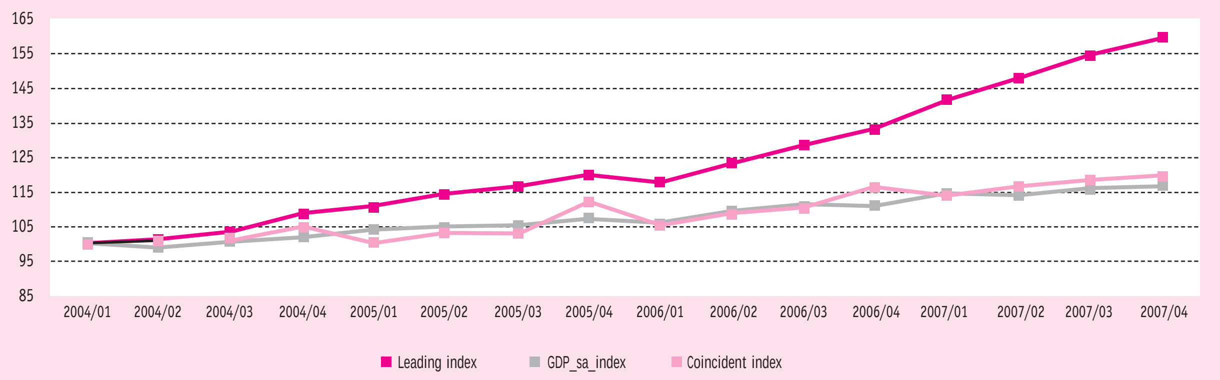
**The leading composite index for the Republic of Macedonia, MakLead,** is an aggregate indicator leading/preceding the economic cycle, comprised of eight leading indicators of the economic cycle, as follows: average salary in processing industry; average number of persons - beneficiaries of pecuniary allowance; assessment of the producers for their production stock for new orders; index of agreed construction works; MSEI-10 stock exchange index; M2 money supply; interest differential (weighted interest on debit balance at the commercial banks minus the primary rate) and capital goods and reproduction materials.

The leading composite index in 2007 increased by 26.3 index points compared to 2006. The subsequent increase in the index has been registered since early 2004, since data therefore has been set. However, the increase was exceptionally intensive from the beginning of 2006.

The **leading diffuse index,** measuring the share of components of the leading index that grew, in 2007 experienced positive trends at 84.4% of the components and in relation to 2006 (68.8%), there was significant increase, being an indicator of strengthened economic activity. The diffusion index includes the standardization factor that stabilizes the variability of each component of the composite index, thus having a deseasoning effect on the series.

On the basis of the values of the leading composite and diffusion indices, acceleration of the economic activity can be expected in the middle of 2008, whereby the economy will remain in the zone of intensified growth (see Chart 2.6.)

**Chart 2.6.** Leading and coincident index and GDP index (deseasonized)



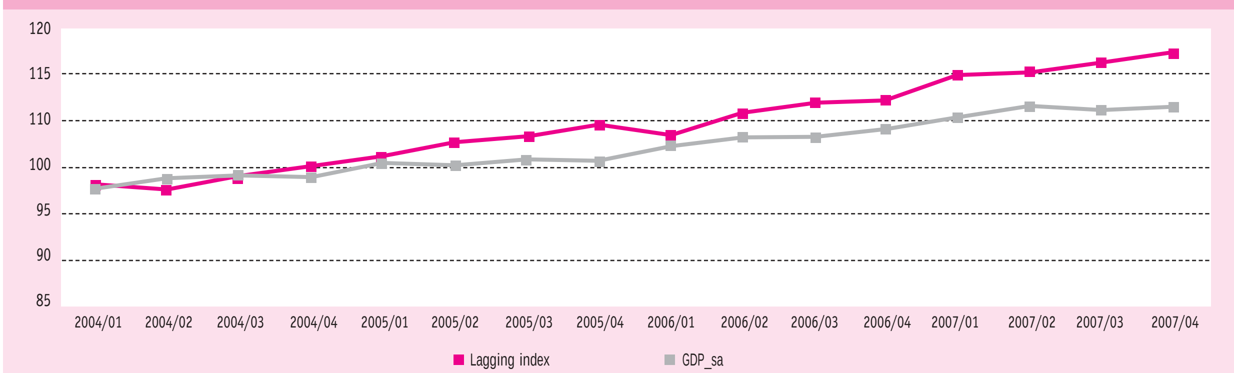

Source: Estimations of the Ministry of Finance

The **coincident composite index of the Republic of Macedonia, MakCoin,** reflects the economic cycle and comprises the following: number of employees in non-agriculture sector; average monthly net salary; industrial production index; income in the trade sector.

The coincident composite index in 2007 increased by 3.2 index points compared to 2006. The subsequent increase in the index has been continuously registered since early 2004, closely following and reflecting the GDP growth (see Chart 2.6.)[5].

In 2007, the **coincident diffusion index** registered positive tends at 71.9% of the components of the coincident index, and in relation to 2006 (68.8%), it slightly increased, thus being in line with the course of the economic activity.

**Chart 2.7.** Lagging composite index



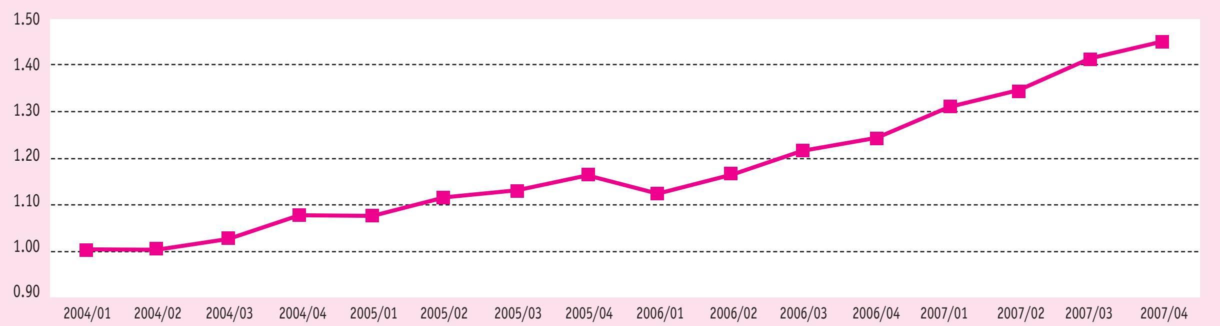

Source: Estimations of the Ministry of Finance

5) For more detailed empiric analysis see: Petreski, M. Indicative Linear Model for Assesment of the Forecasting Power of MakLead - leading composite index of the Republic of Macedonia, Bulletin of the Ministry of Finance, Nov/Dec. 2007, pp. 55-63.

The **lagging composite index of the Republic of Macedonia, MakLag,** monitors the economic cycle and is comprised of the following: average duration of unemployment; ratio of manufacturing and trade inventories to sales; labour cost per unit of output; primary interest rate; credit to enterprises; ratio of consumer instalment credit to personal income; and CPI index for services.

The lagging composite index in 2007 grew by 2.6 index points compared to 2006 (see Chart 2.7.), reflecting the economic growth achieved in the previous quarters.

**Chart 2.8.** Ratio leading/lagging index




Source: Estimations of the Ministry of Finance

The **lagging diffuse index** in 2007 registered positive trends at 75% of the components of the lagging index and in relation to 2006 (68.6%), it grew significantly.

The ratio between the leading and the lagging index is constantly increasing during the whole observation period. The objective of this ratio is to predict the turning points, i.e. the peaks and the floors of the economic activity. The drop in this ratio points out a significant increase in the costs related to running a business, occurring later in the expansion period, shown in the lagging index. This ratio is important because it precedes the turning points, i.e. it signals or "predicts" their occurrence. In the case of the Republic of Macedonia, a more intensive increase of this indicator is evident starting in 2006, which can be taken as approximate turning point in the economy, taking into account that the average value of the indicator in the period before was one. In 2007, this ratio is 1.38, suggesting that the leading index was around 38% higher compared to the lagging index, as well as suggesting stronger economic activity in the future semi-annual period, according to the predictions by the leading index.

### Box 2.1. What are business cycle indicators?

#### *Types of business cycle indicators*

Business cycle indicators are a means to predict and analyze the subsequent stages of expansion and contractions (recession) of the economy, called business cycles. In literature, business cycle indicators are also known as cyclic indicators. Cyclic indicators can be:

Leading cyclic indicators - signal future events of the business cycle, i.e. changes its direction prior to the cycle;

Coincident cyclic indicators - measure the aggregate business activity and thus define the business cycle; and

Lagging cyclic indicators - follow the business cycle, i.e. change their direction after the cycle.

Largest practical value of the three indicators has the leading indicator, since it has strong forecasting effect. Still, its power increases when used with the other two indicators.

#### *What can be business cycle indicator?*

Prior to analyzing the business cycle from the point of view of the cyclic indicators, available time series should be subjected to a series of statistical and economic tests, in particular[6]:

- conformity - series fit into the business cycle;
- time consistency - series have consistent course in time as leading, coincident or lagging indicators;
- economic significance - data are statistically reliable; and
- adjustment - trends from period to period are not turbulent.

#### *Explanatory power of cyclic indicators and their mixing in composite indices*

The best way to emphasize the cyclic component of the indicators, and at the same time to reduce the influence of their variability, is for them to be mixed in composite indices. Logically, it is best to create three indices, comprising leading, coincident and lagging indicators. Even more, composite indices can detect certain turning points in a set of economic data in a clearer and more persuasive manner compared to the behaviour of any individual indicator.

6) The Conference Board: Business Cycle Indicatos Handbook

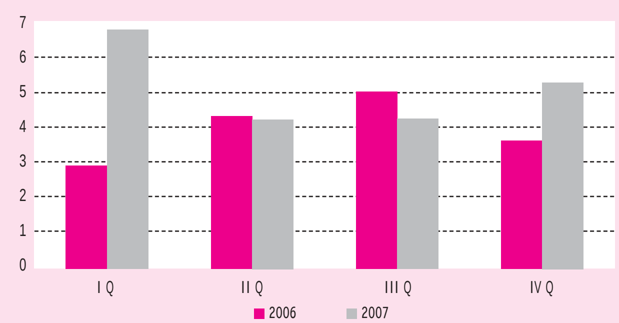
In addition to the composite, another set, the so called diffuse indices, also offer important information on the business cycle. The diffuse indices measure the width and depth of the trends at the business cycle (expansion or contraction). In other words, these indices measure the number of components that increase in a certain period.
Although they are based on same set of data, diffuse indices are important in the analyses of the economic cycles, since they often have the opposite trends compared to the composite indices in the same period. The composite index makes the difference between the small and the large trends in component series, while the diffuse index measures the prevailing influence of these general trends. This difference is of special importance when trying to confirm or predict the cyclic turning points.

## 3. REAL SECTOR

### 3.1. Gross Domestic Product

The Gross Domestic Product (GDP) expresses the value of the total produced final goods in the country for a period of one year and is a basic measure of the economic activity of a country. In 2007, the **real GDP** of the Republic of Macedonia grew by 5.1%. Compared to 2006, it is 1.1 percentage point higher (in 2006 the GDP was 4%). During 2007 economic growth was more intensive in the first quarter, at 6.8% which was followed by a slowdown of growth in the second and the third quarter and in the last quarter the GDP growth was the same as the average of the previous three quarters which contributed to the maintenance of the growth rate so far. (see Chart 3.1.). The **GDP per capita** in 2007 was Denar 166,711 or EUR 2,725. Compared to 2006, it grew in nominal terms by 9.4% or by 1 p.p. (in 2006, the nominal growth was 8.4%).

**Chart 3.1.** GDP real growth rate (Q/Q-4)

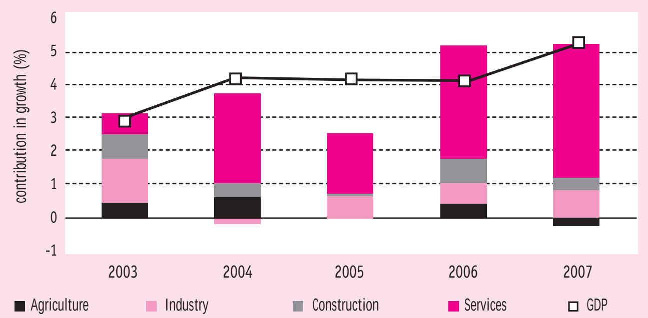



Source: State Statistical Office

If we analyze the **GDP under the revenue (production) method** the services sector has the largest contribution with 51.4% of the GDP. If we analyze separately the services, the share of the trade is 14.5% of the GDP while financial intermediation and public administration contribute with 13.3% and 13.2% respectively. The lowest contributor to the GDP is the sector of hotels and restaurants. Furthermore, industry creates 22.4% of the GDP, agriculture 8.7% while construction 6.1% of the GDP.

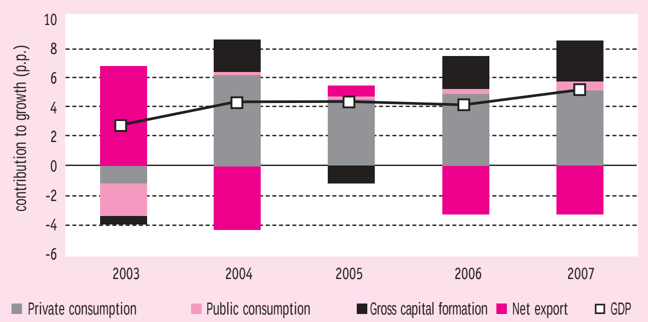
Economic growth in 2007 was led by the services sector which contributes to the total economic growth (5.1%) with 3.9 percentage points (see Chart 3.2.). Of the service activities, the largest growth was observed in the *wholesale and retail trade* by 14.1% and double-digit growth was observed in the *transport sector* by 12.5% where the entry of the third mobile operator VIP had a significant contribution. In addition, within the services sector, *the hotels and restaurants sector* grew by 6.8% as a result of the higher number of domestic and foreign tourists and similar growth was noted in the *financial intermediation* sector which grew by 5.3%, above all due to more competition in the sector (the entry of Société Générale). *The industry* grew modestly by 3.7% contributing to total growth with 1.4 percentage points (see Chart 3.2). In *the construction sector,* unlike last year, there was a slow down in the growth rate which was 5.8%. *The agriculture* noted a decline of economic activity, of 2.8% which is mainly a result of the unfavorable weather conditions (drought which almost halved the yield in agriculture) not only in the Republic of Macedonia but in the broader region.

**Chart 3.2.** GDP - production approach




Source: SSO and MoF

**Chart 3.3.** GDP - expenditure approach



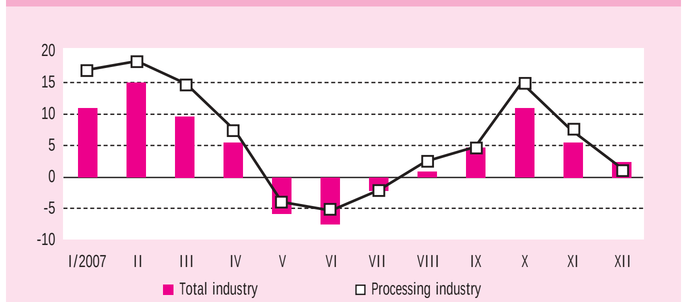

Source: SSO and MoF

The analysis of the **expenditure side of GDP** enables a different view of the economic results in the country. It provides an opportunity to see what stimulates growth, what is the contribution of the personal and public expenditures in the overall growth, if the external demand affects positively the economic growth, i.e. the dependence of the country on import, as well as the dynamics of gross domestic investments. In the absence of data on the real (deflationary) changes of the aforementioned components of the GDP, estimates were made by using nominal amounts. According to these, domestic consumption in nominal GDP in 2007 accounted for 96% (of which 81.3% accounted for personal consumption and 18.7% account for public expenditures). Accordingly, 20.2% of the total demand was met with imports of goods and services. On the basis of qualitative estimates, domestic consumption contributes to 5.5 percentage points of the total real economic growth of the country, of which 0.6 percentage points refer to public final consumption (see Chart 3.3). Gross investments contribute with 2.8 percentage points of the total growth, while the contribution of net export is -3.2 percentage points. Thereby, real growth of total final consumption in 2007 is estimated at 5.7%. Real growth rate of gross domestic investments is estimated at 15.3%, which is by 5 percentage points higher compared to the previous year.

## 3.2. Industrial production

In 2007 as rarely before, the industrial production growth was 3.7% (contrary to the GDP growth of 5.1%). Thus, contribution of services to the GDP growth in 2007 is higher than the contribution of the industrial production, which is actually a regional trend. Positive contribution to the industrial production growth in 2007 was made by all sectors except the electricity. If we exclude the negative contribution of electricity, industrial production growth in 2007 was around 5.1% which points to the fact that the electricity generation is a significant risk for the Macedonian economy.

**Chart 3.4.** Industrial production indices m/m-12



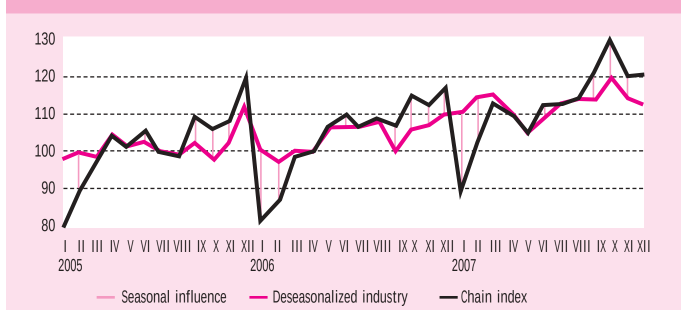

Source: State Statistical Office

Analysed by sectors, industrial production growth in 2007 is due to the higher production in the processing industry by 5.2% which has the largest share in the total index (83.9%) and extraction of ore and stone by 9.8%.

From the aspect of the multi-year quarterly dynamics, industrial production grew significantly by 11.6% in the first quarter and in the fourth quarter when the growth was 6.2%. There was a low growth rate of the industrial production in the third quarter (1.1%) while in the second quarter growth was a negative (-2.8%).

According to the scope, of 24 analysed industrial sectors, in 2007 growth was registered in 12 sectors, which accounted for 53% of the total industrial production. Of the sectors having the most significant share in the structure of the total industrial production, the largest growth was made in the production of metal products in the metal processing phase, except machines and devices by 45.6%, production of machines and devices by 39.1%, production of base metals by 34.3% and production of other means of transport by 33.4%. At the same time, significant growth was registered in the production of food and beverages by 7.7%. More moderate growth in 2007 compared to 2006 was achieved in the wood industry, the production of cellulose, paper and paper products, production of rubber products and products of plastic. On the other hand, the largest decline was registered in the supply of electricity, gas and water, by 9.5%.

**Chart 3.5.** Deseasonalizing of the industrial production

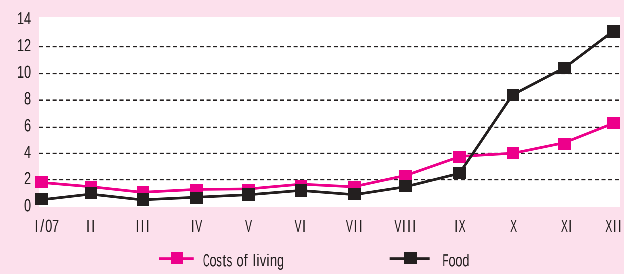



Source: MoF

### 3.3. Inflation

After several years of an exceptionally low inflation rate in the Republic of Macedonia (in the period of 1996-2006 the inflation rate did not go beyond 5%) in the second half of 2007 (starting in October) inflationary pressures intensified significantly. In a small and open economy such as the Republic of Macedonia, with a de facto fixed exchange rate, price changes on the global markets reflect in the domestic market. Having in mind that the exchange rate conduit is fast and direct, the Republic of Macedonia in 2007 was not immune to the price movements on the global stock markets (see Item 1.2. Prices on the global stock markets).

**Chart 3.6.** Costs of living and food




Source: State Statistical Office

In the first half of 2007, the inflation rate was low at 0.9%. The low inflation rate in the first half of the year was a result of the reduction of the prices of oil and oil derivatives at the beginning of 2007, an unrealized planned increase of the electricity price, reduction of the price of the central heating, as well as the unchanged price of tobacco products despite the harmonisation of the excise for domestic and foreign cigarettes. In the third quarter, the inflation rate was 2.4% and the highest inflation rate was observed in the fourth quarter of 2007 when it reached the level of 4.8%.

In addition to different trends by months, the average annual inflation rate in 2007 was low at 2.3%. In the Eurozone the average inflation rate was similar at 2.1%.

Within the CPI (according to COICOP)[7] in 2007 in the Republic of Macedonia, food accounted for 34.3%, meaning that an average Macedonian family spends 34% of all expenditures on food, which is significantly higher compared to the EU countries, where this percent is 15%. The share of food in the inflation rate, (2.3%) is 1.3 percentage points. The share of food in the total consumer basket in other countries in transition is similar as in the Republic of Macedonia, which explains the higher level of inflation in these countries compared to the developed countries. The CPI trend in 2007 was different by consumption groups. Growth was noted in the following groups: housing and hotels and restaurants (4.7%), food (3.9%), culture and entertainment (4.2%), tobacco and beverages and clothing and footwear by 1.8% and other services elsewhere unmentioned by 8.6%.

7) Classification of personal consumption by purpose, by groups and subgroups of products and services.

Retail prices in 2007 grew in average by 2.6%, mainly under the influence of higher prices of agricultural products (5.2%), non-alimentary industrial products and alimentary industrial products (3.4%), services (1.5%) and beverages (0.7%). The retail price index in December 2007 compared to December 2006 grew by 4.6% and the CPI by 6.1%.

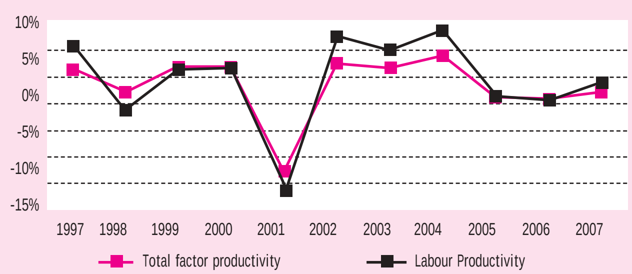
Basic reasons for the price growth in 2007 are the strong growth of prices on the global stock markets (see Item 1.2. Prices on the global stock markets) and the higher import of food from the Republic of Macedonia (in accordance with the global demand and higher global prices), which on the other hand led to a reduced supply on the domestic market and price growth. Although insignificant, the European Union convergence process has a contribution in the general price level in the Republic of Macedonia in 2007 where there is an imminent price growth and their approximation to the price level of the European Union[8].

### 3.4. Total factor productivity

Total factor productivity (TFP), is a total level of efficiency of using traditional production factors-capital and labour. More specifically, TFP includes technology, innovation, know-how etc. TFP is a concept which is the base of growth in the highly developed countries. TFP has an importance in the developing countries as well.

To calculate the total factor productivity in the Republic of Macedonia, we took into account the capital stock depreciated by the assumed weighted depreciation rate of 10%, and the number of employed persons. The calculation used the average value of the capital revenues for the period 1998-2007, 0.41, and the remaining (0.59) is part of the labour revenues. Total factor productivity in the Republic of Macedonia was given in Chart 3.7. which sets the labour productivity for the same period so as to compare it with TFP.

**Chart 3.7.** Total factor productivity and labor productivity




Source: Estimations of the Ministry of Finance

8) In the process of approximation to the EU domestic productivity growth is necessary and as a result, salary growth on one hand and of prices on the other. Productivity growth is only in the trade sector. Non-trade does not face competitive pressure, shows no productivity growth and salary growth follows the salary growth in the trade sector. Unlike the growth of salaries in the trade sector which has a real basis due to the productivity growth, salary growth in the non-trade sector is without any real basis and pressures inflation (Balassa-Samuelson effect)

Chart 3.7. shows that in 2007 TFP is positive, 0.4% and there is a positive trend compared to 2006 (-0.6%). Hence, the share of the TFP in the total economic growth is significant, 8.6%. This suggests relative improvement of the efficiency of utilization of both the labour and fixed assets in 2007. Still, relatively low growth of TFP (0.4%) can be attributed to the high capital growth (6.4%) and labour growth (3.5%) in 2007.

Even more, this number should be taken with reserve due to the possible underestimation of the capital stock in the Republic of Macedonia, as well as due to the significant share of employment in the informal sector, excluded from the TFP calculation. Cumulatively, for the period 1997-2007, the share of the production factors and the total factor productivity of growth is shown in Table 3.1.

The table points to the conclusion that in a longer term (11-year average), contribution of total factor productivity to growth is around 46.1%, which is a significant indicator of the efficiency in using labour and capital. Although in 2007 growth of the TFP is low, it shows a positive trend in relation to the previous years and this number is expected to improve in the next period. Such a statement is based on the fact that expected FDI growth in the next period will strongly affect the total factor productivity, as a result of improved corporate governance, standardisation, more efficient utilisation of the labour force. In the long run, reforms in the education and health sector will positively affect the TFP.

**Table 3.1.** Contribution and share of the factors and the factor productivity to growth in Macedonia (1997-2006)

| Growth of GDP | Capital | Labour | TFP |
|---|---|---|---|
| **2.7%** | 0.9% | 0.6% | 1.3% |
| | (32.9%) | (20.9%) | (46.1%) |

Source: Ministry of Finance calculations

### Box 3.1. Calculation of TFP

Calculation of the TFP is based on the neo-classical production function according to which:

$Y = A*f(K,L)$

Where, Y is the real GDP, K is capital, and L is labour. A is total factor productivity and is a residual, i.e. total efficiency of usage of K and L. The residual was introduced in the 1950s by the economist Robert Sollow and it is often called Sollow residual.

The specification of the production function used to calculate TFP is Cobb-Douglas equation:

$Y = A*K^{\alpha}L^{1-\alpha}$

where $\alpha$ is part of income from capital and it ranges between 0 and 1. By differentiating both sides, the following is obtained:

$$dY/Y=dA/A+\alpha*dK/K+(1-\alpha)*dL/L$$

where *d* refers to the growth rates of the involved variables. If we express the factor productivity element, then:

$$dA/A=dY/Y-\alpha*dK/K-(1-\alpha)*dL/L$$

By entering data on variables on the right side and by calculating $\alpha$ on the basis of data on the income from the production factors, we come to the data on TFP.

*Robert Barro and XavierSala-i-Martin (2001) Economic Growth. Cambridge MIT Press

# 2007

## 4. FISCAL SECTOR

Fiscal trends in 2007 point to a prudent fiscal policy. In addition to reforms in the tax system, the general government budget revenues were 15% higher compared to the previous year and were 35.3% of the GDP. The general government budget expenditures grew by 11.1% compared to the previous year, reaching 34.6% of the GDP. In 2007, the general government budget had a surplus of 0.64% of the GDP. The planned 2007 expenditures were exceeded by 11.1% while planned revenues were exceeded by 4.8%.

### 4.1. Central Budget revenues

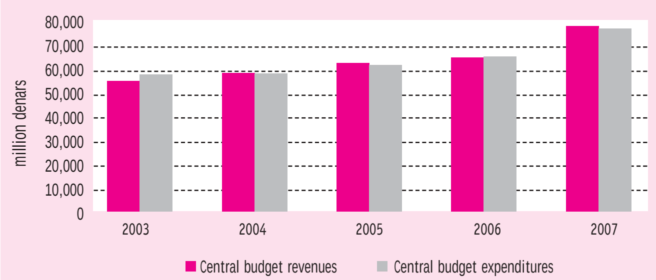
In 2007, the total Central Budget revenues were Denar 76,158 million or 22.7% of the GDP. With regard to the previous year they grew by 21% as a result of the improved economic activity of the entities, undertaken fiscal reforms and the strengthened capacity of the PRO.

**Tax revenues** reached a level of Denar 68,833 million (20.7% of the GDP). They accounted for 90.4% of total budget revenues in 2007.

In the structure of generated tax revenues (see Chart 4.3.) personal income tax accounts for 13.4%, profit tax - 8.9%, VAT - 49.5%, excises - 18.9%, customs and other import duties - 9.3%.

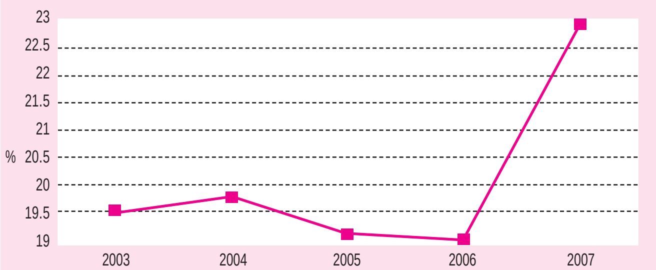
*Revenues from personal income tax* in 2007 amounted to Denar 8,893 million (2.7% of GDP), which is 5.7% more compared to the previous year, despite the reduced and

**Chart 4.1.** Central budget revenues and expenditures (in million of denars)




Source: MoF

**Chart 4.2.** Tax revenues (% of GDP)




Source: MoF

uniformed rate of 12% from the 24%, 18% and 15% rates.

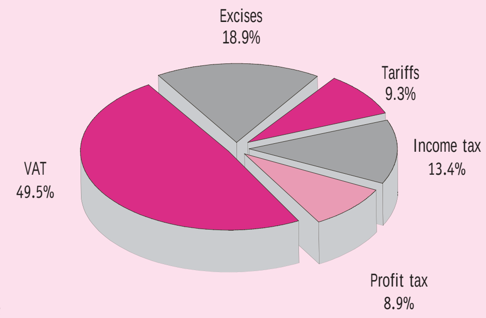


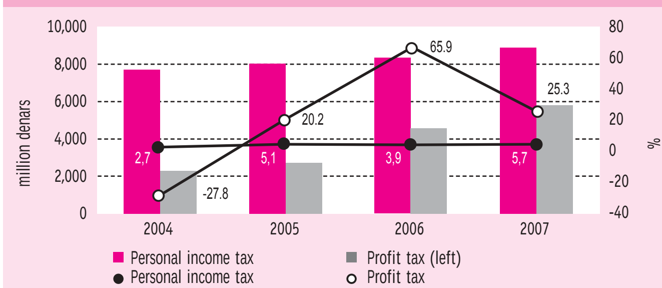

**Chart 4.3.** Tax revenue structure

Source: MoF

This reform contributed to expansion of the tax base whereby together with the strengthened control of PRO, resulted in a reduced informal economy and better collection of PIT and tax revenues in general. Positive economic trends, followed by higher employment, salary growth and reduction of the percentage of employees who did not receive a salary (see Item 9. Social sector) which in certain measures affected the higher realisation of PIT revenues.

In addition, in 2007 there was a historic increase in the turnover in shares on the capital market (see Item 8.2. Capital Market) and high growth of the stock exchange index which points to higher capital gain revenues, which account for 5.6% of the PIT revenues.

**Chart 4.4.** Direct taxes - amount and annual percentage change




Source: MoF

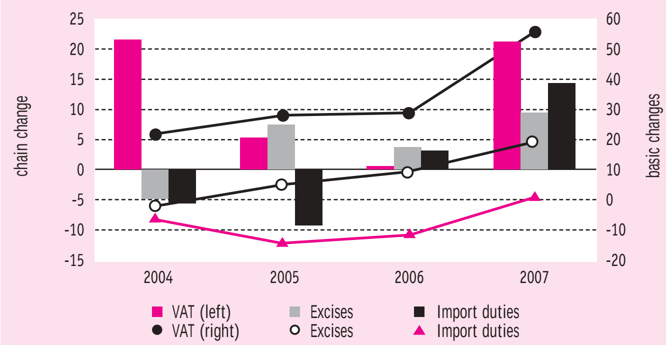
In the structure of these revenues, the largest part is achieved from taxation of salaries and other personal income from employment (61.7%), as well as from revenues on the basis of contractual agreements (8.1%), tax on income from dividends and other revenues from the share in the profit (4.7%) while the share of the revenues on other bases is relatively lower.

*Revenues generated from profit tax* in 2007 in the amount of Denar 5,898 million (1.8% of the GDP), are by Denar 1,190 million higher, or 25.3% compared to 2006. The increase of these revenues in 2007 is a result of the upward economic trend, resulting in the growth of profitability in enterprises in 2006 by 30% on the basis of the paid profit tax for 2007. In addition, the strengthened capacity of the PRO resulted in 33.6% higher fiscalisation in the economy and more realistic disclosure of profits by companies. Higher fiscalisation and a lower profit tax rate resulted in a reduced grey economy and higher revenues on the basis of profit tax.

*Domestic taxes on goods and services (VAT and excises)* account for the largest share of 66.2% in the structure of total tax revenues (13.7% of the GDP).

In September 2007, the general VAT rate of 18% was reduced to 5% rate for the following goods: pharmaceuticals and medical aids, computers and software, thermal solar systems and components and transportation of persons and their accompanying luggage. The fiscal effects of this reform did not have a significant effect on the level of VAT revenues in 2007 but they will have in the future. VAT revenues in 2007 were Denar 32,962 million (9.9% of GDP), and grew by 21% in relation to the previous year. This growth is largely due to the higher final consumption of 8.3% (as a result of the aforementioned economic achievements). Thereby, collected VAT on imported goods grew by 23% due to the higher import of goods compared to the previous year (see Item 5.1. Balance of Payments). Import growth reflected on the increase of import duties in 2007 by 14.4% despite reduced customs rates.

**Chart 4.5.** Indirect taxes - chain and basic rates of change compared to 2003




Source: MoF

*Excise revenues* in 2007 accounted for 3.8% of the GDP and are 10.9% higher compared to 2006. Such realized revenues from excise are a result, above all, of revenues from the excise on oil derivatives (Denar 6,909 million), revenues from excise on tobacco processed goods (Denar 4,003 million), revenues from excise on sale of alcoholic beverages (Denar 1,007 million) and passenger vehicles (Denar 425 million).

*Other tax revenues* amounted to Denar 2,298 million accounting for 0.7% of the GDP and are 48.9% on an annual level. This increase is a result above all of the inclusion of the fees introduced pursuant to the Law on Environmental protection, the Law on Tobacco and the Law on Healthcare.

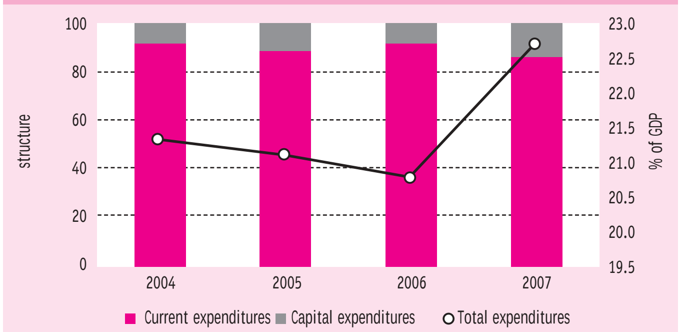
**Non-tax revenues** in 2007 accounted for 1.8% in GDP (Denar 5,806 million), which is almost double compared to 2006. This is mostly due to the payment of resources on the basis of the 2005 dividend from AD Makedonski Telekomunikacii (Denar 2,873 million).

*Capital revenues* in 2007 accounted 0.4% of the GDP and amounted to Denar 1,394 million which is a 47.1% increase compared to 2006. Realization of capital revenues is mainly due to the sale of construction land and flats.

## 4.2. Central Budget expenditures

In 2007, the total central budget expenditures amounted to Denar 75,441 million (22.7% of the GDP) and are by 18.7% higher compared to the previous year. The increase was a result of the increase of almost all expenditure items. In the structure of total expenditures, current expenditures accounted for 85.7% while capital expenditures accounted for 14.3%.

**Chart 4.6.** Total expenditures trend (% of GDP) and current and capital expenditures participation in total expenditures




Source: MoF

**Current expenditures** amounted to Denar 64.620 million (19.5% of GDP), which is a 11.7% increase compared to the previous year. *Expenditures for salaries and allowances* in 2007 amounted to Denar 22,300 million (6.8% of the GDP), which is almost the same realization, i.e. an increase of only 0.4% in relation to 2006 despite the 10% raise of salaries in the public administration in September 2007. This is a result of the fact that part of the funds for payment of salaries in education and kindergartens are registered as transfers for grants to local governments (in 42 municipalities which were transferred to the second phase of decentralization). Expenditures, wages, salaries and allowances as a percentage of the total expenditures are 5.4 percentage points lower compared to 2006.

*For goods and services* in 2007 2.9% of the GDP was spent (Denar 9,526 million) i.e. 20.3% more compared to last year.

*Funds for transfers* that cover the subsidies, current transfers and social benefits in 2007 accounted for 9.1% of the GDP (Denar 30,261 million) a 23.7% growth compared to 2006. This growth in 2007 is above all due to the higher transfers to the municipalities of grants to the PDF (12.7% compared to the previous year) so as to cover the transition deficit of the Fund to introduce the second pillar of the mandatory capital funded pension insurance.

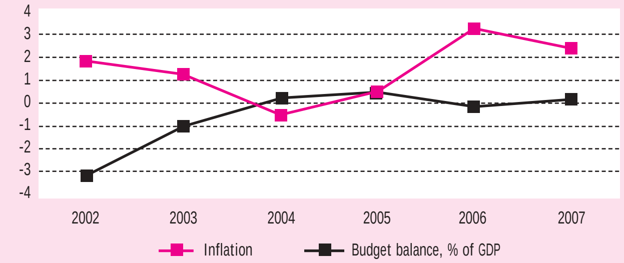
In 2007 for social transfers Denar 2,797 million was spent which compared to 2006 is a decline of 2.3% while transfers for child allowance grew by only 10.2%. For reforms in the *Ministry of Defence Denar* 221 million was spent, almost the same as in 2006. Within the *public administration reform* in 2007 Denar 361 million was spent, a 27.9% decline compared to 2006.

*Interest payments* in 2007 (0.8% of GDP) declined by 9.9% compared to 2006. This decline is above all, a result of the reduced payments on the basis of interest on external debt by Denar 249 million or by 17.3%

compared to the previous year. With regard to interest payments on the basis of domestic debt there was a 2.7% decline.

**Capital expenditures** in 2007 reached 3.3% of the GDP (Denar 10,821 million). This is full completion of the envisaged capital expenditures for 2007 which is 89.2% more compared to 2006. Most of the capital expenditures (66.1%) are costs for the purchase of capital assets.

**Chart 4.7.** Relation between Central budget balance and inflation




Source: MoF

## 4.3. Budgets of the Funds in the Republic of Macedonia

### *4.3.1. Pension and Disability Insurance Fund (PDIF)*

The PDF revenues in 2007 were 8.1% in relation to the previous year and amounted to 10% of the GDP. Of the total PDF revenues, 62.7% were revenues for pension and disability insurance, while transfers from the central budget account for 30.5%. Most of the funds, around 80% were used by PDF for payment of pensions, while 11.4% for ensuring health insurance of pensioners.

### *4.3.2. Health Insurance Fund (HIF)*

The HIF revenues for 2007 grew by 10.2% compared to the previous year, while expenditures grew by 1.3%. The health insurance contributions accounted for 57.9% of total revenues, transfers from the PDF (abovementioned) account for 21.5% while a significant part of the HIF revenues (12.4%) accounted for transfers from the Employment Agency for health insurance of the unemployed persons. The HIF uses the funds to ensure primary health care of the insured (around 90% of total expenditures).

### *4.3.3. Employment Agency (EA)*

The declining trend of revenues and expenditures of the EA continued in 2007. Revenues declined by 11.2% while expenditures by 14.7% compared to the previous year. Around 70% of total revenues were grants from the central budget, while the remaining part is from unemployment contribution. The major part of revenues, around 42.3% was for ensuring health insurance of the unemployed, while 17.2% are transfers to the PDF. 31.7% of the expenditures were related to the payment of unemployment benefit to the unemployed.

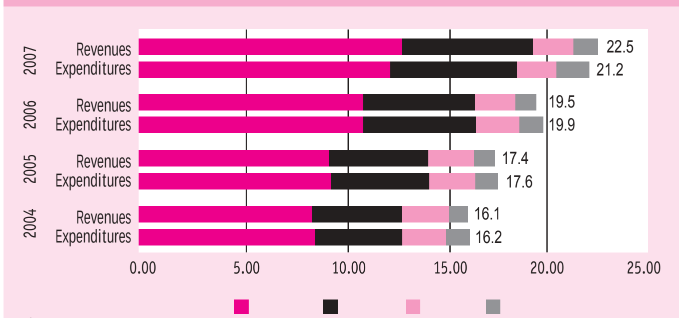
*4.3.4. Road Fund (RF)*

The RF revenues in 2007 grew by 10.5% compared to the previous year, while expenditures grew by 20.2% which resulted in a deficit of 0.3% of the GDP. Transfers from the central budget accounted for 50.2% of the total RF revenues. On the expenditure side, investments accounted for 52.1% while 23.3% were intended for road maintenance.

## 4.4. Balance of the central budget and budgets of the funds

In 2007 trends in the fiscal sector resulted in a surplus of the central budget, accounting for 0.21% of the GDP. PDF and HIF had a surplus in their activities of 0.37% i.e. 0.23% of the GDP. The Employment Agency of the Republic of Macedonia (EA) had a minor deficit of 0.005% of the GDP, while the RF deficit reached 0.28% of the GDP.

**Chart 4.8.** Total revenues and expenditures of extrabudgetary funds (% of GDP)




Source: MoF

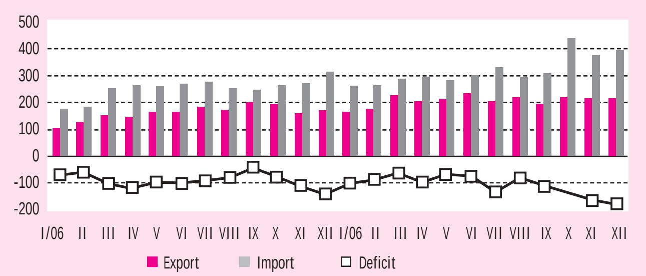
# 5. EXTERNAL SECTOR

## 5.1. Balance of payments

### *5.1.1. Current account*

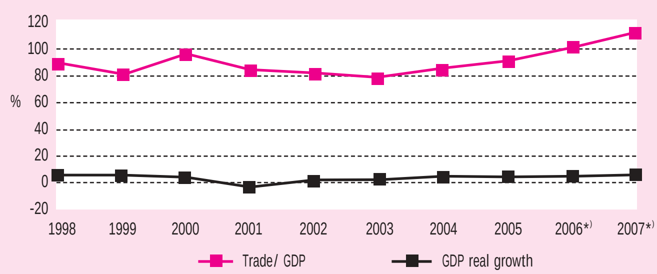
Foreign trade in 2007 in the Republic of Macedonia was fully affected by global trends. The depreciation of the US dollar on the global foreign currency markets and the price growth on the global commodity stock markets continues (see Item 1.2. Prices on the global commodity markets)[9]. Especially influential for the Macedonian economy was the crude oil price growth, as well as the rising prices of the most significant Macedonian export goods - lead, nickel and copper. The price of lamb, another significant Macedonian export commodity, grew minimally. There was a slight decline of the stock market price of zinc and cold-rolled and hot-rolled steel sheets. At the same time, foreign trade continued in conditions of high liberalization and a free trade zone was created in the region.

**Chart 5.1.** Export, import and realized deficit (in million of euros)




Source: State Statistical Office

**Chart 5.2.** Rate of trade openness and real GDP




Source: State Statistical Office

According to the preliminary data on the balance of payments, the **current account deficit** (f.o.b) in 2007 grew by EUR 119 million and amounts to EUR 164 million. Accordingly, the share of the balance on the current account in GDP is 2.9% which is around 2 percentage points more compared to last year.

From the aspect of certain groups of products, the largest contribution to the larger foreign

9) US$ in relation to Denar depreciated by 10.3% in the period 31.12.2006 - 31.12.2007

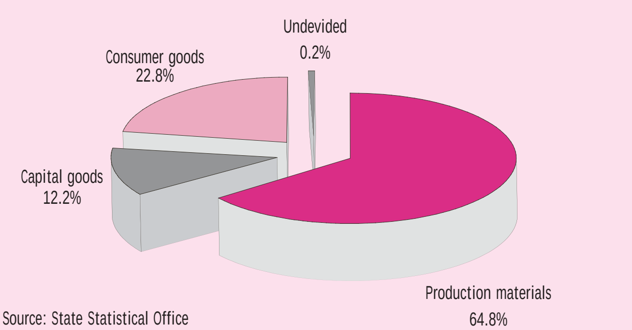
trade deficit has the higher deficit in the exchange of energy and equipment the share of which in 2007 reached 10.6% and 7.4% respectively of the GDP (with regard to the share of both groups of 8.4% and 5.8% in 2006) which points to the technological and energy dependence of the Macedonian economy. To this end, growth of the commodity exchange of 27.5% in relation to the last year points to the integration of the country in global trade and its openness increases even more. Thus, **the rate of trade openness** as from 2003 shows a tendency to increase and in 2007 it grew by 14 index points compared to 2006 and reached 109.8%.

In such conditions, in 2007 for the production of EUR 1 of GDP, the Macedonian economy needed to import 68 cents and to export 54 cents. This ratio in 2006 was 48. i.e. 38 cents, respectively.

**Export of goods.** According to the previous data for 2007 the Macedonian economy for the first time after it gained independence exported over 50% of the GDP. The export per capita of the Republic of Macedonia in 2007 is EUR 1,195 which is an increase by EUR 262 per capita or 28% in relation to 2006. Also, the total cumulative export of goods in 2007 compared to 2006 expressed in euros grew significantly by 28.3% and amounts to EUR 2,446 million. Higher export is a result of the larger production activity of the Macedonian production facilities, the higher volume of goods for export and the favorable price situation on the global markets with the prices of metals in conditions of high global demand.

The analysis of *export according to the economic purpose of products* points to increase in the products for reproduction by 36.7% in relation to 2006 as well as their structural increase in the total export by 3.8 percentage points. The same is due to the higher export of raw materials and semi-finished goods (EUR 436 million) of the production of base metals. Due to the price growth on the global stock markets, in conditions of growth of the exported quantities of raw materials and semi-finished goods by 24% the export value of these products grew in nominal terms (expressed in euros) by 55%. Regarding consumer goods, there was relatively high growth of the export of clothes and footwear (EUR 66 million or 15%), of food (EUR 28 million or 19%) and beverage and tobacco (EUR 8 million or 11%). Due to the temporary halt of the export to Kosovo in April 2007 the export of oil and oil derivatives declined, but despite the decline, the export of this product has significant position in the structure of total export of the country in 2007.

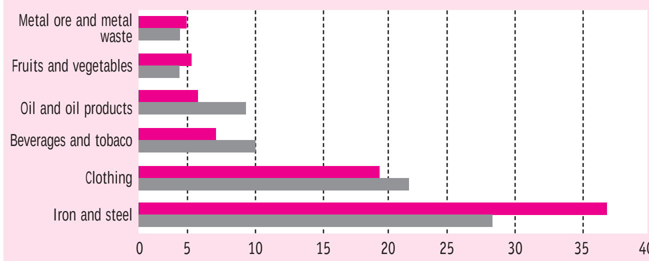
**Chart 5.3.** Structure of imports by economic usage




Source: State Statistical Office

The regional orientation of the commodity exchange in 2007 continues the export growth trend of goods to the European Union. Thus, expressed in euros, the export to the EU grew by 36.7%. Observed by countries, the export is largely focused in five countries: Serbia, Germany, Greece, Italy and Bulgaria, with a share of 63.5% in the total export of the country. The highest export growth was achieved to Spain (225%), Belgium (98%) and Italy (34%). This export growth to these countries is a result of the higher export of ferro-nickel which is a combined effect of the growth of the stock market prices and higher export quantities. High growth of 71% was noted in the export to Bulgaria, above all, due to the higher export of non-stemmed tobacco and cold-rolled products, non-plated, in coils or not, and the 18% growth of the export to Germany is due to the higher export of textile, iron, steel and ferro-nickel.

**Chart 5.4.** Export of main products according to SITC, 2006-2007 (structure in %)




Source: State Statistical Office

If we analyse the share of the products according to SITC[10] it can be noted that iron and steel have the highest share in the export - 37.7% (72% growth in 2007), clothes with 18.9% (export growth by 11% compared to 2006), oil and oil products with 4.7%, fruits and vegetables with 4.2%, metal ore and metal scrap with 3.8% (6% growth compared to 2006) etc. The higher share of iron and steel and metal ore and metal scrap in the total export is due to the higher prices on the global stock markets, but also to the higher exported quantities. In 2007 exported goods in the first 10 production groups according to SITC amount to around EUR 2,026 million which is around 83% of the total export of the country and the remaining 56 product groups account for only 17% of the total export.

**Table 5.1.** Export of the first ten products according to SITC

| Rank | SITC | Products | Kg. | Euros | Value share in % |
|---|---|---|---|---|---|
| 1 | 67 | Iron and steel | 1,119,218,913 | 921,230,079 | 37.7 |
| 2 | 84 | Clothing | 24,042,290 | 462,772,918 | 18.9 |
| 3 | 33 | Oil and oil products | 244,035,972 | 114,853,184 | 4.7 |
| 4 | 05 | Fruit and vegetables | 373,929,188 | 103,460,688 | 4.2 |
| 5 | 28 | Metal ore and metal scrap | 281,846,563 | 92,166,462 | 3.8 |
| 6 | 12 | Tobacco and tobacco processed goods | 25,949,552 | 77,001,637 | 3.1 |
| 7 | 11 | Beverages | 172,837,334 | 74,027,765 | 3.0 |
| 8 | 66 | Items from non-metal minerals | 757,128,694 | 69,944,750 | 2.9 |
| 9 | 85 | Footwear | 2,622,669 | 60,868,187 | 2.5 |
| 10 | 60 | Electric machines and parts | 18,705,544 | 49,383,963 | 2.0 |
| | | Total more important products | 3,020,316,720 | 2,025,709,635 | 82.8 |
| | | **Total Export of the RM** | **3,600,269,959** | **2,446,356,984** | **100.0** |

Source: State Statistical Office

10) Standard International Trade Classification

High dependence on imported raw materials, poor production diversification and small export quantities without a standardized quality are still the features of exports, making the Macedonian exporters marginal partners. Still, the majority of Macedonian export products base their competitiveness on prices, not quality. An additional negative effect over the Macedonian export is also the inexistence of high-quality marketing in the Macedonian industry and disorganized appearance of the Macedonian foreign trade companies on the foreign markets. The industrial structure is still dominated by products in the low phases of processing, such as: tobacco, vegetables, lamb, zinc, ferro-nickel and ferro-silicon.

The value of **total imported goods** in 2007 is EUR 3,795 million i.e. by EUR 807 million more (or 27%) in relation to 2006. Import growth is above all due to the growth of import of: electricity (by EUR 130 million or 261.8%), iron and steel, (EUR 102 million or 35%), metal ore and metal scrap (EUR 97 million or 169%), road vehicles (EUR 70.5 million or 43%), telecommunication devices (EUR 47 million or 73%) textile yarn and similar items (EUR 40 million or 14.7%), etc. Although in 2007 the quantity of oil and oil derivatives imported slightly declined by 26% or EUR 46.7 million less than the previous year, still, this product shows the largest share in the country 12%.

**Table 5.2.** Import of oil and oil products (million)

| | 2004 | 2005 | 2006 | 2007 | Balance 2007 - 2006 | Rates |
|---|---|---|---|---|---|---|
| **Kilograms** | 1,112.3 | 1,229.8 | 1,323.9 | 1,226.4 | -97.5 | -7.4 |
| **Euros** | 254.8 | 395.7 | 497.4 | 459 | -38.5 | -7.7 |
| **Denars** | 14,618.2 | 24,253.9 | 30,436.8 | 28,080.3 | -2,356.5 | -7.7 |
| **Denar/Euro** | 61.3377 | 61.2958 | 61.1885 | 61.1835 | | |

Source: SSO; calculation: MoF

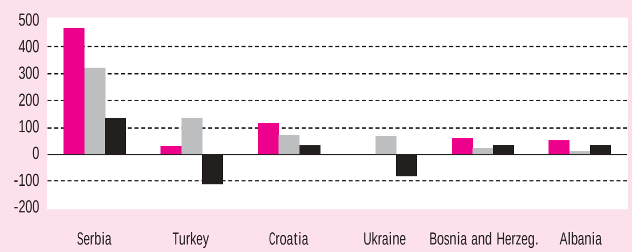
A major part of the imported products, above all, crude oil, machines and equipment, vehicles, part of the raw materials for the industry and some household consumables are not produced in the Republic of Macedonia. The import of crude oil, machines and equipment and vehicles was 32% of total import or 22% of GDP.

Despite the introduced new environmental standards as a condition for the import of used cars, applicable as of January 2007 there was a higher import of used and new vehicles, and their share in the total import is almost at the same level as in 2006 and is 6%. According to the analyses during this year, the value of the imported passenger vehicles (EUR 119.9 million) is 6 times higher than the value of the imported used passenger vehicles (EUR 18.9 million) showing that most of the potential buyers of passenger vehicles in the country, according to their standard, opt for new passenger vehicles.

*Analyzed by activities,* the highest share in import goes to goods related to production of energy raw materials (15.6%) followed by production of base metals (12.5%) production of food and beverages (9.9%), production of textile (9.1%) production of chemicals and chemical products (8.9%).

*Observed by regions,* the largest import was from the developed countries, and within those frameworks, the import from EU member states accounts for 44% of the total import in the Republic of Macedonia. Deficit in the exchange with the EU member states was EUR 286 million, which was almost 21.2% of the total trade deficit of the country, and with the EFTA member states was EUR 76.4 million, with 5.6% share.

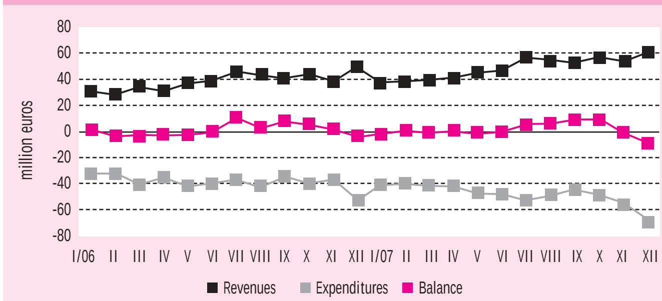
**Chart 5.5.** Foreign trade with countries with FTA's




Source: State Statistical Office

After a few years of upward trend, in 2007 for the first time the foreign trade balance with certain countries with which we have signed free trade agreements is positive. Thus with Bulgaria joining the EU the trade deficit significantly declined from EUR 95 to EUR 18 million. The exports of the Republic of Macedonia to this country in 2007 grew significantly by 71% while imports declined by 2%. But with certain countries (Ukraine and Turkey) of this group, the trade deficit continued.

**Chart 5.6.** Revenues, expenditures and balance of services




Source: State Statistical Office

If the subject to analysis is the *currency structure of export and import of goods,* share of euro in the overall export in 2007 declined by 3 percentage points while the share of US$ is larger in the total export, while the import shows opposite tendencies, the share of euro grew by 1.4 percentage points while the share of US$ declined also by 1.4 percentage points. Due to the dependence on import raw materials on one hand and small domestic market and still insufficiently competitive products on the other, part of the Macedonian exporters, despite the depreciation of the US$ did not have any choice but, despite the consequences, to accept to export in US$, i.e. to import in euros. Hence, a priority task of the Macedonian economy remains to focus all capacities towards development of a structured and high-quality competition, whereby price-based competition will not be a priority. In estimating the export results in euros, one should take into account that part of it is underestimated as a result of the more intensive increase of the part of exports in US$ (56%) and the depreciation of the US$ exchange rate towards the euro and the domestic currency in 2007.

The higher volume of trade in the past several years did not help the Republic of Macedonia in reducing the trade gap. According to the movements in the export and import of goods in 2007, the **foreign trade deficit,** expressed in euros was EUR 1,348 million, which is 24.3% of GDP.

In the area of services in 2007 the *inflow and outflow of funds on the basis of services,* grew by 24.5% and 24.9% respectively which led to an almost identical absolute growth by EUR 117 million in inflow and EUR 113.6 million in outflow. Hence, the balance of services improved further by EUR 3.4 million. In the total amount the balance amounts to EUR 25.5 million which is 0.5% of GDP.

This situation is above all, a result of the higher positive balance from the inflow and outflow on the basis of travel - tourism (31.4% growth compared to 2006). The balance of inflow and outflow on the basis of transport this year is also negative and in relation to 2006 it is higher by EUR 10 million. With regard to other services, there is a relative increase (by EUR 16.6 million) in the inflow of investment activities.

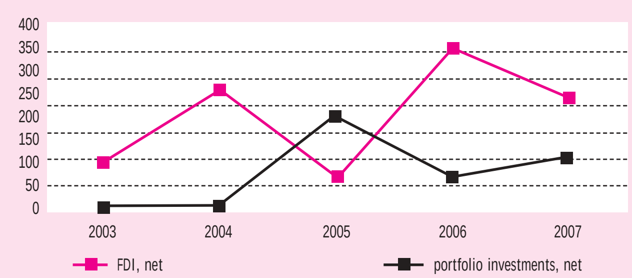
The generated income balance has improved compared to the last year, but still there is a deficit of EUR 26.4 million which negatively affects the current account balance. There is an annual increase of the outflow of funds on the basis of transfer of the generated profits (payment of dividend by TELEKOM) to foreign investors by EUR 45 million (or by 93%) which significantly contributed to the deficit in the income balance. At the same time, as a result of the higher number of resident employees in non-resident companies, there were higher foreign exchange inflows on the basis of resident employed persons by EUR 22 million or 40.3%. Despite the fact that the interest balance does not show significant changes, it is important to mention that in 2007 the trend of reduction of net outflows of funds on the basis of interest continued, in conditions of slow increase of the paid interest towards foreign creditors and more intensive increase of inflows from interest to official foreign currency reserves and deposits of the commercial banks abroad.

Net current transfers grew in 2007 and prevented the high trade deficit leading to high current account deficit. Within this context, in 2007 the continuous trend of growth of net foreign currency funds on the basis of transfers continued, above all, as a result of the more intensive growth of the net inflows in private transfers (6.7% growth) reaching EUR 985.8 million. Within this framework, according to the data from the survey on the private transfers, the majority of private transfers resulted from the relatively high net inflow of foreign currency on the basis of exchange operations. The net inflow on the basis of exchange operations in 2006 was EUR 649.5 million (70.4% of total private transfers), and in 2007 EUR 695.4 million (or 71% of total private transfers). Growth of net inflows on the basis of exchange operations in recent years explains that most of the total growth is from private transfers.

*5.1.2. Capital and financial account*

The capital and financial account of the balance of payments in 2007 has a positive balance in the amount of EUR 194.3 million meaning growth by EUR 156.3 million in relation to last year. The realized volume of transactions is almost fully from the financial account. Thus, *net transactions in the capital account* of the balance of payments amount to EUR 1.3 million which resulted in a higher foreign currency inflow by EUR 2.1 million compared to the previous year. Within the *financial inflows, net,* there is a dominant share of net inflows on the basis of *foreign direct investments* of 81.5% or in the amount of EUR 240.1 million (see Chart 5.7.) which were a significant source of financing of the deficit of the balance of payment current account. The share of foreign direct investments in the GDP in 2007 is 4.3% and is 2.5 percentage points lower compared to last year. Out of the total direct investments in the country, (EUR 239 million) EUR 35 million were observed in capital, EUR 94 million were reinvested profits and EUR 110 million were other capital. FDIs in 2007 are mainly focused on the financial sector, telecommunications, and production (food processing). France, Austria, Slovenia and Serbia were the largest investors in the Republic of Macedonia in 2007.

**Chart 5.7.** Foreign direct and portfolio investments in Republic of Macedonia (in million of euros)




Source: National Bank of RM

In conditions of higher interest by foreign investors to purchase securities in the Macedonian companies which grew by 78.8% in relation to last year, can be seen also through the more intensive activities on the Macedonian stock exchange. There is further *inflow of portfolio investments* (growth by EUR 37.7 million or by 51.6% compared to 2006) whereby the amount reached EUR 110.8 million. However, despite liberalization inflows from portfolio investments are relatively low and mainly from former Yugoslav republics due to the still insufficiently developed financial market, the small range of financial instruments as well as the perception of risk by foreign investors.

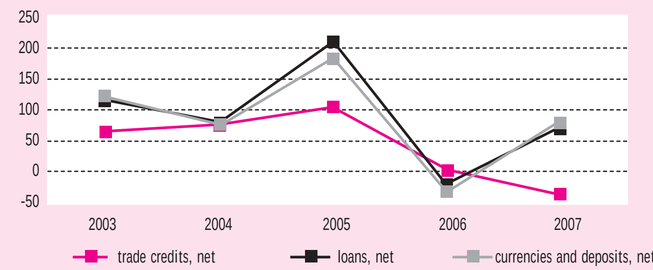
The item *other investments* in 2007 shows a negative balance of around EUR 56 million.

Trends of trade credits, loans and currencies and deposits as integral parts of this item are shown in Chart 4.8. In 2007 trade credit (net) also have a negative sign and an amount of EUR 33.5 million whereby for import of goods credit were used in the amount of EUR 136 million, while approved credit for the export of goods amounted to EUR 148.5 million.

Net loans are negative and amounted to EUR 108 million. This mainly points to a higher repayment of loans from foreign creditors, whereby outflow exceeds inflow, i.e. on the basis of medium-term and long-term credits, around EUR 410 million have been repaid, the repayment of due outstanding liabilities amounted to EUR 18 million, and on the basis of short-term credit, liabilities amounted to EUR 20 million, while loans were used in the amount of EUR 300 million.

Contrary to the trends in 2006 when currencies and deposits had a negative sign and high amount of EUR 83.7 million in 2007 they were noticed to have a positive balance of EUR 6 million as a result of the difference of the positive amount of net foreign currency funds from banks of EUR 68.4 million and the outflow on the basis of other sectors, i.e. foreign currency funds of the population, net, of EUR 62.2 million.

**Chart 5.8.** Other investment (in million of euros)

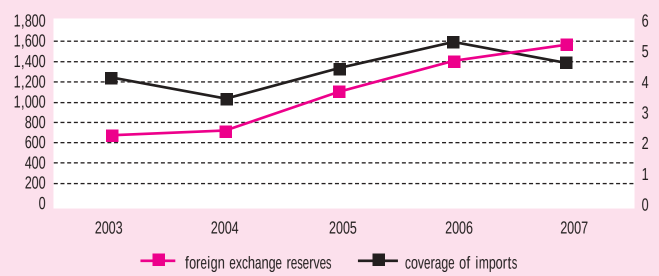



Source: National Bank of RM

### *5.1.3. Foreign exchange reserves*

Certain favourable trends in the current and capital and financial transactions in 2007 resulted in further growth of foreign currency reserves of the country despite their fluctuation by months. Thus, trends on the foreign exchange market, in conditions of a stable denar foreign exchange rate policy resulted in net repurchase of foreign currency on the foreign exchange market, due to the high supply compared to the demand for foreign currency and tendencies for appreciation of the denar nominal exchange rate.

**Chart 5.9.** Foreign exchange reserves and monthly coverage of imports




Source: National Bank of RM

In 2007, the National Bank (NBRM) maintained the existing frame of the types of instruments in which it invests the foreign currency reserves starting from bank deposits, state debentures (bills and bonds) debentures of international financial institutions, and other instruments with a fixed yield, including repo-transactions and instruments on the money market. In accordance with international trends for management of foreign currency reserves the NBRM continued the diversification of the investment portfolio so as to increase investments in securities, thus reducing the credit risk.

In 2007 gross foreign exchange reserves grew by EUR 101.8 million and they amounted to EUR 1,524.4 million, which is 4.7-month coverage of import of goods (f.o.b.) and services for the next year in the Republic of Macedonia (in 2006 the coverage was 5.3.). Compared to 2000 the level of foreign currency reserves was double.

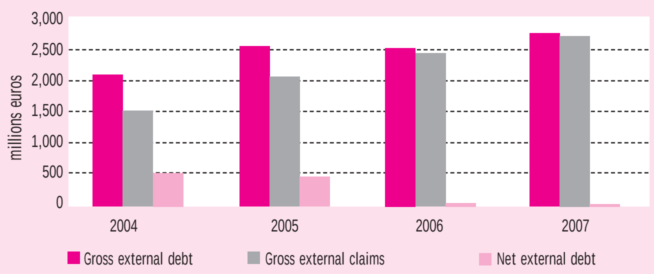
Observed by quarters, in Q1 of 2007 foreign currency reserves remained stable, despite the early repayment of a significant part of the debt towards the Paris Club of creditors. In Q2 as a result of the significant redemption of foreign currency on the foreign exchange market, the level grew, but due to the early redemption of the debt towards the World Bank and the IMF at the end of the quarter the level of foreign currency reserves declined. In the remaining part of the year (second half) the level of foreign currency reserves continued to grow and by the end of the year there were significant outflows for payments of the country abroad.

In 2007 the item errors and omissions had a negative sign and amounted to EUR 30.3 million pointing to an unidentified outflow of foreign currency in 2007.

## 5.2. External debt

**Gross external debt**[11] of the Republic of Macedonia in 2007 grew by 8.6% compared to 2006 as a result of the growth of the debt in the banking sector and other sectors (non - banking financial intermediaries, non-financial companies, households and non-profit institutions). Gross external debt in 2007 amounted to 48.3% of the GDP, while in 2006 it was 50.5%.

**Chart 5.10.** Gross and net external debt




Source: National Bank of RM

In *the public sector* (public authorities and their agencies, government units at all level - central, local and social funds) gross external debt declined by 14.7% as a result of the early repayment of the debt. Debt declined by 16.9% was noted on the basis of long-term loans, and 4.6% on the basis of bonds. One should mention that for the first time in 2007 there was short-term debt in the government sector in the amount of EUR 7.6 million.

11) Ensuring international comparability of data, gross external debt is a stock of all future liabilities of residents towards non-residents, including liabilities upon principal, due outstanding liabilities upon principal and interest and calculated late interest, regardless of the type of instrument and maturity.

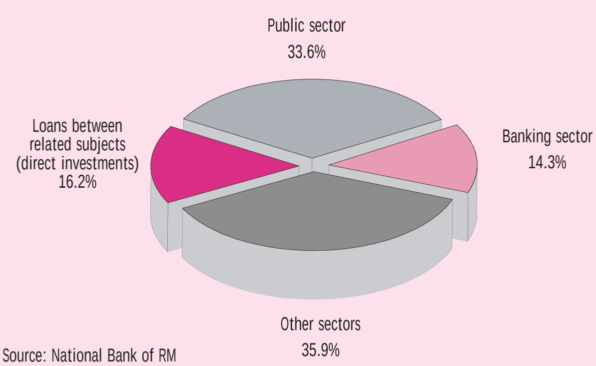
In the *banking sector* (financial intermediaries collecting deposits and extending credits) gross external debt grew by 43.7% whereby long-term debt grew by 37.6% and most of the growth is a result of the growth of debt on the basis of loans. Short-term debt in the banking sector grew by 52.9% as a result of the growth of debt on the basis of currencies and deposits.

The financial crisis in the second half of 2007 in the USA (see Box 1.1.) created overflow effects on all segments on the markets and institutions in the financial system, which additionally underlined the credit risk. Trends on the international markets were affected by the mortgage crisis in the US, which expanded on the market of structured products, with significant effects on the international money market. In conditions of intensified turbulence on the international financial markets, certain foreign commercial banks faced bank losses on credit, liquidity declined and could not continue financing. Uncertainty with regard to the level of losses, as well as indications for the change of credit rating of certain commercial banks was assessed as higher credit risk. In these terms, since the beginning of August 2007 investments started being disbursed from the commercial banks and shifted to investments in the central banks.

In the *other sectors,* gross external debt grew by 23.8% as a result of the growth of the short-term debt by 42.3%, while long-term debt in other sectors is almost at the same level as in 2006. The trend of increases of debt in these sectors is due to the improvement of the credit rating and intensified economic activity and a greater need of foreign capital in the private sector. Within the short-term debt in this sector, the debt grew regarding commercial credit by 26.6% and there is almost a double increase of debt on the basis of outstanding liabilities. Loans to associated entities in 2007 are higher by 33.5% above all as a result of the growth of liabilities towards direct investors.

In 2007 in gross external debt there were structural shifts compared to the previous year, whereby the share of the debt in the government sector declines, while it increases in the banking sector and other sectors (see Chart 5.11.). External borrowing of other sectors has a dominant share (mostly of non-financial companies) of 35.9% in the gross external debt, where commercial credit and used long-term loans accounted for most of it. External borrowing of the government sector accounts for 33.6% of the gross external debt, contrary to 42.7% in 2006. This is a result of the used long-term loans from abroad and

**Chart 5.11.** Structure of gross external debt by sectors

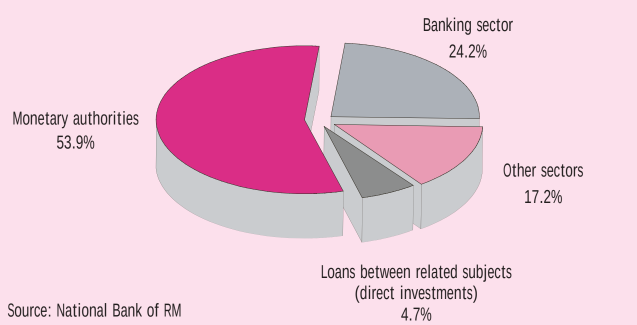



Source: National Bank of RM

issued Eurobonds. Total external borrowing of the banking sector accounts for 14.3% in the total gross external debt and is mostly determined by used long-term loans and liabilities upon deposits of non-residents. With regard to the external borrowing of the monetary authorities (NBRM) which is fully a result of the used credits from the IMF, full early repayment of debt was made in 2007.

**Gross external claims**[12] are by 10.5% in relation to 2006. Claims in other sectors grew by 37.2% (non-banking financial intermediaries, non-financial companies, households and non-profit organizations) mostly due to the growth of commercial credit. Claims of monetary authorities grew by 8.9% as a result of the claims on the basis of bonds, while claims of the banking sector declined by 3%.

**Chart 5.12.** Structure of gross external claims




Source: National Bank of RM

From a structural aspect regarding gross external claims, claims of monetary authorities have a dominant shares (53.9%) resulting from the currencies and deposits as components of gross official reserves. External borrowings of the banking sector account for 24.1% of the gross external claims. Observed by certain types of instruments, external borrowings of this sector mostly resulted from the relatively high level of currencies and deposits of domestic banks abroad (accounting for around 95% of the total claims of the banking sector). Other sectors (mostly non-financial companies) accounted for 13.9% in gross external claims. For certain types of instruments, external claims of this sector result mostly from the relatively high amount of approved short-term commercial credit.

**Net external debt**[13] of the Republic of Macedonia at the end of 2007 amounted to EUR 30.4 million, a 55% decline compared to 2006. Net external debt amounted to around 0.05% of the GDP, while in 2006 it was 1.4%.

On a net basis in 2007 the monetary authorities (NBRM) was net creditor from abroad in the amount of EUR 1,445.5 million which is 12.5% more than the net claims in 2006. The banking sector is also a net creditor of EUR 260.1 million, mostly on the basis of currencies and deposits on short-term debt. The government sector and other sectors are net borrowers from abroad in the amount of EUR 910.4 million and EUR 512.7 million. Net debt of the government sector was reduced by 15% in relation to 2006 as a result of the reduction of long-term loans. In the other sectors, due to the growth of the short-term debt, net external debt grew by 17.9% and long-term debt is almost the same as in 2006.

12) Gross external claims are stock of all current and unconditional claims on the basis of debentures of residents towards non-residents

13) Net external debt is defined as difference between the stock of gross external debt and gross external claims.

*The maturity structure* of total net debt is relatively favourable with regard to the fact that the liabilities of the country are long-term and the resources of the monetary authorities are mostly short-term and liquid. Liabilities of the banking sector are mostly long-term while currencies and deposits are extended as short-term loans.

The Republic of Macedonia, with its gross external debt of 48.3% and 0.05% net debt as percentage of the GDP, shows the lowest level of indebtedness compared to other countries in the region.

## 6. PUBLIC DEBT OF THE REPUBLIC OF MACEDONIA

The Public debt of the Republic of Macedonia is composed of the government debt and all financial liabilities created by the borrowing of the municipalities and the city of Skopje, as well as of the public enterprises and the companies, being in entirely or dominantly state owned.

In 2007, the Public debt of the Republic of Macedonia was reduced by EUR 248.3 million (from EUR 1,831.8 million in 2006 to EUR 1,583.5 million at the end of 2007) and as a percent of the GDP amounted to 29.02% (36.4% in 2006).

The decrease resulted in the early buyout of the debt during 2007, by means of using the deposits of the Government of the Republic of Macedonia, and aimed at decreasing the interest costs for its servicing, as well as improving the portfolio properties by decreasing the exposure to risks. The subject-matter of early buyout were liabilities to the Paris Club of Creditors, part of the liabilities to the International Bank for Reconstruction and Development and European Investment Bank, liabilities to the International Monetary Fund and the structural bond for rehabilitation of Stopanska Banka A.D. - Skopje, amounting to EUR 233.9 million.

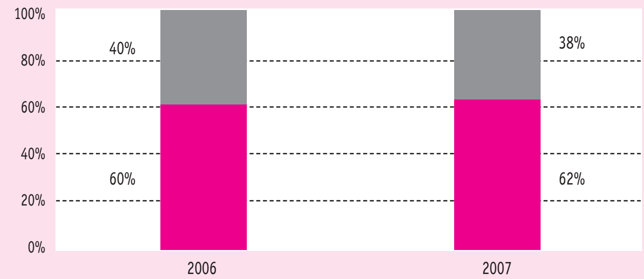
**Table 6.1.** Total public debt according to GFS methodology and according to the Public Debt Law (in million of euros)

| **Basis** | **31.12.2005** | **31.12.2006** | **31.12.2007** |
|---|---|---|---|
| EXTERNAL DEBT | 1,441.16 | 1,223.,01 | 1,027.86 |
| General government debt | 1,245.35 | 1,025.19 | 877.22 |
| Central Bank | 52.66 | 42.39 | 0.00 |
| Public Enterprises | 143.15 | 155.42 | 150.64 |
| DOMESTIC PUBLIC DEBT | 750.39 | 806.48 | 899.95 |
| General government debt | 603.66 | 648.42 | 552.80 |
| out of which Treasury bills for monetary purposes | 0.00 | 75.93 | 75.47 |
| Central Bank | 146.74 | 155.26 | 344.32 |
| Public Enterprises | N/A | 2.80 | 2.83 |
| TOTAL PUBLIC DEBT (GFS methodology) | 2,191.55 | 2,029,49 | 1,927.81 |
| Total public debt as % of average GDP | 46.87 | 40.22 | 35.33 |
| General government debt | 1,848.81 | 1,673.61 | 1,430.02 |
| Total public debt as % of GDP | 39.54 | 33.17 | 26.21 |
| Total public debt pursuant to the Public Debt Law | 1,992.16 | 1,831.83 | 1,583.48 |
| (with included treasury bills for monetary goals) | | | |
| Total public debt as % of average GDP | 42.60 | 36.30 | 29.02 |

Source: MoF

In 2007, favourable changes in the **interest structure of the total public debt** were achieved. In line with the National Methodology, total public debt with a fixed interest rate amounted to EUR 989.5 million, i.e. it amounted to 62.5% in the total public debt at the end of 2007, increasing by 2.5 percentage points compared to 2006.

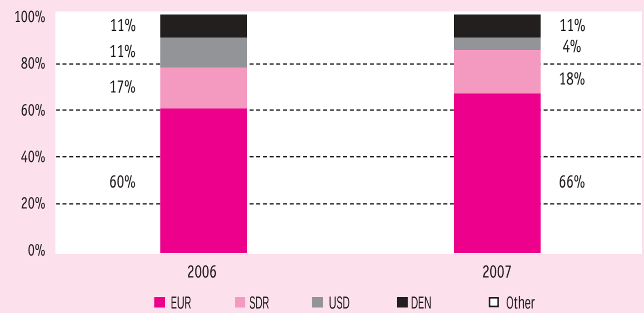
**Chart 6.1.** Interest rate structure of the total public debt




Source: MoF

During 2007, the **currency structure of the public debt** also exhibited positive changes in order to increase the share of the euro-denominated public debt. Thus, as a result of the early buyout, the euro-denominated debt increased by 5.6 percentage points compared to 2006, amounting to 65.8% at the end of 2007, leading to a decrease in the dollar-denominated debt by 6.8 percentage points. Domestic-currency denominated debt noted a slight decrease by 0.3 percentage points (from 11.4% to 11.1%) due to a decrease in the net issue of continuous government securities amounting to EUR 10 million, a decrease of the treasury bills for monetary purposes in the amount of EUR 0.46 million as well as the early buyout of the bond for rehabilitation of Stopanska Banka A.D. - Skopje, denominated in denars in the amount of EUR 21 million.

**Chart 6.2.** Currency structure of the total public debt




Source: MoF

## 6.1. Continuous government securities

### *6.1.1. Primary Market for Government Securities*

In 2007, due to the favourable budget stance, i.e. the budget surplus in the course of the whole year, the stock of **issued government securities** amounted to Denar 4.96 billion, a decrease of about Denar 0.7 billion compared to the stock in 2006, when it amounted to Denar 5.66 billion.

In 2007, 3, 6 and 12-month treasury bills (TB) were issued, as well as three issues of 2-year government bonds (GB) and one issue of 3-year government bonds. When creating the policy of government securities, the increase of their maturity was particularly emphasized, i.e. higher amounts of government securities with longer maturity were offered, compared to the amounts offered in 2006.

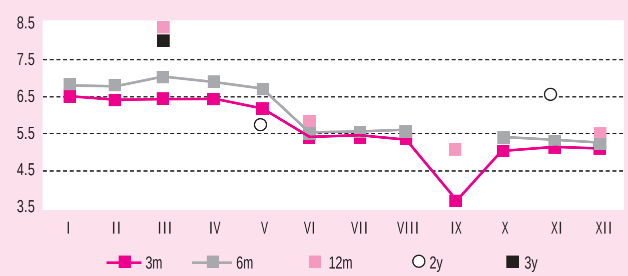
**Table 6.2.** Net issue of continuous government securities (in million of euros)

| | Q1-2007 | Q2-2007 | Q3-2007 | Q4-2007 | Total 2007 |
|---|---|---|---|---|---|
| Net issue continuous government securities | 17.69 | 57.73 | -48.97 | -21.30 | -10.09 |
| 3 - month TB | 9.30 | 40.72 | -35.28 | -19.00 | -4.26 |
| 6 - month TB | 1.78 | -0.75 | -11.04 | -3.14 | -13.15 |
| 12 - month TB | 2.52 | -1.24 | -2.65 | -4.61 | -5.98 |
| 2 - year TB | 4.08 | 0.24 | | 5.45 | 9.77 |
| 3 - year GB | | 3.52 | | | 3.52 |

Source: MoF

**Interest rates on government securities in 2007,** compared to 2006, on average declined by 1 to 2 percentage points, depending on their maturity. For instance, the average weighted interest rate on 3-month treasury bills decreased by 1.11 percentage points, i.e. it was 6.26% in December 2006, while the one attained at the auctions in December 2007 was 5.15%. The interest rate on 6-month treasury bills was 7.02% at the last auction in 2006, decreasing by 1.78 percentage points during 2007 i.e. it was 5.24% at the last auction in 2007.

**Chart 6.3.** Weighted interest rates achieved at government securities auctions




Source: MoF

The same trend in the interest rates on 12-month treasury bills was also observed, these decreasing by 3.36 percentage points during 2007, i.e. the weighted interest rate attained at the last auction in 2006 was 8.86%, while it was 5.50% at the last auction in 2007. A downward trend was also observed in the interest rates on government securities with longer maturity. Thus, coupon interest rates on 2-year government bonds declined by around 2.5 percentage points in 2007 compared to 2006, while the interest rate on 3-year government bonds decreased by around 1.5 percentage points compared to 2006.

*6.1.2. Secondary market for government securities (GS)*

During 2007, the development of the primary market was accompanied by the secondary trading with government securities. Trading was observed at the Macedonian Stock Exchange AD Skopje and on the Over-the-Counter-Market.

A novelty was the modifications of the Rules on the Manner and the Procedure for Trading and Settlement of Transactions with Securities Over-the-Counter Markets ("Official Gazette of the Republic of Macedonia" no. 14/07). In order to promote the trading with government securities on the OTC Market, the National Bank of the Republic of Macedonia in cooperation with the Ministry of Finance made certain changes in the rules on the manner and procedure for trading and settlement of transactions with securities over the counter markets, thus introducing a mandatory listing for the government securities in the amount of Denar 1,000,000. Mandatory listing for treasury bills began as of 1st March 2007, while the mandatory listing for government bonds was introduced on 1st September 2007. Compared to 2006, 24 **transactions in treasury bills** were executed on the OTC market in 2007, an increase by 5 transactions compared to 2006, while the nominal trading amount accounted for Denar 506.76 million, an increase of Denar 435.7 million compared to 2006. In the same period, 109 **transactions in government bonds** were executed on the over-the-counter market, being an increase by 11 transactions compared to 2006, while the nominal trading amount was Denar 693.31 million, an increase by around Denar 186 million compared to 2006.

## 6.2. Credit rating of the Republic of Macedonia in 2007

In 2007, Republic of Macedonia was evaluated by three international credit rating agencies: Standard & Poor's, Fitch and Japanese Credit Rating (for the first time), awarding credit rating to the country. Credit rating grades, which the Republic of Macedonia received in 2006 and 2007 are shown in Table 6.3.:

**Table 6.3.** Credit rating of the Republic of Macedonia

| | Credit Rating Agency Standard & Poor's | | Credit Rating Agency Fitch | | Credit Rating Agency Japanese Credit Rating |
|---|---|---|---|---|---|
| | 2006 | 2007 | 2006 | 2007 | 2007 |
| Foreign currency | BB+/Stable | BB+/ Stable | BB+/ Stable | BB+/Positive | BB+/ Stable |
| Domestic currency | BBB-/ Stable | BBB-/ Stable | BB+/ Stable | BB+/Positive | BBB-/ Stable |

Source: Standard & Poor's; Fitch; Japanese Credit Rating

The reports on evaluation of the credit rating of Republic of Macedonia by the three agencies emphasized the prudent macroeconomic policy, stable economic growth, observation of significant fiscal results and commencement of many structural reforms. Credit rating grades also pointed out the achieved progress in ensuring political safety, supported by the tendency towards accession of the Republic of Macedonia into the EU. Awarded grades for the credit ratings also reflected the structural rigidity, the challenges on the labour market, the limited fiscal flexibility and the remained political tensions between the political parties.

# 2007

# 7. MONETARY SECTOR

## 7.1. Monetary trends

During 2007, the National Bank of the Republic of Macedonia (NBRM) maintained the fixed Denar exchange rate in relation to euro as an intermediary target for achieving the primary goal - low and stable inflation. NBRM mainly realized the repurchase of the excess foreign currencies on the foreign exchange market **(due to the higher supply of foreign currencies and the upward pressure on the nominal denar exchange rate),** while it sterilized the effects of the foreign exchange transactions through a sale of central bank bills so as to maintain the price stability in the country.

In 2007, **the monetary base** increased by 21.8% annually, due to the increased liquidity of banks and the increased cash demand. In December 2007, the monetary base amounted to Denar 30,309 million, whereby the total liquid assets of banks amounted to Denar 12,373 (42.5% annual increase) while cash in circulation amounted to Denar 17,936 million (10.7% annual increase). In 2007, the monetary base, i.e. demand for cash and the liquidity in the banking system increased. There was higher demand of cash and increased liquidity of the banks during the holidays, while decreased demand for cash and liquidity in the banking sector in other periods (most often after the holidays).

**The narrowest monetary aggregate M1** composed of the transaction deposits (deposit money) and the cash in circulation increased highly by 31.7% annually in December 2007, mainly due to the high increase of deposited money, by 50.1% annually. A positive upward tendency of the share of deposited money was observed, due to the increasing frequent usage of payment cards (cash free payment), thus leading to an additional increase in the deposit base of the banks and decreasing the possibilities of the grey economy. Cash in circulation increased by 10.7% annually, but the share in M1 decreased due to the intensive increase of deposited money.

**The larger monetary aggregate M2,** including the narrow monetary aggregate M1 and quasi deposits (short-term deposits), in parallel with the increase of short-term liabilities of the banks, increased by 28.35% annually.

In December 2007, **the largest monetary aggregate M4,** including M2 and non-monetary deposits (long-term deposits), increased by 29.5% annually. Non-monetary deposits even though experienced high annual increases of 53.3%, they have had a small share in the deposit potential of the banking system due to the preferences of the economic agents for investing the funds in more liquid instruments. From the viewpoint of the liquidity risk of banks, the share of the non-monetary deposits was positive.

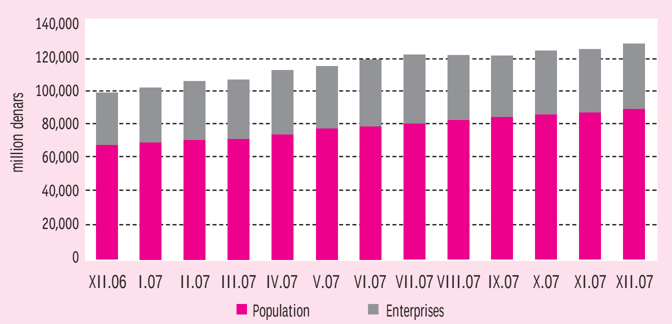
## 7.2. Total deposits

As a result of the higher income of economic agents, the increased propensity to save and partially due to the higher deposit rates, total deposit base of banks, exhibited a continuous increase during 2007. Thus, the total deposits of the non-government sector increased by 28.8% annually at the end of 2007.

From a **currency viewpoint,** an increase was registered in both the denar and the foreign exchange deposits. Denar deposits saw an intensive increase by 52% and as a result they observed a significant increase of the share in the total deposits (from 39.8% in 2006 to 47% in 2007). The increase of the denar deposits was due to the higher confidence in the stability of the domestic currency and the appropriate macroeconomic policy. In addition, the more attractive interest rate compared to that of the foreign exchange deposits was a significant factor for the high increase of the denar deposits. Foreign exchange deposits increased by 13.4% annually, exhibiting a decrease of the share in the total deposits, but remaining further dominant, 53% in the total deposits.

From the viewpoint of **the sectoral structure** of the deposits, households were the main surplus economic agent having a dominant share of 68.2% in total deposits. Increased income of households reflected in the deposit growth rate of this sector and amounted to 30.8% annually. Deposits of companies increased by 21.7% annually, whereby the denar and foreign exchange deposits of companies also increased by 29.1% and 14.2%, respectively.

**Chart 7.1.** Deposits of population and entreprises




Source: NBRM

In 2007, regarding **the term structure** of the deposits, the short-term and long-term deposits increased annually by 27% and 53.2% respectively, whereby, in line with the savers' request for higher liquidity, i.e. saving in more short-term instruments, the short-term deposits predominated.

## 7.3. Bank loans

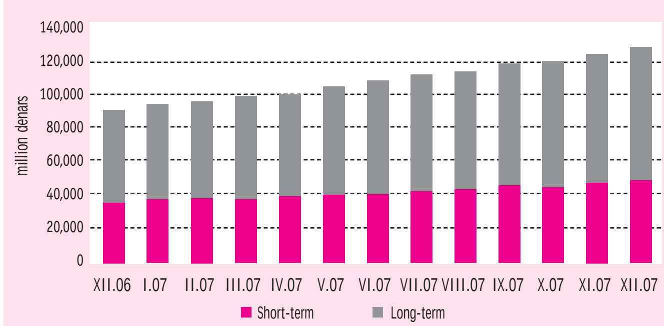
In parallel with the improved general conditions for crediting, the enriched supply of credit products, lower lending rates and higher loan demand during 2007, the credit activity of the banks exhibited a continuous increase. At the same time, positive expectations of the economic activity and increased deposit potential as a basis for credit growth increased loan supply by banks.

*Total loans of banks in the non-government* sector were Denar 124,862 million in December 2007, exhibiting a high growth rate of 39.1% compared to December 2006.

According to the **currency structure,** the denar loans dominated with 75.7% of the total loans to the non-government sector. At the end of 2007, they increased by 42.3% annually, attaining Denar 94,479 million. Foreign exchange denominated loans, however, increased by 30% annually, amounting to Denar 30,379 million. As a result of the intensive growth of denar loans, the foreign-exchange denominated loans decreased their share into total loans to 24.3% in 2007.

From the viewpoint **of the maturity structure,** long-term loans have had a dominant share, increasing at a rate of 44.5% annually, thus increasing their share at 61.7% of the total loans. Within the long-term loans, loans to households increased (48%) and loans to companies (41.5%), as well. Short-term loans increased by 31.1%, mainly due to the intensified crediting to households in the short run.

**Chart 7.2.** Credits to private sector by maturity




Source: NBRM

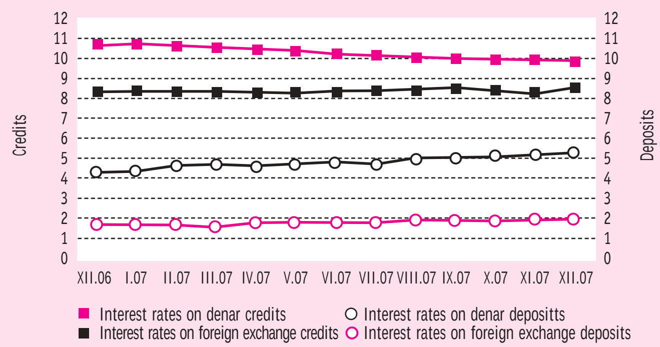
With regard to the **sectoral structure,** banks' orientation towards supporting companies through increased crediting was emphasized, thus loans to companies dominated with above 61% in the total loans. Expectations of the future economic growth encouraged banks to channel more funds towards companies and to continue to facilitate their access to credit. Loans to companies have increased by 29.7% annually, the long-term loans being dominant (56.4%), as a response to the need for higher investment in fixed assets. During 2007, households borrowed at different bases and households loans increased by 56.4% annually. The long-term borrowing also dominated in the household sector.

## 7.4. Interest rates

During 2007, under low and stable inflation, interest rates on Central Bank (CB) bills experienced a downward trend (with the exception of July and December, when interest rate increased).

In 2007, the average annual interest rate on CB bills was 5.1%, decreasing by 0.9 percentage points compared to 2006.

**Chart 7.3.** Interest rates of commercial banks




Source: NBRM

Interest rates on the denar credits, influenced by the intensified competition in the banking sector and the positive economic trends experienced continuous decline during 2007. In 2007, the average interest rate on denar credit was 10.2%, declining by 1.1 percentage points on an annual basis. In 2007, the average interest rate on foreign exchange credit was 8.4%, increasing by 0.3 percentage points compared to the last year.

During 2007, deposit interest rates experienced continuous increase, in line with the policy of banks for attracting deposits. Average interest rate on denar deposits increased from 4.7% in 2006 to 4.9% in 2007, while interest rate on denar deposits increased from 1.5% to 1.9%. Thus, the decline of lending interest rates and the increase of deposit interest rates narrowed interest-rate margins of banks, reflecting their improved operating efficiency.

In 2007, discount interest rate remained unchanged from the last year and was 6.5%. In June 2007, interest rates on Lombard loans experienced one-time decrease by 2 percentage points, i.e. from 9.5% to 7.5% maintaining the same level until the end of 2007.

## 8. FINANCIAL MARKETS AND INSTITUTIONS

### 8.1. Banking

The financial system of the Republic of Macedonia is characterized by the dominant role of the banking sector, participating with about 90% in the total assets of the financial system in 2007. At the end of 2007, the banking sector in the Republic of Macedonia was composed of 17 private banks of universal type, one fully-state-owned bank, having specific functions, hence, not competing with commercial banks, and 12 saving houses. Compared to 2006, the number of banks declined due to the withdrawal of the working license of one bank from the group of small banks. The analysis of the banking sector refers only to the banks, given the negligible share of saving houses, which possess only 1.3% of the total assets of deposit institutions.

Considering **the ownership structure of the banking system,** the share of the state-owned banks was below 7% in 2007, the state participating in the capital of 9 banks in total. The Macedonian Bank for Development Promotion AD Skopje was fully state-owned, in "Postenska banka" AD Skopje the state possessed one third of the issued common stocks, and has a minority share in the other 7 banks, below 5% of their totally issued stocks. The financial sector was particularly attractive to foreign investors. Thus, during 2007, the share of foreign capital in the total banking capital amounted to about 60%, hence retaining the increasing trend of the foreign capital. Foreign capital was present in 17 banks, out of which the majority share in 9 banks belonged to foreign owners (5 out of which were branch offices of foreign banks). Banks with dominant foreign ownership participated with about 50% in the total assets of the banking sector.

From the viewpoint of **the size of the banks,** the banking sector of the Republic of Macedonia included 3 large, 8 medium-sized and 7 small banks. In 2007, one small bank passed to the group of medium-sized banks, one ceased to operate. Hence, the number of small banks decreased. The three large banks have had a dominant market share, which increased in 2007. Large and medium-sized banks experienced an increase of the share in the assets, credits and deposits, while the market share of small banks decreased. Thus, in 2007, large banks participated in the total assets with 67.1%, medium-sized with 27.5% and small with 5.3%.

At the end of 2007, **total assets of the banking sector** were Denar 223,659 million, increasing by 28.5% annually, which almost entirely (92.5%) arises from the increased crediting to non-financial agents (increase by 43.1% annually) and the increase of funds invested in Central Bank bills by 122%. The other elements of the assets have had a very low or negative contribution to the increase of bank funds.

At the end of 2007, the most significant generator of assets' increases were **deposits of non-financial agents.** Deposits of non-financial agents were Denar 160,382 million, increasing by 28% annually. Capital and reserves of banks were Denar 25,465 million, increasing by 9.8% compared to the last year.

In 2007, **banks' profitability** continued to increase. As of 31st December 2007, the banking system recognized a profit of Denar 3,650 million, thus increasing by 30.4% annually. ROA remained unchanged compared to last year at a level of 1.8%, while ROE increased by 2.9 percentage points, reaching 15.2% at the end of 2007.

At the same time, **the level of financial intermediation of the banking system** deepened. As of 31st December 2007, the level of financial intermediation calculated as a ratio of total assets, gross credits and total deposits to the GDP of the Republic of Macedonia was 66.9%, 37.4% and 48% respectively. Compared to 31st December 2006, the ratio of total assets/GDP increased by 9.86 percentage points, gross credits/GDP increased by 8 percentage points and deposits/GDP increased by 7 percentage points.

The new Law on Banking was adopted in 2007. The law further liberalized the market by enabling foreign banks to open subsidiaries in the Republic of Macedonia. Aiming at strengthening banking stability, "fit and proper" criteria for the shareholders and the banks' management were strengthened, as well bank corporate governance by introducing new bodies, the role and responsibilities of supervisory body have been strengthened and gradation of the supervision measures has been made. Banks were obliged to establish management systems with all material risks (liquidity risk, market risk, exposure concentration risk and investment risk).

## 8.2. Capital Market

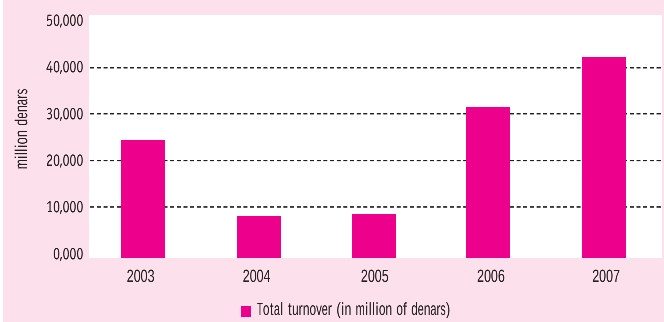
During 2007, the Macedonian Stock Exchange (MSE) experienced intensified activity, reflected in favourable trends of the stock-exchange indicators. Stable economic and political environment, low inflation and exchange-rate stability were the basis for strengthened activity of MSE.

Improved competitiveness of domestic companies listed on the MSE as well as the increased transparency in their operations were factors which supported a greater interest of domestic and foreign investors for trading at MSE. In addition, the emergence of private pension funds as new institutional investors contributed to the turnover increase.

At the beginning of 2007, 43 joint stock companies were listed on the MSE, but part of them (3 upon their request and 2 due to the non-fulfilment of the terms and conditions) were excluded from the listing. Hence, stocks of 38 joint stock companies were listed at the end of the year.

In 2007, 22 authorized participants, 16 out of which were brokerage houses and 6 banks, participated in the trading on the MSE (in the course of the year, 6 new members appeared, and one member was permanently excluded).

**Chart 8.1.** Total turnover (in million of denars)




Source: Macedonian Stock Exchange

In 2007, **the total turnover** on the MSE reached Denar 41,702 million (or EUR 682 million), i.e. it increased by 34.5% annually. The increase was mainly due to the increased stock trading. In 2007, total turnover seen on the MSE as a ratio to the GDP amounted to 12.2% i.e. almost twice more than 2006 (6.8%), reflecting further development and deepening of Macedonian capital market.

Turnover observed during **classical trading** on the MSE reached a peak value of Denar 30,404 million or EUR 496.9 million, which compared to 2006 notes a high increase of 181.7%. The turnover from stock trading was Denar 28,845 million or EUR 471.4 million, increasing by 236.8% annually, while the turnover from government-bonds trading was Denar 1,560 million (EUR 25.4 million), declining by almost 30.1% compared to 2006.

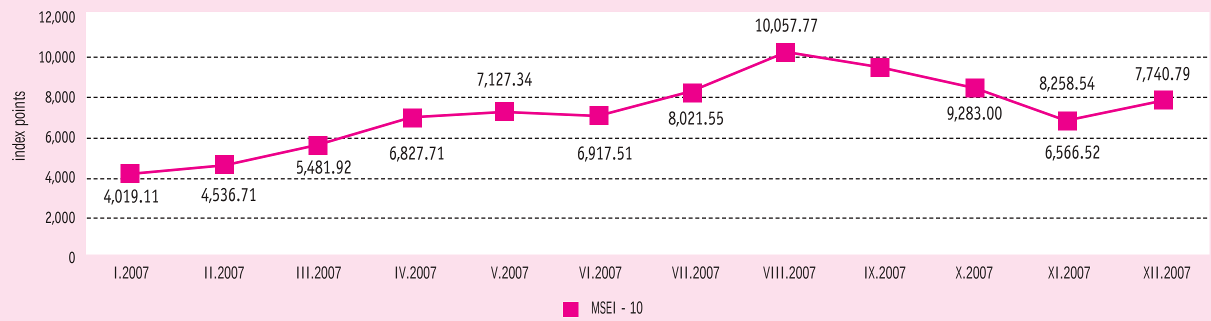
In 2007, 16 **block transactions** were registered, with a turnover of Denar 11,202 million (EUR 183.06 million) and showing a decrease of 19.8% compared to 2006.

During 2007, foreign investors were actively contributed to MSE turnover, 25.2% at stock-buying in December 2007 and 23.2% at stock-selling.

Improved financial results of companies, the increase of the demand and interest in securities on MSE, were followed by upward price trends. The indicator of price movements, **Macedonian Stock Exchange Index, MSEI-10,** was 7,740.79 index points on 31st December 2007, increasing by 109.1% compared to

2006. The highest value of MSEI-10 was achieved on 31st August 2007, reaching 10,057.77 index points, while the lowest value was registered on 4th January 2007, when MSEI-10 was only 3,802.38 index points.

**Chart 8.2.** MSEI-10




Source: Macedonian Stock Exchange

**Total market capitalization** of securities on the MSE was Denar 309.1 billion or about EUR 5 billion on 31st December 2007, which is 91% of the GDP for 2007. Total market capitalization on the MSE increased by 183.8% on 31st December 2007 compared to 31st December 2006.

## 8.3. Investment Funds

In November 2007, the first two investment-fund-management companies were established to manage the funds of the three open-end funds. As of December 2007, the three open-end investment funds collected funds in the total amount of EUR 1.1 billion. During 2007, 9 private funds managed by three private fund-management companies were also registered.

**Window 8.2. Investment Fund**

***What is an Investment Fund?***

Investment Funds are financial institutions collecting cash from investors and placing the allocated cash in short- and long-term investments for the purpose of gaining profit.

Pursuant to the Law on Investment Funds, an investment fund is established for pulling cash intended for investments by domestic and/or foreign natural persons and legal entities and/or the Republic of Macedonia, through public call or private offer, which, for the account of the investors, are managed by investment-fund management companies i.e. private fund management companies.

***Types of Investment Funds***

The Investment Fund may be established as: open-end, closed or private fund.

An Open-end Fund is established for collecting cash through a public call, whereby investors acquire shares. The Open-end Fund is a specific property without capacity of being legal entity, and its owners have the right to a proportional share of the profit and right to request buyout of the shares.

The Closed Fund is a Joint-Stock Company for collecting cash through public call for selling own stocks and investing those funds in securities. The Closed Fund has the capacity of legal entity, being established and managed by the Fund Management Company.

The Private Fund is established for collecting cash through private offer for selling documents for shares. Private Fund is a specific property without the capacity of legal entity. The Private Fund is established for a certain time (not less than 8 years), which may have 20 investors at most. The Private Fund is managed by Private Fund Management Company.

## 8.4. Pension Companies

In 2000, the fundamentals of the reformed pension system as a three-pillar pension system were established by law. The three pillars are: first pillar - insurance on the basis of generation solidarity, second pillar - mandatory fully-funded pension system and third pillar - voluntary fully-funded pension system.

Funds of the insured persons under the second pillar are privately and competitively managed, thus the paid contributions are invested by a specialized licensed pension fund management companies.

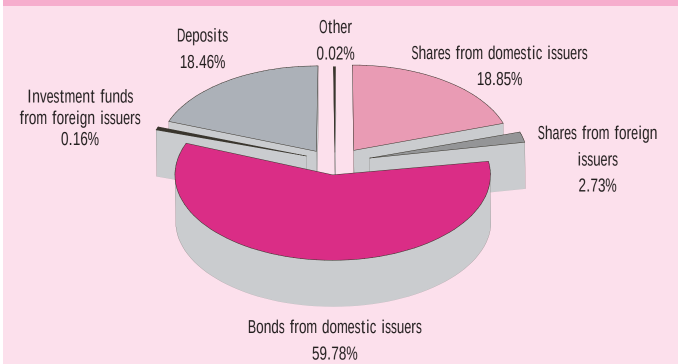
The Pension Fund is an open-end investment fund, established and operating pursuant to the Law on Investment Funds, unless otherwise stipulated in the Law on Mandatory Fully-Funded Pension Insurance or the Law on Voluntary Fully-Funded Pension Insurance.

Starting from 2005, two Pension Investment Funds were established in the Republic of Macedonia: Nov Penziski Fond - Otvoren penziski fond - Skopje managed by the Pension Fund Management Joint Stock Company Nov Penziski Fond and KB Prv Otvoren Penziski Fond - Skopje managed by KB First Pension Fund Management Company AD Skopje.

As of 31st December 2007, the **total number of members** and timely classified insured persons in the pension funds was 162,653. 63,714 out of them or 39.2% were voluntary members, while 98,939 or 60.8% were mandatory members.

The main investment principles of pension funds, regulated by law, were the following: safety of funds, diversification of the investment risk and maintenance of appropriate liquidity for the purpose of achieving the highest yield in favour of members.

**Chart 8.3.** Pension funds portfolio on 31.12.2007




**The structure of the investments** of the Pension Funds was composed of bonds issued by domestic issuers, shares issued by domestic and foreign issuers, investment funds by foreign issuers and by deposits with banks in the Republic of Macedonia on 31st December 2007.

*The Bond Portfolio* of the two Pension Funds included only bonds by domestic issuers in the total amount of Denar 1,869 million or EUR 30.4 million (being 59.78% out of the total portfolio). Bonds issued by domestic issuers included the continuous government bonds, government denationalization bonds and the government bond for the old foreign exchange saving. Investments in continuous government bonds included the bonds from the second to the six issues amounting to Denar 856 million or around EUR 14 million in the total portfolio of the two funds. The government denationalization bonds included the bonds from the first to six issues and being part of the portfolio of the two funds they amounted to Denar 839 million or EUR 13.7 million. Government bonds for the old foreign exchange saving being part of the portfolio of the two funds amounted to Denar 173.4 million or EUR 2.8 million in total.

*Investments in stocks of domestic issuers* in the portfolio of the two funds were Denar 589.2 million or EUR 9.6 million (being 18.85% of the total portfolio).

*Investments in stocks of foreign issuers* in the portfolio of the two funds were Denar 85.3 million or EUR 1.4 million (being 2.73% of the total portfolio), including the following shares: Sanofi-Aventis France, Carrefour SA France, TOTAL SA France, Carrefour SA France, Bank of America Corp USA, General Electric CO USA, Procter Gamble CO USA, Oracle Corp USA, MMM USA, Johnson & Johnson USA, Dell Inc USA, Genentech USA, Cisko System Inc USA, BHP Billiton PLC England, Bayerische Motoren Werke Germany, E.On AG, Germany, Uni Credito Italiano Italy, Royal Bank of Scotland Scotland.

*Invested funds in investment funds by foreign issuers* as part of the portfolio of the two funds were Denar 5 million or EUR 81.2 thousand (being 0.16% of the total portfolio) and starting with the cut-off date 31st December 2007, they were invested in only one fund such as: iShares Inc, Barclays Global Investor N.A. (EFF) seated in USA.

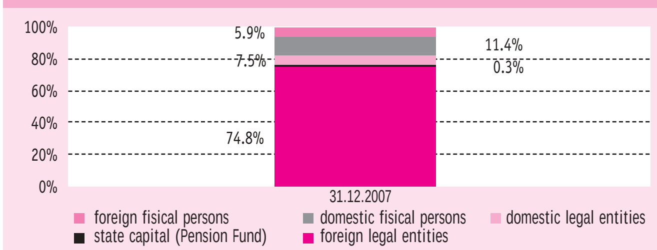
Two Pension Funds invested part of the funds in deposits in Macedonian Banks and as part of the portfolio of the two funds, the deposits in the total amount participated with almost Denar 577 million or EUR 9.4 million (being 0.16% of the total portfolio).

As of 31st December 2007, **total net assets in the Pension Funds,** amounted to about Denar 3 billion or higher than EUR 50 million, being around 0.9% of GDP.

**The pension funds yield was** 6% for the period from the beginning of the system up to the end of 2006, while it was 7.4% annually at the end of 2007.

## 8.5. Insurance market

**Chart 8.4.** Structure of capital ownership of insurance companies




Source: MoF

The insurance market in the Republic of Macedonia marked continues to be an increasing trend, in both the number of active entities and the deepening of the quality of insurance products and the distribution channels. The ownership restructuring trend and the entrance of foreign insurance brands was strongly felt in 2006 and 2007, when Slovenian and Croatian financial insurance undertakings joined the market and which are expected to be a driving force for the development of the Macedonian insurance market. In 2007, the insurance market in the

Republic of Macedonia was characterized by an increase of the gross premium, increase of the number of licensed insurance undertakings and insurance brokers, establishing and managing the funds of the Guarantee Fund within the National Insurance Bureau, employment increases in the sector and further improvement of the primary legal regulation.

In 2007, twelve insurance companies and six insurance brokerages operated in the insurance market in the Republic of Macedonia. Only two insurance companies have had life-insurance activities, and the other ten have had non-life insurance activities. Foreign natural persons and legal entities may establish an insurance company under the same terms and conditions as the domestic ones. What is important to emphasize is that since 2000 the attractiveness of the insurance sector in the Republic of Macedonia is intensified. At the end of 2007, the share of the foreign capital in the insurance companies was 75%. At the end of 2006, the share of foreign capital in the domestic insurance companies was 67%. Six companies were fully foreign-owned, while the foreign capital predominated in other five companies. Only one insurance company was fully domestically-owned.

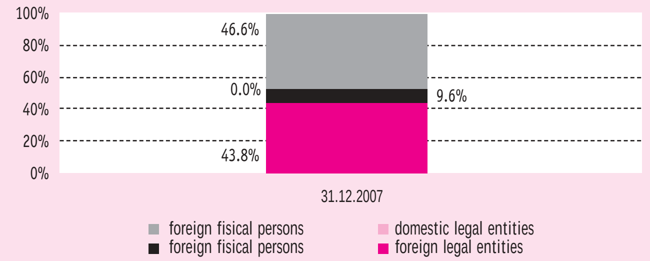
At the end of 2007, *the total capital* **of insurance companies** was Denar 2,662 million and its share in the total assets of the insurance sector was 24% contrary to the share of 18.4% in 2006.

As a result of the significant market penetration, the insurance company Vardar AD Skopje with 25.45% of the market was the leading insurance company in 2007, followed by KJUBI Makedonia with 21.4%, Sava Tabak - 14.35%, Osiguritelna Polisa - 9.3%, Eurolink - 8.6%, Sigma - 5.32% and so on. The leading five insurance companies have had 79.1% of the market, a decrease of 2.34% compared to 2006 (81%).

During 2007, the total gross calculated premium was Denar 6,109 million (EUR 100 million), Denar 5,938 million (EUR 96.5 million) out of which 97.2% referred to non-life insurance, while Denar 171.2 million (EUR 2.8 million) i.e. 2.8% referred to life insurance. Compared to 2006, the total gross calculated premium increased by 12.2%. The gross calculated premium regarding the non-life insurance, increased by 11.4% compared to last year. On the other hand, within life insurance, the total gross calculated premium increased by 48% during 2007, which was mainly due to the entrance of a new life-insurance company on the market. In 2007, the share of gross calculated premium in the gross domestic product in the country was 1.8%, increasing slightly compared to the last year. The increase was mainly due to the increase of the calculated premium from the Motor TPL Insurance. Only this insurance class experienced increase of the calculated premium by 19.4%, compared to last year.

In 2007, 6 **insurance brokers** operated on the insurance market, intermediating in all insurance classes. At the end of 2007, revenues from the main activity of the insurance brokers amounted to Denar 114.9 million, increasing by 77% compared to 2006 (revenues for 2006 amounted to Denar 64.8 million). The increase of revenues was due to entrance of one insurance broker in 2007. Compared to 2006, when the share of one undertaking predominated on the market, the share of two insurance brokers in the total revenues predominated at the end of 2007. At the end of 2007, the share of the foreign capital in the insurance brokers was 53.4%. In line with the Amendments and Modifications to the Insurance Supervision Law adopted in June 2007, the insurance companies were obliged to maintain significantly higher amounts of Guarantee Fund, while the insurance brokers were obliged to maintain the value of the equity in the amount of at least 4%.

**Chart 8.5.** Structure of the capital ownership of the insurance brokerage companies




Source: MoF

## 8.6. Leasing

The financial leasing market exhibited constant increasing trend at all parameters in the last years. At the end of 2007, the total assets of the active leasing companies were Denar 5,223 million and compared to last year they increased by 60.4% (Denar 3,256 million in 2006), which was due to the entrance of two new companies in the financial leasing market in January 2007. In 2007, the capital trend decreased slightly amounting to Denar 222 million (Denar 224.7 million on 31st December 2006) on 31st December 2007.

In 2007, the total number of active financial leasing contracts was 7,471 and their total value was Denar 7,917 million.

The activities of the leasing companies in the Republic of Macedonia were mainly focused on performing leasing activities of non-real estate, mainly of light vehicles. At this moment, the main challenge for the leasing companies is the broadening of the list of subject-matters to leasing contracts and encouraging the development of the secondary market for used equipment, which would be in favour of the reduction of the risk of leasing companies when reselling the equipment.

The share of the leasing companies in the total assets of financial institutions, as well in the GDP was below 1%, pointing out their marginal role on the market.

# 2007

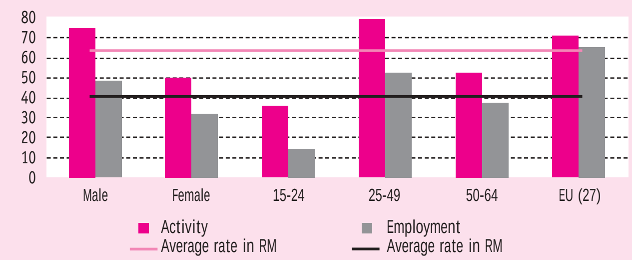
## 9.1. Labour market

Labour market trends in 2007 point to increased activity of the population, increased employment and decreased unemployment. According to 2007 data[14] the activity rate was 62.8%, the employment rate increased to 40.7%, while the unemployment rate was reduced to 35.2%.

### 9.1.1. Gender and age characteristics of the labour force activity

In 2007, the activity rate increased by 0.6 percentage points compared to 2006, reaching 62.8%. However, the labour market activity was relatively low, i.e. it was lower than the average activity rate in the EU by 8.1 percentage points[15].

**Chart 9.1.** Activity and employment rate




Source: State Statistical Office

The gender gap in the labour activity declined by 1.3 percentage points compared to 2006, reaching 24.5 percentage points in 2007.

The activity rate of women was lower than men, mainly due to the traditional family role of women in the society, especially of the women from ethnic minorities. The activity rate for women increased by 1.2 percentage points and was 50.4% in 2007, while for men it remained unchanged compared to 2006 (see Chart 9.1.).

The low rate was also observed in the youngest age group (15-24 years). Postponement of entrance of persons at this age on the labour market was the main reason for such situation, since they decide to continue their education, increasing the possibility for employment and gaining a higher salary. The activity rate of young people was 35.9%, and remained almost unchanged compared to 2006. The other age groups did not experience any significant changes compared to the last year, except persons at age of 50-64 years, where the activity rate increased by 2.1 percentage points compared to 2006.

14) Data on the labour market came from the Labour Force Survey (LFS), State Statistical Office, for the population 15-65 years, unless otherwise stated

15) During the comparison of the activity and employment rates on all bases with the other countries, for the purpose of consistency, data on the third quarter 2007 were used

## 9.1.2. Employment

*9.1.2.1. Gender, age and educational employment structure*

In 2007, the employment rate was 40.7%, increasing by 1.1 percentage points compared to 2006. The employment rate was lower by 24.9 percentage points compared to the EU- 27 average. In the period between 2006 and 2007, 19,667 working posts were created on a net basis.

There was an employment increase regarding men and women, the increase being more emphasized in the employment of women, by 1.6 percentage points (see Chart 9.1.). Employment and activity were characterized by a high gender gap which was 17.6 percentage points in 2007, but the gap experienced a reduction of 1.1 percentage points compared to the last year. This gap was only 2.9 percentage points higher than the EU average. Reduction of the employment differences between genders was more emphasized regarding the higher level of education; at university level, the employment of women was higher than men.

The employment rate of young people (15-25 years) was very low, 15.2%, being an exceptionally unfavourable situation and the increase was insignificant compared to 2006, i.e. only 0.8 percentage points. Low employment of this group was a reflection of the difficulties for finding a first job. With regard to the primary age group (25-49 years) the employment was 53%, increasing by 1 percentage point compared to the last year, while regarding people at the age of 50-64 years, employment was 37.8% increasing by 1.4 percentage points compared to 2006.

*9.1.2.2. Employment by sectors, economic status, ownership and type of agreement*[16]

The employment structure by sectors in the Republic of Macedonia has not significantly changed compared to the last year, with a slight decrease of employment share in agriculture and construction, and higher share of employees in the services sector by 3.2 percentage points. Employment in the primary sector was 18% in 2007. Agriculture further remained the main source of existence of the less qualified workers, as well as of the fired workers facing difficulties finding new job. The services sector remained the main "employer" absorbing 51% of the employees. Employment in the sector of industry amounted to 25%, while the construction participated with 6% in the employment (see Chart 9.2.)

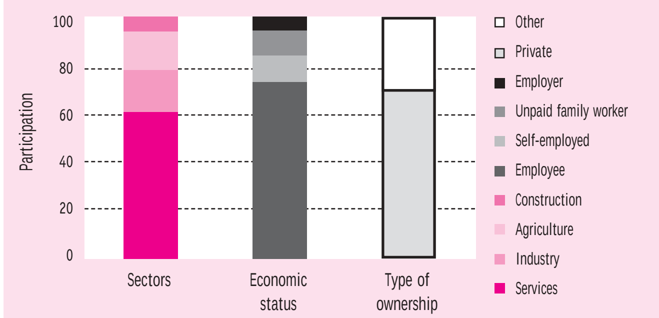
Analysis of the employment structure according to the economic status, pointed out a reduced share (by 0.8 percentage points) of the number of unpaid family workers, in favour of an increased number of employees, participating with 73.2% (see Chart 9.2.). Analysis according to the ownership pointed out to an increase of the share of workers in the private sector by 3 percentage points compared to last year (see Chart 9.2.).

16) Analyses of employment structure were made on the basis on data for population older than 15 years.

### 9.1.3. Age, gender and education unemployment structure

The unemployment rate has been declining continuously, even though it remained at an unacceptably high level. In 2007, it was 35.2%, lower by 1.1 percentage points compared to last year. Regardless of the size of the informal economy in the Republic of Macedonia, the unemployment rate was significantly higher compared to both EU countries and countries in the region.

**Chart 9.2.** Structure of employees by various clasifications



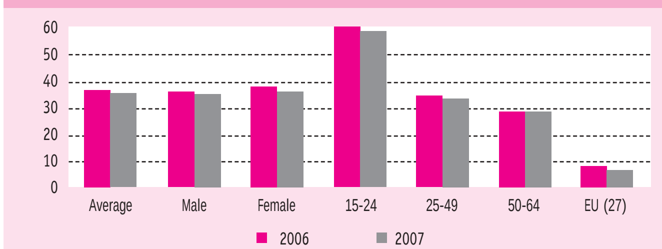

Source: SSO

The unemployment rate of women (38.5%) was higher, showing a higher reduction than the unemployment rate of men. Thus, the gender gap was narrowed, amounting to 1 percentage point and is almost identical with the EU.

The unemployment rate was the highest for the young labour force at the age of 15-24 (see chart 9.3.), being 1.6 higher than the average, and declining by 2 percentage points compared to 2006. The primary age group (25-49) also experienced a significant unemployment reduction (by 3%), causing a decline of the unemployment by 1.2 percentage points. The unemployment rate was insignificantly increased regarding the age group of 50-64 years, being the lowest within the age categories.

Trends are identical in the gender analysis of age groups, whereby women from the youngest age group experienced a higher reduction of unemployment rate. Thus, the gender gap was reduced regarding this group, being positive for the oldest age group.

**Chart 9.3.** Unemployment rate




Source: SSO

Persons with primary education are more likely to be unemployed, unlike those with secondary education, particularly compared with those with higher education. The unemployment rate for persons with an insufficient level of education increased in 2007 by 22% and is higher than the national average. Persons with secondary education experienced the highest unemployment rate reduction, while the one was the lowest for the persons with high education, i.e. by 41% lower than the national average.

Long-term unemployment i.e. unemployment for more than one year was an important characteristic on the labour force market. The Employment Agency data of the Republic of Macedonia showed increases of the long-term unemployment rate, amounting to 82.5% in December 2007, an increase by 2.3 percentage points compared to December 2006.

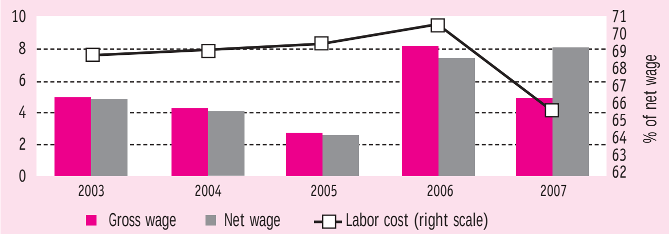
## 9.2. Analysis of the policy of pensions and wages

The productivity increase, profitability increase and the economic policy oriented towards supporting aggregate demand influenced wages. The Government decided to increase the **wages of employees** in the public administration by 10% in September 2007. Hence, the net wage per employee was Denar 14,586, a nominal growth of 7.9%, while the real growth was 5.6%.

The largest increase of the net wage was observed in education, by 12.2%, followed by processing industry, by 9.7%. The average net wage was the highest in the financial sector (95% above the average in the country), while the lowest wage was registered in construction sector (28% below the average wage).

Gross wage did not follow the growth pace of net wage, whereby, the decreased personal income tax might be the main reason. This contributed to a decrease of the difference between gross and net wage (labour tax wedge) to 65.5% of the net wage, a decrease of 5 percentage points compared to 2006 (see Chart 9.4.).

**Chart 9.4.** Percentage change in gross and net wage and labor cost




Source: State Statistical Office

In addition, the percentage of employees who did not receive a salary decreased to 10.6% at the end of 2007, a decline of 3 percentage points compared to December 2006.

In 2007, **the increase of pensions** did not follow the growth dynamics of salaries. Thus, the average pension was 2.7% higher compared to the last year and was Denar 7,782. Therefore, the ratio of average pension to the average net wage was 53.4%, a decline of 2.7 percentage points compared to the ratio in 2006. However, the announced average increase by 15% of the pensions in 2008 is expected to stabilize this ratio at a higher level. The indexing of pensions is done twice a year, so that pensions are adjusted at the beginning of each year, following wage and inflation movements.

The number of pension beneficiaries continued to increase in 2007, reaching 272,386 beneficiaries in December, increasing by 1% compared to December 2006. 55.1% of them were retirement pension beneficiaries, 27.3% were survival pension beneficiaries while 17.6% were disability pension beneficiaries. According to the data from the Pension and Disability Insurance Fund, the number of pension beneficiaries out of 1000 registered insured persons under the pension and disability insurance contribution amounted to 642 (improving) decreasing by 6% compared to last year. However, this proportion (693 pension beneficiaries) was higher by 8% if one excludes the registered persons not paying the contributions.

**Chart 9.5.** Insured persons and pension beneficiaries


Source: Pension Fund

Total expenditures for pensions were 3.5% higher compared to the last year. When expressed as a percentage of the social government budget transfers, the expenditures for pensions were 52.6%, higher by 0.5 percentage points compared to 2006.

## 9.3. Social protection

In 2007, 5.5% of the social government budget transfers were disbursed for safety nets. According to the data from the Ministry of Labour and Social Policy, 61.3% out of these funds were intended for social pecuniary welfare. In December 2007, the number of beneficiaries of social pecuniary welfare amounted to 62,443 households, a decrease by 4.7% compared to December 2006. Payments on the basis of care by a third person participated with 30%, lower by 6% compared to 2006. The number of beneficiaries on the basis of this right was lower by 16.2% in December 2007 compared to December last year. The number of beneficiaries of constant pecuniary assistance decreased by 2.5% on the same comparative basis, but the amount of paid funds increased by 5.8% in 2007, accounting for 7% of the payments upon all bases. Payments on the basis of health protection were higher by 6.2% compared to last year, participating with 1.7% in the total payments. Thereby, the number of beneficiaries was reduced by 2.8% in December 2007 compared to December 2006.

# 2007

# ANNEX

# 2007

## A. REAL SECTOR

**Table A.1.** Macroeconomic indicators

| | 1998 | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 | 2008 | 2009 | 2010 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| REAL SECTOR | | | | | | | | | 0.3 | 0.2 | 0.2 | 0.2 | 0.2 |
| Population | 2,008,000 | 2,017,000 | 2,026,000 | 2,035,000 | 2,020,000 | 2,027,000 | 2,032,000 | 2,037,000 | 2,043,111 | 2,047,197 | 2,051,292 | 2,055,394 | 2,059,505 |
| Gross domestic product | | | | | | | | | | | | | |
| - real growth rate | 3.4 | 4.3 | 4.5 | -4.5 | 0.9 | 2.8 | 4.1 | 4.1 | 4.0 | 5.1 | 6.0 | 6.5 | 6.5 |
| - current prices, in million of denars | 194,979 | 209,010 | 236,390 | 233,841 | 243,970 | 251,486 | 265,257 | 286,626 | 309,546 | 339,257 | 381,190 | 418,146 | 457,794 |
| - in million of US dollars (nominal) | 3,581 | 3,674 | 3,588 | 3,437 | 3,769 | 4,631 | 5,368 | 5,815 | 6,345 | 7,587 | 8,524 | 9,351 | 10,237 |
| - in million of US dollars (PARE methodology) | 3,575 | 3,730 | 3,899 | 3,723 | 3,872 | 4,119 | 4,298 | 4,534 | 4,882 | - | - | - | |
| - in million of euros (nominal) | | | 3,893 | 3,839 | 4,001 | 4,105 | 4,325 | 4,676 | 5,059 | 5,545 | 6,230 | 6,834 | 7,482 |
| GDP per capita (in denars) | 97,101 | 103,624 | 116,678 | 114,910 | 120,777 | 124,068 | 130,540 | 140,710 | 151,507 | 165,718 | 185,829 | 203,438 | 222,284 |
| GDP per capita (in dollars) | 1,783 | 1,821 | 1,771 | 1,689 | 1,866 | 2,285 | 2,642 | 2,855 | 3,106 | 3,706 | 4,156 | 4,549 | 4,971 |
| Industry | 4.5 | -2.6 | 3.5 | 10.1 | -5.3 | 4.7 | -12.7 | 7.0 | 2.6 | 3.7 | 6.1 | 6.6 | 6.5 |
| Inflation (CPI, average) | -0.1 | -0.7 | 5.8 | 5.5 | 1.8 | 1.2 | -0.4 | 0.5 | 3.2 | 2.3 | 6.0 | 3.0 | 2.8 |
| GDP Deflator | 1.4 | 2.7 | 8.2 | 3.6 | 3.4 | 0.3 | 1.3 | 3.8 | 3.8 | 4.3 | 6.0 | 3.0 | 2.8 |
| EXTERNAL SECTOR | | | | | | | | | | | | | |
| Export (f.o.b.), in million of US dollars | 1,292 | 1,190 | 1,321 | 1,155 | 1,112 | 1,363 | 1,675 | 2,041 | 2,396 | 3,349 | 3,518 | 3,918 | 4,324 |
| Import (f.o.b.), in million of US dollar | 1,807 | 1,686 | 2,012 | 1,682 | 1,918 | 2,214 | 2,814 | 3,104 | 3,681 | 4,976 | 5,640 | 6,180 | 6,750 |
| Trade balance (in million of US dollars) | -516 | -496 | -691 | -527 | -806 | -851 | -1,139 | -1,063 | -1,285 | -1,627 | -2,122 | -2,262 | -2,426 |
| Trade balance (f.o.b.) (% of GDP) | -14.4 | -13.5 | -19.3 | -15.3 | -21.4 | -18.4 | -21.2 | -18.3 | -20.3 | -21.4 | -24.9 | -24.2 | -23.7 |
| Current account deficit (in million of US dollars) | -279 | -65 | -98 | -236 | -378 | -184 | -453 | -158 | -56 | -238 | -396 | -431 | -480 |
| Current account deficit (% of GDP) | -7.8 | -1.8 | -2.7 | -6.9 | -10.0 | -4.0 | -8.4 | -2.7 | -0.9 | -3.1 | -4.6 | -4.6 | -4.7 |
| Foreign direct investment (in million of dollars) | 150 | 88 | 216 | 446 | 105 | 117 | 322 | 94 | 424 | 321 | 403 | 495 | 443 |
| - % of GDP | 4.2 | 2.4 | 6.0 | 13.0 | 2.8 | 2.5 | 6.0 | 1.6 | 6.7 | 4.2 | 4.7 | 5.3 | 4.3 |
| Export (f.o.b.), growth rate | 4.4 | -7.9 | 11.0 | -12.5 | -3.7 | 22.5 | 22.9 | 21.8 | 17.4 | 39.8 | 5.0 | 11.4 | 10.4 |
| Import (f.o.b.), growth rate | 11.3 | -6.7 | 19.3 | -16.4 | 14.0 | 15.4 | 27.1 | 10.3 | 18.6 | 35.2 | 13.3 | 9.6 | 9.2 |
| Exchange rate denar/euro | | | 60.7250 | 60.9133 | 60.9783 | 61.2639 | 61.3377 | 61.2958 | 61.1885 | 61.1838 | 61.1838 | 61.1838 | 61.1838 |
| Exchange rate denar/dollar | 54.4506 | 56.8964 | 65.8856 | 68.0421 | 64.7341 | 54.3031 | 49.4105 | 49.2919 | 48.7854 | 44.7184 | 44.7184 | 44.7184 | 44.7184 |
| FISCAL SECTOR | | | | | | | | | | | | | |
| (GENERAL GOVERNMENT BALANCE, IN MILLION OF DENARS) | | | | | | | | | | | | | |
| Total revenues | 64,944 | 74,007 | 86,583 | 80,503 | 86,254 | 84,167 | 88,176 | 100,877 | 104,044 | 119,609 | 128,740 | 138,210 | 146,975 |
| Total expenditures | 68,280 | 73,946 | 80,678 | 95,349 | 99,808 | 86,760 | 88,169 | 100,219 | 105,744 | 117,441 | 134,280 | 144,074 | 153,483 |
| SURPLUS/DEFICIT | -3,336 | 61 | 5,905 | -14,846 | -13,554 | -2,593 | 7 | 658 | -1,700 | 2,168 | -5,540 | -5,864 | -6,508 |
| (GENERAL GOVERNMENT BALANCE, IN % OF GDP) | | | | | | | | | | | | | |
| TOTAL REVENUES | 33.3 | 35.4 | 36.6 | 34.4 | 35.4 | 33.5 | 33.2 | 35.2 | 33.6 | 35.3 | 33.8 | 33.1 | 32.1 |
| TOTAL EXPENDITURES | 35.0 | 35.4 | 34.1 | 40.8 | 40.9 | 34.5 | 33.2 | 35.0 | 34.2 | 34.6 | 35.2 | 34.5 | 33.5 |
| Surplus/Deficit | -1.7 | 0.0 | 2.5 | -6.3 | -5.6 | -1.0 | 0.0 | 0.2 | -0.5 | 0.6 | -1.5 | -1.4 | -1.4 |
| Total public debt (GFS methodology) | | 40.7 | 57.1 | 55.5 | 48.6 | 44.9 | 42.6 | 46.9 | 40.4 | 35.2 | | | |

| | | | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| SOCIAL SECTOR | | | | | | | | | | | | | |
| Wages (monthly average, net) | | | | | | | | | | | | | |
| - nominal growth | 3.7 | 2.9 | 5.5 | 3.5 | 6.9 | 4.8 | 4.0 | 4.0 | 7.3 | 7.9 | 7.5 | 8.0 | 8.5 |
| - real growth | 3.8 | 3.6 | -0.3 | -2.0 | 5.1 | 3.6 | 4.4 | 3.5 | 4.1 | 5.6 | 1.5 | 5.0 | 5.7 |
| Unemployment rate (ILO definition) | | 32.4 | 32.2 | 30.5 | 31.9 | 36.7 | 37.2 | 37.3 | 36.0 | 34.5 | 33.0 | 31.5 | 30.0 |
| Employment (% increase) | 5.4 | 1.0 | 0.8 | 9.0 | -6.3 | -2.9 | -4.1 | 4.3 | 4.6 | 4.0 | 4.0 | 4.0 | 4.0 |
| Productivity growth (in %) | -1.9 | 3.3 | 3.7 | -12.4 | 7.7 | 5.9 | 8.5 | -0.1 | -0.8 | 6.5 | 1.9 | 2.4 | 2.4 |
| Unit labor cost | | | | | | | -4.0 | 2.8 | 8.9 | -1.6 | 5.5 | 5.5 | 6.0 |
| Monetary sector | | | | | | | | | | | | | |
| Nominal changes (end of period) | | | | | | | | | | | | | |
| Net foreign assets | | | 73.8 | 57.6 | -19.1 | 5.3 | 4.7 | 30.3 | 20.4 | 1.6 | | | |
| Credit to private sector | | | 17.2 | 7.3 | 12.7 | 15.8 | 18.7 | 20.5 | 30.5 | 39.1 | | | |
| Money in circulation | | | 16.6 | 48.5 | 0.0 | 0.3 | -0.1 | 2.0 | 12.2 | 10.7 | | | |
| M1 | | | 22.6 | 5.6 | 4.6 | 1.1 | -1.1 | 7.5 | 17.1 | 31.7 | | | |
| M2 | | | 29.4 | 61.9 | -7.0 | 15.9 | 15.1 | 16.0 | 24.6 | 28.3 | | | |
| M4 | | | 25.6 | 56.7 | | 13.2 | 15.3 | 15.1 | 24.9 | 29.5 | | | |
| Foreign exchange reserves/M1 ratio | | | 1.7 | 1.9 | 1.5 | 1.5 | 1.6 | 2.3 | 2.6 | 2.2 | | | |

## B. FISCAL SECTOR

**Table B.1.** General Government Budget

| | Q1 2006 | Q2 2006 | Q3 2006 | Q4 2006 | Total 2006 | Q1 2007 | Q2 2007 | Q3 2007 | Q4 2007 | Total 2007 |
|---|---|---|---|---|---|---|---|---|---|---|
| TOTAL REVENUES | 23,069 | 26,306 | 26,222 | 28,504 | 104,101 | 26,445 | 27,882 | 32,599 | 32,683 | 119,609 |
| Tax revenues and contributions | 19,848 | 22,782 | 23,080 | 24,888 | 90,598 | 23,478 | 24,648 | 26,586 | 28,507 | 103,219 |
| Tax revenues (special revenue account) | 79 | 50 | 35 | 35 | 199 | 59 | 45 | 46 | 97 | 247 |
| Taxes | 12,658 | 15,097 | 15,460 | 16,360 | 59,575 | 15,755 | 16,514 | 18,282 | 18,964 | 69,515 |
| Personal income tax | 1,933 | 2,098 | 2,025 | 2,358 | 8,414 | 1,844 | 2,006 | 2,220 | 2,823 | 8,893 |
| Profit tax | 1,725 | 914 | 950 | 1,119 | 4,708 | 2,035 | 1,237 | 1,278 | 1,348 | 5,898 |
| VAT | 5,228 | 7,342 | 7,155 | 7,534 | 27,259 | 7,106 | 8,150 | 8,968 | 8,738 | 32,962 |
| Excises | 2,542 | 2,839 | 3,374 | 3,419 | 12,174 | 2,780 | 3,234 | 3,788 | 3,463 | 13,265 |
| Import duties | 993 | 1,494 | 1,982 | 3,243 | 7,712 | 1,502 | 1,380 | 1,403 | 1,914 | 6,199 |
| Other taxes | 237 | 410 | 390 | 176 | 1,213 | 488 | 507 | 625 | 678 | 2,298 |
| Contributions | 7,111 | 7,635 | 7,586 | 8,493 | 30,825 | 7,664 | 8,089 | 8,258 | 9,446 | 33,457 |
| Pension and Disability Insurance Fund | 4,619 | 4,969 | 4,893 | 5,467 | 19,948 | 4,971 | 5,219 | 5,444 | 6,302 | 21,936 |
| Employment Agency | 322 | 336 | 337 | 375 | 1,370 | 343 | 364 | 372 | 444 | 1,523 |
| Health Insurance Fund | 2,170 | 2,330 | 2,356 | 2,651 | 9,507 | 2,350 | 2,506 | 2,442 | 2,700 | 9,998 |
| Non-tax revenues | 2,306 | 2,721 | 2,627 | 2,826 | 10,480 | 2,521 | 2,844 | 5,517 | 3,080 | 13,962 |
| Non-tax revenues (special revenue account) | 1,234 | 1,117 | 1,496 | 1,656 | 5,503 | 1,501 | 1,455 | 1,286 | 1,670 | 5,912 |
| Profit from public financials institutions | 103 | 406 | 56 | 258 | 823 | 72 | 368 | 3,032 | 60 | 3,532 |
| Administrative fees | 395 | 426 | 308 | 364 | 1,493 | 419 | 384 | 406 | 474 | 1,683 |
| Co-payment for health services | 80 | 76 | 65 | 22 | 243 | 70 | 78 | 81 | 138 | 367 |
| Other administrative fees | 65 | 70 | 59 | 26 | 220 | 72 | 68 | 67 | 117 | 324 |
| Other non-tax revenues | 109 | 176 | 209 | 125 | 619 | 78 | 72 | 220 | 157 | 527 |
| Road Fund Contribution | 321 | 452 | 434 | 374 | 1,581 | 309 | 419 | 425 | 464 | 1,617 |
| Capital revenues | 143 | 390 | 143 | 272 | 948 | 167 | 151 | 301 | 778 | 1,397 |
| Foreign donations | 727 | 299 | 166 | 231 | 1,423 | 259 | 200 | 180 | 267 | 906 |
| Income on the basis of loan repayment | 45 | 74 | 153 | 288 | 560 | 20 | 39 | 15 | 51 | 125 |
| TOTAL EXPENDITURES | 23,538 | 26,265 | 25,085 | 30,871 | 105,759 | 24,144 | 25,968 | 26,376 | 40,948 | 117,436 |
| Current expenditures | 22,475 | 24,145 | 22,335 | 27,569 | 96,524 | 23,038 | 24,296 | 23,995 | 32,366 | 103,695 |
| Salaries and allowances | 5,750 | 5,878 | 5,707 | 6,086 | 23,421 | 6,025 | 6,112 | 5,940 | 5,530 | 23,607 |
| Goods and services | 2,856 | 3,264 | 2,655 | 4,128 | 12,903 | 2,739 | 3,074 | 3,138 | 5,862 | 14,813 |
| Transfers | 13,080 | 14,265 | 13,167 | 16,163 | 56,675 | 13,715 | 14,235 | 14,545 | 19,906 | 62,401 |
| Transfers (special revenue account) | 167 | 209 | 165 | 240 | 781 | 191 | 164 | 106 | 176 | 637 |
| Social transfers | 11,566 | 12,726 | 12,072 | 12,466 | 48,830 | 12,336 | 12,449 | 12,769 | 12,437 | 49,991 |
| Pension and Disability Fund | 6,396 | 6,640 | 6,751 | 6,947 | 26,734 | 6,880 | 6,968 | 7,066 | 7,271 | 28,185 |
| Employment Agency | 659 | 521 | 487 | 450 | 2,117 | 417 | 437 | 411 | 389 | 1,654 |
| Social welfare | 948 | 945 | 1,114 | 1,090 | 4,097 | 1,026 | 876 | 1,118 | 1,027 | 4,047 |
| Structural reforms | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Public Administration Reforms | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Health care | 3,561 | 4,621 | 3,718 | 3,979 | 15,879 | 4,013 | 4,168 | 4,174 | 3,750 | 16,105 |

| | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| Other transfers | 1,326 | 1,308 | 911 | 3,451 | 6,996 | 1,171 | 1,603 | 1,658 | 7,267 | 11,699 |
| Refugee-related costs | 21 | 22 | 20 | 7 | 70 | 17 | 19 | 12 | 26 | 74 |
| Interest payments | 790 | 736 | 418 | 1,193 | 3,137 | 559 | 875 | 372 | 1,068 | 2,874 |
| Interest on domestic debt | 140 | 444 | 79 | 419 | 1,082 | 94 | 455 | 126 | 378 | 1,053 |
| Interest on external debt | 650 | 292 | 339 | 774 | 2,055 | 465 | 420 | 246 | 690 | 1,821 |
| Guarantees | 0 | 0 | 387 | 0 | 387 | 0 | 0 | 0 | 0 | 0 |
| Capital expenditures | 1,063 | 2,120 | 2,751 | 3,301 | 9,235 | 1,106 | 1,672 | 2,381 | 8,582 | 13,741 |
| Budget balance | -469 | 2 | 1,083 | -2,365 | -1,749 | 2,301 | 1,914 | 6,223 | -8,265 | 2,173 |
| Financing | 469 | -2 | -1,083 | 2,355 | 1,739 | -2,301 | -1,914 | -6,223 | 8,265 | -2,173 |
| Inflow | 9,759 | 3,097 | -166 | 5,390 | 18,080 | 3,039 | 8,944 | -5,230 | 12,542 | 19,295 |
| Privatization revenues | 13,928 | 3,846 | 0 | 0 | 17,774 | 662 | 0 | 0 | 0 | 662 |
| Foreign loans | 159 | 496 | 484 | 534 | 1,673 | 273 | 375 | 804 | 2,191 | 3,643 |
| Deposits | -4,835 | -4,101 | -695 | 3,741 | -5,890 | 1,985 | 8,503 | -4,848 | 9,814 | 15,454 |
| Treasury bills | 484 | 422 | 43 | 1,070 | 2,019 | 118 | 58 | -1,232 | 530 | -526 |
| Sale of shares | 24 | 2,433 | 2 | 0 | 2,459 | 1 | 8 | 46 | 7 | 62 |
| Outflow | 9,290 | 3,099 | 917 | 3,025 | 16,331 | 5,340 | 10,858 | 993 | 4,277 | 21,468 |
| Principal repayment | 9,290 | 3,099 | 917 | 3,025 | 16,331 | 5,340 | 10,858 | 993 | 4,277 | 21,468 |
| External debt | 9,159 | 381 | 917 | 487 | 10,944 | 5,340 | 7,021 | 862 | 977 | 14,200 |
| Domestic debt | 131 | 2,718 | 0 | 2,538 | 5,387 | 0 | 3,837 | 131 | 3,300 | 7,268 |

Source: MoF

## C. EXTERNAL SECTOR

**Table C.1.** Balance of payment of RM

| | 2003 | 2004 | 2005 | 2006 | Q1 | Q2 | Q3 | Q4 | 2007 |
|---|---|---|---|---|---|---|---|---|---|
| CURRENT TRANSACTIONS | -168.2 | -367.7 | -121.3 | -44.9 | 41.0 | 51.0 | 8.4 | -264.3 | -164.0 |
| Goods, net | -753.0 | -914.3 | -858.5 | -1,020.4 | -211.0 | -207.7 | -298.4 | -455.8 | -1,172.8 |
| Export, f.o.b. | 1,203.2 | 1,345.0 | 1,642.9 | 1,902.6 | 558.7 | 641.7 | 605.1 | 635.9 | 2,441.5 |
| Import, f.o.b.2 | -1,956.2 | -2,259.3 | -2,501.4 | -2,923.1 | -769.0 | -849.4 | -903.5 | -1,091.7 | -3,614.3 |
| Services, net | -6.0 | -43.4 | -24.7 | 22.2 | -1.2 | -1.1 | 23.3 | 2.4 | 25.5 |
| Income, net | -55.3 | -33.2 | -91.5 | -28.4 | 29.7 | -9.2 | -37.7 | -9.2 | -26.4 |
| Of which interest rate, net | -27.7 | -20.8 | -20.7 | -19.4 | -2.0 | -5.1 | -2.5 | -8.3 | -17.9 |
| Current transfers, net | 646.1 | 628.2 | 853.3 | 981.1 | 223.5 | 266.8 | 321.2 | 198.3 | 1,009.8 |
| Official | 89.4 | 55.5 | 53.4 | 58.7 | 8.6 | 17.1 | 10.7 | -12.4 | 23.9 |
| Private | 556.7 | 572.7 | 799.9 | 923.1 | 214.9 | 249.7 | 310.5 | 210.7 | 985.8 |
| CAPITAL AND FINANCIAL ACCOUNT | 193.9 | 347.1 | 127.7 | 38.0 | -42.9 | -46.9 | 8.9 | 275.2 | 194.3 |
| Capital account, net | -5.8 | -3.8 | -1.7 | -0.8 | -1.3 | 1.4 | 3.7 | -2.5 | 1.3 |
| Capital transfers, net | -5.8 | -3.8 | -1.7 | -0.8 | -1.3 | 1.5 | 0.6 | -1.9 | -1.1 |
| Official | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |
| Others | -5.8 | -3.8 | -1.7 | -0.8 | -1.3 | 1.5 | 0.6 | -1.9 | -1.1 |
| Acquisition/ availability of non-production/ non-financial assets | -0.1 | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 | 3.1 | -0.6 | 2.4 |
| Financial account, net | 199.7 | 350.9 | 129.4 | 38.8 | -41.6 | -48.3 | 5.2 | 277.7 | 240.1 |
| Direct investments, net | 100.1 | 259.7 | 74.9 | 344.6 | 20.1 | 63.9 | 40.4 | 115.7 | 240.1 |
| Portfolio investments, net | 4.9 | 9.5 | 200.2 | 73.1 | 20.5 | 45.6 | 24.5 | 20.2 | 110.8 |
| Other investments, net | 133.3 | 97.6 | 202.2 | -81.4 | -87.5 | -146.7 | 41.7 | 136.1 | -56.3 |
| Trade credits, net | 67.4 | 71.0 | 105.9 | 2.9 | -33.6 | -65.0 | 1.7 | 63.4 | -33.5 |
| Loans, net | 50.3 | 6.1 | 100.2 | -22.3 | -42.3 | -124.7 | 12.6 | 46.7 | 107.7 |
| Currencies and deposits, net | 5.9 | -2.3 | -20.3 | -83.7 | -16.8 | 20.2 | 12.8 | -10.3 | 5.9 |
| Of which: monetary authority, net | 15.5 | 23.2 | 0.0 | -5.7 | 0.1 | 0.0 | 0.0 | -0.1 | -0.2 |
| Commercial banks, net | -44.7 | -84.4 | 22.4 | -10.4 | -3.8 | 41.2 | 26.9 | 4.2 | 68.4 |
| Population, net | -35.1 | 58.9 | -42.7 | -67.6 | -12.9 | -20.9 | -14.0 | -14.5 | -62.3 |
| Others, net | 9.8 | 22.8 | 16.5 | 21.7 | 5.2 | 22.9 | 14.6 | 36.3 | 78.9 |
| Gross official reserves ("-" means increase)3 | -38.6 | -15.9 | -347.9 | -297.6 | 5.3 | -11.2 | -101.4 | 5.6 | -101.8 |
| ERRORS AND OMISSIONS | -25.7 | 15.6 | -6.4 | 6.9 | 2.0 | -4.1 | -17.2 | -10.9 | -30.3 |

**Table C.2.** Foreign trade (in million of euros)

| | 2001 | 2002 | 2003 | 2004 | 2005 | 2006*) | 2007*) |
|---|---|---|---|---|---|---|---|
| Export | 1,293 | 1,178 | 1,207 | 1346 | 1,644 | 1,906 | 2,446 |
| Import | 1,893 | 2,105 | 2,038 | 2,353 | 2,604 | 2,987 | 3,795 |
| Deficit | -600 | -1,027 | -939 | -1007 | -960 | -1,081 | -1,349 |

*) Preliminary data
Source: State Statistical Office

| | 2001 | 2002 | 2003 | 2004 | 2005 | 2006*) | 2007*) |
|---|---|---|---|---|---|---|---|
| Export | 1,293 | 1,178 | 1,207 | 1,346 | 1,644 | 1,906 | 2,446 |
| - regular | 672 | 621 | 666 | 831 | 1,115 | 1,402 | 1,845 |
| - further processing | 621 | 558 | 541 | 515 | 529 | 504 | 601 |
| Import | 1,893 | 2,105 | 2,038 | 2,353 | 2,604 | 2,987 | 3,795 |
| - regular | 1,461 | 1,700 | 1,644 | 1,986 | 2,230 | 2,617 | 3,374 |
| - further processing | 432 | 405 | 393 | 368 | 375 | 371 | 421 |

*) Preliminary data
Source: State Statistical Office

**Table C.3.** Export and Import by groups of countries

| | 2001 | 2002 | 2003 | 2004 | 2005 | 2006*) | 2007*) |
|---|---|---|---|---|---|---|---|
| EXPORT | 1,293 | 1,178 | 1,207 | 1,314 | 1,644 | 1,906 | 2,446 |
| Developed countries | 711.4 | 663.8 | 704.6 | 773.6 | 877.1 | 1,062 | 1,602 |
| European Union | 668.1 | 634.6 | 687.1 | 768.2 | 870.6 | 1,053 | 1,594 |
| EFTA | 43.3 | 29.2 | 17.6 | 5.5 | 6.3 | 9 | 8 |
| Other developed countries | 129.4 | 99.1 | 101.4 | 109.4 | 150.2 | 0.0 | 0.0 |
| Central and Eastern European countries and former USSR countries | 52.8 | 55.2 | 53.9 | 80.3 | 108.8 | 0.0 | 0.0 |
| Undeveloped countries | 3.2 | 1.6 | 8.5 | 1.7 | 1.4 | 0.0 | 0.0 |
| Developing countries | 13.6 | 17.1 | 24.5 | 9.8 | 27.9 | 0.0 | 0.0 |
| Former Yugoslav countries | 382.2 | 341.1 | 321.4 | 370.6 | 477.9 | 0.0 | 0.0 |
| Other countries | 2 | 1 | 2 | 2 | 2 | 0.0 | 0.0 |
| IMPORT | 1,893 | 2,105 | 2,038 | 2,353 | 2,604 | 2,987 | 3,795 |
| Developed countries | 1,025 | 1,185 | 1,109 | 1,210,9 | 1,235,9 | 1,359 | 1,966 |
| European Union | 995 | 1,152 | 1,083 | 1,173,4 | 1,183,6 | 1,310 | 1,881 |
| EFTA | 29 | 32 | 26 | 37.5 | 52.4 | 49 | 85 |
| Other developed countries | 151 | 173 | 161 | 163.6 | 189.9 | **) | **) |
| Central and Eastern European countries and former USSR countries | 133 | 147 | 148 | 544 | 664.8 | **) | **) |
| Undeveloped countries | 1.6 | 3.4 | 1.9 | 0.9 | 1.1 | **) | **) |
| Developing countries | 98 | 115 | 117 | 172.2 | 216.7 | **) | **) |
| Former Yugoslav countries | 233 | 268 | 254 | 262 | 292.3 | **) | **) |
| Other countries | 0 | 0 | 0 | 0 | 0 | **) | **) |

*) Preliminary data
**) Due to the change in the groups of countries and the methodology of calculation, 2006 and 2007 data are not comparable with those from the previous years
Source: State Statistical Office

**Table C.4.** Export and import by main trading countries

| | - in million of euros | | | | | | | - structure in % | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | 2001 | 2002 | 2003 | 2004 | 2005 | 2006*) | 2007*) | 2001 | 2002 | 2003 | 2004 | 2005 | 2006*) | 2007*) |
| EXPORT | 1,293 | 1,178 | 1,207 | 1,314 | 1,644 | 1,906 | 2,446 | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 |
| Of which: | | | | | | | | 82.5 | 82.1 | 78.3 | 80.8 | 78.5 | 80.2 | 74.6 |
| Serbia and Montenegro | 298 | 259 | 242 | 279 | 371 | 442 | 465 | 23.0 | 21.9 | 20.0 | 21.2 | 22.5 | 23.1 | 19.0 |
| Germany | 266 | 248 | 247 | 254 | 292 | 298 | 352 | 20.5 | 21.0 | 20.4 | 19.3 | 17.7 | 15.6 | 14.3 |
| Italy | 101 | 87 | 84 | 107 | 136 | 188 | 252 | 7.8 | 7.3 | 6.9 | 8.1 | 8.2 | 9.8 | 10.3 |
| Greece | 113 | 123 | 159 | 183 | 251 | 286 | 306 | 8.7 | 10.4 | 13.1 | 13.9 | 15.2 | 15.0 | 12.5 |
| USA | 111 | 81 | 63 | 58 | 36 | 18 | 37 | 8.5 | 6.8 | 5.2 | 4.4 | 2.1 | 0.9 | 1.5 |
| Croatia | 65 | 62 | 58 | 65 | 65 | 98 | 118 | 5.0 | 5.2 | 4.8 | 4.9 | 3.9 | 5.1 | 4.8 |
| The Netherlands | 51 | 47 | 41 | 38 | 36 | 44 | 52 | 3.9 | 3.9 | 3.3 | 2.8 | 2.1 | 2.3 | 2.1 |
| Bulgaria | 23 | 23 | 22 | 41 | 62 | 103 | 176 | 1.7 | 1.9 | 1.8 | 3.1 | 3.7 | 5.4 | 7.1 |
| Slovenia | 23 | 23 | 18 | 22 | 25 | 33 | 50 | 1.7 | 1.9 | 1.4 | 1.6 | 1.5 | 1.7 | 2.0 |
| Russia | 16 | 15 | 12 | 16 | 17 | 20 | 18 | 1.2 | 1.2 | 0.9 | 1.2 | 1.0 | 1.0 | 0.7 |
| | | | | | | | | | | | | | | |
| IMPORT | 1,893 | 2,105 | 2,038 | 2,353 | 2,604 | 2,987 | 3,795 | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 | 100.0 |
| Of which: | | | | | | | | 68.9 | 68.7 | 68.2 | 65.5 | 63.4 | 62.4 | 56.8 |
| Germany | 240 | 299 | 268 | 295 | 270 | 293 | 381 | 12.6 | 14.2 | 13.1 | 12.5 | 10.3 | 9.8 | 10.0 |
| Serbia and Montenegro | 177 | 195 | 188 | 196 | 212 | 224 | 324 | 9.3 | 9.2 | 9.2 | 8.3 | 8.1 | 7.4 | 8.5 |
| Greece | 206 | 250 | 268 | 227 | 239 | 254 | 301 | 10.8 | 11.8 | 13.1 | 9.6 | 9.1 | 8.5 | 7.9 |
| Italy | 120 | 125 | 108 | 135 | 156 | 180 | 220 | 6.3 | 5.9 | 5.2 | 5.7 | 5.9 | 6.0 | 5.7 |
| Russia | 155 | 132 | 156 | 271 | 343 | 452 | 467 | 8.1 | 6.2 | 7.6 | 11.5 | 13.1 | 15.1 | 12.3 |
| USA | 57 | 62 | 50 | 38 | 36 | 41 | 57 | 3.0 | 2.9 | 2.4 | 1.6 | 1.3 | 1.3 | 1.5 |
| Slovenia | 132 | 136 | 122 | 113 | 103 | 103 | 112 | 6.9 | 6.4 | 5.9 | 4.8 | 3.9 | 3.4 | 2.9 |
| Bulgaria | 115 | 136 | 132 | 169 | 188 | 198 | 194 | 6.0 | 6.4 | 6.4 | 7.1 | 7.2 | 6.6 | 5.1 |
| Croatia | 52 | 58 | 55 | 53 | 61 | 62 | 80 | 2.7 | 2.7 | 2.6 | 2.2 | 2.3 | 2.0 | 2.1 |
| The Netherlands | 51 | 55 | 43 | 46 | 43 | 59 | 21 | 2.6 | 2.6 | 2.1 | 1.9 | 1.6 | 1.9 | 0.5 |

*) Preliminary data
Source: State Statistical Office

**Table C.5.** Export and Import by economic purpose

| In million of euros | 2001 | 2002 | 2003 | 2004 | 2005 | 2006*) | 2007*) |
|---|---|---|---|---|---|---|---|
| EXPORT | 1,293 | 1,178 | 1,207 | 1,346 | 1,644 | 1,906 | 2,446 |
| Reproduction materials | 640 | 540 | 590 | 654 | 893 | 1,105 | 1,511 |
| Operating assets | 32 | 29 | 20 | 25 | 32 | 40 | 55 |
| Consumer goods | 619 | 606 | 596 | 665 | 718 | 758 | 880 |
| Undistributed | 1 | 2 | 1 | 1 | 1 | 1 | 0 |
| | | | | | | | |
| IMPORT | 1,893 | 2,105 | 2,038 | 2,353 | 2,604 | 2,987 | 3,795 |
| Reproduction materials | 1,256 | 1,337 | 1,320 | 1,529 | 1,691 | 1,946 | 2,461 |
| Operating assets | 234 | 267 | 252 | 251 | 280 | 333 | 462 |
| Consumer goods | 397 | 497 | 463 | 570 | 631 | 704 | 867 |
| Undistributed | 5 | 4 | 2 | 2 | 2 | 3 | 3 |

*) Preliminary data
Source: State Statistical Office

**Table C.6.** Export and Import by level of processing

| | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007*) |
|---|---|---|---|---|---|---|---|
| EXPORT | 1,293 | 1,178 | 1,207 | 1,346 | 1,644 | 1,906 | 2,446 |
| Unprocessed products | 104 | 123 | 122 | 114 | 174 | 209 | 234 |
| General-level processing products | 392 | 341 | 403 | 482 | 678 | 860 | 1,224 |
| High-level processing products | 660 | 711 | 680 | 747 | 790 | 834 | 988 |
| Undistributed | 1 | 2 | 1 | 1 | 1 | 1 | 0 |
| IMPORT | 2,271 | 2,105 | 2,038 | 2,354 | 2,604 | 2,987 | 3,795 |
| Unprocessed products | 306 | 214 | 275 | 319 | 464 | 598 | 696 |
| General-level processing products | 420 | 471 | 409 | 643 | 734 | 818 | 1139 |
| High-level processing products | 1,539 | 1,416 | 1,350 | 1,389 | 1,404 | 1,568 | 1,956 |
| Undistributed | 6 | 4 | 2 | 2 | 2 | 3 | 3 |

*) Preliminary data

Source: State Statistical Office

**Table C.7.** Gross external debt - status

| | 31/12/2004 | 31/12/2005 | 31/03/2006 | 30/06/2006 | 30/09/2006 | 31/12/2006 | 31/03/2007 | 30/06/2007 | 30/09/2007 | 31/12/2007 |
|---|---|---|---|---|---|---|---|---|---|---|
| 1. STATE SECTOR | 1,016.46 | 1,282.82 | 1,078.76 | 1,079.64 | 1,076.08 | 1,066.92 | 1,003.13 | 894.08 | 887.29 | 910.45 |
| 1.1 Short-term | 0.01 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 7.64 | 0.00 |
| 1.1.1. Instrument on the money market | 0.01 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| 1.1.2. Loans | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 7.63 | 0.00 |
| 1.1.3. Commercial credits | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| 1.1.4. Other liabilities | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.01 | 0.00 |
| Outstanding liabilities due | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.01 | 0.00 |
| Other | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| 1.2 Long-term | 1,016.45 | 1,282.82 | 1,078.76 | 1,079.64 | 1,076.08 | 1,066.92 | 1,003.13 | 894.08 | 879.65 | 910.45 |
| 1.2.1. Bonds | 23.25 | 187.47 | 190.99 | 191.87 | 191.67 | 191.74 | 191.04 | 187.07 | 185.00 | 183.03 |
| 1.2.2. Loans | 993.20 | 1,095.36 | 887.76 | 887.77 | 884.41 | 875.19 | 812.09 | 707.01 | 694.65 | 727.41 |
| 1.2.3. Commercial credits | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| 1.2.4. Other liabilities | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| 2. MONETARY AUTHORITY (NBRM) | 45.97 | 52.66 | 51.81 | 47.82 | 47.26 | 42.39 | 38.09 | 0.00 | 0.00 | 0.00 |
| 2.1 Short-term | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| 2.1.1. Instrument on the money market | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| 2.1.2. Loans | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| 2.1.3. Currencies and deposits | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| 2.1.4. Other liabilities | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| Outstanding liabilities due | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| Other | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| 2.2 Long-term | 45.97 | 52.66 | 51.81 | 47.82 | 47.26 | 42.39 | 38.09 | 0.00 | 0.00 | 0.00 |
| 2.2.1. Bonds | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| 2.2.2. Loans | 45.97 | 52.66 | 51.81 | 47.82 | 47.26 | 42.39 | 38.09 | 0.00 | 0.00 | 0.00 |
| 2.2.2. Currencies and deposits | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| 2.2.4. Other liabilities | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| 3. BANK SECTOR | 123.24 | 192.02 | 181.68 | 191.44 | 205.47 | 269.88 | 266.70 | 312.94 | 340.70 | 387.92 |
| 3.1 Short-term | 67.32 | 81.41 | 72.25 | 77.76 | 83.57 | 115.44 | 111.15 | 144.87 | 165.51 | 175.93 |
| 3.1.1. Instrument on the money market | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| 3.1.2. Loans | 7.04 | 1.30 | 0.00 | 0.00 | 0.00 | 0.00 | 24.22 | 30.76 | 41.67 | 16.50 |

| | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| 3.1.3. Currencies and deposits | 51.71 | 69.46 | 61.74 | 67.18 | 72.85 | 104.70 | 77.56 | 104.54 | 114.30 | 152.26 |
| 3.1.4. Other liabilities | 8.57 | 10.66 | 10.52 | 10.58 | 10.72 | 10.74 | 9.37 | 9.56 | 9.55 | 7.17 |
| Outstanding liabilities due | 8.57 | 10.66 | 10.52 | 10.58 | 10.72 | 10.74 | 9.37 | 9.56 | 9.55 | 7.17 |
| Other | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| 3.2 Long-term | 55.93 | 110.60 | 109.42 | 113.68 | 121.90 | 154.44 | 155.55 | 168.07 | 175.19 | 211.99 |
| 3.2.1. Bonds | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| 3.2.2. Loans | 55.79 | 106.40 | 103.29 | 107.48 | 115.91 | 146.31 | 147.36 | 159.90 | 166.73 | 202.07 |
| 3.2.3. Currencies and deposits | 0.14 | 4.20 | 6.14 | 6.20 | 5.99 | 8.13 | 8.20 | 8.17 | 8.47 | 9.92 |
| 3.2.4. Other liabilities | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| 4. OTHER SECTORS | 600.40 | 721.01 | 664.92 | 727.28 | 701.21 | 786.69 | 823.94 | 846.00 | 868.99 | 973.37 |
| 4.1 Short-term | 370.02 | 475.84 | 409.86 | 425.28 | 390.24 | 435.42 | 448.80 | 473.29 | 501.86 | 619.50 |
| 4.1.1. Instrument on the money market | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| 4.1.2. Loans | 4.78 | 53.03 | 15.56 | 30.32 | 17.16 | 11.65 | 26.15 | 19.93 | 34.60 | 31.70 |
| 4.1.3. Currencies and deposits | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| 4.1.4. Commercial credits | 322.58 | 362.86 | 341.53 | 343.08 | 314.62 | 349.59 | 359.78 | 364.52 | 371.00 | 442.89 |
| 4.1.5. Other liabilities | 42.66 | 59.95 | 52.76 | 51.89 | 58.46 | 74.17 | 62.87 | 88.84 | 96.26 | 144.92 |
| Outstanding liabilities due | 42.66 | 58.40 | 52.76 | 51.89 | 58.46 | 74.17 | 62.87 | 88.84 | 96.26 | 144.92 |
| Other | 0.00 | 1.54 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| 4.2 Long-term | 230.39 | 245.18 | 255.06 | 302.00 | 310.97 | 351.27 | 375.14 | 372.71 | 367.13 | 353.87 |
| 4.2.1. Bonds | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| 4.2.2. Loans | 207.63 | 234.14 | 242.23 | 283.70 | 290.16 | 331.68 | 357.18 | 358.06 | 354.13 | 341.67 |
| 4.2.3. Currencies and deposits | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| 4.2.4. Commercial credits | 22.76 | 11.04 | 12.83 | 18.30 | 20.81 | 19.59 | 17.96 | 14.65 | 13.00 | 12.20 |
| 4.2.5. Other liabilities | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 | 0.00 |
| 5. DIRECT INVESTMENTS: loans between associated entities | 284.52 | 269.57 | 327.43 | 334.18 | 332.61 | 329.30 | 337.70 | 386.11 | 394.89 | 439.80 |
| 5.1. Liabilities towards directly invested entities | 3.70 | 5.68 | 5.68 | 5.68 | 5.68 | 13.16 | 13.16 | 13.16 | 13.16 | 13.16 |
| 5.2. Liabilities towards direct investors | 280.82 | 263.89 | 321.75 | 328.50 | 326.93 | 316.14 | 324.54 | 372.95 | 381.73 | 426.63 |
| GROSS EXTERNAL DEBT | 2,070.61 | 2,518.09 | 2,304.60 | 2,380.36 | 2,362.63 | 2,495.18 | 2,469.56 | 2,439.14 | 2,491.88 | 2,711.54 |

Source: NBRM

# 2007

## D. MONETARY SECTOR

**Table D.1.** Monetary survey (in million of denars)

| | XII.06 | III.07 | VI.07 | IX.07 | XII.07 |
|---|---|---|---|---|---|
| I. Net foreign assets | 108,042 | 108,475 | 107,566 | 111,578 | 109,791 |
| National Bank | 85,116 | 85,066 | 87,790 | 94,209 | 94,343 |
| Assets | 87,761 | 87,526 | 87,849 | 94,209 | 94,343 |
| Liabilities | 2,645 | 2,460 | 59 | 0 | 0 |
| Deposit banks | 22,926 | 23,409 | 19,776 | 17,369 | 15,448 |
| Assets | 39,707 | 39,614 | 39,000 | 38,175 | 38,412 |
| Liabilities | 16,781 | 16,205 | 19,224 | 20,806 | 22,964 |
| | | | | | |
| II. Net domestic assets | 28,288 | 34,538 | 48,712 | 50,327 | 66,205 |
| | | | | | |
| 1. Domestic credits | 77,176 | 85,601 | 100,434 | 104,481 | 123,140 |
| Of which: claims from the government | -17,184 | -15,513 | -9,477 | -15,736 | -5,921 |
| a) Deposit banks | 107,866 | 115,570 | 126,931 | 134,410 | 142,100 |
| - in denars | 84,368 | 90,626 | 99,837 | 105,391 | 111,467 |
| Government | 13,377 | 14,337 | 16,907 | 14,020 | 12,784 |
| Credits | 13,355 | 14,314 | 16,883 | 13,999 | 12,763 |
| a) Budget and ministries | 13,095 | 14,052 | 16,777 | 13,946 | 12,724 |
| b) Funds | 260 | 262 | 106 | 53 | 39 |
| c) Central government authority institutions: courts, etc. | 0 | 0 | 0 | 0 | 0 |
| Calculated outstanding interest | 22 | 23 | 24 | 21 | 21 |
| Non-government sector | 70,991 | 76,289 | 82,930 | 91,371 | 98,683 |
| Credits | 66,410 | 71,537 | 78,031 | 86,908 | 94,484 |
| Of which: Outstanding claims | 9,810 | 9,560 | 10,049 | 10,125 | 8,966 |
| Calculated outstanding interest | 4,581 | 4,752 | 4,899 | 4,463 | 4,199 |
| - in foreign currency | 23,498 | 24,944 | 27,094 | 29,019 | 30,633 |
| Government | 129 | 119 | 113 | 173 | 255 |
| Of which: Outstanding claims | 0 | 0 | 0 | 0 | 0 |
| Non-government sector | 23,369 | 24,825 | 26,981 | 28,846 | 30,378 |
| Of which: Outstanding claims | 1,650 | 1,511 | 1,611 | 1,763 | 1,516 |
| b) Claims by the National Bank from the Government | -30,690 | -29,969 | -26,497 | -29,929 | -18,960 |
| 2. Other items, net | -48,888 | -51,063 | -51,722 | -54,154 | -56,935 |
| Of which: claims from the Government for frozen currency saving deposits | 0 | 0 | 0 | 0 | 0 |
| Calculated outstanding interest | -4,603 | -4,775 | -4,923 | -4,484 | -4,220 |
| Other | -44,285 | -46,288 | -46,799 | -49,670 | -52,715 |
| M4 Total | 136,330 | 143,013 | 156,278 | 161,905 | 175,996 |
| M4 (non government sector) | 135,131 | 141,473 | 155,152 | 160,861 | 175,031 |
| M1 (Total) | 35,436 | 35,281 | 36,864 | 39,864 | 46,201 |
| M1 (non government sector) | 34,747 | 34,254 | 36,319 | 39,348 | 45,758 |

| | | | | | |
|---|---|---|---|---|---|
| Money in circulation | 16,206 | 15,034 | 15,844 | 16,746 | 17,936 |
| Deposit money (total) | 19,230 | 20,247 | 21,020 | 23,118 | 28,265 |
| Deposit money (non government sector) | 18,541 | 19,220 | 20,475 | 22,602 | 27,822 |
| Deposit money | 19,207 | 19,824 | 20,814 | 22,645 | 28,117 |
| Deposit money of non government sector | 18,518 | 18,797 | 20,269 | 22,129 | 27,674 |
| Deposit money of the Government | 689 | 1,027 | 545 | 516 | 443 |
| a) Budget and ministries | 551 | 226 | 232 | 276 | 271 |
| b) Funds | 138 | 801 | 312 | 239 | 172 |
| c) Central government authority institutions: courts, etc. | 0 | 0 | 1 | 1 | 0 |
| National Bank- deposit money of non-government sector | 23 | 423 | 206 | 473 | 148 |
| M2 (Total) | 129,644 | 136,240 | 147,785 | 152,443 | 165,709 |
| M2 (non government sector) | 128,494 | 134,750 | 146,709 | 151,450 | 164,857 |
| Quasy deposits (total) | 94,208 | 100,959 | 110,921 | 112,579 | 119,508 |
| Quasy deposits (non government sector) | 93,747 | 100,496 | 110,390 | 112,102 | 119,099 |
| Deposit banks | 94,208 | 100,959 | 110,921 | 112,579 | 119,508 |
| Non government sector | 93,747 | 100,496 | 110,390 | 112,102 | 119,099 |
| Denars | 36,317 | 40,511 | 48,389 | 50,045 | 55,057 |
| Foreign currency | 57,430 | 59,985 | 62,001 | 62,057 | 64,042 |
| Government deposits | 461 | 463 | 531 | 477 | 409 |
| Denars | 460 | 462 | 531 | 477 | 408 |
| Foreign currency | 1 | 1 | 0 | 0 | 1 |
| NBRM -quasy deposits | 0 | 0 | 0 | 0 | 0 |
| Non-monetary deposits (total) | 6,686 | 6,773 | 8,493 | 9,462 | 10,287 |
| Non-monetary deposits in denars (total) | 3,678 | 3,799 | 4,938 | 5,549 | 5,783 |
| Non-monetary deposits in foreign currency (total) | 3,008 | 2,974 | 3,555 | 3,913 | 4,504 |
| Non-monetary deposits (non government sector) | 6,637 | 6,723 | 8,443 | 9,411 | 10,174 |
| Non-monetary deposits in denars (non government sector) | 3,629 | 3,749 | 4,888 | 5,498 | 5,670 |
| Non-monetary deposits in foreign currency (non government sector) | 3,008 | 2,974 | 3,555 | 3,913 | 4,504 |
| - Deposit banks | 6,686 | 6,773 | 8,493 | 9,462 | 10,287 |
| Non-monetary deposits in denars (non government sector) | 3,629 | 3,749 | 4,888 | 5,498 | 5,670 |
| Non-monetary deposits in foreign currency (non government sector) | 3,008 | 2,974 | 3,555 | 3,913 | 4,504 |
| Non-monetary deposits in denars (government) | 49 | 50 | 50 | 51 | 113 |
| Non-monetary deposits in foreign currency (government sector) | 0 | 0 | 0 | 0 | 0 |
| - NBRM non-monetary deposits (non-government sector | 0 | 0 | 0 | 0 | 0 |
| Denars | 0 | 0 | 0 | 0 | 0 |
| Foreign currency | 0 | 0 | 0 | 0 | 0 |
| Total deposits | 120,124 | 127,979 | 140,434 | 145,159 | 158,060 |
| Total deposits (non government sector) | 118,925 | 126,439 | 139,308 | 144,115 | 157,095 |
| Source: NBRM | | | | | |

# E. SOCIAL SECTOR

**Table E.1.** Activity measurements of population

| | Activity rate | | | Employment rate | | | Unemployment rate | | |
|---|---|---|---|---|---|---|---|---|---|
| | 2005 | 2006 | 2007 | 2005 | 2006 | 2007 | 2005 | 2006 | 2007 |
| Total (15-64) | 60.7 | 62.2 | 62.8 | 37.9 | 39.6 | 40.7 | 37.6 | 36.3 | 35.2 |
| Male | 71.9 | 74.9 | 74.9 | 45.4 | 48.3 | 48.8 | 36.9 | 35.6 | 34.8 |
| Female | 49.1 | 49.2 | 50.4 | 30.1 | 30.7 | 32.3 | 38.8 | 37.5 | 35.8 |
| 15-24 | 32.9 | 35.8 | 35.9 | 12.3 | 14.4 | 15.2 | 62.6 | 59.8 | 57.7 |
| 2549 | 77.6 | 78.8 | 79.0 | 49.8 | 52.0 | 53.0 | 35.9 | 34.0 | 32.9 |
| 50-64 | 49.9 | 50.8 | 52.9 | 36.0 | 36.4 | 37.8 | 27.9 | 28.4 | 28.5 |
| By education | | | | | | | | | |
| - Primary education | 35.2 | 36.8 | - | 19.9 | 21.4 | - | 43.3 | 41.8 | 42.6 |
| - Secondary education | 68.4 | 69.4 | - | 42.0 | 43.7 | - | 38.6 | 36.9 | 35.1 |
| - High education | 80.6 | 82.3 | - | 64.0 | 64.9 | - | 20.5 | 21.2 | 20.5 |

Source: SSO, Labour Force Survey (LFS)

**Table E.2.** Employed persons according to the economic status, sectors and property (age 15+)

| | 2003 | 2004 | 2005 | 2006 | 2007 |
|---|---|---|---|---|---|
| | Employed persons according to the sectors | | | | |
| Agriculture | 22.1 | 16.8 | 19.5 | 18.5 | 50.4 |
| Industry | 27.3 | 25.8 | 25.8 | 26.4 | 24.9 |
| Construction | 6.6 | 7.0 | 6.5 | 7.6 | 18.3 |
| Services | 44.0 | 50.4 | 48.2 | 47.5 | 6.4 |
| | Employed persons according to the economic status | | | | |
| Employees | 72.7 | 75.4 | 71.8 | 70.8 | 72.3 |
| Employers | 7.6 | 5.9 | 5.7 | 5.9 | 12.1 |
| Self-employees | 8.2 | 10.2 | 12.0 | 12.4 | 10.1 |
| Unpaid family workers | 11.4 | 8.5 | 10.4 | 10.9 | 5.5 |
| | Employed persons according to the property | | | | |
| Private ownership | 54.4 | 56.7 | 62.4 | 65.8 | 69.0 |
| Other (social, mixed, cooperative, state) | 45.6 | 43.3 | 37.6 | 34.2 | 31.0 |

Source: SSO, LFS

**Table E.3.** Social protection

| | 2001 | 2002 | 2003 | 2004 | 2005 | 2006 | 2007 |
|---|---|---|---|---|---|---|---|
| Average pension - end of period- | 6,524 | 6,760 | 7,205 | 7,417 | - | 7,580 | 7,782 |
| Pension beneficiaries | 247,200 | 249,421 | 254,267 | 260,075 | 265,152 | 269,681 | 272,386 |
| Number of households receiving welfare | 80,160 | 82,673 | 64,453 | 66,940 | 66,485 | 65,540 | 62,443 |
| Number of beneficiaries of unemployment benefit | 41,375 | 46,772 | 47,324 | 45,867 | 40,124 | 30,572 | 24,686 |

Source: PDIFRM, EARM, Ministry of Labour and Social Policy

# 2007

**Publisher** Ministry of Finance of Republic of Macedonia

**Editor-in-chief** Trajko Slaveski, Ph.D.

**Editorial board** Nikica Mojsoska - Blazevski, Ph.D.
Snezana Delevska, Aneta Dimovska

**Pre-press/print** Global Communications, Skopje