



# FORMER YUGOSLAV REPUBLIC OF MACEDONIA

## STAFF REPORT FOR THE FOURTH POST-PROGRAM MONITORING DISCUSSIONS; AND PRESS RELEASE

January 27, 2015

In the context of the fourth review under the Post Program Monitoring Discussions, the following documents have been released and are included in this package:

- The **Staff Report** prepared by a staff team of the IMF for the Executive Board's consideration on a lapse of time basis, following discussions that ended on November 10, 2014, with the officials of the Former Yugoslav Republic of Macedonia on economic developments and policies under the Post Program Monitoring Discussions. Based on information available at the time of these discussions, the staff report was completed on December 17, 2014.
- A **Press Release** summarizing the staff report.

The following documents have been or will be separately released.

The publication policy for staff reports and other documents allows for the deletion of market-sensitive information.

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# FORMER YUGOSLAV REPUBLIC OF MACEDONIA

## FOURTH POST-PROGRAM MONITORING DISCUSSIONS

December 17, 2014

### KEY ISSUES

**The jobs and growth agenda should remain a top policy priority, with efforts focused on relaxing key constraints for domestic firms.** Priorities include properly implementing and monitoring recent initiatives to enforce payment discipline in both public and private sector contracts, as well as upgrading the professional status of inspection bodies, clarifying their mandate, and streamlining their work.

**The public-sector led growth strategy will put pressure on other types of spending if consolidation is to proceed in the current low-tax environment.** Investment spending should target gaps in transport and energy infrastructure to maximize the payoff for medium-term growth. At the same time, with public debt rising steadily to over 50 percent of GDP by 2017, fiscal policy should aim at reducing the deficit to below 2.6 percent of GDP by 2016. In the absence of further tax policy changes to boost revenues, a comprehensive spending review that seeks to minimize the growth impact of current expenditure compression should therefore be undertaken.

**More comprehensive public debt management is needed to support external sustainability.** To further reduce risks, particularly currency risk, the strategy should be expanded to cover the debt of SOEs and contingent liabilities. Increased reliance on foreign currency borrowing also has important implications for central bank reserve developments and domestic liquidity that should be taken into account in evaluating government financing options.

**The monetary easing cycle has reached its end.** The combination of relaxed financial conditions and tight prudential regulation has helped revive credit growth while preserving the health of the financial sector. While temporary supply-side developments have recently generated deflationary pressures, the focus of monetary policy henceforth should be on maintaining the attractiveness of holding denar-denominated assets in support of the exchange rate peg.

**Outstanding credit is scheduled to fall below 200 percent of quota at end-year.** The external position and capacity to pay are sufficiently strong to allow for a cessation of post-program monitoring.

Approved By  
**Philip Gerson and  
 Dhaneshwar Ghura**

Discussions were held in Skopje, October 27–November 10, 2014. A team comprised of Ms. Vladkova Hollar (head), Messrs. Gerard and Mikkelsen, Ms. Taheri Sanjani (all EUR), and Messrs. Gitton and Nacevski (Res Rep office) met with Finance Minister and Deputy Prime Minister Stavreski, NBRM Governor Bogov, other senior officials, and private sector representatives. Mr. Clicq (OED) and Mr. Shimbov (World Bank) joined some of the discussions. A joint press conference was held at the conclusion of the mission. Ms. Mahadewa and Ms. Chen assisted in the preparation of the staff report.

## CONTENTS

<b>A HOME-GROWN RECOVERY</b>	<b>4</b>
<b>OUTLOOK AND RISKS: A GRADUAL REBALANCING</b>	<b>5</b>
<b>POLICY DISCUSSIONS</b>	<b>7</b>
A. Fiscal Policy—Managing the Risks from Public Sector-Led Growth	7
B. Monetary and Financial Policy—a Focus on Maintaining Stability	11
C. Structural Issues—Ensuring A Handover to Private Sector-Led Growth	13
<b>POST-PROGRAM MONITORING</b>	<b>14</b>
<b>STAFF APPRAISAL</b>	<b>15</b>
<b>BOX</b>	
Implications of Government Borrowing on Monetary Policy Implementation	10
<b>FIGURES</b>	
1. Recent Developments	16
2. Real Sector Developments, 2008–2014	17
3. Credit Developments, 2008–2014	18
4. Monetary Policy Developments, 2008–2014	19
5. Banking Sector Developments, 2008–2014	20
6. External Sector Developments, 2008–2014	21
7. External Debt Sustainability: Bound Tests	31
<b>TABLES</b>	
1. Macroeconomic Framework, 2010–2019	22
2. Central Government Operations, 2010–2019	23
3. Balance of Payments, 2010–2019	26

4. Monetary Survey, 2010–2019	26
5. Central Bank Survey, 2010–2019	27
6. Financial Soundness Indicators of the Macedonian Banking System, 2010–2014	28
7. Capacity to Repay Indicators, 2013–2019	29
8. External Debt Sustainability Framework, 2009–2019	30

**ANNEX**

Debt Sustainability Analysis	32
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## A HOME-GROWN RECOVERY

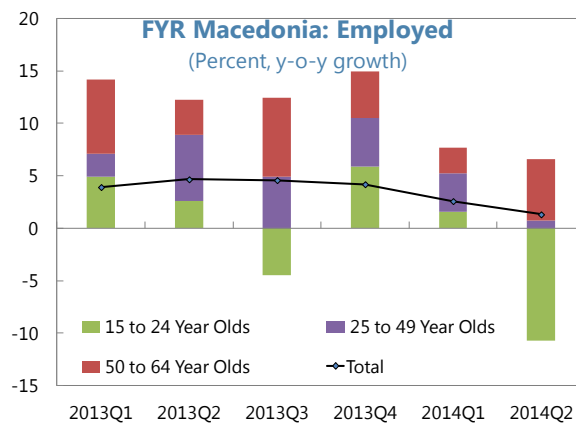
The authorities continue to take a proactive approach to generating jobs and growth, anchored in public capital expenditure and policies to attract FDI. Along with a delay in fiscal consolidation, this strategy seems to have contributed to near-term payoffs in employment (which received a large 4.3 percent boost in 2013), exports (up by 15 percent ytd despite slowing external demand), and overall economic growth, which, at 3½ percent, is running about 2 percentage points above the average for south-eastern Europe.

**1. Growth is picking up, supported by strong exports and domestic demand.** Economic activity accelerated in Q2, resulting in growth of almost 4 percent over the first half of 2014. Government consumption growth turned positive, and strong gross capital formation likely reflects the impact of public infrastructure projects. Private consumption growth steepened in line with higher consumer credit growth, real wages, and pensions. The contribution from net exports remained negative, but exports have been dynamic, increasing by about 15 percent over the first eight months of the year, buoyed by new capacity from firms in the special economic zones.

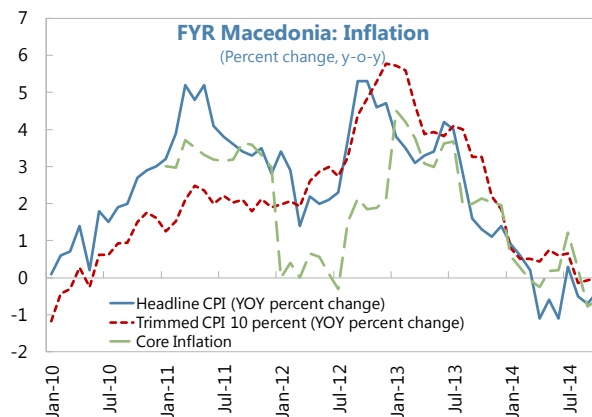
**2. Despite strong export performance, an 18-month decline in reserves was halted only by a €500 million Eurobond issuance in July.** Given muted portfolio and other investment flows, reserves continued to decline throughout the first semester. The Eurobond issuance (3.975 percent, 7 years) provided large cash buffers to both the external and fiscal accounts, fully pre-financing the €150 million Eurobond maturing in 2015.

**3. The labor market continues to improve, but more slowly than in 2013.** The unemployment rate decreased to 28.2 percent by the first half of 2014 from 29 percent last year and 31 percent in 2012. This is chiefly attributable to a decline in the number of the unemployed aged 25–64. Employment growth slowed in 2014, mainly due to a decline in youth employment. For the first half of the year, the employment rate stood at 41.1 percent, reflecting a deceleration in the pace of job creation, mainly in the agricultural sector.

**4. Consumer prices are still declining, driven by low food prices.** Deflation eased to 0.4 percent year-on-year by October. Core inflation over the first nine months stood at 0.2 percent. Deflation has been driven by food prices, which contracted by 1.1 percent, and generally low imported inflation. Prices are expected to pick up slightly going forward, in line with



Source: Republic of Macedonia State Statistical Office.



Sources: FYR Macedonia State Statistical Office and IMF staff calculations.

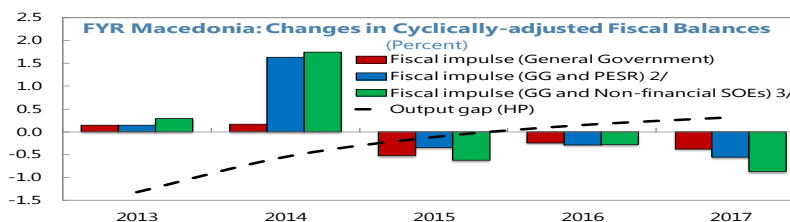
expected price developments in the Euro area and a rise in food prices in the second half of 2015.

**5. The banking sector appears healthy, although NPLs have recently increased.** As of 2014 Q2, banks are well-capitalized (CAR at 16.9 percent), liquid (liquidity ratio at 26 percent) and increasingly funded by long-term domestic currency deposits. With contained overhead costs, slightly improved net interest margins have allowed for a rebound in profitability. Non-performing loans, which had been falling since the second half of 2013, have edged up to 11.3 percent of gross loans, but remain more than fully provisioned.

**6. As a result, credit growth has steadily strengthened, and is close to historical averages.** Credit growth accelerated to 9.7 percent year-on-year in October. Lending has been especially dynamic for households (up 12.3 percent year-on-year), but credit to the corporate sector has also picked up (accelerating to about 7.8 percent year-on-year from the trough of mid-2013), though mostly to provide working capital rather than to finance new projects.

**7. Fiscal policy is delivering a stronger impulse than expected at the time of the Article IV discussions, driven by a wider central government deficit.**

As foreshadowed during the Article IV consultation, revenues significantly underperformed over the first nine months (by roughly 0.8 percent of GDP) despite strong domestic demand. In September—with the nine-month budget deficit at 89 percent of the 3.5 percent of GDP annual target—Parliament adopted a supplementary budget that offsets roughly half of the underperformance, and is expected to result in a full year deficit of 3.8 percent of GDP.

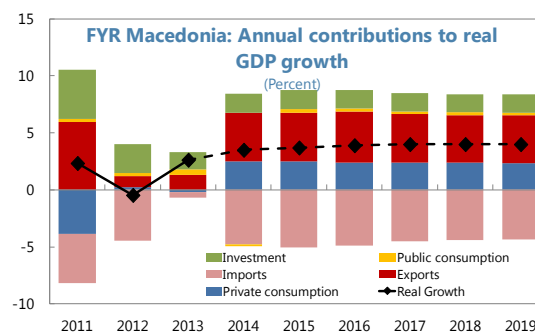


Sources: MoF and IMF Staff estimates.

Note: 1) HP stands for Hedrick-Prescott Filter. The fiscal impulse (primary balance here) is the difference in the cyclically-adjusted balance between the previous and the current year (a negative fiscal impulse means a cyclically-adjusted contraction). Cyclical adjustment of fiscal balances is done with respect to output gap. The fiscal deficit is adjusted for a structural break to include central government and the off-budget PESR deficit in 2013. 2) This includes the operation of the public Enterprise for State Roads. 3) This includes the operation of all non-financial SOEs.

## OUTLOOK AND RISKS: A GRADUAL REBALANCING

**8. Growth is expected to converge to 4 percent annually in the medium term on current fundamentals.** Investment—bolstered by large public infrastructure projects—is expected to contribute 1½–2 percentage points to growth over the next few years. The contribution from net exports would remain negative as higher investment-related imports offset the positive impact of increasing exports, although support to growth from exports would gradually strengthen. The authorities are exploring new projects to foster high-skill



Sources: Republic of Macedonia State Statistics Office, and IMF staff calculations.

Note: 2011-2013 historical vintages of national account are revised based on ESA 2010 methodology.

jobs creation through promoting foreign investment in the financial sector (see ¶25 and ¶28) and, potentially, the health sector, modeled on the existing technological and industrial development zones.

**9. Credit growth rates are expected to stabilize around historical rates of 7–8 percent.**

Credit growth is expected to reach 7.8 percent by the end of the year, and then stabilize at this level against the backdrop of continued denar deposit growth, net foreign assets accumulation and increasing competition in the banking sector, notably among medium-sized banks. With fifteen banks operating in Macedonia, some further mergers among the smaller banks—a process that the authorities are trying to encourage—should help increase the efficiency of intermediation.

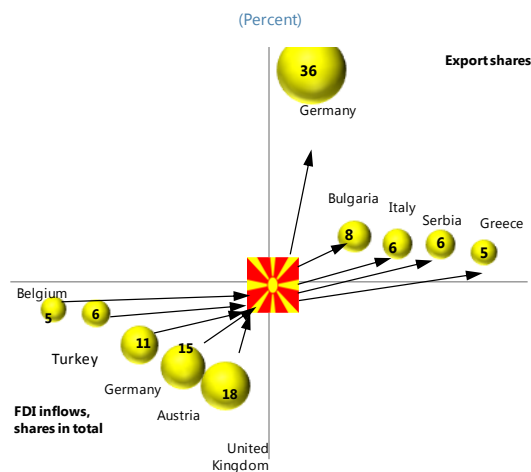
**10. The external position is expected gradually to improve over the medium term, but the contribution of the private sector to reserve accumulation would remain limited.** After peaking at 20 percent of GDP in 2016 due to an expected pick-up in investment-related imports, the deficit on the goods and services balance should gradually improve to about 17 percent by 2019 under the effect of dynamic export volume growth and higher value added of manufacturing products assembled in the new facilities. Even under the assumption that private transfers would decline over the medium term, the current account deficit, at around 4 percent of GDP, would remain broadly covered by FDI flows. Without an acceleration of other private capital inflows, reserve accumulation would mainly reflect public sector external borrowing associated with the implementation of large infrastructure projects.

**11. Public sector debt is expected to increase to about 52 percent of GDP by 2019.** The key drivers are the gradual increase in general government debt, to just over 40 percent and the debt of non-financial SOEs which is projected rise by about 7 percentage points of GDP between 2013 and 2019 (DSA annex).

## Risks

**12. A protracted slump in the Euro area, continued deflation, and oil supply disruptions are key risks.** A stalling recovery in the Euro area would weigh on foreign demand and potentially weaken—or postpone—FDI inflows. However, Macedonia’s export reorientation is to inputs for the automotive industry, the dynamics of which may differ from those of the broader European economy. With an energy trade deficit of about 8.5 percent of GDP, energy supply disruptions resulting from geopolitical conflicts would rapidly increase capacity constraints. While inflation is expected to pick up, continued deflation could disrupt growth and complicate fiscal adjustment.

**FYR Macedonia: Trade and FDI linkages, 2013**



Sources: NBRM; and IMF staff calculation.

**13. Uncertainties related to the framework of cooperation with the single European supervisor are an additional source of risk.** The framework for cooperation with the SSM remains to be articulated, with the Vienna Initiative expected to provide inputs into the design of a MoU between the ECB and non-EU states. Meanwhile, the authorities continue to engage in cross-border coordination with the Greek and Slovenian supervisors. However, the forthcoming differential treatment of home and host central bank and sovereign securities for risk-weighted asset computation by parent banks may have unintended consequences for the conduct of monetary policy and shift preferences toward holdings of foreign liquid assets.

**14. The EU accession process is at an impasse.** In its October 2014 progress report, the European Commission maintained its recommendation to open accession negotiations, but expressed concerns about increasing politicization of state institutions, the independence of the judiciary and government control over the media, including in the context of elections. Political dialogue is blocked as the main opposition party refuses to sit in Parliament, and the name dispute with Greece remains unresolved.

### Data Issues

**15. Given the key role of statistics in policymaking, efforts should focus on reducing recent volatility in key macroeconomic data.** The moves to improve source data and, more recently, to produce national accounts data in line with the ESA 2010 methodology, while welcome, have introduced notable volatility. Successive data releases over the last 12 months have introduced significant and frequent revisions in historical series, complicating the analysis of economic developments. Support should be given to alleviate capacity constraints in the statistical office.

## POLICY DISCUSSIONS

### A. Fiscal Policy—Managing the Risks from Public Sector-Led Growth

*Fiscal consolidation—embedded in a medium-term fiscal strategy and underpinned by measures—is needed to rebuild buffers and safeguard the sustainability of public finances, and to support the exchange rate peg<sup>1</sup>. The increasing role played by the state in the economy—notably through higher public expenditure—requires a careful evaluation of spending priorities for the consolidation to proceed.*

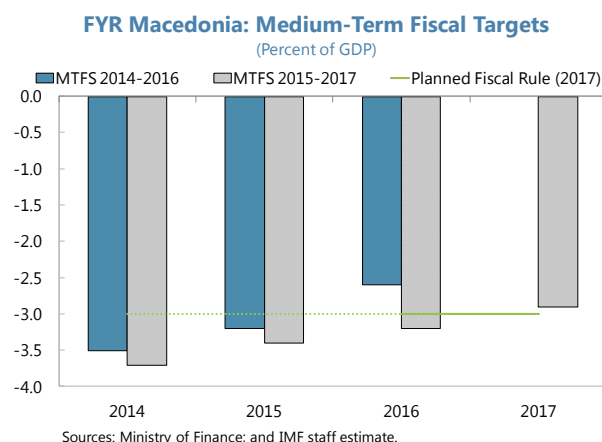
**16. Stronger fiscal consolidation is needed.** The adjustment path previously set under the 2014–2016 fiscal strategy appropriately aimed at bringing the central government deficit to 2.6 percent of GDP by 2016, a level that would broadly stabilize the debt-to-GDP ratio. The upward revision of the budget deficit target for 2014 and the relaxation of fiscal targets in the newly

<sup>1</sup> The exchange rate regime is referred to as a peg to the euro in this report. Formally, the official (*de jure*) exchange rate classification is “floating”, even though the NBRM buys or sells foreign exchange to keep the denar trading in a very narrow band around the rate of 61.5 denars per euro; thus, the *de facto* classification is “stabilized.”



approved 2015–2017 fiscal strategy (see text chart) mean that central government debt will likely continue to rise through 2019. More positively, budgeted tax revenues—in 2015, but also in the

medium-term fiscal strategy (text table, ¶17)—are now underpinned by credible macroeconomic assumptions. Any over-performance on revenues should be used to improve the fiscal balance, rather than to boost spending. Frontloading the consolidation will help ensure compliance with the planned fiscal rule, which will cap the deficit at 3 percent of GDP starting in 2017.



**17. Meeting the key objectives of fiscal policy will require a careful evaluation of spending priorities.** The available revenue envelope reflects a strategic decision to maintain a low corporate tax environment. Moreover, looking forward, the growth of tax revenues may not keep pace with that of output, reflecting in large part the expansion of activity in special economic zones subject to preferential tax schemes. Under these circumstances, the needed fiscal consolidation implies some trade-offs and requires careful prioritization of spending, in line with long-term developmental goals.

- Capital expenditure will remain high in the medium term in order to meet large infrastructure needs and support growth. Embedding the public investment decision-making process in a rigorous economic cost-benefit analysis would ensure maximum payoff.

- To allow for planned increases in pension and other social transfers as outlined in the fiscal strategy for 2016 and 2017, other current spending will have to remain frozen in nominal terms. Within that

envelope, particular pressures may emerge on the wage bill, as highlighted during the 2014 Article IV consultation (see EBS/14/75). In order to reduce salary compression and offer

**FYR Macedonia: Medium Term Fiscal Strategy, 2015- 2017**  
(billions of denars unless otherwise indicated)

	2015	2016	2017	(% change)	
				2016	2017
Total Revenues	163.3	168.9	175.2	3.4	3.7
Tax Revenues	89.0	91.6	95.2	2.9	3.9
Total Expenditures	181.8	187.9	193.4	3.4	3.0
Primary Expenditures	175.8	180.8	185.3	2.9	2.5
Priority Expenditures	103.9	108.9	113.2	4.8	4.0
Capital	21.2	22.2	22.2	4.6	0.2
Social Transfers and Allowances	82.6	86.7	91.0	4.9	4.9
Other Primary Expenditure	71.9	72.0	72.1	0.0	0.2
Deficit	-18.5	-19.0	-18.3		
(percent of GDP)	-3.4%	-3.3%	-3.0%		
Memo:					
Nominal GDP	546.9	579.6	617.3	6.0	6.5

Sources: Ministry of Finance; and IMF staff estimate.

competitive pay in the context of upgrading the quality of civil service, as well as to ensure sufficient staffing for key public institutions, a broad review of public administration is needed.

- Potential pressures on expenditure stemming from new projects or any additional transfers to the Health Fund for the gradual reduction in arrears (currently about 0.4 percent of GDP) would have to be accommodated within the expenditure ceilings<sup>2</sup> in the medium-term fiscal framework. This, too, would require finding offsetting expenditure savings elsewhere.

**18. Broader risks and costs associated with the public sector financing mix should be integrated in the debt management strategy.** Staff welcomed the inclusion of explicit targets for refinancing, interest, and currency risks in the debt management strategy, which accompanies the medium-term fiscal strategy. The planned lengthening of the average maturity of domestic debt should help reduce refinancing risks, and caps on the share of variable interest rate loans and the share of non-euro foreign currency borrowing in total FX borrowing diminish interest rate and currency risks. However, staff emphasized the need for the risk management strategy to take a broader perspective on public sector debt, notably by covering the debt of SOEs and contingent liabilities.

**19. Increased reliance on foreign currency borrowing has implications for external sustainability and the conduct of monetary policy.** As of 2015, financing plans envisage that domestic borrowing would only be used to refinance maturing domestic debt, implying that deficits would primarily be financed through foreign currency borrowing. Such a reliance on foreign currency borrowing to finance domestic currency payments would lead to an increasing supply of local currency liquidity, which the central bank would have to sterilize. Staff suggested that the debt management strategy should explicitly take into account the costs and risks arising from the impact of government financing choices on central bank reserve developments and domestic liquidity (see Box 1).

#### ***Authorities' views***

**20. The authorities reiterated their commitment to a formal fiscal rule that will cap the deficit at 3 percent of GDP.** They saw this year's postponement of consolidation as a necessary response to continued uncertainty about the sustainability of the recovery, and noted that, in their view, there was still some fiscal space to support demand. They were confident that they would not breach the deficit ceiling in 2017, and intend to use an operational deficit target of 1.5 percent of GDP in the longer term.

<sup>2</sup> Parliament approves the medium-term fiscal strategy, but expenditure ceilings are purely indicative.

### Box 1. Implications of Government Borrowing on Monetary Policy Implementation

#### Government borrowing is expected to significantly rely on foreign currency obligations.

The issuance of local currency bonds and bills in 2014–17 is expected to roughly match maturing local currency debt. Thus, borrowing in foreign currency will cover both maturing foreign currency debt as well as the fiscal deficit. This will have two important monetary policy implications: i) central bank reserve accumulation will depend on continued government FX borrowing, covering higher financing needs; ii) government transactions will have a positive impact on domestic currency liquidity.

#### Government foreign currency debt exceeds total central bank reserves.

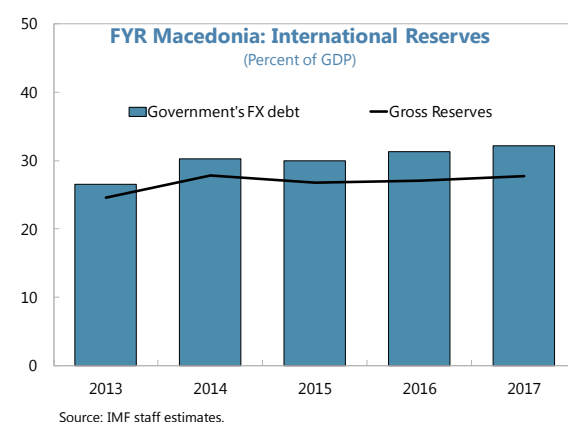
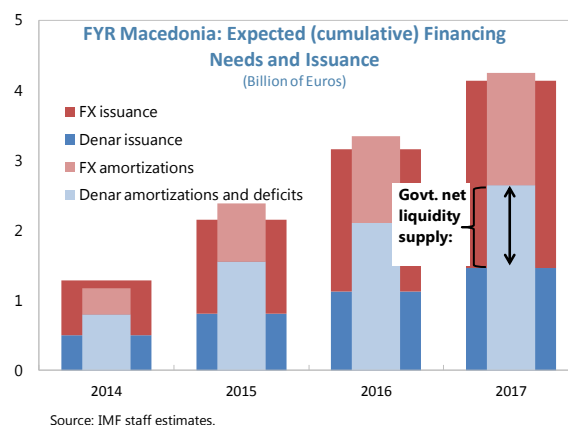
By the end of 2014, the FX debt of the government is expected to reach 30 percent of GDP<sup>1</sup>, which slightly exceeds the level of central bank reserves. In the outer years, reserves will continue to depend on government access to foreign currency borrowing. In light of increased future government FX financing needs, it will be all the more important to orient policies toward stimulating a stronger private sector contribution to reserve accumulation.

#### The government's financing mix will result in a cumulative €1.2 billion positive liquidity impact over 2014–17.

Over that time frame, the government will supply a total of €2.6 billion in liquidity through its domestic currency debt repayment (€1.4 billion) and deficits (cumulative €1.2 billion). This exceeds the government's planned €1.5 billion local currency issuance over the period, so that the financing mix will result in a €1.2 billion net supply of liquidity.

#### Maintaining the peg requires the central bank to sterilize the positive impact of government transactions on domestic liquidity.

The NBRM can do so by issuing one-month central bank bills. The cost of these sterilizations corresponds to the policy interest rate (currently 3¼ percent). Alternatively, the NBRM can tighten monetary policy to support local currency demand to match the increased liquidity supply. Higher reliance on foreign currency borrowing is thus associated with increased costs for the central bank and is an indirect cost for the government, which should be integrated in the government's debt management strategy.



1/ For calculating the government's FX debt, it is assumed that all external debt is denominated in foreign currency, that 1/3 of future T-bills issuance will be foreign currency-denominated and that the currency mix of T-bonds issuance in 2015–17 will be as in 2014 (about 40 percent in foreign currency).

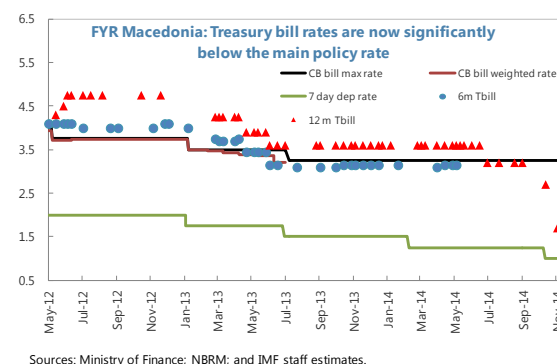
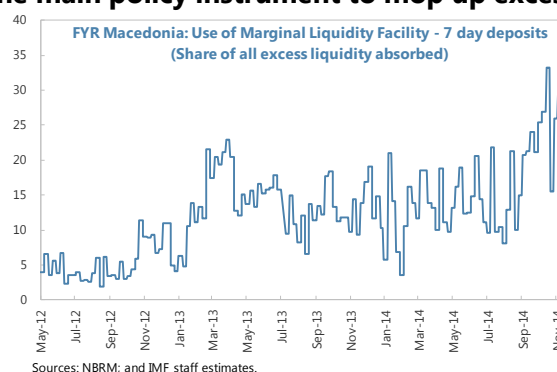
**21. The authorities agreed with the need to carefully prioritize expenditures, but saw scope for annual adjustments in expenditure levels as the revenue outturn evolves.** Clear priority will be given to capital expenditure—road, railway, energy, and health infrastructure—and social transfers. They emphasized that the free trade zones carry low budgetary costs (average expenditure of about €12 million a year, clearly identifiable in the budget), and that the envisaged special economic zones for health and financial firms would have limited fiscal cost.

## B. Monetary and Financial Policy—a Focus on Maintaining Stability

*The combination of relaxed financial conditions and tight prudential regulation has helped revive credit growth while preserving the health of the financial sector. Abundant liquidity in the system, strengthening credit growth, and currency spreads at seven-year lows argue against loosening the stance of monetary policy, and for reasserting the central role of the main policy instrument.*

**22. The monetary easing cycle has reached its end.** Credit growth is accelerating from previously low levels, reflecting both a host of measures taken by the central bank over the last two years (see Box 1 in EBS/14/75) and the intermediation of external credit lines to ensure access to finance for SMEs. While foreign and temporary supply-side developments have recently generated deflationary pressures, the focus of monetary policy should be exclusively on maintaining the attractiveness of holding denar-denominated assets in support of the exchange rate peg, which aims to deliver the ultimate objective of price stability. Amidst high banking sector liquidity and falling currency spreads, there does not seem to be room for easing monetary policy.

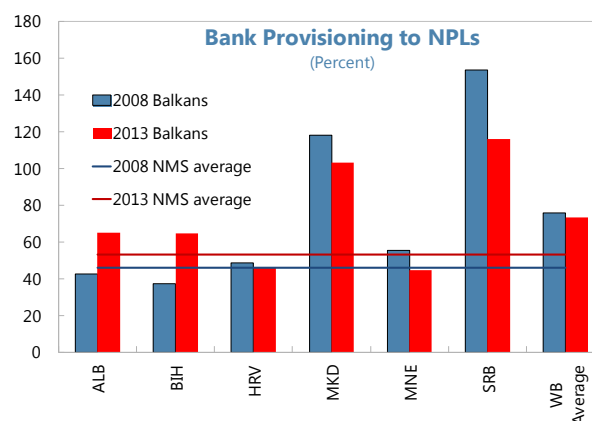
**23. Reasserting the central bank bill rate as the main policy instrument to mop up excess liquidity should improve signaling.** The central bank has tried to balance the benefits and challenges of a system characterized by a structural liquidity surplus. Since mid-2013, despite strong excess demand for central bank bills—the main policy instrument for draining liquidity—the central bank has resisted increasing their volume offered at each auction, with a view to spurring banks to revive credit. Starting in July 2013, the central bank switched to fixed price auctions while also capping the issuance of central bank bills. Banks have been increasingly placing liquidity at the seven-day deposit facility (originally intended to manage short-term excess liquidity). Despite a recent pick-up in credit, balances in this facility have risen, driving a reduction in short-term interest rates, against an unchanged policy rate of 3.25 percent (text chart).



Staff advocated for a normalization of the framework, by not limiting the supply of CB bills at the regular auctions, which should improve the signaling aspect of the policy rate.

**24. Weak collateral valuation practices and a slow process of NPL liquidation weigh on bank profitability.**

Along with Serbia, Macedonia stands out as a regional outlier for the high coverage ratio of non-performing loans by provisions, and this high provisioning has been instrumental in preserving bank health over the crisis. Yet in addition to reflecting stringent prudential requirements, this situation also appears largely attributable to the fact that in practice banks do not take into account the value of some categories of collateral (typically, commercial real estate) when computing provisions. This weighs on bank profitability, possibly limiting capacity to make



new loans. In this context, the mission discussed the take-up of the 2012 reform, aimed, *inter alia*, at enlarging the class of collateral considered by banks in computing provisions. Progress appears to have been limited on this front, as banks seem reluctant to make use of the flexibility offered by the new rules. NPL restructuring and resolution is hampered by an uneven judicial processes, weak land registries and auditing standards, and the absence of specialized asset management firms.

**25. The envisaged establishment of offshore financial centers should not be allowed to jeopardize the carefully preserved stability of the Macedonian financial system.** The proposed constitutional amendments would create the legal basis for establishing free financial zones. While the operating framework remains to be determined, it will be important to consider best practices—notably with the goal of limiting risks, particularly from potential deposit taking and money laundering. Key considerations in this respect would pertain to the licensing, supervisory, and enforcement framework. This would include, critically, ensuring adequate information provision from home jurisdictions.

**Authorities' views**

**26. The authorities see current monetary policy settings as adequate and concurred on the need to end the monetary easing cycle.** They noted that conditions had been implicitly tightened, as the NBRM did not follow the latest reductions in the ECB's policy rate since June. Rates on euro-denominated loans and deposits remain very low, and despite compressed currency spreads, the authorities emphasized that there have been no systematic signs of pressure in foreign exchange markets, which they continue to monitor closely. They reiterated their steadfast commitment to raising the main policy rate should pressures emerge.

**27. The authorities do not perceive any weakening of the signaling function of their main policy instrument.** The authorities consider the outstanding balances in seven-day deposits as

excess liquidity that could safely be channeled into credit without creating risks. Furthermore, they see current levels of high excess liquidity as attributable to a number of one-off factors, including a decrease in bank holdings of government bonds following the lengthening of their maturity and negative interest rates in the Euro area that entice private agents to keep their denar deposits. The authorities reaffirmed the primacy of the main policy rate in signaling the monetary policy stance, and noted that all other measures—such as reserve requirements to manage liquidity needs—are used for prudential purposes only.

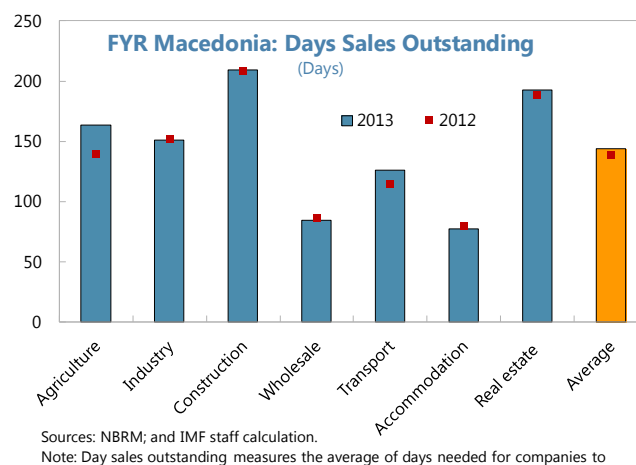
**28. The authorities will disallow domestic deposit taking by companies in the financial zones.** They reiterated that the project aims to attract regional financial firms—largely non-bank institutions—by marketing the lower cost of support services in Macedonia, and will require a physical presence in the country of a minimum number of employees and a clear management structure.

### C. Structural Issues—Ensuring A Handover to Private Sector-Led Growth

*Foreign direct investment is developing new export sectors. Some transfer of managerial skills is underway, but transfers of technology and the creation of international marketing networks will need to follow. Efforts should focus on relaxing key constraints for domestic firms, particularly younger and smaller ones, to allow for high-quality and durable job creation.*

**29. Notable system-wide liquidity bottlenecks could weigh on the handover to private sector-led growth.** Recent work by the NBRM<sup>3</sup>

reveals that corporate balance sheets, particularly those of SMEs, remain strained. Corporate sector debt stands at about 65 percent of GDP and is mostly foreign-currency denominated and at variable interest rates. Although rising, interest coverage ratios remain below 2 in the manufacturing sector, suggesting that some firms may still struggle with servicing debt. This appears more pronounced for the leveraged micro enterprises group, which continued to post losses in 2013. More generally, firms appear to operate under strong liquidity constraints, needing to wait about four months on average to collect claims (text chart).



**30. Upgrading the quality of the inspections process is also a key input to fostering a competitive business environment for all firms.** In order to improve evenhandedness in the application of the law and to strengthen the integrity of inspection bodies, an Inspection Council was established in January 2014 to supervise and coordinate the work of 29 inspection bodies,

<sup>3</sup> NBRM, 2014, *Financial Stability Report for the Republic of Macedonia in 2013*, July 2014.

covering all but tax, customs and financial intelligence inspections. The work program of the council is laudably ambitious, but high-impact measures, such as clarification of the hierarchy of various overlapping legislation, rationalization of the fine structure, and improved communication on firms' rights vis-à-vis inspection bodies should be the priorities.

## POST-PROGRAM MONITORING

**31. Capacity to repay is projected to remain adequate.** The recent €500 million Eurobond issuance covers all external debt amortizations falling due in 2015, by which time Fund exposure to Macedonia is expected to fall to just 36 percent of quota. Reserve adequacy is projected to remain adequate on standard metrics, although over the medium run and on current policy settings reserve accumulation depends exclusively on net public sector external borrowing. Risks are broadly balanced: on the upside, FDI could pick up from staff's baseline estimates, which are well below pre-crisis levels; nonetheless, the high rollover requirements of trade credit and intercompany loans represent a source of vulnerability, even if rollover rates did not decline significantly in a stressed global environment.

<b>FYR Macedonia: External Financing Requirements</b> (Millions of euros, unless specified otherwise)					
	2012	2013	2014	2015	2016
			Projections		
Gross financing requirements	2157	2367	2145	2390	2350
Current account deficit	226	147	247	368	420
ST debt amortization (original maturity)	1588	1725	1569	1573	1596
MLT debt amortization 1/	344	321	329	299	334
of which: public sector	99	102	159	189	244
Sovereign Eurobond amortization	0	175	0	150	0
Financing sources	2157	2367	2145	2390	2350
FDI (net)	78	253	322	338	358
ST debt disbursements	1725	1569	1573	1596	1690
MLT debt disbursements	410	667	405	437	425
of which: Public sector	161	379	219	250	223
Banks	120	107	77	79	80
Other private sector	151	177	114	116	124
Sovereign Eurobond disbursement	0	0	491	150	300
Other 2/	67	-422	-216	-182	-220
Net change in reserves (-: increase)	-123	301	-430	50	-202
Gross international reserves (GIR)	2193	1993	2440	2372	2593
Short-term debt (residual maturity)	2172	1898	2022	1930	1920
GIR as % of ST debt	101.0	105.0	120.7	122.9	135.1
GIR as % of Fund New Metric	135.1	124.9	137.1	127.4	128.6
Sources: NBRM; and IMF staff estimates.					
1/ Excluding the amortization of MLT intercompany loans, which is included in FDI (net).					
2/ Including the capital account balance, net errors and omissions, currency and deposits, portfolio investments, and discrepancies between ST debtflows and stock data.					

## STAFF APPRAISAL

**32. The jobs and growth agenda should remain a top policy priority, and efforts should focus on alleviating key constraints for domestic firms.** Key measures include properly implementing and monitoring recent initiatives to enforce payment discipline in both public and private sector contracts, as well upgrading the professional status of inspection bodies, clarifying their mandate, and streamlining their work.

**33. The public-sector led growth strategy will put pressure on other types of spending if consolidation is to proceed while maintaining the low-tax environment.** To support the economy, the focus should be filling gaps in transport and energy infrastructure to maximize the payoff for medium-term growth. At the same time, with public debt rising steady to over 50 percent by 2017, fiscal policy should aim at reducing the deficit to below 2.6 percent of GDP by 2016. In the absence of tax policy changes to boost revenues, a comprehensive spending review that seeks to minimize the growth impact of expenditure compression should be undertaken. The forthcoming World Bank-led Public Finance Review should help guide that effort.

**34. Renewed presence in international capital markets highlights the role of public debt management in supporting external sustainability.** The move to disseminate public sector level debt data is welcome, as is the inclusion of explicit targets for refinancing needs, interest payments and currency risks in the debt management strategy that accompanies the medium-term fiscal strategy. To further reduce risks, the strategy should encompass the debt of SOEs as well as contingent liabilities, particularly to manage currency risk. In addition, the increased reliance on foreign currency borrowing has implications for external sustainability and the conduct of monetary policy—looking forward, the debt management strategy should take into account the costs and risks arising from the impact of government financing choices on central bank reserve developments and domestic liquidity.

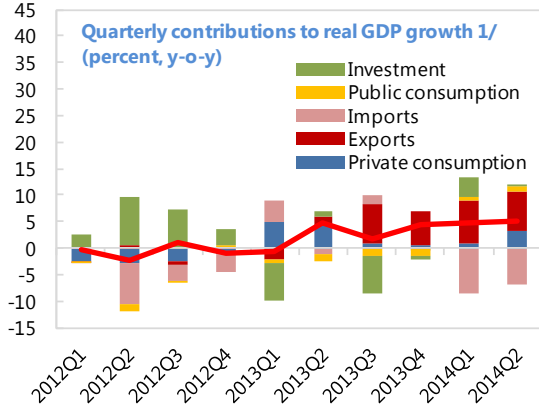
**35. The monetary easing cycle has reached its end.** The combination of relaxed financial conditions and tight prudential regulation has helped revive credit growth, all while preserving the health of the financial sector. The focus of monetary policy henceforth should be exclusively on maintaining the attractiveness of holding denar-denominated assets in support of the exchange rate peg. Amidst high banking sector liquidity and falling currency spreads, there does not seem to be room for easing. With some short-term rates consistently below the main policy rate, there is scope to improve signaling of the monetary policy stance by reasserting the role of auctions of CB bills—the central bank’s main policy instrument.

**36. It is recommended that Post-Program Monitoring with Macedonia should be discontinued in line with guidance.** Post-Program Monitoring was initiated in January 2013 upon the expiration of the PLL arrangement, as Fund credit outstanding (286 percent of quota) exceeded exceptional access levels. Outstanding credit is scheduled to fall below 200 percent at end-2014. Staff does not see risks to external sustainability or capacity to repay that would warrant an extension of the PPM.

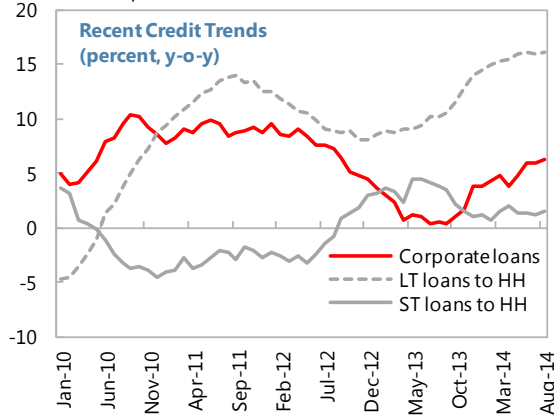


**Figure 1. FYR Macedonia: Recent Developments**

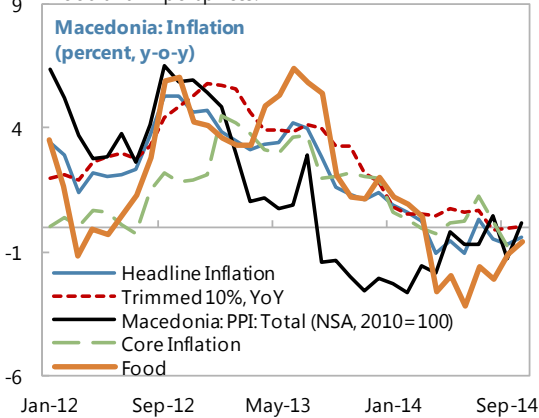
Growth has picked up, driven by exports and private consumption...



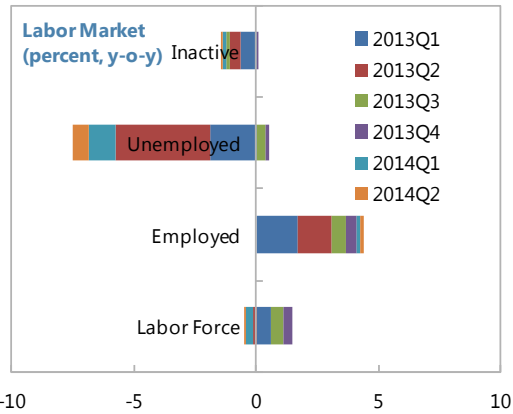
... against the backdrop of strengthening credit developments.



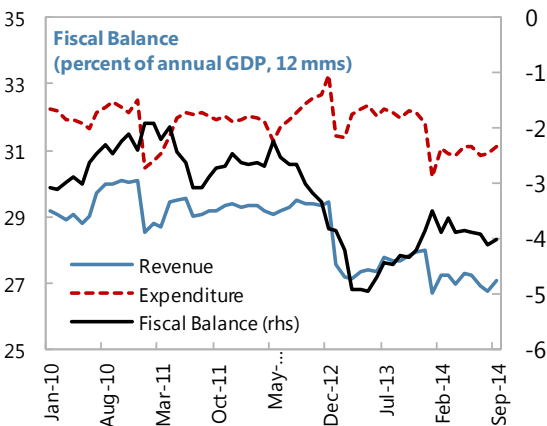
Inflation has trended downward, due to declining food and import prices.



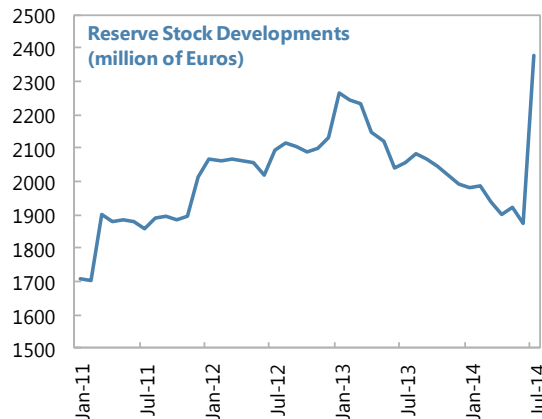
Labor market conditions have improved.



The fiscal stance has turned pro-cyclical...



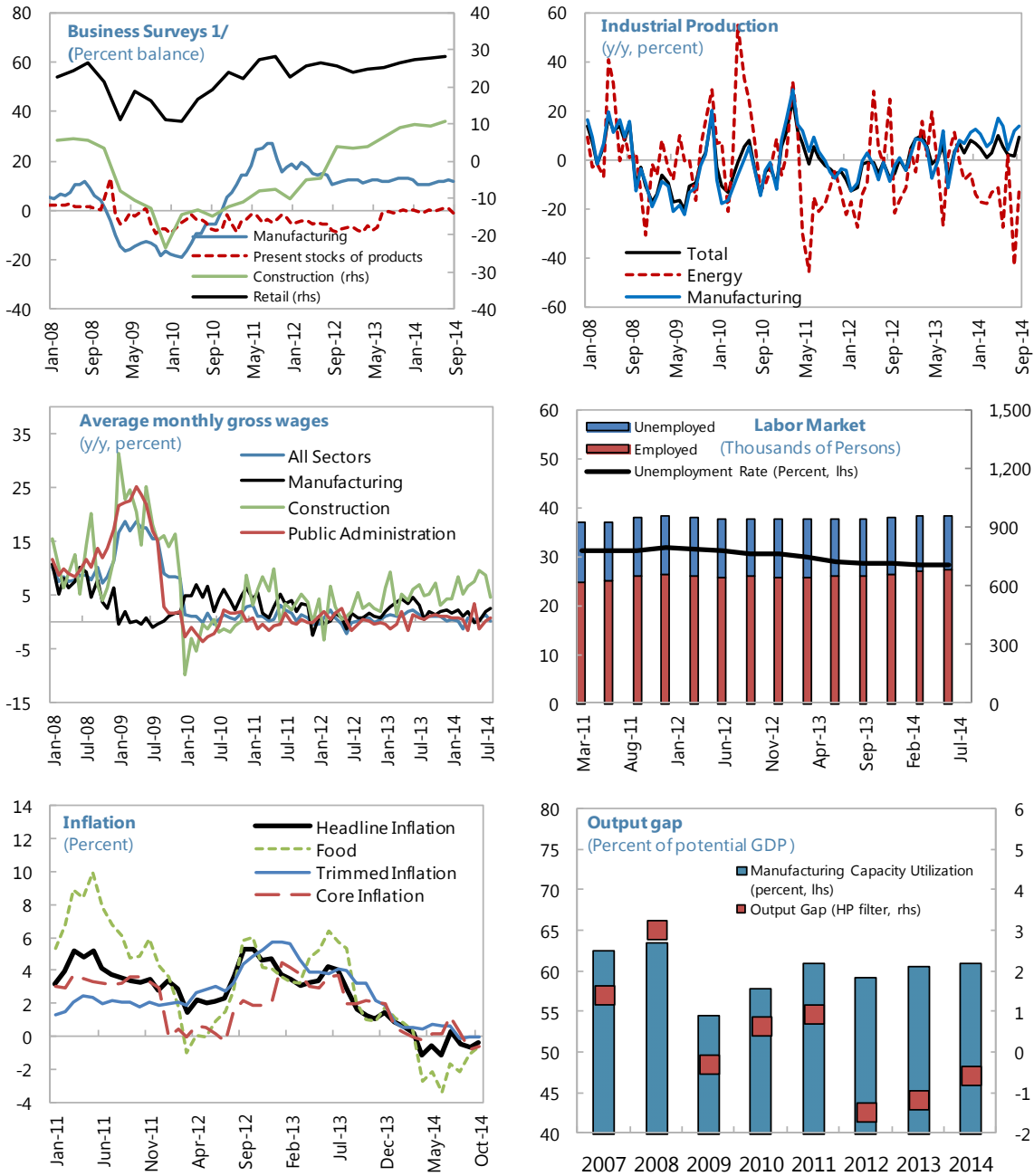
... while the decline in reserves could only be halted by sovereign borrowing.



Sources: Ministry of Finance; NBRM; SSO; and IMF staff calculations.

Note: Historical vintages of national account are revised based on ESA2010 methodology.

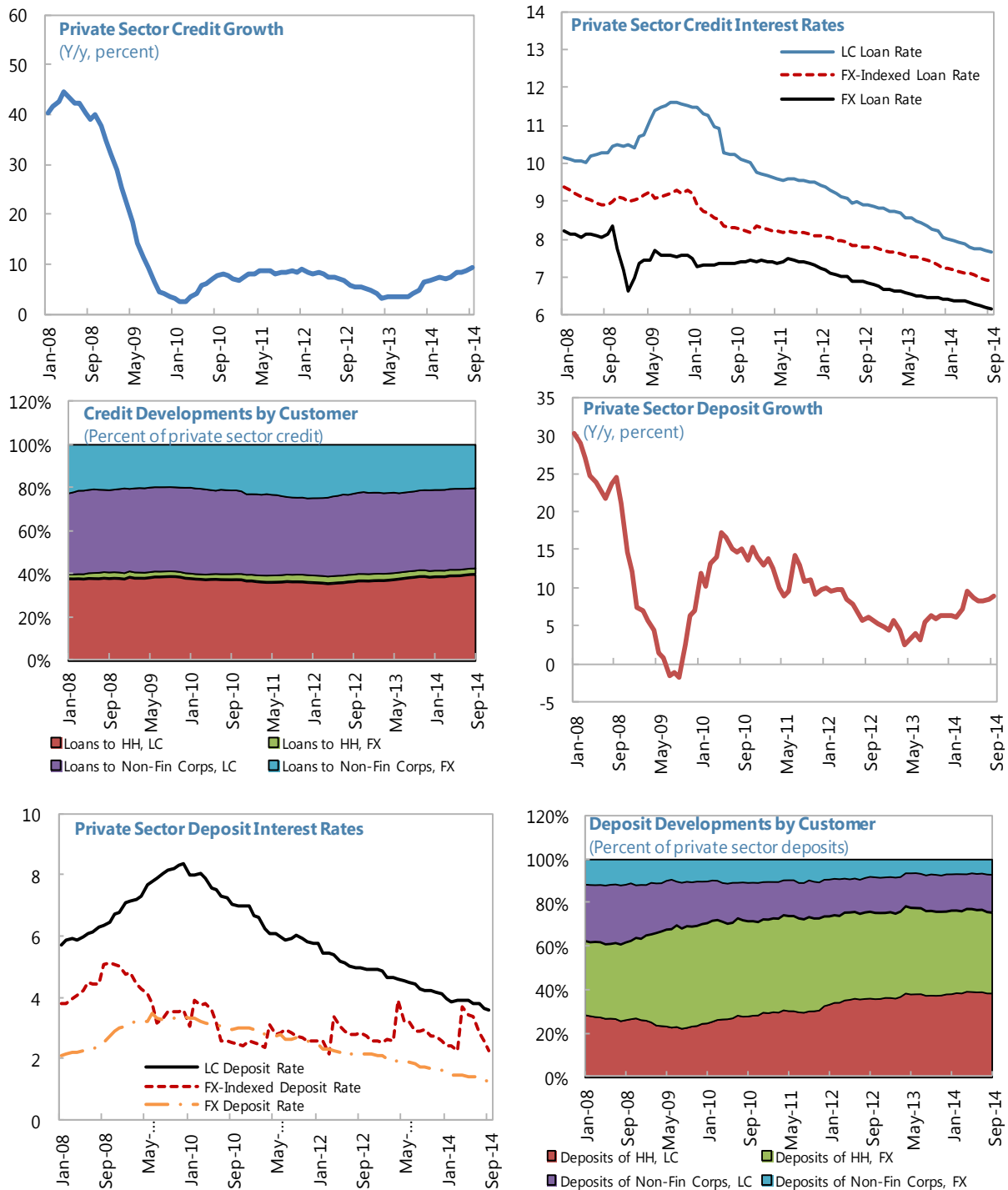
**Figure 2. FYR Macedonia: Real Sector Developments, 2008-2014**



Sources: Haver Analytics; SSO; and IMF staff calculations.

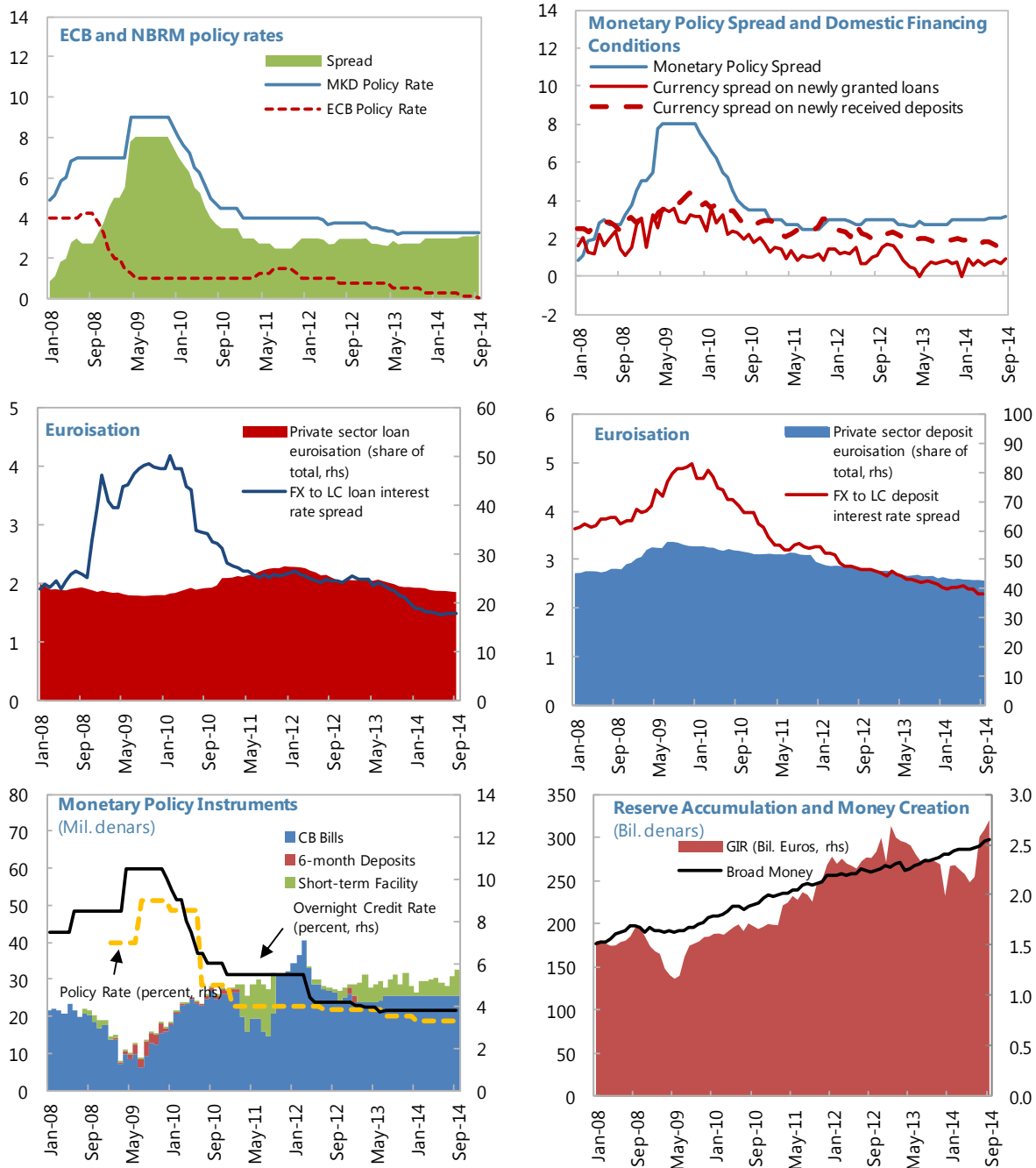
1/ Note: the percent balance is the difference in percentage shares between the 'positive' and 'negative' assessments on the current business situation.

**Figure 3. FYR Macedonia: Credit Developments, 2008-2014**  
(Percent, unless otherwise indicated)



Sources: NBRM; and IMF staff calculations.

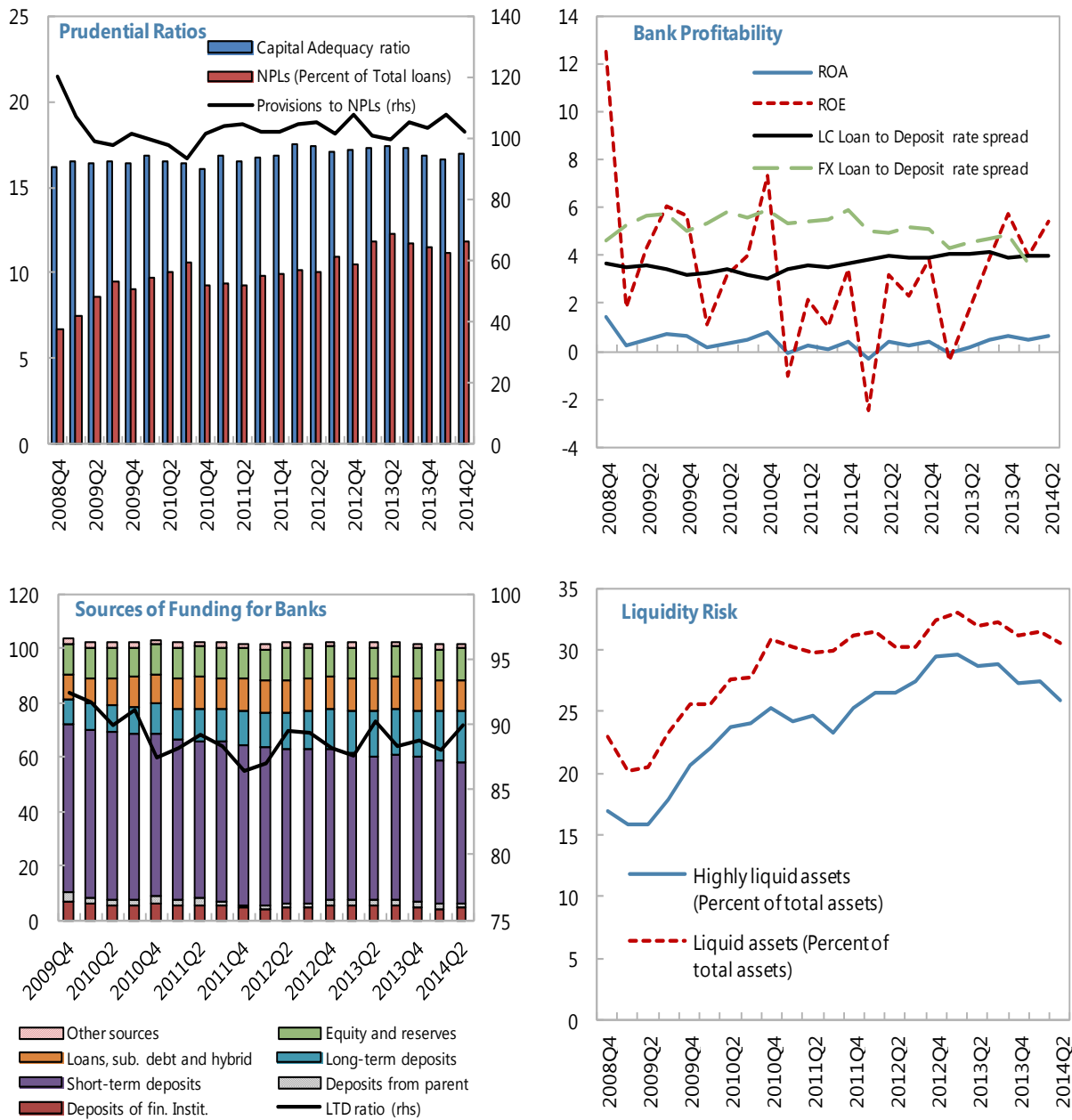
**Figure 4. FYR Macedonia: Monetary Policy Developments, 2008-2014**  
(Percent, unless otherwise indicated)



Sources: NBRM; Haver Analytics; and IMF staff calculations.

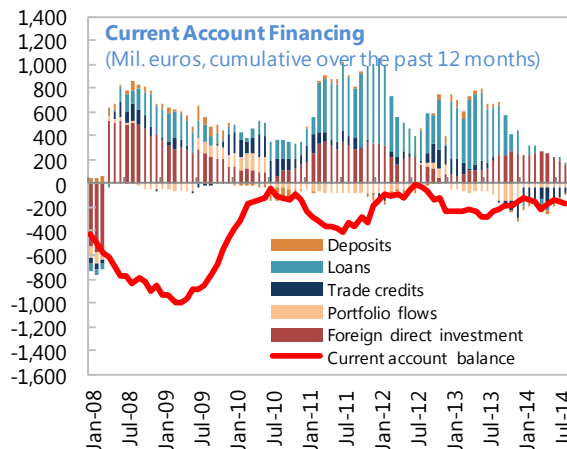
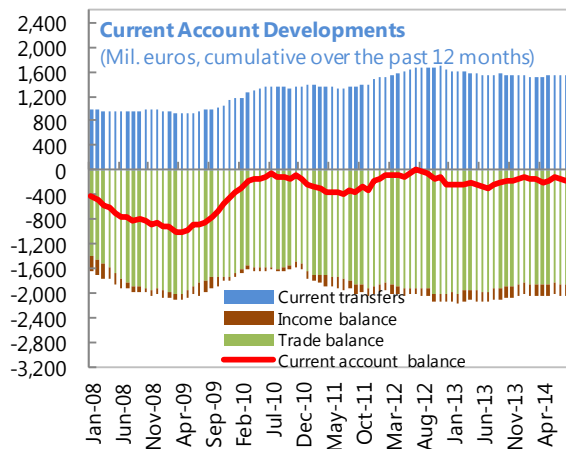
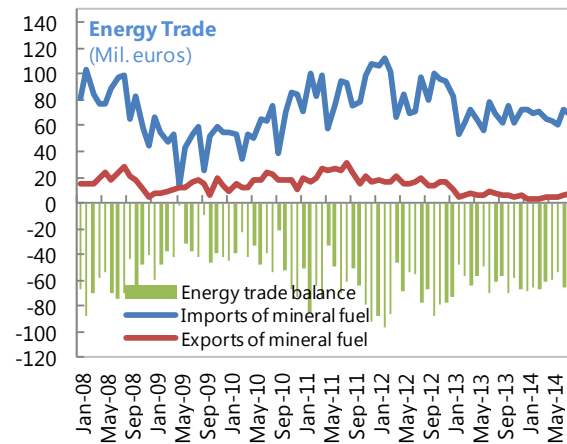
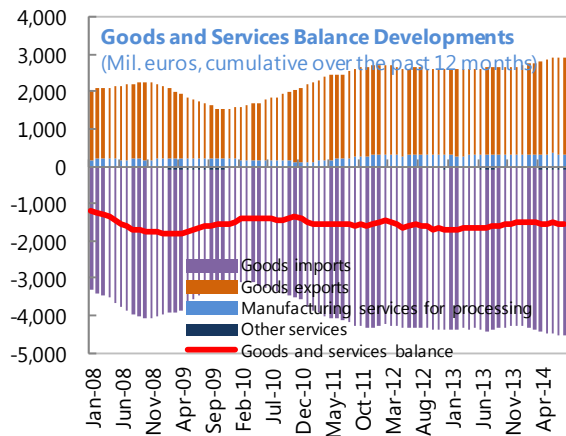
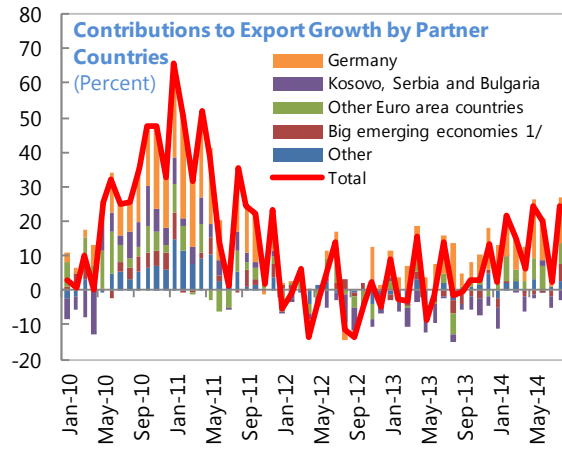
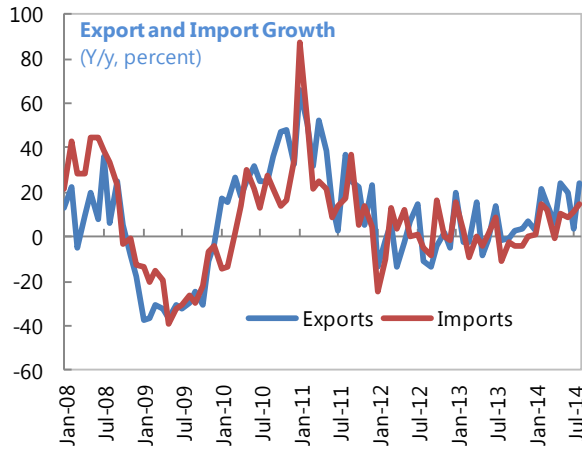
**Figure 5. FYR Macedonia: Banking Sector Developments, 2008-2014**

(Percent, unless otherwise indicated)



Sources: NBRM; and IMF staff calculations.

**Figure 6. FYR Macedonia: External Sector Developments, 2008-2014**



Sources: NBRM; and IMF staff calculations.  
1/ Brazil, China, India, Russia and Turkey.

**Table 1. FYR Macedonia: Macroeconomic Framework, 2010–2019**

(Year-on-year percentage change, unless otherwise indicated)

	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
					Proj.					
Real GDP	3.4	2.3	-0.5	2.6	3.5	3.7	3.9	4.0	4.0	4.0
Real domestic demand	1.2	0.6	2.6	1.5	3.4	3.8	3.7	3.6	3.6	3.6
Consumption	2.5	-3.9	0.6	0.3	2.7	3.2	3.1	3.1	3.1	3.1
Private	3.8	-5.0	0.3	-0.3	3.5	3.5	3.4	3.4	3.4	3.4
Public	-3.6	1.6	1.6	3.2	-0.8	2.0	1.8	1.5	1.9	1.7
Gross investment	-3.6	18.2	9.2	4.9	5.4	5.3	5.2	5.0	4.8	4.8
Exports (volume)	23.5	16.2	2.4	3.1	9.9	9.4	9.2	8.4	7.9	7.6
Imports (volume)	10.5	8.0	7.8	0.8	7.9	8.0	7.4	6.6	6.3	6.1
Contributions to growth										
Domestic demand	1.4	5.1	3.8	4.8	4.0	4.5	4.3	4.2	4.2	4.2
Net exports	1.9	-1.6	-1.9	-2.6	-0.5	-0.8	-0.4	-0.2	-0.2	-0.2
Central government operations (percent of GDP)										
Revenues	30.1	29.4	29.4	28.0	28.7	29.4	28.9	28.2	28.2	28.2
Expenditures	32.5	31.9	33.3	31.8	32.5	32.8	32.1	31.1	31.1	31.1
Of which: capital	3.5	3.8	4.0	3.3	3.5	3.6	3.6	3.5	3.5	3.5
Balance	-2.4	-2.5	-3.8	-3.9	-3.8	-3.4	-3.2	-2.9	-2.8	-2.8
Savings and investment (percent of GDP)										
Domestic saving	22.4	21.7	26.0	26.7	26.9	26.0	26.1	26.1	26.0	25.9
Public	1.1	2.5	0.2	-0.5	-0.3	0.2	0.4	0.6	0.7	0.7
Private	21.4	19.2	25.7	27.2	27.1	25.8	25.6	25.4	25.3	25.2
Foreign saving	2.0	2.5	3.0	1.8	2.9	4.1	4.5	4.1	3.9	3.7
Gross investment	24.5	26.9	28.9	28.5	29.8	30.2	30.5	30.2	29.9	29.6
Consumer prices										
Period average	1.7	3.9	3.3	2.8	-0.2	1.1	1.7	1.9	2.0	2.0
End-period	3.0	2.8	4.7	1.5	0.5	1.6	1.8	2.0	2.0	2.0
Private sector credit growth	7.3	7.7	5.2	6.3	7.8	7.8	7.7	7.5	7.5	7.4
Memorandum items:										
Current account balance (percent of GDP)	-2.0	-2.5	-3.0	-1.8	-2.9	-4.1	-4.5	-4.1	-3.9	-3.7
Gross official reserves (millions of euros)	1,715	2,069	2,193	1,993	2,440	2,372	2,593	2,918	3,251	3,544
in percent of ST debt	103	112	101	105	121	123	135	137	149	174
in months of prospective imports	4.1	4.9	5.2	4.3	4.8	4.3	4.3	4.5	4.6	4.8
Gross Central Government Debt (percent of GDP)	24.3	27.7	33.7	34.1	38.1	35.9	37.6	38.9	39.9	40.4
Public Sector Gross Debt (percent of GDP) 1/	27.8	31.8	38.5	40.6	46.6	46.2	48.8	50.4	51.7	52.2
Foreign direct investment (percent of GDP)	2.2	4.5	1.0	3.1	3.8	3.8	3.8	3.8	3.8	3.8
External debt (percent of GDP)	57.8	64.2	68.2	64.3	64.4	59.5	57.6	56.4	54.9	52.9
Nominal GDP (billions of denars)	437	464	467	500	521	547	580	617	659	703
Nominal GDP (millions of euros)	7,109	7,546	7,587	8,121	8,473	8,892	9,423	10,035	10,708	11,426

Sources: NBRM; SSO; MOF; IMF staff estimates and projections. National Accounts are revised by SSO, using ESA 2010 Methodology.

Note: 1/ Total Public Sector (including MBDP, municipalities, public sector non-financial enterprises; w/o NBRM).

Table 2. FYR Macedonia: Central Government Operations, 2010–2019

(Billions of denars)

	2010	2011	2012	2013	2014		2015		2016		2017		2018		2019	
					Budget											
					Original	Revised	Proj.	MTS	Proj.	MTS	Proj.	MTS	Proj.	MTS	Proj.	MTS
Total Revenues 1/	131.6	136.4	137.4	139.7	158.2	155.6	149.8	162.5	161.1	168.1	167.3	174.4	174.4	186.1	198.6	
Tax Revenues and Contributions	112.4	118.7	117.4	121.0	133.9	131.4	130.9	137.7	136.3	142.5	141.7	148.5	148.5	158.5	169.1	
PIT	8.9	9.5	9.6	10.3	10.7	11.2	11.2	11.5	11.5	11.8	11.8	12.3	12.3	13.1	14.0	
CIT	3.7	3.9	3.7	4.4	4.2	5.0	5.0	5.1	5.1	5.3	5.3	5.5	5.5	5.9	6.3	
VAT (net)	37.7	42.2	38.5	39.8	48.5	44.5	44.0	45.7	45.7	47.1	47.1	48.9	48.9	52.2	55.7	
Excises	14.9	15.5	16.6	16.0	15.8	16.9	16.9	17.4	17.4	17.9	17.9	18.6	18.6	19.8	21.2	
Custom Duties	4.7	3.8	4.1	4.3	4.1	4.7	4.7	4.8	4.8	5.0	5.0	5.2	5.2	5.5	5.9	
Other Taxes 2/	3.9	4.0	4.3	3.8	5.3	4.4	4.4	4.4	4.4	4.5	4.5	4.6	4.6	5.0	5.3	
Social Contributions	38.7	39.8	40.8	42.5	45.2	44.7	44.7	48.7	47.3	51.0	50.1	53.3	53.3	56.9	60.7	
Pensions	26.1	26.9	27.5	28.7	30.6	30.2	30.2	33.3	32.1	34.8	34.0	36.5	36.5	39.0	41.6	
Unemployment	1.7	1.7	1.7	1.8	1.9	1.9	1.9	2.0	2.0	2.1	2.1	2.1	2.1	2.2	2.3	
Health	10.9	11.2	11.5	12.0	12.6	12.6	12.6	13.4	13.2	14.1	14.0	14.8	14.8	15.8	16.8	
Non-Tax Revenues 3/	12.1	12.5	12.4	11.6	14.5	14.2	12.2	17.1	17.1	17.9	17.9	18.2	18.2	19.4	20.7	
Capital Revenues 4/	5.6	4.1	4.6	3.7	5.7	4.6	3.1	4.2	4.2	4.2	4.2	4.2	4.2	4.4	4.7	
Of which: Telecom dividend	2.5	2.3	2.5	2.2	2.5	0.9	0.9	0.9	0.9	0.9	0.9	0.9	0.9	0.9	0.9	
Grants	1.5	1.1	3.0	3.5	3.5	4.5	3.5	3.6	3.6	3.6	3.6	3.6	3.6	3.8	4.1	
Expenditures 1/	142.2	147.9	155.2	159.0	176.5	175.2	169.4	181.0	179.6	187.1	185.8	192.6	192.3	204.8	218.5	
Current Expenditures 5/	127.4	130.9	137.1	142.9	154.1	154.1	152.1	160.6	160.6	165.7	165.7	171.2	171.2	182.7	194.9	
Wages and salaries	22.6	23.1	22.7	22.6	23.7	23.6	23.1	24.5	24.5	24.4	24.4	24.4	24.4	26.1	27.8	
Goods and services	14.7	14.0	14.7	14.9	18.7	18.6	17.6	18.7	18.7	18.7	18.7	18.7	18.7	20.0	21.3	
Transfers	86.9	90.4	95.5	100.8	107.4	107.4	106.9	111.4	111.4	115.5	115.5	119.9	119.9	127.9	136.5	
Interest	3.2	3.5	4.2	4.6	4.4	4.4	4.4	6.0	6.0	7.0	7.0	8.2	8.2	8.7	9.3	
Capital Expenditures	15.3	17.7	18.8	16.6	22.4	21.1	18.1	21.2	19.8	22.2	20.9	22.2	21.9	23.4	24.9	
Lending minus repayment 6/	-0.5	-0.8	-0.6	-0.6	-0.6	-0.8	-0.8	-0.8	-0.8	-0.8	-0.8	-0.8	-0.8	-0.9	-0.9	
Overall fiscal balance	-10.5	-11.5	-17.8	-19.3	-18.3	-19.6	-19.6	-18.5	-18.5	-19.0	-18.5	-18.3	-17.9	-18.7	-20.0	
Financing	10.5	11.5	17.7	19.3	18.3	19.6	19.6	18.5	18.5	19.0	18.5	18.3	17.9	18.7	20.0	
Domestic	5.3	-9.4	13.3	13.1	22.0	-8.3	-8.7	22.2	20.2	9.9	6.6	9.0	5.6	6.7	12.0	
Central Bank deposits	3.4	-7.3	-12.3	-0.3	13.9	-12.7	-7.0	23.4	21.2	0.3	-3.0	-1.0	-4.5	-4.1	-0.5	
Other domestic financing	1.9	-2.1	25.6	13.4	8.1	4.4	-1.7		-1.0		9.7		10.1	10.8	12.5	
Privatization receipts	0.0	0.3	0.1	0.6	0.1	0.1	0.0	0.1	0.0	0.1	0.0	0.1	0.0	0.0	0.0	
Foreign	5.2	20.6	4.3	5.6	-3.9	27.8	28.3	-3.8	-1.7	9.0	11.9	9.1	12.3	12.0	8.0	
Memo items:																
Gross Central Government Debt (as share of GDP)	24.3	27.7	33.7	34.1	38.1	38.1	38.1	35.9	35.9	37.6	37.6	38.9	38.9	39.9	40.3	
Nominal GDP (billions of denars)	437	464	467	500	521	521	521	547	547	580	580	617	617	659	703	
Stock of government deposits at the NBRM (EUR mln eop)	11.4	7.7	19.5	18.8	26	26	25.7	4.5	4.5	7.6	7.6	12.1	12.1	16.1	16.7	

Sources: IMF Staff and MoF estimates.

Notes:

1/ Excluding revenues from lending.

2/ Including Tax Revenues (SRA).

3/ Excluding profits from financial institutions.

4/ Including profits from financial institutions.

5/ Excluding lending guarantees.

6/ Resulting from excluding: (i) revenues from lending from total expenditure; and (ii) lending guarantees from current expenditures.



Table 2. FYR Macedonia: Central Government Operations, 2010–2019 (concluded)

(Percent of GDP)

	2010	2011	2012	2013	2014		2015		2016		2017		2018		2019
					Budget										
					Original	Revised	Proj.	MTS	Proj.	MTS	Proj.	MTS	Proj.	Proj.	Proj.
Total Revenues 1/	30.1	29.4	29.4	28.0	30.4	29.8	28.7	29.7	29.4	29.0	28.9	28.2	28.2	28.2	28.2
Tax Revenues and Contributions	25.7	25.6	25.2	24.2	25.7	25.2	25.1	25.2	24.9	24.6	24.4	24.1	24.1	24.1	24.1
PIT	2.0	2.0	2.0	2.1	2.1	2.1	2.1	2.1	2.0	2.0	2.0	2.0	2.0	2.0	2.0
CIT	0.8	0.8	0.8	0.9	0.8	1.0	1.0	0.9	0.9	0.9	0.9	0.9	0.9	0.9	0.9
VAT (net)	8.6	9.1	8.2	8.0	9.3	8.5	8.4	8.4	8.4	8.1	8.1	7.9	7.9	7.9	7.9
Excises	3.4	3.3	3.6	3.2	3.0	3.2	3.2	3.2	3.2	3.1	3.1	3.0	3.0	3.0	3.0
Custom Duties	1.1	0.8	0.9	0.9	0.8	0.9	0.9	0.9	0.9	0.9	0.9	0.8	0.8	0.8	0.8
Other Taxes 2/	0.9	0.9	0.9	0.8	1.0	0.8	0.8	0.8	0.8	0.8	0.8	0.8	0.8	0.8	0.8
Social Contributions	8.8	8.6	8.7	8.5	8.7	8.6	8.6	8.9	8.6	8.8	8.6	8.6	8.6	8.6	8.6
Pensions	6.0	5.8	5.9	5.7	5.9	5.8	5.8	6.1	5.9	6.0	5.9	5.9	5.9	5.9	5.9
Unemployment	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.4	0.3	0.3	0.3	0.3
Health	2.5	2.4	2.5	2.4	2.4	2.4	2.4	2.4	2.4	2.4	2.4	2.4	2.4	2.4	2.4
Non-Tax Revenues 3/	2.8	2.7	2.7	2.3	2.8	2.7	2.3	3.1	3.1	3.1	3.1	2.9	2.9	2.9	2.9
Capital Revenues 4/	1.3	0.9	1.0	0.7	1.1	0.9	0.6	0.8	0.8	0.7	0.7	0.7	0.7	0.7	0.7
Of which: Telecom dividend	0.6	0.5	0.5	0.4	0.5	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.1	0.1
Grants	0.3	0.2	0.7	0.7	0.7	0.9	0.7	0.7	0.7	0.6	0.6	0.6	0.6	0.6	0.6
Expenditures 1/	32.5	31.9	33.3	31.8	33.9	33.6	32.5	33.1	32.8	32.3	32.1	31.2	31.1	31.1	31.1
Current Expenditures 5/	29.1	28.2	29.4	28.6	29.6	29.6	29.2	29.4	29.4	28.6	28.6	27.7	27.7	27.7	27.7
Wages and salaries	5.2	5.0	4.9	4.5	4.5	4.5	4.4	4.5	4.5	4.2	4.2	4.0	4.0	4.0	4.0
Goods and services	3.4	3.0	3.1	3.0	3.6	3.6	3.4	3.4	3.4	3.2	3.2	3.0	3.0	3.0	3.0
Transfers	19.9	19.5	20.5	20.2	20.6	20.6	20.5	20.4	20.4	19.9	19.9	19.4	19.4	19.4	19.4
Pensions	8.6	8.5	8.8	9.0	9.2	9.3	9.2	9.2	9.2	9.2	9.2	9.1	9.1	9.1	9.1
Health	4.4	4.4	4.5	4.3	4.3	4.3	4.3	4.3	4.3	4.2	4.2	4.1	4.1	4.1	4.1
Local Governments	3.0	3.0	3.3	3.1	3.1	3.1	3.1	3.0	3.0	2.8	2.8	2.7	2.7	2.7	2.7
Other	3.8	3.6	3.9	3.8	4.0	4.0	4.0	3.9	3.9	3.7	3.7	3.5	3.5	3.5	3.5
Interest	0.7	0.7	0.9	0.9	0.8	0.8	0.8	1.1	1.1	1.2	1.2	1.3	1.3	1.3	1.3
Capital Expenditures	3.5	3.8	4.0	3.3	4.3	4.0	3.5	3.9	3.6	3.8	3.6	3.6	3.5	3.5	3.5
Lending minus repayment 6/	-0.1	-0.2	-0.1	-0.1	-0.1	-0.2	-0.2	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1
Overall fiscal balance	-2.4	-2.5	-3.8	-3.9	-3.5	-3.8	-3.8	-3.4	-3.4	-3.3	-3.2	-3.0	-2.9	-2.8	-2.8
Financing	2.4	2.5	3.8	3.9	3.5	3.8	3.8	3.4	3.4	3.3	3.2	3.0	2.9	2.8	2.8
Domestic	1.2	-2.0	2.8	2.6	4.2	-1.6	-1.7	4.1	3.7	1.7	1.1	1.5	0.9	1.0	1.7
Central Bank deposits	0.8	-1.6	-2.6	-0.1	2.7	-2.4	-1.3	4.3	3.9	0.0	-0.5	-0.2	-0.7	-0.6	-0.1
Other domestic financing	0.4	-0.5	5.5	2.7	1.6	0.8	-0.3		-0.2		1.7		1.6	1.6	1.8
Privatization receipts	0.0	0.1	0.0	0.1	0.0	0.0		0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Foreign	1.2	4.4	0.9	1.1	-0.7	5.3	5.4	-0.7	-0.3	1.6	2.1	1.5	2.0	1.8	1.1
Memo items:															
Gross Central Government Debt (as share of GDP)	24.3	27.7	33.7	34.1	38.1	38.1	38.1	35.9	35.9	37.6	37.6	38.9	38.9	39.9	40.3
Nominal GDP (billions of denars)	437.3	464.2	466.7	499.6	521.2	521.2	521.2	546.9	546.9	579.6	579.6	617.3	617.3	658.7	702.8
Stock of government deposits at the NBRM (EUR mln e)	11.4	7.7	19.5	18.8	25.7	25.7	25.7	4.5	4.5	7.6	7.6	12.1	12.1	16.1	16.7

Sources: IMF Staff and MoF estimates.

Notes:

1/ Excluding revenues from lending.

2/ Including Tax Revenues (SRA).

3/ Excluding profits from financial institutions.

4/ Including profits from financial institutions.

5/ Excluding lending guarantees.

6/ Resulting from excluding: (i) revenues from lending from total expenditure; and (ii) lending guarantees from current expenditures.

Table 3. FYR Macedonia: Balance of Payments, 2010–2019

(Millions of euros, unless otherwise indicated)

	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019
	Projections									
Current account	-144	-189	-226	-147	-247	-368	-420	-411	-418	-425
Trade balance	-1531	-1904	-2008	-1859	-1980	-2109	-2227	-2283	-2347	-2407
Exports	1982	2397	2304	2383	2677	2976	3298	3691	4118	4581
Imports	3513	4301	4312	4242	4657	5085	5524	5975	6465	6988
Services (net)	120	353	298	352	365	336	343	376	408	442
Primary Income (net)	-100	-131	-148	-182	-191	-201	-211	-253	-303	-364
Secondary Income (transfers, net)	1367	1494	1632	1542	1559	1606	1674	1750	1824	1904
<i>Of which</i>										
Official	31	77	60	43	60	55	53	56	54	54
Private	1337	1417	1572	1499	1499	1551	1621	1694	1770	1850
<i>Of which: Cash exchange</i>	1155	1237	1389	1321	1376	1430	1493	1566	1641	1720
Capital account (net)	12	9	20	18	16	15	16	17	16	16
Net lending (+) / Net borrowing (-)	-131	-180	-206	-129	-231	-353	-405	-394	-402	-409
Financial account	-191	-503	-347	-79	-678	-285	-626	-718	-734	-702
Direct investment (net)	-159	-337	-117	-253	-322	-338	-358	-381	-407	-434
Portfolio investment (net)	57	76	-77	159	-468	16	-289	-217	-319	-221
<i>Of which: Eurobonds amortizations</i>	0	0	0	175	0	150	0	0	0	0
<i>Of which: Eurobonds disbursements</i>	0	0	0	0	491	150	300	225	325	225
Other investment	-89	-242	-153	15	112	37	20	-120	-8	-47
Trade credits (net)	-71	13	-170	126	22	22	-66	-70	-75	-80
MLT loans (net)	-67	-463	-67	-345	-76	-139	-91	-211	-92	-127
Public sector	-39	-367	-62	-277	-60	-61	20	-61	42	84
Disbursements	98	457	161	379	219	250	223	224	182	141
Amortization	-59	-89	-99	-102	-159	-189	-244	-162	-224	-226
<i>of which: Repayment to the IMF</i>	0	0	0	0	86	115	29	0	0	
Banks	-94	-53	24	-35	-4	-27	-42	-55	-49	-79
Other sectors	66	-43	-29	-33	-12	-51	-69	-94	-85	-133
ST loans (net)	-62	27	4	-18	-34	-36	-38	-40	-43	-46
Currency and deposits (net)	171	232	115	254	200	189	214	201	202	206
<i>Of which: Commercial banks</i>	81	98	-113	37	7	-23	7	-3	-6	-1
Other (net)	-60	-50	-35	-2	0	0	0	0	0	0
Errors and omissions	1	9	-21	28	0	0	0	0	0	0
Overall Balance	61	332	120	-22	447	-68	222	324	333	293
	(Percent of GDP)									
Current account	-2.0	-2.5	-3.0	-1.8	-2.9	-4.1	-4.5	-4.1	-3.9	-3.7
<i>Of which</i>										
Goods and services balance	-19.8	-20.6	-22.5	-18.6	-19.1	-19.9	-20.0	-19.0	-18.1	-17.2
Private transfers	18.8	18.8	20.7	18.5	17.7	17.4	17.2	16.9	16.5	16.2
FDI (net)	2.2	4.5	1.0	3.1	3.8	3.8	3.8	3.8	3.8	3.8
	(Year-on-year percent change)									
Exports of G&S (Value)	27.7	25.6	-2.2	4.6	13.6	14.1	12.1	10.3	9.7	9.5
Volume	23.5	16.2	2.4	3.1	9.9	9.4	9.2	8.4	7.9	7.6
Price	3.4	8.1	-4.4	1.5	3.4	4.3	2.7	1.8	1.7	1.8
Imports of G&S (Value)	12.5	20.3	1.7	-0.9	14.1	11.8	9.4	8.2	7.8	7.7
Volume	10.5	8.0	7.8	0.8	7.9	8.0	7.4	6.6	6.3	6.1
Price	1.8	11.4	-5.7	-1.7	5.7	3.5	1.9	1.5	1.4	1.5
Terms of trade (2008=100)	97.0	94.2	95.4	98.6	98.1	97.0	96.3	97.0	97.6	98.3
Memorandum Items:										
Nominal GDP	7109	7546	7587	8121	8473	8892	9423	10035	10708	11426
ST debt at residual maturity (year-end)	1666	1846	2172	1898	2022	1930	1920	2127	2188	2035
Gross foreign exchange reserves	1715	2069	2193	1993	2440	2372	2593	2918	3251	3544
Months of prospective imports of G&S	4.1	4.9	5.2	4.3	4.8	4.3	4.3	4.5	4.6	4.8
Percent of short-term debt (residual maturity)	102.9	112.1	101.0	105.0	120.7	122.9	135.1	137.2	148.6	174.1
External debt (percent of GDP)	57.8	64.2	68.2	64.3	64.4	59.5	57.6	56.4	54.9	52.9
Medium and long-term	39.3	43.2	45.4	44.9	45.8	41.6	39.7	38.5	37.0	35.1
Short-term	18.5	21.0	22.7	19.3	18.6	18.0	17.9	17.9	17.9	17.8
External debt service	1559	1753	1918	2240	1970	2091	2000	1992	2200	2262
Percent of exports of G&S	56.8	50.8	56.8	63.4	49.1	45.6	38.9	35.2	35.4	33.2
Percent of exports of G&S and private transfers	37.9	35.5	38.3	44.1	35.4	33.8	29.4	26.9	27.4	26.0

Sources: NBRM; and IMF staff estimates.

Table 4. FYR Macedonia: Monetary Survey, 2010-2019

(Billions of denars, unless specified otherwise)

	2010	2011	2012	2013				2014				2015	2016	2017	2018	2019
				1Q-13	2Q-13	3Q-13	4Q-13	1Q-14	2Q-14	3Q-14	4Q-14					
				NFA	99.9	124.7	126.1	128.6	114.3	119.6	114.8					
Central Bank	100.6	122.5	128.9	132.8	121.8	122.5	118.2	115.3	111.0	145.5	143.5	123.3	126.9	128.8	129.3	129.9
Commercial Banks	-0.7	2.2	-2.8	-4.2	-7.6	-2.9	-3.4	-4.4	-5.0	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1	-0.1
NDA	132.7	130.3	140.2	141.9	152.0	154.2	165.6	175.4	181.8	152.7	163.2	208.3	235.4	257.0	282.4	309.5
Credit to Government (net)	9.0	-1.8	1.9	5.0	6.5	7.7	10.8	19.8	22.8	-6.1	-6.4	22.1	28.6	28.5	30.5	32.7
From Banks (net)	15.0	14.0	29.1	32.4	32.9	34.0	37.0	40.7	37.9	37.4	44.0	51.3	60.8	70.2	79.9	88.2
of which: Credit (Tbills)	18.1	16.7	31.7	34.3	34.7	35.8	38.8	42.5	39.6	39.0	45.7	53.0	62.5	71.9	81.6	89.9
From Central Bank (net)	-6.0	-15.8	-27.2	-27.4	-26.4	-26.3	-26.2	-20.9	-15.1	-43.5	-50.5	-29.2	-32.2	-41.7	-49.4	-55.5
of which: Deposits	-9.0	-19.1	-30.4	-30.4	-29.3	-29.2	-29.5	-24.0	-18.0	-46.6	-53.6	-32.3	-35.3	-39.9	-43.5	-43.7
Credit to Private Sector (Gross)	193.4	208.2	218.9	220.0	224.1	225.5	232.7	236.0	242.7	246.3	250.9	270.5	291.2	313.0	336.4	361.2
From Banks	191.9	208.1	218.8	220.0	224.1	225.4	232.7	236.0	242.6	246.2	250.8	270.4	291.1	312.9	336.3	361.1
Denars	143.6	150.6	164.4	165.0	168.3	171.3	178.4	181.4	187.7	191.1	194.7	209.9	226.0	242.9	261.0	280.3
FX	48.3	57.6	54.4	55.0	55.8	54.1	54.3	54.6	54.9	55.1	56.1	60.5	65.1	70.0	75.2	80.8
From Central Bank	1.5	0.1	0.1	0.1	0.1	0.1	0.0	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1
Other Items (net)	-69.7	-76.0	-80.6	-83.1	-78.6	-79.0	-78.0	-80.5	-83.7	-87.4	-87.4	-87.4	-87.4	-87.4	-87.4	-87.4
Broad Money (M3)	232.6	255.0	266.3	270.5	266.3	273.8	280.4	286.2	287.7	298.2	306.6	331.5	362.3	385.8	411.7	439.3
Currency in Circulation	17.0	19.3	20.1	20.7	20.1	20.0	20.7	20.9	21.2	22.1	23.1	24.2	25.7	27.4	29.2	31.2
Total Deposits	215.6	235.7	246.2	249.8	246.2	253.8	259.7	265.4	266.5	276.1	283.5	307.2	336.6	358.4	382.5	408.1
Denars	106.8	122.3	135.1	137.4	138.4	142.7	147.9	152.1	153.2	159.4	162.7	176.3	193.2	205.7	219.5	234.2
FX	108.8	113.5	111.1	112.4	107.8	111.0	111.7	113.3	113.3	116.7	120.8	130.9	143.4	152.7	162.9	173.9
	(Year-on-year percent change)															
Private Sector Credit	7.3	7.7	5.2	3.9	3.1	3.3	6.3	7.3	8.3	9.2	7.8	7.8	7.7	7.5	7.5	7.4
Broad Money	12.2	9.7	4.4	5.0	3.0	5.1	5.3	5.8	8.0	8.9	9.3	8.1	9.3	6.5	6.7	6.7
Private Sector Deposits	12.9	9.3	4.4	4.2	2.7	5.2	5.5	6.2	8.3	8.8	9.2	8.4	9.6	6.5	6.7	6.7
	(Contribution to annual growth in broad money)															
NFA	2.5	10.7	0.5	2.7	-0.4	-1.7	-4.2	-6.6	-3.1	9.5	10.2	-6.6	1.1	0.5	0.1	0.1
NDA	9.7	-1.0	3.9	2.3	3.5	6.8	9.5	12.4	11.2	-0.5	-0.9	14.7	8.2	6.0	6.6	6.6
	(Percent of GDP)															
Private Sector Credit	41.3	41.9	43.6	44.3	44.8	44.7	45.7	45.2	45.8	61.5	48.1	49.5	50.2	50.7	51.1	51.4
Broad Money	49.6	51.3	53.1	54.5	53.2	54.3	55.1	54.8	54.2	74.4	58.8	60.6	62.5	62.5	62.5	62.5
Private Sector Deposits	46.0	47.4	49.0	50.3	49.2	50.3	51.0	50.8	50.3	68.9	54.4	56.2	58.1	58.1	58.1	58.1
Memorandum Items:																
Money Multiplier	4.7	4.8	4.8	4.9	5.0	5.2	5.2	5.4	5.3	5.3	5.2	5.3	5.4	5.4	5.4	5.5
Reserve Requirement Ratio (% of deposits)																
Denars	10.0	10.0	10.0	10.0	10.0	8.0	8.0	8.0	8.0	8.0	8.0	8.0	8.0	8.0	8.0	8.0
FX Indexed	20.0	20.0	20.0	20.0	20.0	20.0	20.0	20.0	20.0	20.0	20.0	20.0	20.0	20.0	20.0	20.0
FX	13.0	13.0	13.0	13.0	13.0	15.0	15.0	15.0	15.0	15.0	15.0	15.0	15.0	15.0	15.0	15.0
Velocity	2.0	1.9	1.9	1.8	1.9	1.8	1.8	1.8	1.8	1.3	1.7	1.7	1.6	1.6	1.6	1.6

Sources: NBRM; and IMF staff estimates.

**Table 5. FYR Macedonia: Central Bank Survey, 2010-2019**

(Billions of denars, unless specified otherwise)

	2010	2011	2012	2013				2014				2015	2016	2017	2018	2019
				1Q-13	2Q-13	3Q-13	4Q-13	1Q-14	2Q-14	3Q-14	4Q-14					
NFA	100.6	122.5	128.9	132.8	121.8	122.5	118.2	115.3	111.0	145.5	143.5	123.3	126.9	128.8	129.3	129.9
Assets	105.5	141.6	143.3	156.2	148.2	144.5	122.7	138.6	134.3	169.1	168.0	148.8	153.4	156.4	157.8	159.4
Liabilities	-4.9	-19.1	-14.4	-23.5	-26.3	-22.0	-4.5	-23.3	-23.4	-23.5	-24.5	-25.5	-26.5	-27.5	-28.5	-29.5
NDA	-51.6	-68.9	-73.0	-77.5	-68.4	-70.2	-64.7	-62.0	-56.4	-89.3	-84.8	-60.8	-59.7	-57.6	-53.6	-49.3
Banks (net)	-26.9	-32.2	-26.1	-29.9	-29.3	-31.3	-28.2	-29.6	-29.2	-32.6	-21.1	-18.4	-14.3	-7.7	0.0	4.4
of which:																
NBRM Bills and short-term facilities	-25.9	-32.2	-27.1	-31.2	-29.3	-31.3	-28.3	-29.6	-29.3	-32.6	-30.6	-30.6	-30.6	-29.6	-29.6	-29.6
Central Government (net)	-3.5	-13.4	-24.9	-24.8	-23.8	-23.8	-24.1	-18.6	-12.5	-41.0	-48.0	-26.7	-29.7	-34.3	-37.9	-38.1
of which:																
Deposits at Central Bank	-9.0	-19.1	-30.4	-30.4	-29.3	-29.2	-29.5	-24.0	-18.0	-46.6	-53.6	-32.3	-35.3	-39.9	-43.5	-43.7
Denar	-5.9	-7.0	-19.5	-8.2	-11.1	-14.4	-16.3	-12.3	-7.7	-7.1	-10.2	-0.6	-2.0	-4.0	-5.7	-5.7
FX	-3.1	-12.1	-10.9	-22.1	-18.2	-14.8	-13.1	-11.8	-10.3	-39.6	-43.4	-31.7	-33.4	-35.8	-37.9	-37.9
State and Local Governments (net)	-2.5	-2.3	-2.3	-2.6	-2.5	-2.5	-2.1	-2.3	-2.5	-2.5	-2.5	-2.5	-2.5	-2.5	-2.5	-2.5
Other items (net)	-18.7	-20.9	-19.7	-20.2	-12.8	-12.7	-10.2	-11.5	-12.1	-13.2	-13.2	-13.2	-13.2	-13.2	-13.2	-13.2
Reserve Money	49.0	53.6	55.9	55.3	53.4	52.3	53.5	53.3	54.6	56.2	58.7	62.5	67.1	71.2	75.7	80.5
Currency in Circulation	17.0	19.3	20.1	20.7	20.1	20.0	20.7	20.9	21.2	22.1	23.1	24.2	25.7	27.4	29.2	31.2
Other	32.0	34.3	35.8	34.6	33.3	32.3	32.8	32.4	33.4	34.0	35.6	38.2	41.4	43.9	46.5	49.4
Cash in Vaults	3.2	3.5	3.9	3.8	4.0	4.1	4.3	4.3	4.2	4.2	4.2	4.2	4.2	4.2	4.2	4.2
Total Reserves	28.8	30.9	32.0	30.8	29.3	28.2	28.4	28.1	29.2	29.8	31.4	34.0	37.2	39.7	42.3	45.2
on Denar Deposits	15.7	16.7	18.9	17.7	16.3	15.7	16.2	15.8	16.7	17.1	18.1	19.6	21.5	22.9	24.4	26.1
on FX Deposits	13.2	14.1	13.0	13.2	13.0	12.6	12.2	12.3	12.5	12.7	13.3	14.4	15.7	16.8	17.9	19.1
(Contribution to annual growth in reserve money)																
NFA	16.0	44.7	11.9	21.0	4.3	-4.2	-19.2	-31.6	-20.3	44.0	47.3	-34.4	5.8	2.9	0.7	0.7
NDA	-9.4	-35.2	-7.7	-7.7	-1.9	3.0	14.8	28.0	22.5	-36.5	-37.6	40.9	1.7	3.2	5.7	5.6
Reserve Money	6.6	9.5	4.3	13.3	2.3	-1.2	-4.4	-3.6	2.2	7.5	9.7	6.4	7.5	6.1	6.3	6.3
Memorandum Items:																
NBRM Bills (percent of GDP)	5.5	6.5	5.2	4.8	4.8	5.1	5.0	4.9	4.8	6.4	5.3	5.2	4.9	4.5	4.2	3.9
Govt Deposits at Central Bank (Percent of GDP)	1.9	3.8	6.1	6.1	5.9	5.8	5.8	4.6	3.4	11.6	10.3	5.9	6.1	6.5	6.6	6.2

Sources: NBRM; and IMF staff estimates.

**Table 6. FYR Macedonia: Financial Soundness Indicators of the Macedonian Banking System, 2010-2014**

(Percent)

	2010	2011	2012	2013				2014	
	2010Q3			2013Q1	2013Q2	2013Q3	2013Q4	2014Q1	2014Q2
<b>Capital adequacy</b>									
Regulatory capital/risk weighted assets	16.1	16.8	17.1	17.3	17.3	17.3	16.8	16.7	16.9
Tier I capital/risk weighted assets 1/	13.4	14.1	14.5	14.7	14.7	14.6	14.4	14.3	14.7
Equity and reserves to Assets	10.6	11.0	11.2	11.1	11.2	11.3	11.3	11.2	11.5
<b>Asset composition</b>									
<b>Structure of loans</b>									
Enterprises (loans to enterprises/total loans)	58.9	58.2	56.9	56.7	56.2	55.5	55.4	55.4	55.1
Households (loans to households/total loans)	37.1	36.5	36.4	36.5	37.1	37.9	37.7	37.9	38.5
<b>Lending with foreign currency component to private sector</b>									
Foreign currency lending/total credit to private sector	25.8	28.2	25.5	25.5	25.4	24.5	23.8	23.5	23.0
<b>Foreign currency indexed lending/total credit to private sector</b>									
	33.0	31.0	29.8	29.5	29.2	29.1	28.9	28.4	27.8
<b>NPLs 2/</b>									
NPLs/gross loans	9.0	9.5	10.1	11.4	11.8	11.2	10.9	10.6	11.3
NPLs net of provision/own funds	-0.3	-0.9	-3.7	-0.1	0.4	-2.7	-1.8	-4.3	-1.0
Provisions to Non-Performing Loans	100.7	101.9	107.1	100.1	99.4	104.7	103.1	107.4	101.7
Large exposures/own funds	200.4	189.6	205.1	208.0	195.4	195.0	188.5	200.0	193.7
<b>Connected lending</b>									
Banking system exposure to subsidiaries and shareholders/own funds	6.3	4.6	3.5	1.5	1.3	1.9	4.2	3.4	3.5
Banking system equity investments/own funds	1.5	1.6	1.8	1.7	1.6	1.6	1.7	1.7	1.7
<b>Earning and profitability</b>									
ROAA 3/	0.8	0.4	0.4	0.0	0.2	0.4	0.6	0.4	0.6
ROAE 3/	7.3	3.4	3.8	-0.4	1.8	3.9	5.7	4.0	5.4
Interest margin/gross income 4/	61.8	60.0	60.7	62.5	62.9	63.3	62.2	65.0	64.0
Noninterest expenses/gross income 5/	68.2	69.7	65.3	62.9	62.2	62.1	62.8	60.9	61.0
Personnel expenses/noninterest expenses	36.1	34.1	33.1	35.3	35.5	35.6	35.0	35.6	35.5
<b>Interest Rates</b>									
Local currency spreads	2.3	3.2	3.5	3.6	3.6	3.7	3.6	3.7	3.7
Foreign currency spreads	4.4	4.8	4.6	4.8	4.6	4.8	4.8	4.9	4.9
Interbank market interest rate	2.7	2.2	2.1	1.9	2.0	2.0	2.2	1.9	1.9
<b>Liquidity</b>									
Highly liquid assets/total assets 6/	25.3	25.3	29.4	29.6	28.7	28.8	27.3	27.4	26.0
Highly liquid assets/total short-term liabilities 7/	38.5	39.6	48.2	49.1	49.0	49.9	47.6	48.2	45.8
Liquid assets/total assets	30.9	31.2	32.4	33.1	32.0	32.2	31.2	31.5	30.5
Liquid assets/total short-term liabilities	46.9	48.9	53.0	54.9	54.6	55.9	54.5	55.5	53.9
Customer deposits/total (noninterbank) loans	114.3	115.7	113.5	114.2	110.8	113.3	112.7	113.6	111.1
Foreign currency deposits/total deposits	53.5	50.8	47.3	47.3	45.8	45.7	44.9	44.5	44.5
Including foreign exchange-indexed 8/	55.5	52.7	48.3	48.2	46.2	46.2	45.5	45.2	44.8
Central bank credit to banks/bank liabilities	0.01	0.01	0.4						
<b>Sensitivity to market risk</b>									
Net open foreign exchange position/own funds	18.9	21.3	11.4	7.3	12.1	16.1	15.6	11.0	9.7

Sources: NBRM's Financial Stability Unit.

Notes:

1/ Until 2007Q3 Tier I Capital includes common shares, non-cumulative preference shares, general reserves and undistributed profits, net of uncovered loss from previous years, current loss and goodwill. Starting from 2007Q4, Tier I Capital includes nominal value of common and non-cumulative preference shares, premiums from common and noncumulative preference shares, general reserves and distributed profits, positions as a result of consolidation, net of uncovered loss from previous years, current loss and intangible goods, owned common and non-cumulative preference shares and the difference between the amount of necessary and the amount of allocated reserves for potential losses.

2/ Includes loans to financial and nonfinancial sector.

3/ Adjusted for unallocated provisions for potential loan losses. Since 2009Q1 these items have been adjusted for unrecognized impairment.

4/ Interest margin represents interest income less interest expense. Gross income includes net interest income, fees and commissions income (gross, not net) and other gross income excluding extraordinary income.

5/ Noninterest expenses include fees and commissions expenses, operating expenses and other expenses excluding extraordinary expenses.

6/ Highly liquid assets are defined as cash and balance with the NBRM, treasury bills, NBRM bills, and correspondent accounts with foreign banks. Assets in domestic banks are excluded from total assets.

7/ Short-term liabilities are defined as deposits and other liabilities with a maturity of one year or less (without deposits and borrowings from domestic banks).

8/ FX indexed deposits include deposits and other FX indexed liabilities. However FX indexed deposits comprise the majority of these items. Since 2009Q1, the figure refers only to FX indexed deposits.

Table 7. FYR Macedonia: Capacity to Repay Indicators, 2013-2019

	2013	2014	2015	2016	2017	2018	2019
Exposure and Repayments (Millions of SDR)							
GRA credit to Macedonia 1/ (In percent of quota)	197.0 286	123.1 179	24.6 36	0.0 0	0.0 0	0.0 0	0.0 0
Charges 2/ Repurchase	2.2 0.0	2.1 73.9	1.1 98.5	0.2 24.6	0.0 0.0	0.0 0.0	0.0 0.0
Debt and Debt Service Ratios							
In percent of GDP							
Total external debt	64.3	64.4	59.5	57.6	56.4	54.9	52.9
External debt, public	19.7	24.4	23.0	23.7	24.2	24.5	24.1
Total public debt	35.2	40.6	40.0	43.0	45.5	48.6	48.4
GRA credit to Macedonia	2.8	1.6	0.3	0.0	0.0	0.0	0.0
Total external debt service	27.6	23.3	23.5	21.2	19.8	20.5	19.8
Public external debt service	3.7	2.6	4.7	3.4	2.4	3.0	2.5
Debt service due on GRA credit	0.0	1.0	1.3	0.3	0.0	0.0	0.0
In percent of Central Government Revenues							
Public external debt service	13.1	8.9	16.1	11.8	8.6	10.4	8.9
Debt service due on GRA credit	0.0	3.4	4.3	1.0	0.0	0.0	0.0
In percent of Gross International Reserves							
Total external debt	261.9	281.4	266.0	250.0	242.1	229.5	214.8
External debt, public	80.2	106.8	102.5	102.8	104.1	102.5	98.0
GRA credit to Macedonia	11.3	7.2	1.4	0.0	0.0	0.0	0.0
Debt service due on GRA credit	0.0	4.3	5.7	1.3	0.0	0.0	0.0
In percent of Exports of Goods and Services							
Total external debt service	54.9	44.7	40.7	34.5	31.3	31.7	30.0
Public external debt service	7.3	4.9	8.2	5.5	3.9	4.6	3.8
Debt service due on GRA credit	0.0	1.9	2.2	0.5	0.0	0.0	0.0
In percent of Total External Debt							
GRA credit to Macedonia	4.3	2.6	0.5	0.0	0.0	0.0	0.0
In percent of Total External Debt Service							
Debt service due on GRA credit	0.0	4.3	5.4	1.4	0.0	0.0	0.0
In percent of Total Public External Debt							
GRA credit to Macedonia	14.1	6.8	1.4	0.0	0.0	0.0	0.0
In percent of Total Public External Debt Service							
Debt service due on GRA credit	0.0	38.5	26.7	8.7	0.0	0.0	0.0

Sources: Macedonian authorities; Finance Department; World Economic Outlook; and IMF staff estimates.

Notes:

1/ Repurchases are assumed to be made as scheduled.

2/ Includes GRA basic rate of charge, surcharges and service fees.

**Table 8. FYR Macedonia: External Debt Sustainability Framework, 2009-2019**  
(Percent of GDP, unless otherwise indicated)

	2009	2010	2011	2012	2013	Projections						Debt-stabilizing non-interest current account 6/ -5.7
						2014	2015	2016	2017	2018	2019	
<b>Baseline: External debt</b>	55.9	57.8	64.2	68.2	64.3	<b>64.4</b>	<b>59.6</b>	<b>57.7</b>	<b>56.5</b>	<b>55.0</b>	<b>53.0</b>	
Change in external debt	7.1	1.9	6.5	3.9	-3.9	0.1	-4.8	-1.9	-1.2	-1.5	-2.0	
Identified external debt-creating flows (4+8+9)	2.8	-2.3	-4.7	0.4	-4.2	-2.3	-1.2	-0.8	-1.1	-1.3	-1.4	
Current account deficit, excluding interest payments	6.2	1.3	1.4	2.0	1.0	2.1	3.4	3.7	3.4	3.2	3.1	
Deficit in balance of goods and services	22.8	19.8	20.6	22.5	18.6	19.1	19.9	20.0	19.0	18.1	17.2	
Exports	31.8	38.6	45.7	44.5	43.5	46.8	49.2	50.9	53.0	54.9	56.7	
Imports	54.6	58.5	66.3	67.0	62.0	65.9	69.1	70.9	72.0	73.0	73.9	
Net non-debt creating capital inflows (negative)	-4.0	-1.7	-3.9	-2.2	-1.5	-3.0	-3.0	-3.0	-3.0	-3.0	-3.0	
Automatic debt dynamics 1/	0.5	-2.0	-2.2	0.6	-3.6	-1.3	-1.5	-1.4	-1.4	-1.4	-1.4	
Contribution from nominal interest rate	0.5	0.7	1.1	0.9	0.8	0.9	0.8	0.7	0.7	0.7	0.7	
Contribution from real GDP growth	0.2	-1.8	-1.3	0.3	-1.7	-2.2	-2.3	-2.2	-2.2	-2.1	-2.1	
Contribution from price and exchange rate changes 2/	-0.1	-0.9	-2.1	-0.6	-2.8	...	...	...	...	...	...	
Residual, incl. change in gross foreign assets (2-3) 3/	4.3	4.2	11.2	3.5	0.3	2.4	-3.7	-1.1	-0.1	-0.2	-0.6	
External debt-to-exports ratio (in percent)	175.7	149.5	140.5	153.2	147.8	137.5	121.1	113.4	106.6	100.2	93.4	
<b>Gross external financing need (in billions of euros) 4/</b>	1.8	1.7	1.9	2.1	2.3	2.1	2.4	2.4	2.3	2.5	2.6	
in percent of GDP	26.8	23.3	24.6	27.3	28.5	25.3	26.9	24.9	23.2	23.8	22.9	
<b>Scenario with key variables at their historical averages 5/</b>						<b>63.6</b>	<b>57.3</b>	<b>54.1</b>	<b>52.3</b>	<b>50.6</b>	<b>48.5</b>	<b>-6.8</b>
<b>Key Macroeconomic Assumptions Underlying Baseline</b>						<u>10-Year Historical Average</u>	<u>10-Year Standard Deviation</u>					
Real GDP growth (in percent)	-0.4	3.4	2.3	-0.5	2.7	3.4	2.4	3.5	3.7	3.9	4.0	4.0
GDP deflator in euros (change in percent)	0.3	1.6	3.7	1.0	4.3	2.9	2.1	0.8	1.2	2.0	2.4	2.6
Nominal external interest rate (in percent)	1.0	1.3	2.1	1.5	1.3	1.0	0.5	1.4	1.3	1.3	1.3	1.3
Growth of exports (euro terms, in percent)	-25.4	27.7	25.6	-2.2	4.6	13.3	17.3	12.4	10.2	9.6	10.8	10.6
Growth of imports (euro terms, in percent)	-20.4	12.5	20.3	1.7	-0.9	11.1	14.1	10.8	10.1	8.6	8.1	8.2
Current account balance, excluding interest payments	-6.2	-1.3	-1.4	-2.0	-1.0	-4.1	4.0	-2.1	-3.4	-3.7	-3.4	-3.2
Net non-debt creating capital inflows	4.0	1.7	3.9	2.2	1.5	4.4	2.2	3.0	3.0	3.0	3.0	3.0

1/ Derived as  $[r - g - r(1+g) + ea(1+r)] / (1+g+r+gr)$  times previous period debt stock, with  $r$  = nominal effective interest rate on external debt;  $r$  = change in domestic GDP deflator in euro terms,  $g$  = real GDP growth rate,  $e$  = nominal appreciation (increase in dollar value of domestic currency), and  $a$  = share of domestic-currency denominated debt in total external debt.

2/ The contribution from price and exchange rate changes is defined as  $[-r(1+g) + ea(1+r)] / (1+g+r+gr)$  times previous period debt stock.  $r$  increases with an appreciating domestic currency ( $e > 0$ ) and rising inflation (based on GDP deflator).

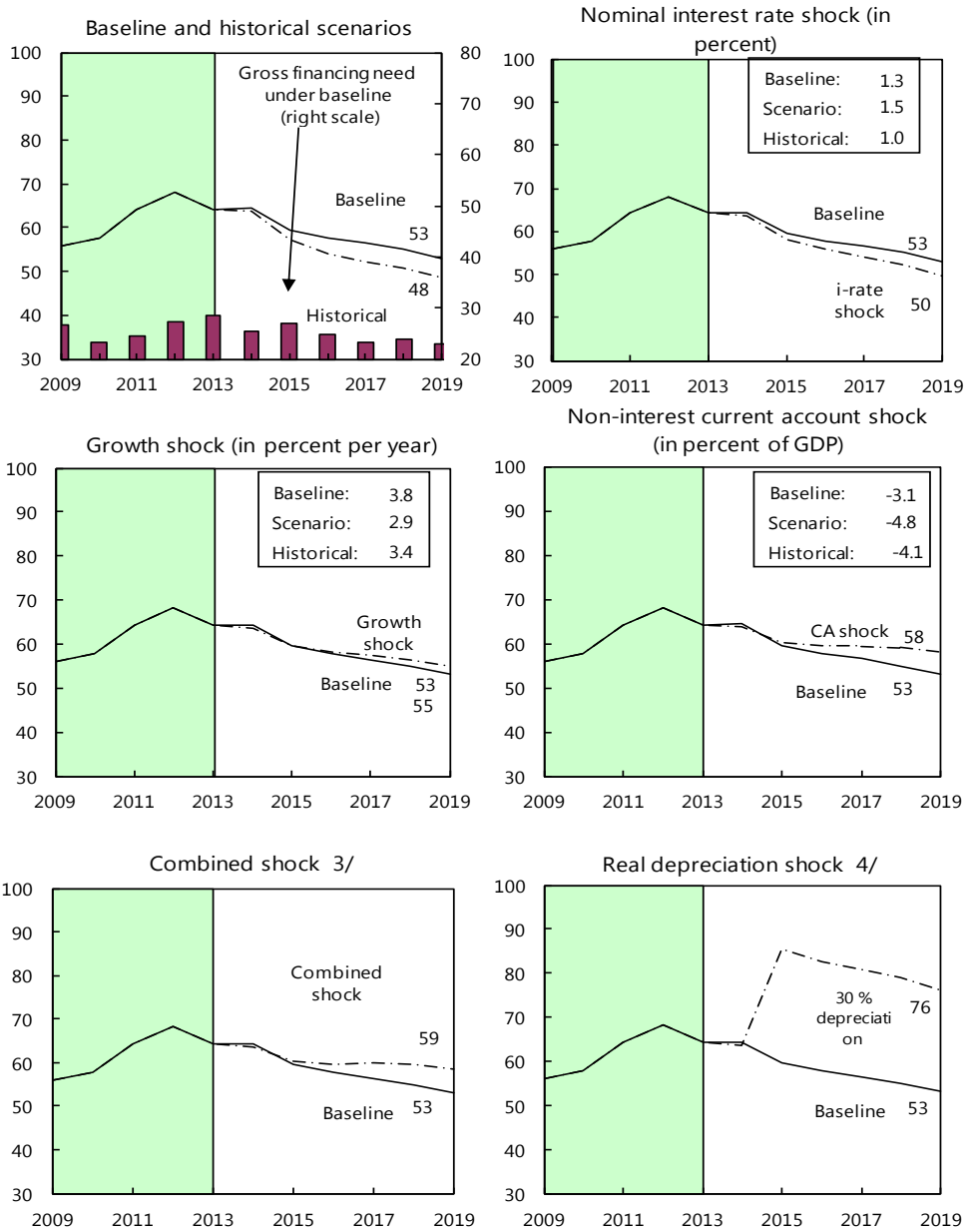
3/ For projection, line includes the impact of price and exchange rate changes.

4/ Defined as current account deficit, plus amortization on medium- and long-term debt, plus short-term debt at end of previous period.

5/ The key variables include real GDP growth; nominal interest rate; dollar deflator growth; and both non-interest current account and non-debt inflows in percent of GDP.

6/ Long-run, constant balance that stabilizes the debt ratio assuming that key variables (real GDP growth, nominal interest rate, dollar deflator growth, and non-debt inflows in percent of GDP) remain at their levels of the last projection year.

**Figure 7. FYR Macedonia: External Debt Sustainability: Bound Tests 1/ 2/**  
(External debt in percent of GDP)



Sources: International Monetary Fund, Country desk data, and staff estimates.

1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.

2/ For historical scenarios, the historical averages are calculated over the ten-year period, and the information is used to project debt dynamics five years ahead.

3/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and current account balance.

4/ One-time real depreciation of 30 percent occurs in 2014



## Annex. Debt Sustainability Analysis

*Persistent low inflation, high ratio of foreign currency-denominated debt, and still high external financing requirements are key risk factors. Stress tests show that the debt path is robust to individual shock scenarios but sensitive to a combined macro-fiscal shock. Nonetheless, the general government debt ratio remains below 60 percent of GDP under both symmetric and asymmetric shocks over the forecast horizon.*

- 1. General government debt is expected to rise by about 6 percent of GDP over the forecast horizon, to just above 40 percent<sup>1</sup>.** The large Eurobond issuance in July pre-finances external debt repayments in 2015; the resulting large balance in cash deposits is expected to be drawn down in 2015. In cumulative terms, a slowly closing primary gap is the main debt-creating flow, accounting for 11.9 percentage points. This is partially offset by favorable interest rate/growth differential (5.4 percentage points). Cash deposits are assumed to evolve in line, with maintaining a buffer of one quarter of net domestic financing requirements.
- 2. Non-financial public sector debt is expected to rise to about 52 percent of GDP over the forecast horizon from 38 percent of GDP in 2014.** The increase is mainly due to rising debt in the two largest SOEs, PESR (road infrastructure) and ELEM (electricity generation). The debts of these are expected to increase from 1.1 to 8.1 and 1.9 to 3.2 percent of GDP, respectively over the forecast horizon. Under most stress test scenarios the debt ratio remains below the 60 percent of GDP threshold set by the envisaged fiscal rule. However, a combined macro fiscal shock would increase debt to about 67.5 percent of GDP.
- 3. Low inflation is an important risk.** Persistent low inflation would increase the real debt burden and make it harder to reduce debt ratios. Low inflation shock stress tests show that public debt ratios will increase on average by 1.2 percentage points of GDP per year over the period 2015–2019, driven both by a worsening of the primary balance and less favorable interest-growth differentials. The debt path is fairly robust to individual shock scenarios, but a combined macro-fiscal shock could lead to a large increase in debt (text table).

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<sup>1</sup> The changes in the path relative to the 2014 Article IV consultation are partially due to revisions in GDP. National accounts have been revised based on the new methodology of SSO, ESA 2010. These revisions affect the debt-to-GDP ratios: e.g., 2013 nominal GDP was reported as MKD 474 billion in the 2014 Article IV Staff Report; in September it was revised to MKD 500 billion; this lowered the debt-to-GDP ratio in 2013 from 35.8 percent to 34.1.

**Table 1. FYR Macedonia General Government Debt Stress Test Scenarios**

Name	Description	Impact on debt 1/
Primary Balance Shock	Minimum shock equivalent to 50 percent of planned adjustment (50 percent implemented), or baseline minus half of the 10-year historical standard deviation, whichever is larger. There is an increase in interest rates of 25bp for every 1 percent of GDP worsening in the primary balance.	1.9
Real GDP Growth Shock	Real GDP growth is reduced to 2.5 percent in the period 2017–19 relative to a baseline of 4 percent; revenue-to-GDP ratio remains the same as in the baseline; level of non-interest expenditures is the same as in the baseline; deterioration in primary balance leads to higher interest rate (see above); decline in growth leads to lower inflation (0.25 percentage points per 1 percentage point decrease in GDP growth).	5.0
Interest Rate Shock	Interest rate increases by difference between average real interest rate level over projection and maximum real historical level, or by 200bp, whichever is larger.	1.4
Real Exchange Rate Shock	Estimate of overvaluation or maximum historical movement of the exchange rate, whichever is higher; pass-through to inflation with default elasticity of 0.25 for EMs and 0.03 for AEs.	3.1
Combined Macro-Fiscal Shock	Shock size and duration based on the underlying shocks.	12.4
Debt guarantee shock	Central Government guarantees as of 2013 on SOEs borrowing fully called over 2015–19 forecast horizon. There is an increase in interest rates of 100bps for every 1 percent of GDP worsening in the primary balance.	4.9
Low Inflation Shock	Constant deflator growth between 2014–19	2.5

Notes:

1/ Percentage points in excess of the baseline at the end of the projection period.

## FYR Macedonia General Government Debt Sustainability Analysis (DSA) - Baseline Scenario

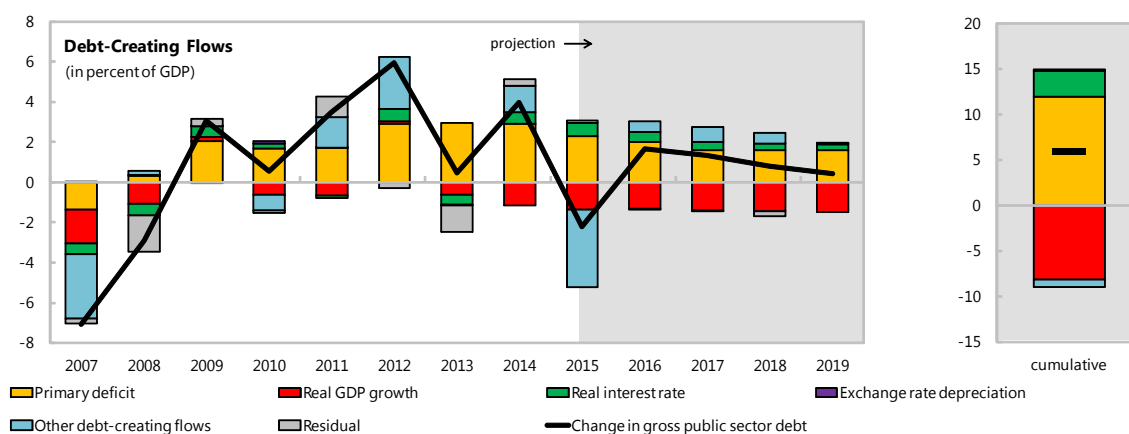
(in percent of GDP unless otherwise indicated)

Debt, Economic and Market Indicators <sup>1/</sup>

	Actual			Projections						As of September 15, 2014		
	2007-2011 <sup>2/</sup>	2012	2013	2014	2015	2016	2017	2018	2019	Sovereign Spreads		
Nominal gross general government debt	24.0	33.7	34.1	38.1	35.9	37.6	38.9	39.7	40.1	Spread (bp) <sup>3/</sup>	268	
General government gross financing needs	2.0	8.8	14.1	13.8	13.9	10.2	8.6	10.2	9.3	CDS (bp)	401	
Real GDP growth (in percent)	3.2	-0.5	2.1	3.5	3.8	3.9	4.0	4.0	4.0	Ratings	Foreign	Local
Inflation (GDP deflator, in percent)	3.2	1.0	4.3	0.8	1.2	2.0	2.4	2.6	2.6	Moody's	n.a.	n.a.
Nominal GDP growth (in percent)	6.8	0.5	7.0	4.3	4.9	6.0	6.5	6.7	6.7	S&P's	BB-	BB-
Effective interest rate (in percent) <sup>4/</sup>	3.0	3.3	2.9	2.6	3.0	3.6	3.7	3.6	3.6	Fitch	BB+	BB+

## Contribution to Changes in General Government Debt

	Actual			Projections						cumulative	debt-stabilizing primary balance <sup>9/</sup>
	2007-2011	2012	2013	2014	2015	2016	2017	2018	2019		
Change in gross general government debt	-0.6	5.94	0.46	4.0	-2.2	1.7	1.3	0.8	0.4	6.0	
Identified debt-creating flows	-0.4	6.26	1.77	3.6	-2.3	1.7	1.3	1.0	0.4	5.8	
Primary deficit	0.9	2.9	2.9	2.9	2.3	2.0	1.6	1.6	1.6	11.9	-1.2
Primary (noninterest) revenue and grants	31.1	29.4	28.0	28.7	29.4	28.9	28.2	28.2	28.2	171.8	
Primary (noninterest) expenditure	31.9	32.4	30.9	31.6	31.8	30.8	29.8	29.8	29.8	183.7	
Automatic debt dynamics <sup>5/</sup>	-0.8	0.8	-1.1	-0.6	-0.7	-0.8	-1.0	-1.1	-1.2	-5.4	
Interest rate/growth differential <sup>6/</sup>	-0.9	0.8	-1.1	-0.6	-0.7	-0.8	-1.0	-1.1	-1.2	-5.4	
Of which: real interest rate	-0.1	0.6	-0.5	0.6	0.6	0.5	0.4	0.3	0.3	2.8	
Of which: real GDP growth	-0.8	0.1	-0.6	-1.2	-1.4	-1.3	-1.4	-1.5	-1.5	-8.2	
Exchange rate depreciation <sup>7/</sup>	0.0	0.0	0.0	...	...	...	...	...	...	...	
Other identified debt-creating flows	-0.4	2.6	-0.1	1.3	-3.9	0.5	0.7	0.6	0.0	-0.7	
Privatization receipts (negative)	-0.2	0.0	-0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Changes in cash, deposits, and securities held for	-0.2	2.6	0.1	1.3	-3.9	0.5	0.7	0.6	0.0	-0.7	
Residual, including asset changes <sup>8/</sup>	-0.2	-0.3	-1.3	0.3	0.1	0.0	0.0	-0.2	0.0	0.2	



Source: IMF staff.

1/ Public sector is defined as general government.

2/ Based on available data.

3/ Bond Spread over German Bonds.

4/ Defined as interest payments divided by debt stock at the end of previous year.

5/ Derived as  $[(r - p(1+g) - g + ae(1+r))/(1+g+p+gp)]$  times previous period debt ratio, with  $r$  = interest rate;  $p$  = growth rate of GDP deflator;  $g$  = real GDP growth rate; $a$  = share of foreign-currency denominated debt; and  $e$  = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).6/ The real interest rate contribution is derived from the denominator in footnote 4 as  $r - \pi(1+g)$  and the real growth contribution as  $-g$ .7/ The exchange rate contribution is derived from the numerator in footnote 2/ as  $ae(1+r)$ .

8/ For projections, this line includes exchange rate changes during the projection period.

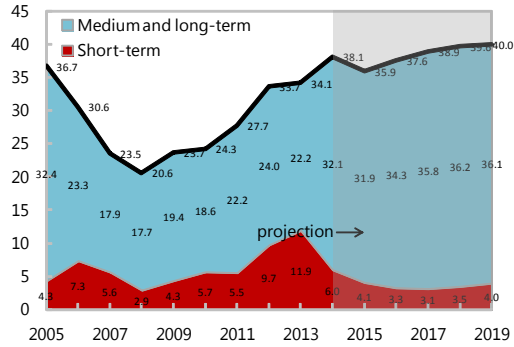
9/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

## FYR Macedonia General Government DSA - Composition of General Govt. Debt and Alternative Scenarios

### Composition of General Government Debt

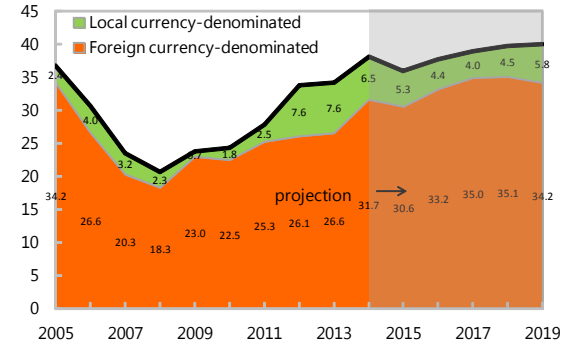
#### By Maturity

(in percent of GDP)



#### By Currency

(in percent of GDP)



### Alternative Scenarios

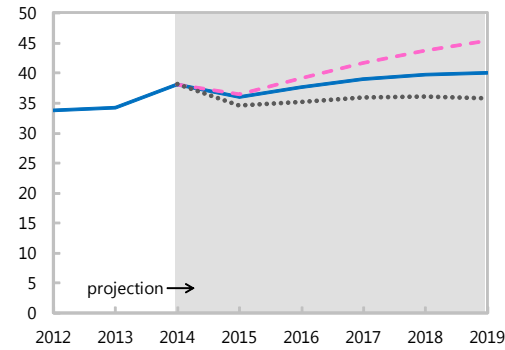
— Baseline

..... Historical

- - - - - Constant Primary Balance

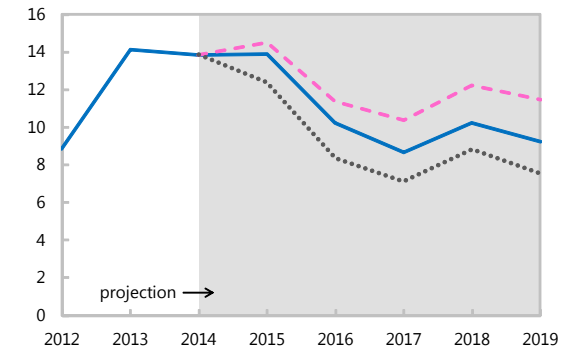
#### Gross Nominal General Government Debt

(in percent of GDP)



#### General Government Gross Financing Needs

(in percent of GDP)



### Underlying Assumptions

(in percent)

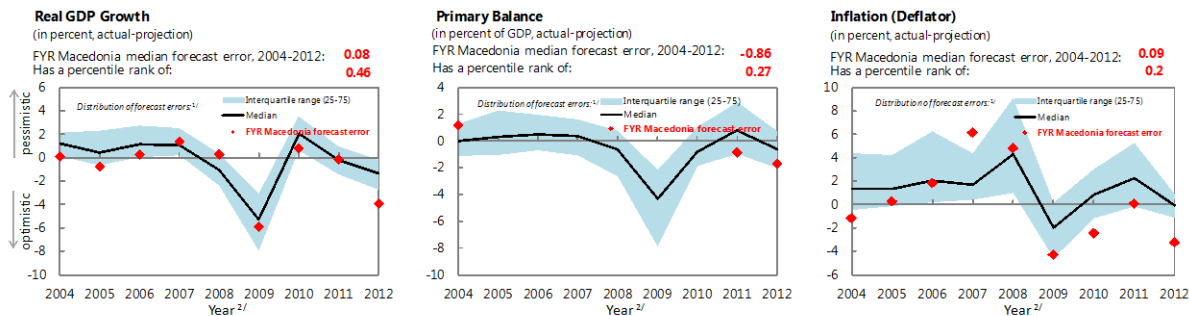
Baseline Scenario	2014	2015	2016	2017	2018	2019
Real GDP growth	3.5	3.8	3.9	4.0	4.0	4.0
Inflation	0.8	1.2	2.0	2.4	2.6	2.6
Primary Balance	-2.9	-2.3	-2.0	-1.6	-1.5	-1.5
Effective interest rate	2.6	3.0	3.6	3.7	3.6	3.6
<b>Constant Primary Balance Scenario</b>						
Real GDP growth	3.5	3.8	3.9	4.0	4.0	4.0
Inflation	0.8	1.2	2.0	2.4	2.6	2.6
Primary Balance	-2.9	-2.9	-2.9	-2.9	-2.9	-2.9
Effective interest rate	2.6	3.0	3.6	3.7	3.6	3.5

Historical Scenario	2014	2015	2016	2017	2018	2019
Real GDP growth	3.5	3.2	3.2	3.2	3.2	3.2
Inflation	0.8	1.2	2.0	2.4	2.6	2.6
Primary Balance	-2.9	-0.7	-0.7	-0.7	-0.7	-0.7
Effective interest rate	2.6	3.0	3.3	3.3	3.0	2.8

Source: IMF staff.

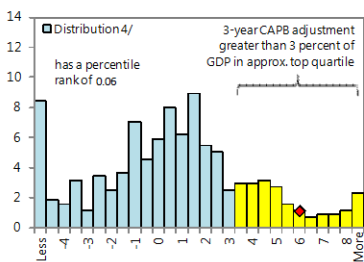
**FYR Macedonia General Government DSA - Realism of Baseline Assumptions**

**Forecast Track Record, versus all countries**

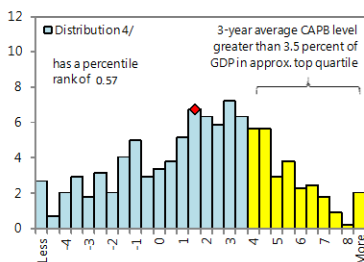


**Assessing the Realism of Projected Fiscal Adjustment**

**3-Year Adjustment in Cyclically-Adjusted Primary Balance (CAPB)**  
(Percent of GDP)



**3-Year Average Level of Cyclically-Adjusted Primary Balance (CAPB)**  
(Percent of GDP)



Source : IMF Staff.

1/ Plotted distribution includes all countries, percentile rank refers to all countries.

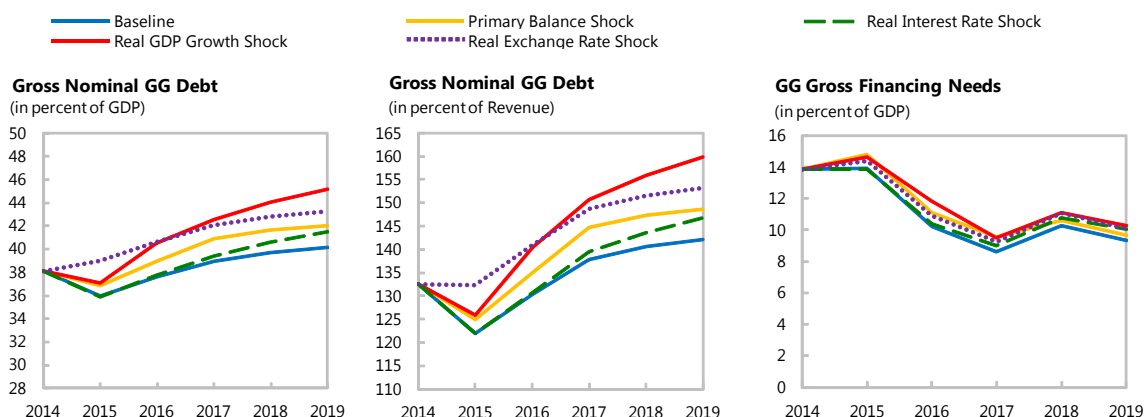
2/ Projections made in the spring WEO vintage of the preceding year.

3/ Not applicable for Macedonia, Former Yugoslav Republic of.

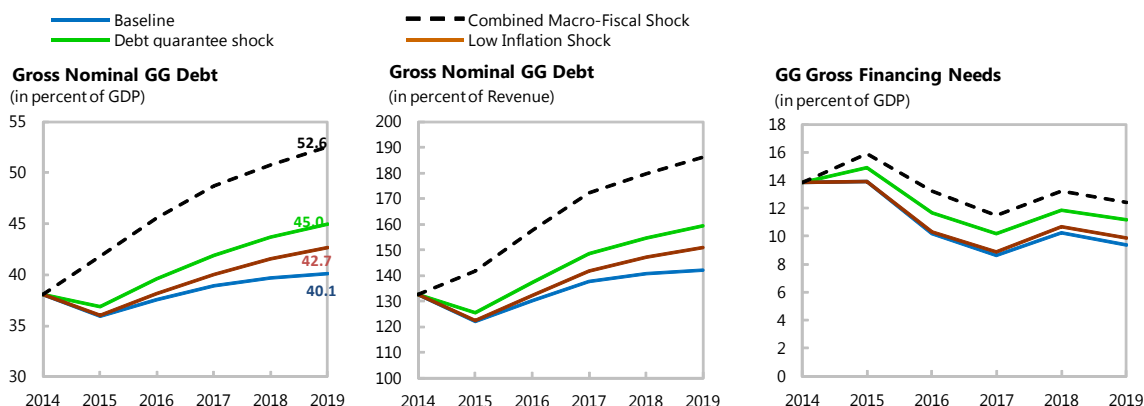
4/ Data cover annual observations from 1990 to 2011 for advanced and emerging economies with debt greater than 60 percent of GDP. Percent of sample on vertical axis.

FYR Macedonia General Government DSA - Stress Tests

Macro-Fiscal Stress Tests



Additional Stress Tests



Underlying Assumptions (in percent)

	2014	2015	2016	2017	2018	2019		2014	2015	2016	2017	2018	2019
<b>Primary Balance Shock</b>							<b>Real GDP Growth Shock</b>						
Real GDP growth	3.5	3.8	3.9	4.0	4.0	4.0	Real GDP growth	3.5	2.3	2.4	2.5	2.5	2.5
Inflation	0.8	1.2	2.0	2.4	2.6	2.6	Inflation	0.8	0.8	1.6	2.0	2.2	2.2
Primary balance	-2.9	-3.2	-2.5	-2.2	-1.6	-1.6	Primary balance	-2.9	-2.9	-3.1	-1.6	-1.6	-1.6
Effective interest rate	2.6	3.0	3.6	3.8	3.7	3.6	Effective interest rate	2.6	3.0	3.6	3.8	3.7	3.6
<b>Real Interest Rate Shock</b>							<b>Real Exchange Rate Shock</b>						
Real GDP growth	3.5	3.8	3.9	4.0	4.0	4.0	Real GDP growth	3.5	3.8	3.9	4.0	4.0	4.0
Inflation	0.8	1.2	2.0	2.4	2.6	2.6	Inflation	0.8	4.5	2.0	2.4	2.6	2.6
Primary balance	-2.9	-2.3	-2.0	-1.6	-1.6	-1.6	Primary balance	-2.9	-2.3	-2.0	-1.6	-1.6	-1.6
Effective interest rate	2.6	3.0	4.1	4.6	4.7	4.9	Effective interest rate	2.6	3.3	3.5	3.7	3.6	3.5
<b>Combined Shock</b>							<b>Baseline Scenario</b>						
Real GDP growth	3.5	2.3	2.4	2.5	2.5	2.5	Real GDP growth	3.5	3.8	3.9	4.0	4.0	4.0
Inflation	0.8	0.8	1.6	2.0	2.2	2.2	Inflation	1.6	1.5	1.6	2.0	2.2	2.5
Primary balance	-2.9	-3.2	-3.1	-2.2	-1.6	-1.6	Primary Balance	-2.8	-2.2	-2.2	-2.2	-2.2	-2.2
Effective interest rate	2.6	3.3	4.1	4.5	4.7	4.9	Effective interest rate	2.5	2.7	2.9	3.0	3.6	2.9
<b>Debt guarantee shock</b>							<b>Low Inflation Shock</b>						
Real GDP growth	3.5	3.8	3.9	4.0	4.0	4.0	Real GDP growth	3.5	3.8	3.9	4.0	4.0	4.0
Inflation	0.8	1.2	2.0	2.4	2.6	2.6	Inflation	0.8	0.8	0.8	0.8	0.8	0.8
Primary balance	-2.9	-3.3	-2.9	-2.5	-2.4	-2.4	Primary balance	-2.9	-2.3	-2.0	-1.6	-1.6	-1.6
Effective interest rate	2.6	3.0	3.8	4.1	4.1	4.1	Effective interest rate	2.6	3.0	3.6	3.7	3.6	3.6

Source: IMF staff.

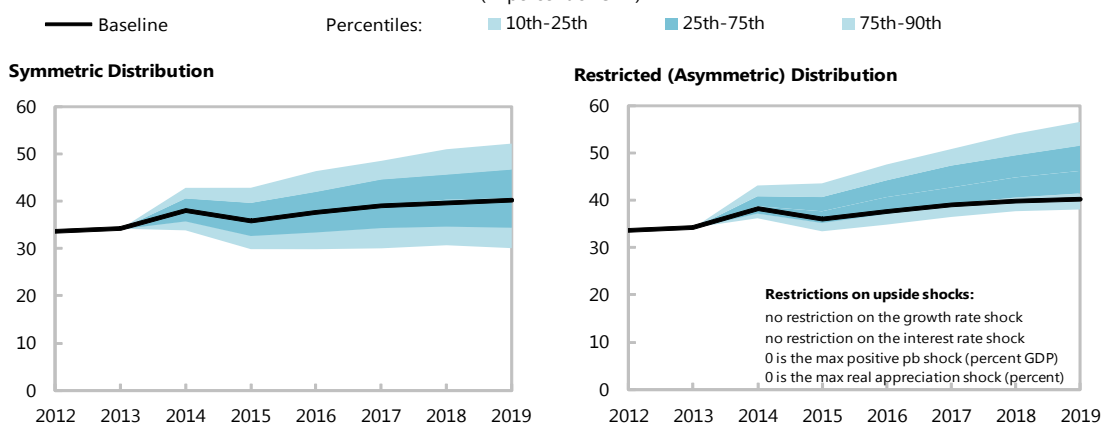
## Macedonia, Former Yugoslav Republic of General Government DSA Risk Assessment

### Heat Map

Debt level <sup>1/</sup>	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability shock
Gross financing needs <sup>2/</sup>	Real GDP Growth Shock	Primary Balance Shock	Real Interest Rate Shock	Exchange Rate Shock	Contingent Liability Shock
Debt profile <sup>3/</sup>	Market Perception	External Financing Requirements	Change in the Share of Short-Term Debt	Public Debt Held by Non-Residents	Foreign Currency Debt

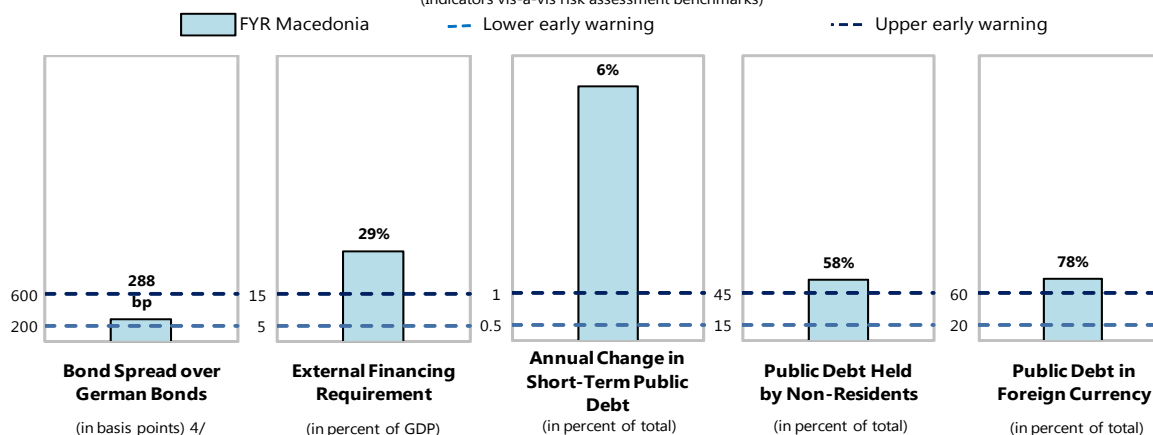
### Evolution of Predictive Densities of Gross Nominal General Government Debt

(in percent of GDP)



### Debt Profile Vulnerabilities

(Indicators vis-à-vis risk assessment benchmarks)



Source: IMF staff.

1/ The cell is highlighted in green if debt burden benchmark of 70% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

2/ The cell is highlighted in green if gross financing needs benchmark of 15% is not exceeded under the specific shock or baseline, yellow if exceeded under specific shock but not baseline, red if benchmark is exceeded under baseline, white if stress test is not relevant.

3/ The cell is highlighted in green if country value is less than the lower risk-assessment benchmark, red if country value exceeds the upper risk-assessment benchmark, yellow if country value is between the lower and upper risk-assessment benchmarks. If data are unavailable or indicator is not relevant, cell is white. Lower and upper risk-assessment benchmarks are:

200 and 600 basis points for bond spreads; 5 and 15 percent of GDP for external financing requirement; 0.5 and 1 percent for change in the share of short-term debt; 15 and 45 percent for the public debt held by non-residents; and 20 and 60 percent for the share of foreign-currency denominated debt.

4/ An average over the last 3 months, 17-Jun-14 through 15-Sep-14.

Table 1. FYR Macedonia Non-Financial Public Sector Debt Stress Test Scenarios

Name	Description	Impact on debt 1/
Primary Balance Shock	Minimum shock equivalent to 50% of planned adjustment (50% implemented), or baseline minus half of the 10-year historical standard deviation, whichever is larger. There is an increase in interest rates of 25bp for every 1% of GDP worsening in the primary balance.	3.4
Real GDP Growth Shock	Real GDP growth is reduced to 2.5 percent in the period 2017-19 relative to a baseline of 4 percent; revenue-to-GDP ratio remains the same as in the baseline; level of non-interest expenditures is the same as in the baseline; deterioration in primary balance leads to higher interest rate (see above); decline in growth leads to lower inflation (0.25 percentage points per 1 percentage point decrease in GDP growth).	5.9
Interest Rate Shock	Interest rate increases by difference between average real interest rate level over projection and maximum real historical level, or by 200bp, whichever is larger.	1.8
Real Exchange Rate Shock	Estimate of overvaluation or maximum historical movement of the exchange rate, whichever is higher; pass-through to inflation with default elasticity of 0.25 for EMs and 0.03 for AEs.	3.6
Combined Macro-Fiscal Shock	Shock size and duration based on the underlying shocks.	15.8
Debt guarantee shock	Central Government guarantees as of 2013 on SOEs borrowing fully called over 2015-19 forecast horizon. There is an increase in interest rates of 100bps for every 1% of GDP worsening in the primary balance.	5.1
Low Inflation Shock	Constant deflator growth between 2014-19	3.2

Notes:

1/ Percentage points in excess of the baseline at the end of the projection period.



## FYR Macedonia Non-Financial Public Sector Debt Sustainability Analysis (DSA) - Baseline Scenario

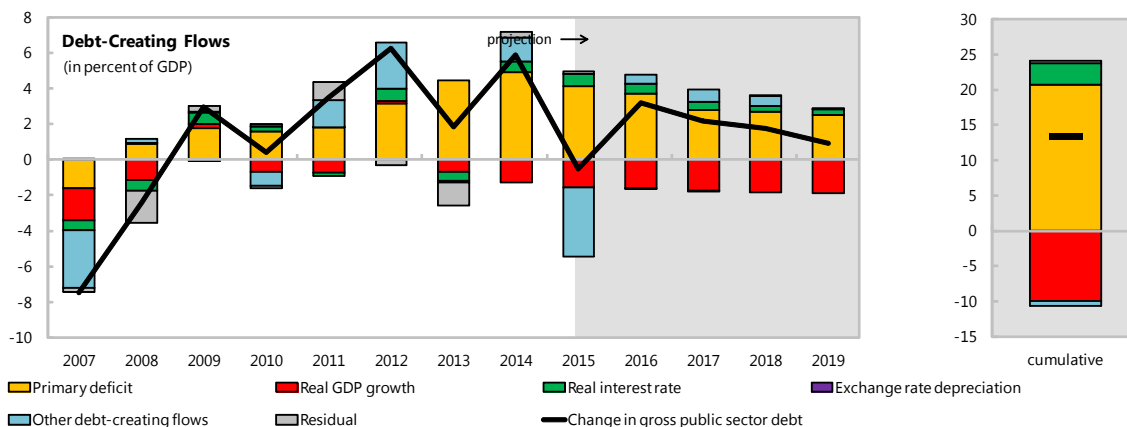
(in percent of GDP unless otherwise indicated)

Debt, Economic and Market Indicators <sup>1/</sup>

	Actual			Projections						As of September 15, 2014		
	2007-2011 <sup>2/</sup>	2012	2013	2014	2015	2016	2017	2018	2019	Sovereign Spreads		
Nominal gross public debt	26.4	36.4	38.2	44.1	43.6	46.8	49.0	50.7	51.6	Spread (bp) <sup>3/</sup>		268
Public gross financing needs	2.1	9.1	15.6	16.3	16.3	12.7	10.7	11.6	10.7	CDS (bp)		401
Real GDP growth (in percent)	3.2	-0.5	2.1	3.5	3.8	3.9	4.0	4.0	4.0	Ratings	Foreign	Local
Inflation (GDP deflator, in percent)	3.2	1.0	4.3	0.8	1.2	2.0	2.4	2.6	2.6	Moody's	n.a.	n.a.
Nominal GDP growth (in percent)	6.8	0.5	7.0	4.3	4.9	6.0	6.5	6.7	6.7	S&Ps	BB-	BB-
Effective interest rate (in percent) <sup>4/</sup>	3.1	3.2	2.9	2.5	2.9	3.4	3.5	3.4	3.3	Fitch	BB+	BB+

## Contribution to Changes in Public Debt

	Actual			Projections						cumulative	debt-stabilizing primary balance <sup>9/</sup>
	2007-2011	2012	2013	2014	2015	2016	2017	2018	2019		
Change in gross public sector debt	-0.6	6.25	1.87	5.9	-0.5	3.2	2.2	1.7	0.9	13.4	
Identified debt-creating flows	-0.5	6.58	3.19	5.5	-0.6	3.2	2.2	1.7	0.9	13.0	
Primary deficit	0.9	3.2	4.5	4.9	4.1	3.7	2.8	2.7	2.5	20.8	
Primary (noninterest) revenue and grants	31.1	29.4	28.0	28.7	29.4	28.9	28.2	28.2	28.2	171.8	
Primary (noninterest) expenditure	31.9	32.6	32.4	33.6	33.6	32.6	31.0	30.9	30.8	192.5	
Automatic debt dynamics <sup>5/</sup>	-0.9	0.8	-1.2	-0.7	-0.9	-1.1	-1.3	-1.5	-1.6	-7.0	
Interest rate/growth differential <sup>6/</sup>	-0.9	0.8	-1.2	-0.7	-0.9	-1.1	-1.3	-1.5	-1.6	-7.0	
Of which: real interest rate	-0.1	0.7	-0.5	0.6	0.7	0.6	0.5	0.3	0.3	2.9	
Of which: real GDP growth	-0.8	0.1	-0.7	-1.3	-1.6	-1.6	-1.7	-1.8	-1.9	-10.0	
Exchange rate depreciation <sup>7/</sup>	0.0	0.0	0.0	...	...	...	...	...	...	...	
Other identified debt-creating flows	-0.4	2.6	-0.1	1.3	-3.9	0.5	0.7	0.6	0.0	-0.7	
Privatization receipts (negative)	-0.2	0.0	-0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Contingent liabilities	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Changes in cash, deposits, and securities held for	-0.2	2.6	0.1	1.3	-3.9	0.5	0.7	0.6	0.0	-0.7	
Residual, including asset changes <sup>8/</sup>	-0.2	-0.3	-1.3	0.3	0.1	0.0	0.0	0.0	0.0	0.4	

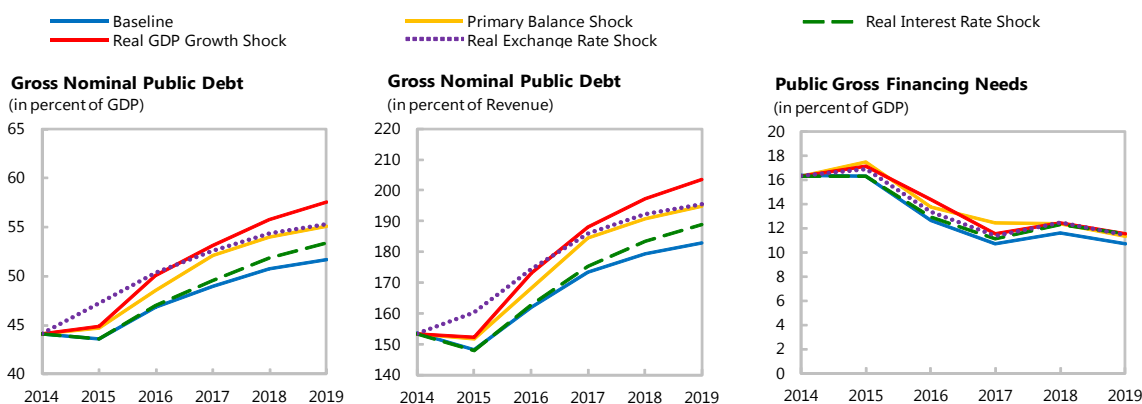


Source: IMF staff.

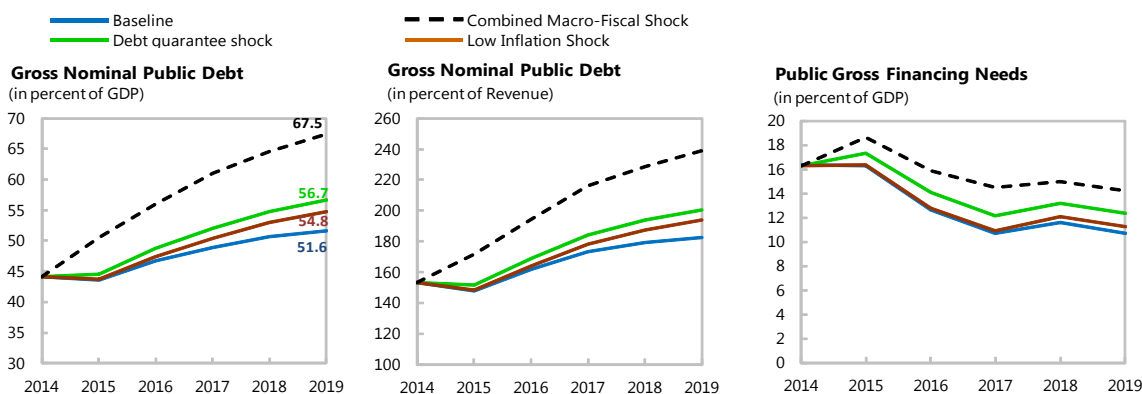
<sup>1/</sup> Public sector is defined as non-financial public sector.<sup>2/</sup> Based on available data.<sup>3/</sup> Bond Spread over German Bonds.<sup>4/</sup> Defined as interest payments divided by debt stock at the end of previous year.<sup>5/</sup> Derived as  $[(r - p(1+g) - g + ae(1+r))/(1+g+p+gp)]$  times previous period debt ratio, with  $r$  = interest rate;  $p$  = growth rate of GDP deflator;  $g$  = real GDP growth rate; $a$  = share of foreign-currency denominated debt; and  $e$  = nominal exchange rate depreciation (measured by increase in local currency value of U.S. dollar).<sup>6/</sup> The real interest rate contribution is derived from the denominator in footnote 4 as  $r - \pi(1+g)$  and the real growth contribution as  $-g$ .<sup>7/</sup> The exchange rate contribution is derived from the numerator in footnote 2/ as  $ae(1+r)$ .<sup>8/</sup> For projections, this line includes exchange rate changes during the projection period.<sup>9/</sup> Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

**FYR Macedonia Non-Financial Public Sector DSA - Stress Tests**

**Macro-Fiscal Stress Tests**



**Additional Stress Tests**



**Underlying Assumptions**  
(in percent)

	2014	2015	2016	2017	2018	2019		2014	2015	2016	2017	2018	2019
<b>Primary Balance Shock</b>							<b>Real GDP Growth Shock</b>						
Real GDP growth	3.5	3.8	3.9	4.0	4.0	4.0	Real GDP growth	3.5	2.3	2.4	2.5	2.5	2.5
Inflation	0.8	1.2	2.0	2.4	2.6	2.6	Inflation	0.8	0.8	1.6	2.0	2.2	2.2
Primary balance	-4.9	-5.3	-4.4	-4.2	-2.8	-2.8	Primary balance	-4.9	-4.7	-4.9	-2.8	-2.7	-2.5
Effective interest rate	2.5	2.9	3.5	3.6	3.5	3.4	Effective interest rate	2.5	2.9	3.5	3.6	3.5	3.4
<b>Real Interest Rate Shock</b>							<b>Real Exchange Rate Shock</b>						
Real GDP growth	3.5	3.8	3.9	4.0	4.0	4.0	Real GDP growth	3.5	3.8	3.9	4.0	4.0	4.0
Inflation	0.8	1.2	2.0	2.4	2.6	2.6	Inflation	0.8	4.5	2.0	2.4	2.6	2.6
Primary balance	-4.9	-4.1	-3.7	-2.8	-2.7	-2.5	Primary balance	-4.9	-4.1	-3.7	-2.8	-2.7	-2.5
Effective interest rate	2.5	2.9	4.0	4.4	4.6	4.7	Effective interest rate	2.5	3.2	3.4	3.5	3.4	3.3
<b>Combined Shock</b>							<b>Baseline Scenario</b>						
Real GDP growth	3.5	2.3	2.4	2.5	2.5	2.5	Real GDP growth	3.5	3.8	3.9	4.0	4.0	4.0
Inflation	0.8	0.8	1.6	2.0	2.2	2.2	Inflation	1.6	1.5	1.6	2.0	2.2	2.5
Primary balance	-4.9	-5.3	-4.9	-4.2	-2.8	-2.8	Primary Balance	-2.8	-2.2	-2.2	-2.2	-2.2	-2.2
Effective interest rate	2.5	3.2	3.9	4.4	4.5	4.7	Effective interest rate	2.5	2.7	2.9	3.0	3.6	2.9
<b>Debt guarantee shock</b>							<b>Low Inflation Shock</b>						
Real GDP growth	3.5	3.8	3.9	4.0	4.0	4.0	Real GDP growth	3.5	3.8	3.9	4.0	4.0	4.0
Inflation	0.8	1.2	2.0	2.4	2.6	2.6	Inflation	0.8	0.8	0.8	0.8	0.8	0.8
Primary balance	-4.9	-5.2	-4.7	-3.7	-3.5	-3.3	Primary balance	-4.9	-4.1	-3.7	-2.8	-2.7	-2.5
Effective interest rate	2.5	2.9	3.7	4.0	3.9	4.0	Effective interest rate	2.5	2.9	3.4	3.5	3.4	3.3

Source: IMF staff.



INTERNATIONAL MONETARY FUND



Press Release No. 15/16  
FOR IMMEDIATE RELEASE  
January 27, 2015

International Monetary Fund  
700 19<sup>th</sup> Street, NW  
Washington, D. C. 20431 USA

### **IMF Executive Board Concludes the Fourth Post-Program Monitoring Discussion with Former Yugoslav Republic of Macedonia**

On January 15, 2015, the Executive Board of the International Monetary Fund concluded the fourth Post-Program Monitoring (PPM)<sup>1</sup> with the Former Yugoslav Republic of Macedonia and considered and endorsed the staff appraisal without a meeting.<sup>2</sup>

Macedonia's economic growth is accelerating, driven by strong exports, public infrastructure projects and private consumption. At 3½ percent, growth is about 2 percentage points above the average for south-eastern Europe, and has allowed the unemployment rate to further recede to 27.9 percent. Monetary policy has been supportive, and private credit growth is returning to pre-crisis averages. The fiscal deficit target was adjusted from 3.5 to 3.8 percent of GDP as revenues came in lower than budgeted, which has resulted in a stronger-than-expected boost to the economy.

The short-term outlook appears broadly stable. The external position has been improved thanks to a €500 million Eurobond issuance in July that halted the decline in reserves and pre-financed the repayment of external debt maturing in 2015. The current account deficit, projected below 3 percent of GDP, would remain largely covered by foreign direct investment (FDI) inflows.

Public sector debt is expected to continue to rise to about 52 percent of GDP by 2019, driven by an increase in the debt of both the general government and non-financial state-owned enterprises (SOEs), projected respectively at 38.1 and 6 percent of GDP at end-2014.

Near-term risks primarily include a stalling recovery in the Euro area, which would weigh on external demand and potentially weaken—or postpone—FDI inflows. Energy supply disruptions

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<sup>1</sup> The central objective of PPM is to provide for closer monitoring of the policies of members that have substantial Fund credit outstanding following the expiration of their arrangements. Under PPM, members undertake more frequent formal consultation with the Fund than is the case under surveillance, with a particular focus on macroeconomic and structural policies that have a bearing on external viability.

<sup>2</sup> The Executive Board takes decisions under its lapse-of-time procedure when the Board agrees that a proposal can be considered without convening formal discussions.

resulting from the geopolitical conflicts would rapidly increase capacity constraints. Continued deflation—which has recently eased but averaged 0.3 percent year-on-year through December—could complicate fiscal adjustment. Regulatory spillovers from EU parent banks, particularly through differential treatment of home and host central bank and government securities for risk-weighted asset computation, may complicate the conduct of monetary policy.

### **Executive Board Assessment<sup>3</sup>**

In concluding the fourth Post-Program Monitoring with the Former Yugoslav Republic of Macedonia, Executive Directors endorsed the staff's appraisal as follows:

The improving economic outlook and employment situation are encouraging. The jobs and growth agenda should remain a top policy priority. Efforts should focus on alleviating key constraints for domestic firms, which generally operate under strong liquidity constraints, so as to ensure a handover to private sector-led growth. Key measures would include enforcing payment discipline in both public and private sector contracts, as well as upgrading the professional status of inspection bodies, clarifying their mandate, and streamlining their work.

The current public-sector led growth strategy will require careful expenditure prioritization if consolidation is to proceed as planned. In the absence of further tax policy changes to boost revenues, a comprehensive spending review that seeks to minimize the growth impact of current expenditure compression should be undertaken. Investment spending should target gaps in transport and energy infrastructure to maximize the payoff for medium-term growth. At the same time, with public debt rising steadily over the next years, the authorities should aim at frontloading fiscal consolidation. This will help secure compliance with the envisaged rules of a 3 percent of GDP deficit ceiling and a 60 percent of GDP debt threshold by 2017.

Renewed presence in international capital markets highlights the role of public debt management in supporting external sustainability. To further reduce risks, the debt management strategy should encompass the debt of SOEs as well as contingent liabilities, particularly in managing currency risk. Importantly, increased reliance on foreign currency borrowing has implications for external sustainability and the conduct of monetary policy through its impact on central bank reserve developments and domestic liquidity.

The monetary easing cycle has reached its end. The combination of relaxed financial conditions and tight prudential regulation has helped revive credit growth while preserving the health of the financial sector. The focus of monetary policy henceforth should be exclusively on maintaining the attractiveness of holding denar-denominated assets in support of the exchange rate peg. High banking sector liquidity and falling currency spreads argue against further easing.

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<sup>3</sup> At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities. An explanation of any qualifiers used in summings up can be found here: <http://www.imf.org/external/np/sec/misc/qualifiers.htm>.

IMF credit outstanding to Macedonia has fallen below the relevant threshold of 200 percent of quota at end-2014 and current risks to external sustainability or capacity to repay do not warrant an extension of the PPM, which will be discontinued.

## FYR Macedonia: Selected Economic Indicators, 2009–14

	2009	2010	2011	2012	2013	2014
	Annual percentage change, unless otherwise specified					
Real GDP	-0.4	3.4	2.3	-0.5	2.7	3.5
Real domestic demand	-2.2	1.0	0.4	3.5	2.6	3.7
Consumption	-3.3	3.8	-5.4	1.2	2.1	3.5
Gross investment	-0.6	-3.8	17.9	10.2	16.6	5.4
Net exports 1/	2.0	1.9	1.7	-3.5	0.8	-0.5
CPI inflation (annual average)	-0.6	1.7	3.9	3.3	2.8	-0.2
Unemployment rate (annual average)	32.2	32.1	31.4	31.0	29.0	27
	In percent of GDP					
Current account balance	-6.8	-2.0	-2.5	-3.0	-1.8	-2.9
Goods and services balance	-22.8	-19.8	-20.6	-22.5	-18.6	-19.1
Exports of goods and services	31.8	38.6	45.7	44.5	43.5	46.8
Imports of goods and services	54.6	58.5	66.3	67.0	62.0	65.9
Private transfers	16.2	18.8	18.8	20.7	18.5	17.7
External debt (percent of GDP)	55.9	57.8	64.2	68.2	64.3	64.4
Gross investment	25.7	24.5	26.9	28.9	28.5	29.1
Domestic saving	19.0	22.4	24.4	26.0	26.7	26.9
Public	0.6	1.1	1.3	0.2	-0.5	-0.3
Private	18.4	21.4	23.1	25.7	27.2	27.1
Foreign saving	6.8	2.0	2.5	3.0	1.8	2.9
Central government gross debt	23.7	24.3	27.7	33.7	34.1	38.1
Public sector gross debt 2/	26.7	27.8	31.8	38.5	40.6	46.6
Central government balance	-2.6	-2.4	-2.5	-3.8	-3.9	-3.8
Memorandum items:						
Nominal GDP (billions of denars)	415	437	464	467	499.6	521.2
Nominal GDP (billions of euros)	6.8	7.1	7.5	7.6	8.1	8.5
GDP per capita (EUR)	3296	3455	3664	3679	3931	...

Sources: NBRM; SSO; MOF; IMF staff estimates.

1/ Contribution to growth.

2/ Total Public Sector (including MBDP, municipalities, public sector non-financial enterprises; w/o NBRM).