

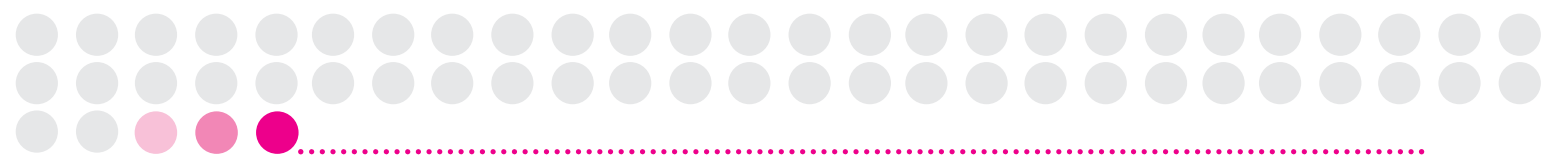


Republic of Macedonia  
MINISTRY OF FINANCE

Macroeconomic Policy Department

**2006**  
**ANNUAL ECONOMIC REPORT**  
**OF THE REPUBLIC OF MACEDONIA**

Skopje, May 2007



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## PREDGOVOR

Government of the Republic of Macedonia, which took its term of office after the parliamentary elections in July 2006, focuses on the realisation of two strategic goals within the adopted economic program: maintenance of macroeconomic stability, in terms of low inflation and stable Denar exchange rate, and stimulation of sustainable economic growth and accelerated structural reforms in order to ensure higher living standard of Macedonian citizens.

To that end, a sound basis for strengthening economic growth in the Republic of Macedonia were set in 2006, especially in the second half of the year, reflected in a growth of the industrial production, fiscal discipline, low inflation rate, balanced external accounts, downward trend of interest rates, etc. The closer relations with the European Union also gave strong impetus to the institutional capacity strengthening, acceleration of the reforms and achievement of more dynamic economic growth.

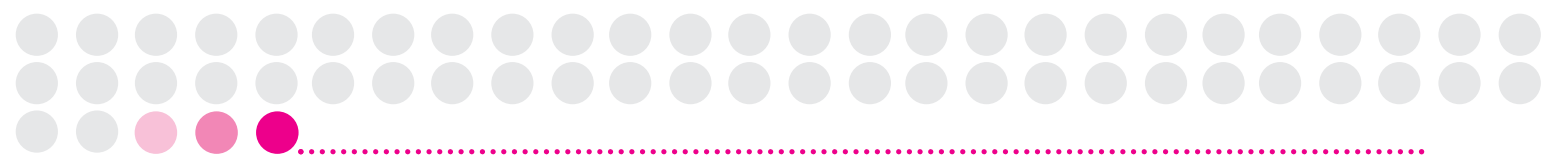
According to the 2006 data based on the quarterly surveys, gross domestic product grew by 3.1%. However, some indirect indicators of economic activity show that real GDP growth is higher. This conclusion is also contained in the Letter of Intent signed between the Government of the Republic of Macedonia and the IMF, one of the documents presented when adopting the Second Review under the Stand-By Arrangement in front of the IMF Board of Executive Directors on April 27, 2007. Thereby, GDP growth was achieved in conditions of low and one-digit inflation (3.2%), disciplined fiscal policy with central budget deficit of 0.5% of GDP, reduced general government debt by 6.6 percentage points in relation to the previous year, unemployment reduction by two percentage points, as well as a strong increase of crediting to the private sector by 27%. Such positive macroeconomic climate is a good basis for realisation of the ambitious economic program of the Government of the Republic of Macedonia in the forthcoming period.

Growth of the economic activity in 2006 also led to an increase in the volume of the commodities trade, whereby in the analysed period, the export of goods increased by 17.6%, with a simultaneous increase of the import by around 16.5%. Such developments led to an increase of the trade deficit with abroad by around 15% compared to the one realised last year (2005), which was mainly due to the high increase of oil prices on the world stock market. Oil participated with approximately 51% in the increase of the trade deficit.

Greater import activity and the high inflow of private transfers in the previous period led to a reduced current account deficit (0.6% of GDP) and pressures for appreciation of the Denar exchange rate on the foreign exchange market. During the analysed period, stability of the nominal Denar exchange rate in relation to the euro was maintained by a net purchase of foreign currencies on the foreign exchange market, through foreign currency transactions of the NBRM.

Positive trends in the external sector influenced the level of the foreign exchange reserves, as well. At the end of 2006, foreign currency reserves amounted to EUR 1.4 billion, which compared to the same period in 2005 grew by 25%. Such level of foreign currency reserves provided for 5.5-month import coverage, encouraging the Ministry of Finance to undertake activities to minimize the costs related to government debt servicing and the issued sovereign guarantees, as well as to reduce the risks related to the public debt structure.

With regard to the performance of the banking system, total deposit potential of the banks grew by 26% in 2006, contributing to exceeding the projected level of  $\square$ 4 money supply. Higher deposit potential of the banks, coupled by the proactive credit policy in utilization of the foreign currencies, led to an annual growth rate of credits to the private sector of



27% in 2006. Moreover, it is important that the credit growth was particularly high for the long-term credits to the enterprises since such credits are aimed at investment activity.

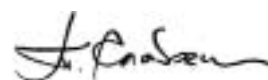
Real sector performance and economic activity intensification had an adequate positive influence on the social sector, i.e. on the employment. In 2006, employment increased by 4.6% relative to 2005. According to the data from the Employment Agency, 150,815 new employment contracts were registered in the Agency during 2006, that is by 2% higher compared to last year. Unemployment rate amounted to 35.9% at the end of 2006, being an annual decline of two percentage points.

Regarding the accession of the Republic of Macedonia to EU, it is important to point out that at the end of 2006, the Ministry of Finance prepared the first Pre-Accession Economic Program for the period 2007-2009, assessed by the EU as a quality comprehensive document on the economic policy of the Republic of Macedonia, reflecting a sound and coherent mid-term macroeconomic framework. It was a confirmation for the credibility of the Macedonian macroeconomic policy, as well as for the fiscal policy and the strengthened fiscal discipline.

We are sure that the fulfilment of the ambitious economic program of the Government of the Republic of Macedonia, mainly in the field of structural microeconomic reforms, will significantly contribute to the acceleration of the economic growth. Sustainable growth is the basis for the higher living standard of the citizens. Economic progress of a country is achieved when many people at many places perform useful activities. Diligent professionals from the Ministry of Finance and all other state and public institutions are part of the mechanism that guides the Macedonian economy to the right direction.

Enjoy reading the 2006 Annual Report on the Republic of Macedonia.

*Sincerely yours,  
Trajko Slaveski Ph.D.*



## 1. WORLD ECONOMIC TRENDS

### 1.1. World Economy in 2006

Consequences of the natural disasters and political instability in the world in recent years had economic implications in 2006 as well. In particular, world prices of crude oil continued to rise this year, whereby the annual average reached the amount of US \$ 65.4 per barrel, that is a 20.14% annual increase. Highest prices were recorded in July when monthly average reached the record level of US\$ 73.9 per barrel (see Chart 1.1). However, this price jump did not fuel inflation in developed countries which remained unchanged compared to the previous year (2.3%) despite the increase in the prices of primary products by 28.4%, whereas there was a higher increase in consumer prices in the rest of the world. For example, in Africa prices grew by 9.5%, in the Middle East by 7.9%, in the Western Hemisphere<sup>1</sup> by 5.4%, etc.

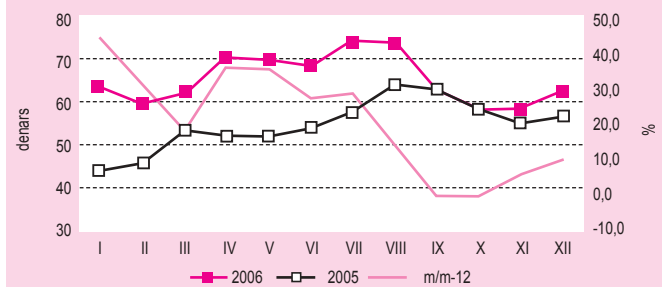
In general, the world economic activity in 2006 strengthened as measured by the world output that increased by 5.4% in real terms compared to the last year. China had the highest contribution to world growth of 1.65 percentage points, accounting for 30.6% of the growth. The share of developed countries in the growth was almost the same as previous year (30.1%), and the USA participated with 12.3%. Consequently, the world output structure by countries did not change by much. In particular, the USA had the biggest share of 19.7% in the total world GDP, followed by China with 15.1% and the Euro zone with 14.7% (see Chart 1.2).

In 2006, volume of the world trade grew by 9.2% in real terms on annual basis, whereas the commodities trade grew by 9.5%, a 2.1 - percentage points higher growth compared to the one in 2005. The Euro zone had the biggest share of 29% in the total world export of goods and services, whereas, inside the Euro zone, Germany was the biggest exporter with a share of 31% in total exports.

### 1.2. Developed countries

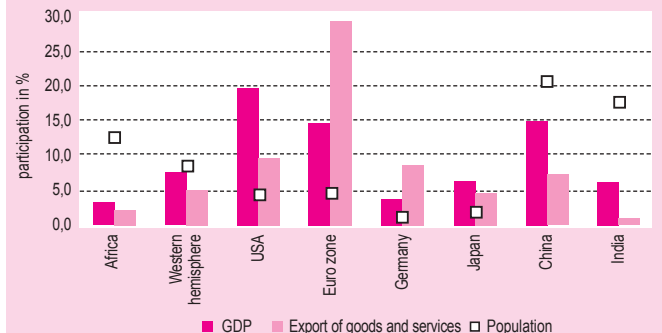
After the relative slowdown of GDP growth in developed countries in 2005, growth in 2006 exceeded 3%. As in

Chart 1.1. Trend of crude oil world price in 2005 and 2006



Source: The World Bank

Chart 1.2. Share of world regions and bigger countries in total population, GDP and export of goods and services



Izvor: IMF World Economic Outlook, April 2007

1) It includes South and Central America and Mexico.

previous years, growth in 2006 was initiated by the gross domestic investments, which grew by 4.1%. In addition, public consumption in 2006 increased compared to the last year.

USA was the main growth driver (41% share in the GDP growth of developed countries), which began the year furiously and reached real economic growth of 5.6% in the first quarter, followed by slowdown of the economy, so that the average annual growth reached the level of 3.3%. Private consumption contributed the most to the growth with 2.24 percentage points, of which 56% are service costs. The negative balance of net import grew by 6.8%. In addition, BOP current account deficit deepened and amounted to 6.5% of GDP. Trade deficit with the Euro zone declined by 0.22%, though with an insignificant change of the inter-currency value of dollar in relation to the euro. Dollar stability was also supported by the FED measures for stable domestic currency.

In the Euro zone, driving force of the economic growth were gross domestic investments, which grew by 4.5%, compared to their growth of 2.5% in 2005. Public consumption grew by 2.1%, contributing to doubling the growth, which "stabilised" at 2.6%. We should emphasize that, despite the greater budget spending, the average fiscal deficit of Euro zone declined to 1.6% of GDP. Progress was also achieved in the social sphere where the unemployment rate declined to 7.9%, a 0.7-percentage points drop from 2005.

Lowest inflation rate in 2006 was recorded in Japan, where the consumer prices grew by only 0.2%. The unemployment rate in Japan, which had a downward tendency, amounted to 4.1% in 2006, being among the lower rates in the developed economies. Still, Japan, along with Italy, had the highest budget deficit of 4.3% of GDP.

The Euro zone recorded an economic growth of 2.6% in 2006. Highest growth rates were recorded in Luxembourg, where the real GDP increased by 6.2%, in Ireland by 6% and 5.5% in Finland. However, Germany with a growth rate of

**Table 1.1.** Selected economic indicators for several countries

	Real GDP growth			Inflation (CPI)			Unemployment rate		
	2004	2005	2006	2004	2005	2006	2004	2005	2006
Developed countries*	3.3	2.5	3.1	2.0	2.3	2.3	6.3	6.0	5.5
Euro zone	2.0	1.4	2.6	2.1	2.2	2.2	8.8	8.6	7.9
- Germany	1.2	0.9	2.7	1.8	1.9	1.8	9.5	9.5	8.4
- Greece	4.7	3.7	4.2	3.0	3.5	3.3	10.5	9.8	8.9
- Italy	1.2	0.1	1.9	2.3	2.2	2.2	8.0	7.7	6.8
- The Netherlands	2.0	1.5	2.9	1.4	1.5	1.7	4.6	4.7	3.9
Great Britain	3.3	1.9	2.8	1.3	2.1	2.3	4.7	4.8	5.3
USA	3.9	3.2	3.3	2.7	3.4	3.2	5.5	5.1	4.6
Japan	2.7	1.9	2.2	0.0	-0.3	0.2	4.7	4.4	4.1

Source: Eurostat

\* IMF World Economic Outlook, April 2007

2.7% in 2006 (three times the growth rate in 2005) was the main driver of the growth, participating with 29% in overall Euro zone growth. Improved external demand had a largest contribution to the GDP growth in Germany, or 1.1 percentage points out of the total growth rate. The lowest inflation rate in the Euro zone was recorded in Finland, where the consumer prices grew by 1.3%, while the highest inflation was registered in Spain (3.6%), which, along with Greece (3.3%), exceeded the limit set by the Maastricht criteria for this indicator (3.1% in 2006, i.e. 1.5 percentage point above the average of the three countries with the lowest inflation rate). Lowest unemployment rates (below 4%) were registered in the Netherlands and Norway, followed by Luxembourg (4.7%) and Ireland (4.4%).



Concerning the main Macedonian trade partners, Greece showed highest GDP growth (4.2%), and Germany had very strong growth relative to previous years. The growth in these countries is particularly important because it contributes to the external demand for Macedonian products, i.e. potentially increases Macedonian exports.

### 1.3. Central and Eastern Europe

Table 1.2 shows specific macroeconomic indicators for Central and Eastern European (CEE) countries. It shows that the GDP growth remained stable in the CEE countries, with a moderate inflation rate and slightly improved fiscal discipline.<sup>2</sup> However, the position in the economic relations with the rest of the world worsened, in particular the BOP current account deficit grew by 41% and reached 6.7% of GDP. Increased trade deficit and reduced positive balance in the trade of services led to increase of the net import by 44% compared to 2005.

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

	Real GDP growth			Inflation (CPI)			BOP Current account (% of GDP)*		
	2004	2005	2006	2004	2005	2006	2004	2005	2006
Central and Eastern Europe*	6.6	5.5	6.0	6.1	4.8	5.0	-5.8	-5.3	-6.7
EU - 10	5.3	5.9	6.7	3.9	3.1	3.4	-7.1	-6.8	-8.8
Slovenia	4.4	4.0	5.2	3.7	2.5	2.5	-2.7	-2.0	-2.3
Poland	5.3	3.5	5.8	3.6	2.2	1.3	-4.2	-1.7	-2.1
Estonia	8.1	10.5	11.4	3.0	4.1	4.4	-12.5	-10.5	-13.8
Latvia	8.7	10.6	11.9	6.2	6.9	6.6	-12.9	-12.7	-21.3
Bulgaria	5.6	5.5	6.1	6.1	6.0	7.4	-5.8	-11.3	-15.9
Romania	8.5	4.1	7.7	11.9	9.1	6.6	-8.4	-8.7	-10.3
Turkey	9.0	7.4	6.1	8.6	8.2	9.6	-5.2	-6.3	-7.9
Western Balkans**	5.8	5.1	5.1	3.0	5.4	5.5	-9.6	-8.8	-7.4
Albania	6.7	5.5	5.0	2.9	2.4	2.4	-3.9	-6.5	-5.9
Bosnia and Herzegovina	6.0	5.5	6.0	0.5	4.3	6.0	-19.3	-21.3	-11.4
Serbia	8.4	6.2	5.7	10.1	16.5	12.7	-11.7	-8.4	-11.5
Croatia	3.8	4.3	4.8	2.0	3.3	3.2	-5.2	-6.5	-7.6
Macedonia	4.1	3.8	4.0	-0.4	0.5	3.2	-7.7	-1.3	-0.4

Source: Eurostat

\*IMF World Economic Outlook, April 2007

\*\*Average of the countries indicated below (Source: European commission)

New EU member states (including Bulgaria and Romania) recorded a significant economic growth of 6.7%. Driving force for the growth were the Baltic countries (Latvia and Estonia), which together recorded an average GDP growth of 11.6% (see Chart 1.3). These two countries recorded a strong growth of above 10% for two subsequent years, while the ten-year average real growth amounted to 7.9% in Estonia and 7.6% in Latvia. However, the current account deficit in Latvia drastically increased reaching 21.35% of GDP at the end of 2006, which is almost three-times higher than the EU-10 average. In addition, inflation rate in Latvia remained relatively high (6.6%), whereas the lowest inflation of 1.3% was

2) Budget deficit was reduced by almost one percentage point, and it amounted to 2.7% of GDP.

registered in Poland. Within the EU-10 countries, Poland had the highest unemployment rate of 13.8%, although it decreased by 4 percentage points compared to 2005, while lowest unemployment rate of 4.7% was registered in Cyprus.

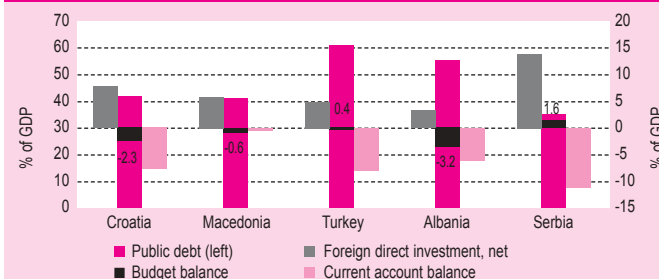
**Chart 1.3.** Basic indicators for EU-10, Bulgaria and Romania



Source: Eurostat

Average economic growth in the Western Balkans was by almost one percentage point lower than in the CEE countries. Bosnia and Herzegovina and Serbia had the highest growth rates of 6% and 5.7%, respectively. However, these countries had the biggest current account deficit (exceeding 11% of GDP), which was lowest in Macedonia, 0.4% of GDP. Though, in Bosnia and Herzegovina, the deficit significantly declined by 10 percentage points compared to the last year, mainly due to the reduced trade deficit.<sup>3</sup> Serbia experienced significant growth of net foreign direct investments, which amounted to 13.8% of GDP in 2006, which financed the increased current account deficit.

**Chart 1.4.** Selected economic indicators for the candidate - countries (potential) for EU



Source: European Commission

Inflation rate in Serbia remained at the two-digit level (12.7%), being one of the highest in Europe, while the lowest inflation of 2.4% was registered in Albania. However, contrary to the "strong" monetary policy, a relatively liberal fiscal policy was conducted in Albania. In particular, though the budget deficit was permanently decreasing, as well as the public debt, these categories were on higher level among the countries of the Western Balkans in 2006 (see Chart 1.4).

3) Percentage annual increase of the export of goods was 29%, and 0% for the imports.

4) Procentualnata godišna promena na izvozot na stoki e 29%, a na uvozot e 0%



## 2. MACROECONOMIC TRENDS IN THE REPUBLIC OF MACEDONIA IN 2006

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Macroeconomic performance in recent past, reflected in a fiscal discipline, low inflation rate, balanced external accounts, downward trend of the interest rates, growth of the industrial production is a sound basis for better economic growth in the next period. In addition, closer relations with the European Union are a strong impulse for the institutional capacity strengthening, acceleration of reforms and achievement of a more dynamic economic growth.

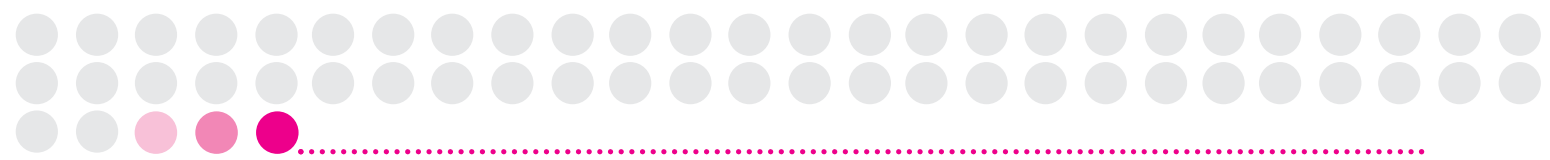
According to the 2006 data based on quarterly surveys, gross domestic product in Macedonia grew by 3.1%, a 0.9 percentage points lower than the projected growth. However, the projection for 2006 remained at 4%, taking into consideration that annual GDP data is calculated on the basis of financial statements of enterprises, and hence is a more precise method of calculation, unlike the quarterly data that are calculated from surveys.

Maintenance of the macroeconomic stability, improvement of the business environment and restart of part of the production capacities in 2006 contributed to the economic growth, which was most pronounced in services (trade, traffic and communications). However, the performance in the real sector as a whole was somewhat lower than the projected one, due to the low growth of industry and the negative growth in the construction sector. In particular, the industrial production grew by 3.7% in 2006, while the projected annual growth amounted to 4.1%. Unfavourable results were also registered in the construction sector, mainly due to the delay of the construction of several important infrastructure projects, as well as in the agricultural sector.

Economic growth in 2006 was accompanied by positive trends in the fiscal sphere. General government budget deficit amounted to 0.5% in 2006, a significant success in an election year when public expenditures are usually high. Such fiscal policy was a strong support to the monetary policy, to the end of stable foreign exchange rate and further decrease of interest rates, both the reference rate (the interest rate of the Central Bank bills) and active interest rates of commercial banks. At the same time, indebtedness of the Republic of Macedonia decreased significantly in 2006, whereby the debt of the general government budget amounted to 33.6% at the end of the year, a 6.2 percentage points decline from the end 2005.

Greater economic activity led to an increase in the volume of commodities trade in 2006, with a growth of the export of goods of 17.6%, and an increase of imports by around 16.5%. Hence the trade deficit increased by 1.1 percentage points compared to 2005, reaching 20.2% of GDP, mainly as a result of the significant rise of the oil price on the world stock markets, i.e. the share of oil in the increase of the trade deficit was 51%. Significant inflow on the basis of private transfers in 2006 contributed to a decline of the current account deficit to US\$ 24 million, which is a decrease by US\$ 55 million compared to the last year.

Increased import activity and high inflow of private transfers contributed to a decline in the BOP current account deficit and put upward pressure on the value of the Denar on the foreign exchange market. To the end of maintaining the nominal Denar exchange rate stability relative to euro, NBRM conducted a net purchase of foreign currencies on the foreign exchange market.



These positive trends in the external sector had a positive reflection on the level of the foreign exchange reserves. In particular, at the end of 2006, foreign currency reserves amounted to EUR 1.4 billion, a 25% increase compared to the end 2005, and equalled to 5.5-month import coverage.

Actual average inflation in 2006 deviated from initial projections, where, according to the projections, average rate of 1.8% was expected for 2006. The high price rise of oil and oil derivatives on the world stock market, the rise of prices of tobacco and tobacco products (due to the excise changes), as well as the significantly higher rise of prices of food than the projected, caused for the inflation rate, measured through the costs of living, to reach 3.2% in 2006.

With regard to the operational position of the monetary policy, in 2006, NBRM continued implementing a fixed exchange rate policy, with minor fluctuations of Denar relative to the euro. The auctions of Central Bank bills, as well as the treasury bills issued for monetary purposes, were basic monetary policy instrument, whereby in 2006, the principle "interest rate tender" was used, which assumed market establishment of interest rates of Central Bank bills through auctions by the banks. A relatively high level of liquidity and higher average demand than offer of Central Bank bills led to a reduction of interest rates on Central Bank bills, the average weighted interest rate on Central Bank bills amounted 5.5% at the end 2006, as opposed to 8.5% at the end 2005.

The trend of the real effective exchange rate (REER) is an important indicator of the domestic economy competitiveness. In the period 2001-2006, Denar REER was relatively stable, indicating maintenance of competitiveness of exporters on foreign markets, mainly as a result of the lower prices in the domestic economy relative to the main trade partners. Thereby, REER in 2006 remained almost unchanged compared to 2005. Though, competitiveness relative to the countries that are major trade partners from the Euro zone (the calculation includes 8 countries), somewhat declined in 2006, in particular higher prices in the Macedonian economy compared to the Euro zone led to a moderate appreciation of the real effective exchange rate of around 1%.

Regarding the performance of the banking system, total deposit potential of banks grew by 26% in 2006, so that the projected level of  $\square 4$  money supply was outperformed. Higher banks' deposit potential, coupled with a pro-active credit policy in utilisation of foreign assets, led to a relatively high annual growth of credits to the private sector of 27%. Moreover, there was improvement in the term structure of credits, in that long-term credits to enterprises, which are credits used for economic activity, increased faster than the short-term credits.

The real sector performance and intensified economic activity were also reflected in the social sector, i.e. employment. In 2006, total employment (according to the Labour Force Survey) grew by 4.6% compared to 2005. This growth was confirmed by the Employment Agency data, according to which 150,815 persons signed employment contracts in 2006, a 2% increase compared to last year. According to the LFS data, unemployment rate at end 2006 amounted 35.9%, a 2 - percentage points decline compared to the end of 2005.

### 3. REAL SECTOR

#### 3.1. Gross domestic product

Gross domestic product is a main measure of the economic activity in a country, measuring the value of the total produced final goods and services for a period of one year. In 2006, gross domestic product in the Republic of Macedonia grew by 3.1%, a 0.9 percentage points lower growth than the projected one. However, the 2006 projection remained at 4%, since annual data on GDP are calculated on the basis of financial statements of enterprises and hence is a more precise method of calculation, unlike the quarterly data that are survey-based.

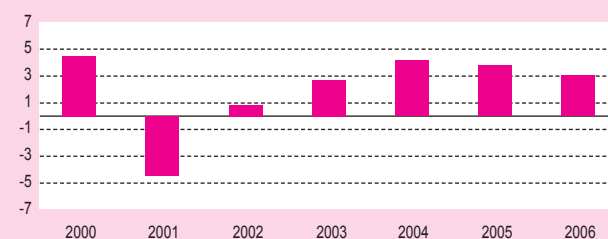
A production approach analysis of GDP in 2006 shows that positive growth rates were recorded in all sectors, except in the Construction sector (decline by 0.4%), as well as in the Hotels and restaurants (zero growth rate). Indeed, the real sector performance as a whole was somewhat lower than the projected, due to the lower growth of the industry and of the services.

Industrial production in 2006 grew by moderate 3.6%. Taking into account that the Industry has highest share in the value added (23.6%), its growth has greatest effect on the overall growth. Regarding services, value added in the Trade showed real growth of 5.5%, while in 2006, Traffic and communications showed a highest growth rate of 7.5%. Low positive growth rate was recorded in the Financial intermediation and Public administration sectors.

Regarding the quarterly dynamics, positive real growth rates were recorded in all quarters. More intensive growth of 3.4 % and 4% was recorded in the second and third quarter, respectively. In the fourth quarter, intensity of GDP growth declined to 2.6%.

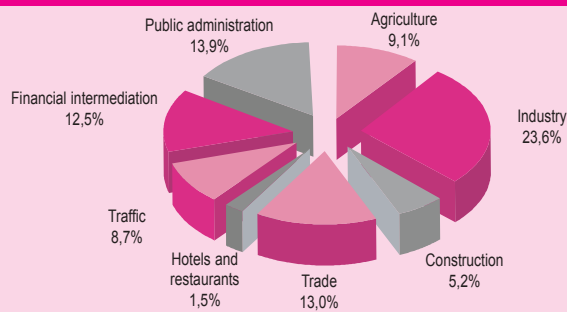
Given the lack of comprehensive and timely data on domestic consumption in the Republic of Macedonia, analysis of the expenditure side of the gross domestic product is based on an expert-opinion taking into account domestic consumption trends, as well as leading indicators. This analysis shows higher GDP growth in 2006 than the one measured by the production side. In particular, registered increase in public expenditures in the first three quarters of 2006, as well as the

Chart 3.1. GDP growth rate



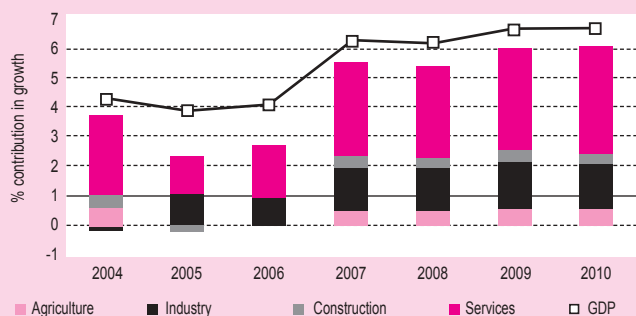
Source: State Statistical Office

Chart 3.2. GDP by sectors



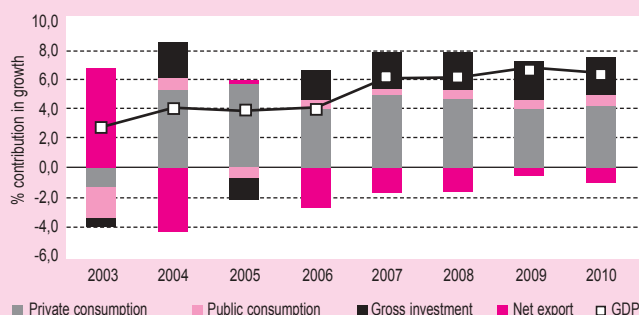
Source: State Statistical Office

**Chart 3.3. GDP - production approach**



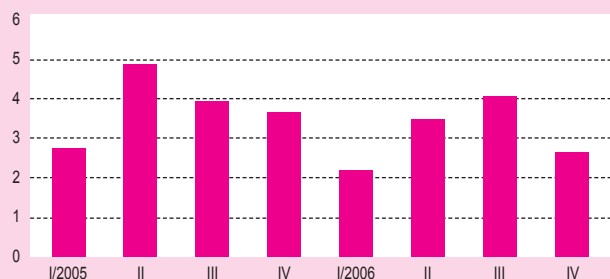
Source: State Statistical Office

**Chart 3.4. GDP - expenditure approach**



Source: State Statistical Office

**Chart 3.5. Gross domestic product (quarterly real growth rate)**



Source: State Statistical Office

presumed increase in personal consumption on the basis of the real wage growth, increase in credits to households, recorded retail trade, higher private transfers and higher import of consumption goods, indicate an increase in the final consumption by 4.5-5% and positive effect on the GDP growth by around 5%. At the same time, significant growth of investments in machines and equipment of 20.2% in 2006 should lead to a high positive impact of gross investments on GDP growth. Risk to this assumption is a lack of preliminary data on investments in construction, though if we take into consideration the very low growth of Construction sector in 2006, it is likely that the growth of construction investments was relatively low. On the basis of the preliminary data, import and export growth rates showed negative contribution of the net export to GDP growth of around 2-2.5%.

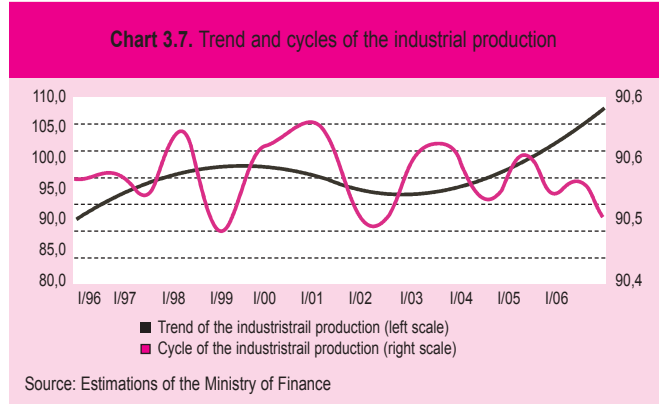
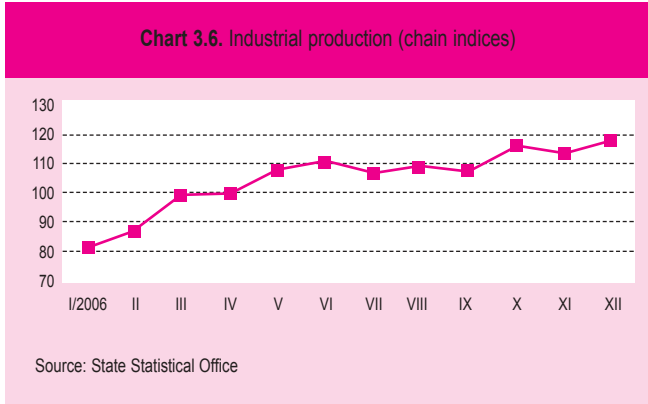
### 3.2. Industrial production

Given the high share in value added, increased industrial production was the main driver of the Macedonian economy in 2006. In particular, the volume of industrial production grew by 3.6% in 2006 compared to last year, which is still lower than the projected one.

The annual industrial production growth was achieved through the intensified activity in 15 out of the total of 24 industrial branches. Within the activities with biggest share in the total industrial index, high growth rates were achieved in the basic metals. In particular, the main driver of the growth were ore and metal extraction, which grew by 47%, as well as extraction of other ores and stone with a 21.9% growth. In addition to these branches, positive results were registered in the tobacco industry, textile industry, oil industry, production of construction materials, production of basic metal products and recycling.

During the 2006, industrial production showed usual monthly changes, though with certain deviations in the intensity of changes. In particular, high monthly growth of the industrial production was registered in March, May and October,

whereas the biggest decline was recorded in January and July. High monthly growth in March (13.2%) was due to the fact that it had more working days compared to the previous month, as well as due to activities regarding the tobacco buyout and processing. On the other hand, the biggest decline of the industrial production in January (31.7%) can be contributed to the seasonal factors.



### Box 3.1. The trend and cycles of industrial production

The time series that we analyse, such as the industrial production, export or import, employment or unemployment, often include components that are trend, seasonal variability or cycle.

A trend in the business, finances or economy appears as a result of technological advances and growth, changes in institutions and tastes. The most often elaborated models are the ones with deterministic trend, which evolves in a perfectly predictive way. Models with deterministic trend are very useful in practice, where the simple linear function of time is as follows:

$$T = B_0 + B_1 \text{Time}_t + e_t$$

Seasonal component of time series is the one that reiterates regularly, and can be deterministic (when it is in precise determined interval) or stochastic. Seasonal component arises from the advance in the technology, institutions, tastes and the growth of technology, connected with the calendar. The simplest example is the weather in the Republic of Macedonia, which is always warmer in summer than in winter. Basic way of modelling the seasonal component is regression of seasonal dummy variables (where the dummy variable  $D$  takes certain value in the analysed season):

$$Y_t = \sum Y_i D_{it} + e_t$$

The dynamics in the time series, which is not included in the trend or the seasonal component in the business, finances and economy is covered by a cycle. The cycle is relatively more complicated statistical phenomenon, which helps explaining why the economy in a country shows ups and downs over time despite the significant unchanged environment.

### 3.3. Total factor productivity

Analysis of the economic growth in a country is increasingly important for the creation and implementation of the economic policies. In particular, economic policymakers have to be aware what drives the economic growth, observed by sectors or production factors in order to focus future efforts on improving the economic growth. Theory of economic growth ascribes growth to three sets of factors:

- growth of capital in the economy (i.e. accumulated capital in the economy plus gross investments in the current year, minus asset-weighted depreciation);
- labour force growth (the number of employees in the economy); and
- total factor productivity growth (TFP), the level of efficiency at which production factors are used - capital and labour.

#### Box 3.2. Calculation of total factor productivity

*Estimation of total factor productivity (TFP) is based on the neoclassical production function, according to which:*

$$Y = A \cdot f(K, L)$$

*Where, Y is real GDP, K is capital, and L is labour force.  $A$  is called TFP and is a residual value, i.e. the total efficiency with which K and L are being used. The economist Robert Solow introduced this residual in the 50's and it is often called Solow residual.*

*The specification of the production function used for total factorial productivity estimation is the Cobb-Douglas function:*

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

*where  $\alpha$  is the share of the income coming from the capital and can have a value between 0 and 1. When differentiating both sides, the following is obtained:*

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

*where d stands for the growth rates of the included variables. If the TFP term is derived, the following is obtained:*

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

*By plugging the data for the included variables in the right-hand side and by estimating  $\alpha$  on the basis of income data for the production factors, results for the total factor productivity are obtained.*

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

Following assumptions are used in estimation of the total factor productivity for the Republic of Macedonia: the capital stock depreciated with assumed weighted depreciation rate of 10% and labour is approximated by the number of employees. During the estimation, alpha ( $\alpha$ ) is assumed to be 0.4, representing the share of the income coming from the capital, and the remaining share from the labour. Total factor productivity for the Republic of Macedonia in the period 1997-2006 is presented in Chart 3.8.



Chart 3.8 shows that total factor productivity was negative in 2006, and it amounted to -1.25%. Consequently, the share of total factor productivity in total economic growth was also negative and amounted -40%. It suggests inefficient utilisation of both labour and fixed assets in 2006. However, this number should be observed with caution due to the possible capital stock underestimation in the Republic of Macedonia, as well as due to the significant share of employment in the informal sector, which are excluded from TFP calculation.

When analysing the period from 1997 to 2006 cumulatively, the contribution and the share of the production factors and of the TFP in the growth are as follows (Table 3.1.):

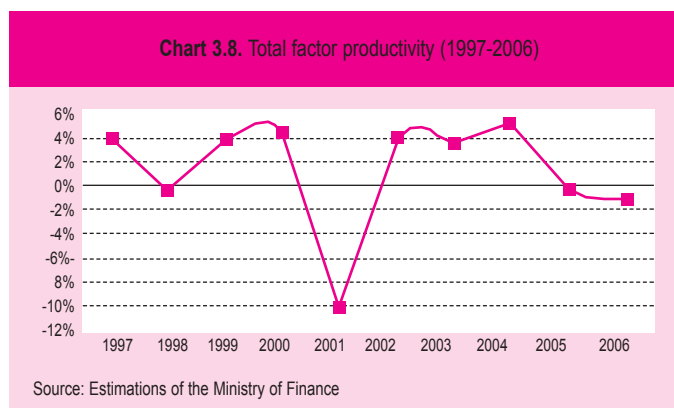
It could be inferred from the table that, on a longer run (10-year average), the contribution of the TFP in the growth was about 45%, which is a significant indicator of the efficient utilisation of labour and capital. The share of capital is also significant, being a good approximation of the share of physical capital in the GDP growth in the developed and developing countries. For comparison purposes, the following table shows the average for three groups of countries:

### 3.4. Sectoral labour productivity

Efficiency of labour force in the production is measured through labour productivity, defined as output per unit time. In practice, productivity is calculated as ratio between GDP and the number of employees, or as a ratio between GDP and total annual number of working hours. Due to data constraints, the former method was used in this analysis.

Observed by sectors, productivity growth was achieved in agriculture, industry, trade and transport and communications in 2006 compared to 2005.

Productivity growth was achieved in the industrial sector, as a result of the GDP growth, only partially



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

GDP growth	Capital	Labour	TFP
2,4%	0,9%	0,4%	1,1%
	(37,7%)	(17,8%)	(44,5%)

Source: Ministry of Finance calculations

**Table 3.2. Contribution and share of factors and factor productivity in the growth in three group of countries**

	GDP growth	Capital	Labour	TFP
Developed countries (1960-1990)	3,9%	2,1%	0,5%	1,3%
		(54%)	(13%)	(33%)
Latin-American countries (1940-1980)	4,9%	2,4%	1,3%	1,2%
		(48%)	(28%)	(24%)
Countries of Eastern Asia (1966-1990)	8,8%	4,4%	3,2%	1,2%
		(50%)	(36%)	(14%)

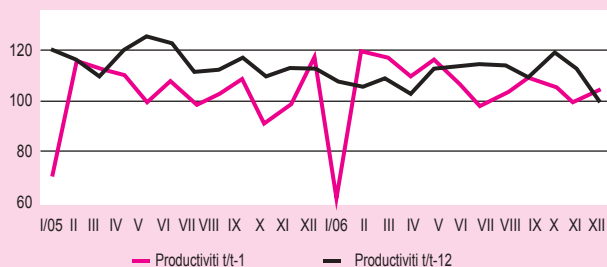
Source: Barro and Sala-I-Martin, Table 10.8., p. 380-381

**Table 3.3. Productivity by sectors**

	2005	2006
Agriculture, hunting and forestry	82.8	94.6
Industry	100.2	102.6
Civil engineering	98.9	83.5
Trade	101.4	108.3
Hotels and restaurants	93.0	72.8
Transport and communications	100.3	116.0
Financial intermediation	99.5	96.3
Public administration	106.8	96.6

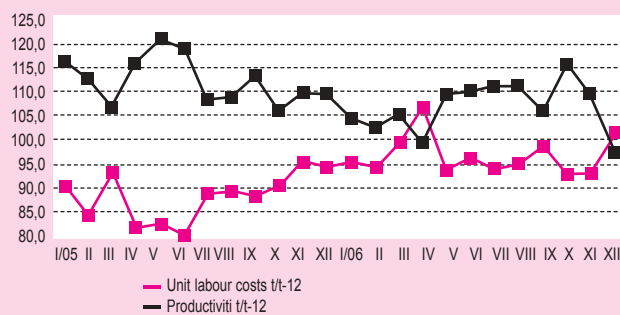
Source: Ministry of Finance

**Chart 3.9. Industrial productivity**



Source: Estimations of the Ministry of Finance

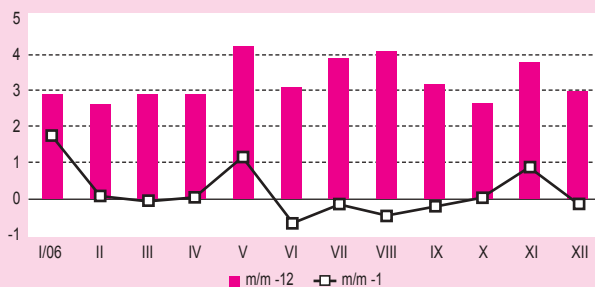
**Chart 3.10. Productivity and unit labour costs**



Source: Ministry of Finance

In 2006, the trend of CPI index was different for specific consumption groups. Prices increased in the following groups: tobacco and beverages (17.8%), culture and entertainment (6.4%), food (2.2%), housing and hygiene and health (2.0%), transport vehicles and services (1.8%) and clothing and footwear (0.2%).

**Chart 3.11. Consumer price index**



Source: State Statistical Office

followed by the increase in the number of employees. Manufacturing showed high level of productivity growth (4.8%), though lower compared to the last year. Analysis of productivity trend and unit labour costs (Chart 3.10.) during 2005 and 2006 points to a specific phenomenon in our economy. In particular, the series of data for these two years shows that the trend of the productivity and that of the unit labour costs move in opposite direction (with exception of some months). This means that the decline of workers' productivity was not accompanied by decline of labour costs. According to the economic theory, productivity decline should result in a decrease of the number of workers or decrease of gross wages<sup>4</sup>, thus the producers' labour costs would remain at the same level. Though, there should be a time lag in the effect of changed labour productivity on employment and/or wages.

### 3.5. Inflation

The average annual inflation, measured through the consumer prices, was 3.2%, pointing to a certain boost of the economic activity (inflation was 0.5% in 2005).

Inflation rate grew, mostly influenced by the price increase of tobacco products, due to the greater excises starting from January 2006, as well as the increase of electricity price in September 2006.

Retail prices grew by 3.9% on average in 2006, mainly due to the increased prices of the non-food industrial products (5.5%), agricultural products (4.8%), industrial products (3.9%), services (3.7%) and goods (4.0%).

Producer prices increased on average by 4.5% in 2006, due to the higher prices in 15 out of 22 industrial

4) Gross salaries were used as indicator of labour-related costs.

branches. Main drivers of increased producer price index were the higher prices of producers in the tobacco industry (21.6%) and oil industry (16.7%), metal products in metal-processing stage, except machines and devices (8.7%) and the production of electrical machines and devices (7.6%).

### 3.6. Wage policy

Wage policy in 2006, coordinated with the fiscal and monetary policy, was focused on maintaining the macroeconomic stability in the country. Thereby, the Law on Payment of Wages in the Republic of Macedonia continued to be valid in 2006, limiting the wage increase within government institutions. Wages in the private sector were paid in line with the profitability of the economic entities and labour productivity, in conditions of non-existence of institutional minimum wage.

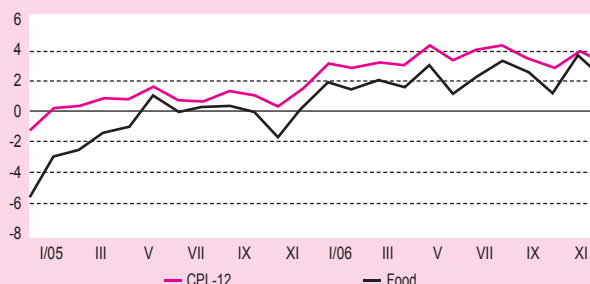
According to the State Statistical Office, during 2006, average net wage by employee was 13,517 (approximately EUR 220), which compared to 2005, grew by 7.3% in nominal terms, whereas in real terms (in line with the inflationary trends) by 4.0% (see Chart 3.14.).

The highest wage increase by sectors was realised in industry (9.9%), followed by services (3.4%) and agriculture (2.2%).

Thereby, the process of civil servants wage decompression was implemented in 2006, and wages in education and health increased, which contributed to wage increase in the service sector as well.

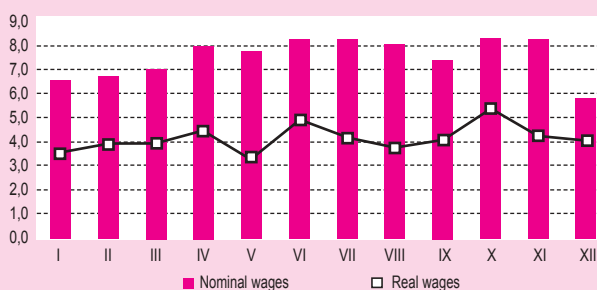
Within sectors, the highest average wage was registered in Financial intermediation (Denar 26,575 or 92% above the average), and the lowest one in the Construction sector (Denar 9,912 or 27% below the average).

Chart 3.12. Consumer price index and food prices

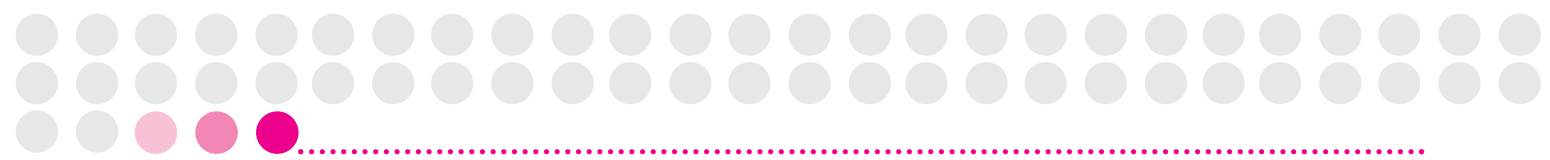


Source: State Statistical Office

Chart 3.13. Growth rates of nominal and real wages



Source: State Statistical Office



## 4. EXTERNAL SECTOR

### 4.1. Balance of payments

#### 4.1.1. Current account

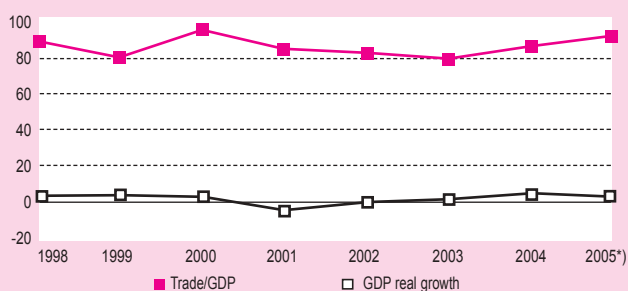
Indicators for the condition of the foreign economic relations in 2006 indicated continuation of the tendency of improvement of the external position of the country, which was mainly evident in the greater export performance in most sectors and high import of investment goods. In this context, relatively high trade balance deficit did not result in high current account deficit, mainly due to the relatively high transfer inflows (private and official). Thus, according to the preliminary data on BOP performance, current account deficit (on F.O.B. basis) declined by US\$ 57.8 million in 2006 and amounted to only US\$ 23.7 million, being historically the lowest actual value. Accordingly, current account balance expressed as percent of GDP decreased and amounted to less than 0.4%, which was by around 1 percentage point less than in 2005.

In 2006, foreign trade in the Republic of Macedonia was strongly influenced by the world economic developments. In particular, US dollar continued to depreciate on the international foreign exchange markets (US dollar in relation to the Denar depreciated by 10.4% in the period 31st December 2005 - 31st December 2006). At the same time, the crude oil price on the world stock market showed high increase (20.14% on average annually), and the stock exchange prices of one of the most important Macedonian export products - metals (nickel, copper, lead, zinc) showed high increase. Stock exchange price of lamb meat and the cold - and hot-rolled steel sheet metal decreased.

At the same time, the process of further liberalisation continued, by creating free trade zone in the region. To that end, the following agreements were concluded: Interim Free Trade Agreement between the Republic of Macedonia and UNMIK-Kosovo in force from 3rd February 2006, Free Trade Agreement between the Republic of Macedonia and Serbia and Montenegro in force from 1st June 2006, Agreement on Accession of the Republic of Macedonia to the Central European Free Trade Agreement in force from 24th August 2006.

The insatiable need of the Macedonian economy for import goods (import of raw materials and production intermediate goods, as well as consumption goods) and the improved competitiveness of domestic products on certain foreign markets increased the role of foreign trade in the total economy. Economic openness index showed upward tendency and moved towards the economies of the region.

Chart 4.1. Rate of trade openness and real GDP

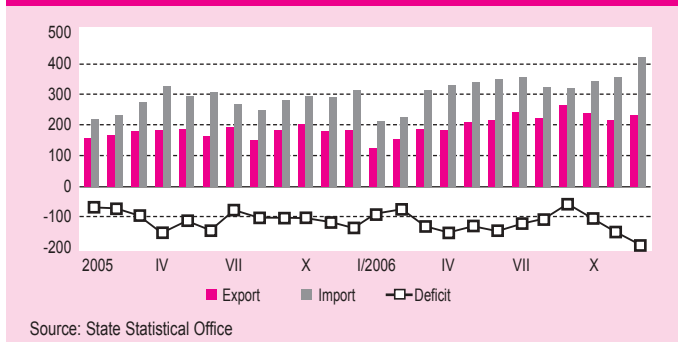


\*) Preliminary data  
Source: State Statistical Office

Under such conditions, in 2006, Macedonian economy needed to import 61 cents and to export 35 cents to produce US\$ 1 of GDP. In 2005, this ratio amounted to 54 and 35 cents, respectively.

**Export of goods.** According to the previous data for 2006, Macedonian economy exported around 38% of the gross domestic product (for comparison, the export in Hungary, Czech Republic and Slovakia amounted to over 50% of GDP for many years now). Export per capita in the Republic of Macedonia amounted US\$ 1,187 in 2006, being an increase by US\$ 180 per capita or 17.8% compared to 2005.<sup>5</sup>

**Chart 4.2.** Exports and imports of goods and the trade deficit (mil. denars)

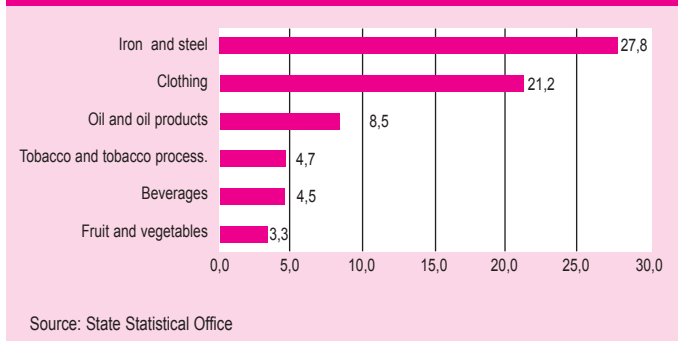


Export of goods in 2006, compared to 2005, expressed in dollars, increased significantly by 17.6% and amounted to US\$ 2,401 million. This increase was mainly due to the successful restarting of several former loss-makers, after their sale to foreign investors; increase of the volume of import-oriented production; further expansion of the preferential status of our products on the foreign markets; and the favourable prices of metals on the world stock markets. When assessing the import results, it should be taken into consideration that part of the increase of commodity import reflected the annual depreciation rate of dollar exchange rate in relation to the euro and the domestic

currency in 2006. This is even more accurate taking into consideration that in the currency structure of the foreign trade, the euro accounted for three quarters, and the dollar for one quarter.

**The analysis of export according to the economic purpose** of the products shows an increase of export of reproduction products by 25.5% compared to 2005, as well as their structural increase in the total export of goods by 3.7

**Chart 4.3.** Exports of main products according to SITC (2006, structure in %)



percentage points, mainly due to the higher export of raw materials and semi-products from the production of basic metals. Regarding the consumption goods, there was a relatively high increase in the export of beverages and tobacco (34%) and food (14.4%).

Strong increase in the value of export of oil and oil derivatives (28.5%), accounting for around 13% of the total increase of export of goods, also contributed to an increase of the total export of goods in 2006. Taking into consideration that the quantity of exported oil increased only by 8.9%, the major part of the actual export value of oil was due to the increased oil price on the world market.

The regional orientation of trade in 2006 continued its tendency of increasing the export of goods to the European Union: exports to EU increased by 22.4%.

5) For comparison purposes, Republic of Serbia realised US\$ 857 export per capita in 2006.

Regarding the country-structure, export continued to be mainly concentrated to only four countries: Serbia and Montenegro, Germany, Greece and Italy, participating with 63.7% in the total export of the country. Highest increase in the export was realised with Bulgaria (71%), Croatia (53%), Italy (40%) and Serbia and Montenegro (21%).

**Main export products** according to the Standard International Trade Classification (SITC) in 2006 were: iron and steel, clothing, oil and oil products, tobacco and processed tobacco, fruit and vegetables, beverages, metal ore and scrap metal. These seven groups of products comprised 73% of the total export of the country.

Observations regarding the export concentration indicate that the Republic of Macedonia was among the countries in the region with the greatest value of the Hirschmann index. In general, the increase of the Hirschmann index was due to the trade improvement or through modernisation or export of technological-intensive products. However, Macedonian economy still comprises products that include or add, to a large extent, low-qualified labour force, which makes the Hirschmann index assessment complex: clothing, iron and steel still account for more than half of the total Macedonian export.

#### Box 4.1. Hirshmann index of export concentration

*Hirshmann index of concentration is calculated as:  $Hlx = \sum xi/X^2$ , where  $i$  is number of the groups of products,  $xi$  is the export of the product  $i$ , and  $X$  is the total export of the country.*

*This index varies between 0 and 1 (or 0% and 100%), as normal values. In line with UNCTAD, the average index of the transition countries is around 0.16, and the index of developed countries should be over 0.17. Lower values indicate smaller concentration (greater number of products with a small share in the total trade structure), while high values indicate greater concentration (several products with a large share in the total country trade).*

The indicator for the share of the ten leading groups of products in the total Macedonian export measures whether and how much Macedonia use its comparative advantages. This indicator shows the same findings as the Hirschmann index, that is a high concentration in exports. In particular, in 2006, the export of the 10 leading product groups, according to SITC, amounted to US\$ 1,943 million, or 81% of the total export of the country. The rest of the total export (only 19%) covered as much as 56 product groups (see Table 4.2.).

In addition, the ranking of the Macedonian ten leading groups of products on the list of major international export products shows a rather poor market conditions for our export products.

Small-volume production and variable export quantities, lacking standardised quality, still characterise Macedonian export, making Macedonian exporters minor and unreliable partners. In addition, unorganised appearance of

Table 4.1. Export value and Hirschmann export concentration ratio

	2002	2003	2004	2005	2006
Export (US\$ million)	1.112	1.359	1.672	2.041	2.401
Hirschmann index	0.1274	0.1391	0.1554	0.1438	0.1397

Source: State Statistical Office  
Calculation: MoF

**Table 4.2.** Export of the ten leading products according to STIC

Rank	STIC	name_department	Kg	US\$	Value share in %
1	67	Iron and steel	888,817,932	668,284,253	27.8
2	84	Clothing	22,070,846	508,515,335	21.2
3	33	Oil and oil products	332,362,492	203,626,221	8.5
4	12	Tobacco and tobacco processing	31,617,804	111,695,766	4.7
5	05	Fruit and vegetable	304,169,512	109,058,903	4.5
6	11	Beverages	155,778,385	80,254,457	3.3
7	28	Metal ore and scrap metal	177,507,631	75,624,088	3.2
8	66	Products from non-metal minerals	611,498,425	70,027,522	2.9
9	77	Electric machines and spare parts - elsewhere non-specified	19,319,368	59,076,465	2.5
10	85	Footwear	2,310,640	56,718,817	2.4
Total more important products			2,545,453,033	1,942,881,826	80.9
Total export of the Republic of Macedonia			3,085,308,133	2,400,714,689	100.0

Source: State Statistical Office

Macedonian foreign - trade enterprises on foreign markets without a marketing strategy has an additional negative influence on the Macedonian export.

Low level of export was also a consequence of the unfavourable industrial structure still dominated by capacities with low processing stages, technical and technological obsolescence, insufficient utilisation of production capacities, high import and energy dependence and low profitability, leading to a low competitiveness of the export goods.

**Import of goods.** In 2006, value of the total imported goods amounted to US\$ 3,762.7 million, that is US\$ 534.7 million or 16.6% higher than in 2005. Import increase was mainly due to increased export of: oil and oil products (by US\$ 135 million, or 27.4%), iron and steel (US\$ 83.4 million or around 29%), road vehicles (which, following the drop by around 14% in 2005,

increased by US\$ 45 million or 41% in 2006), metal ore and scrap metal (US\$ 23.6 million or 48.4%).

**Table 4.3.** Import of oil and oil products

	2003	2004	2005	2006	Balance 2006-2005	Rates
Kilograms	1.166.870.592	1.112.268.032	1.229.815.330	1.323.936.752	94.121.421	7,7
US\$	258.972.299	316.296.568	492.046.572	627.078.060	135.031.488	27,4
Denars	14.062.998.647	14.618.227.088	24.253.910.410	30.592.253.986	6.338.343.576	26,1
Denar/US dollar	54,3031	49,4105	49,2919	48,7854		

Source: State Statistical Office  
Calculation: Ministry of Finance

One of the reasons for the increased import in 2006 was certainly increased crude oil price on the world stock market by 20.14% (average annual). Thus, should the oil price remain at the same level as in 2005, import of the total quantity of oil in 2006 (1,324 tones) would cost around US\$ 97.4 million less than the actual value of the oil import.

Analysed by activities, goods related to the production of energy raw materials participated the most in the import (15.6%), followed by production of basic metals (12.5%), production of food products and beverages (9.9%), production of textile fabric (9.1%), production of chemicals and chemical products (8.9%), etc.

Observed by regions, highest import originated from the developed countries, including the import from the EU member states which accounted for around 44% of the total import to the Republic of Macedonia.

**Trade balance.** Despite the increase in the trade quantity in the last few years, Republic of Macedonia did not manage to decrease the negative trade gap. Thus, in line with the movements of export and import of goods, trade deficit in the foreign trade, expressed in US dollars, amounted to US\$ 1,362 million (on C.I.F. basis) in 2006, being 21.7% of GDP. Increased



deficit in 2006 relative to 2005, amounted to US\$ 175.3 million, 51% out of which was due to the deficit increased in the trade with oil and oil derivatives.

The situation of negative trade balance with countries with which the Republic of Macedonia has free trade agreements continued in 2006. For instance, deficit with only five such countries, Bulgaria, Slovenia, Romania, Ukraine and Turkey amounted to around 32% of the total deficit in the foreign trade of the Republic of Macedonia in 2006 (see Chart 4.5).

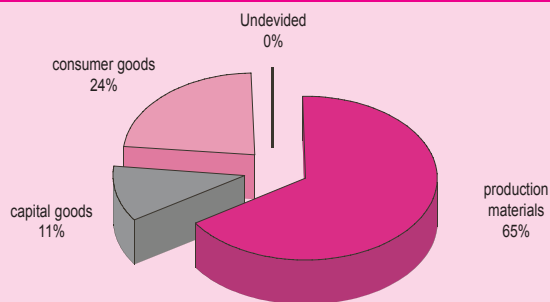
Trade deficit with the EU member states amounted to US\$ 324 million, almost 25% of the total trade deficit of the country, and the trade deficit with the EFTA member states amounted to US\$ 51.3 million, participating with 3.8% in total trade deficit.

**Services.** In 2006, following the five-year negative service balance, a positive balance of US\$ 25.2 million was realised due to the greater annual increase of the inflow of funds from exported services (around US\$ 130 million increase from 2005 to 2006) relative to the increase of outflow of funds for the rendered services (US\$ 70.6 million increase from 2005 to 2006). This was mainly due to the high inflow of funds on the basis of transport (annual increase of 40.8%) and the inflow for the realised trips - tourism (increase by 54% compared to 2005). Regarding other services, relatively mild drop (by US\$ 7 million) was registered in the inflow from investment activities.

**Income.** Income balance improved compared to last year, with a small deficit of only US\$ 3 million. The outflow of funds on the basis of transfer of the earned profit of foreign investors decreased by US\$ 45 million (or by 54.7%) and, at the same time, the inflow on the basis of employment allowance increased by US\$ 11.6 million or by 20.3%.

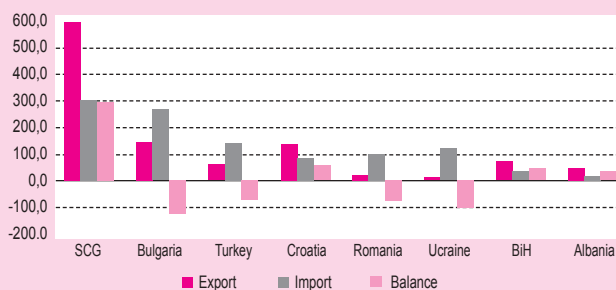
Although the interest balance did not show significant changes, annual increase regarding the collected interest by around US\$ 24 million should be mentioned, out of which US\$ 17.7 million are on the basis of official reserves. Total amount of interest on official reserves was US\$ 37.2 million, which increased almost twice relative to 2005. At the same time, the interest paid on the basis of used loans increased by US\$ 22,3 million, out of which 91.7% was on the basis of interest on medium- and long-term equity.

Chart 4.4. Structure of imports by economic usage in 2006



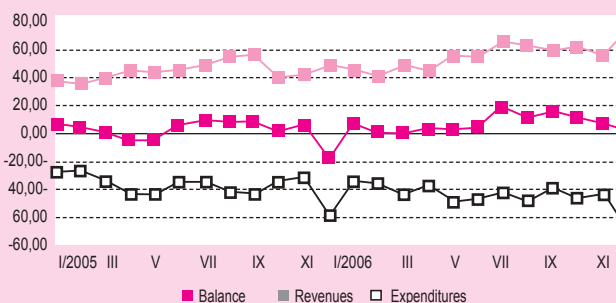
Source: State Statistical Office

Chart 4.5. Foreign trade with countries with FTA's



Source: State Statistical Office

Chart 4.6. Revenues, expenditures and balance of services (mil. denars)



Source: State Statistical Office

**Transfers.** Positive changes in the BOP were also recorded at the balance of international aid in goods and money, which, in 2006, increased by US\$ 174.6 million, or by 16.3% compared to 2005. Although slight fall of balance of the official transfers was envisaged, it showed a positive increase of 12.7%. Thereby, inflow of goods increased by US\$ 11 million, and money inflow decreased by US\$ 1.5 million.

High increase by US\$ 165.2 million (16.5%) was recorded in private transfers (net), mainly due to the increased inflow on the basis of purchased foreign currency in the amount of US\$ 151 million (or 18.3%), as well as the increased inflow on the basis of remittances by US\$ 28.3 million (or 16.7%). Regarding other transfers, inflow on the basis of rents, pensions and disability pensions increased by US\$ 8.4 million or by around 12%.

#### 4.1.2. Capital financial account

The volume of transactions on the BOP capital-financial account in 2006, as well as in the previous years, was almost entirely achieved on the financial account, rather than on the capital one.

Most important item on the BOP financial account was foreign direct investments (FDI), which amounted to US\$ 350 million in 2006 (see Chart 4.7.), which is the highest amount of FDIs recorded in the Republic of Macedonia following 2001, when the company Macedonian Telecommunications was privatised. In fact, during whole transition period, FDIs in the Republic of

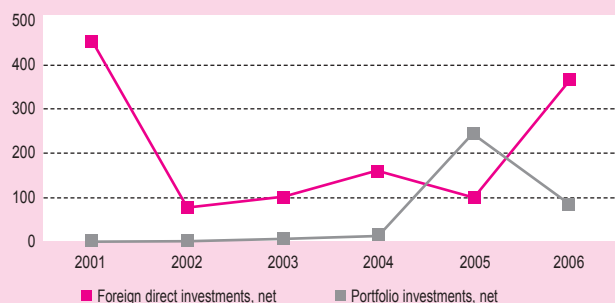
Macedonia were connected with privatisation inflows from larger (and successful) state-owned enterprises. Similarly, in 2006, the high amount of FDIs was due to the privatisation of the company ESM Distribution. Though, a significant share of the total FDIs in 2006 came from the first more significant greenfield investment in the Republic of Macedonia, that of Johnson Controls.

Portfolio investments in 2006 slightly declined compared to 2005, though they are still on a relatively high level if we take into consideration their trivial level in the previous years, which did not exceed the amount of US\$ 15 million. Such phenomenon of increase of portfolio investments was also important from the point of view of movement on the capital market in the Republic of Macedonia, which was still in its early development stage. It is also worth mentioning that in 2006, equity instruments prevailed in the structure of the portfolio investments in the Republic of Macedonia as compared to the debt instruments.

The item other investments had negative balance of around US\$ 43 million in 2006. Trends of trade credits, loans and currencies and deposits, as integral parts of these items, are shown in Chart 4.8.

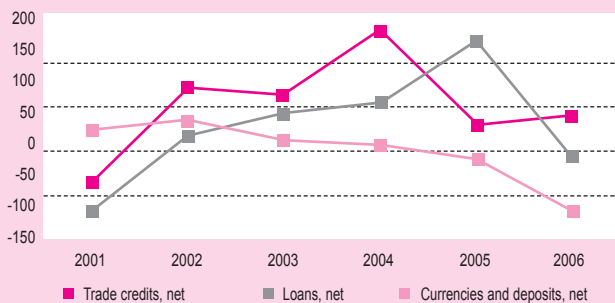
In 2006, trade credits (net) amounted to US\$ 41 million, which was due to the import credits of around US\$

Chart 4.7. FDI and portfolio investments (mil. denars)



Source: National bank of the RM

Chart 4.8. Other investment (mil. denars)



Source: National bank of the RM

98 million, and export credits of around US\$ 50 million. Unlike the trade credits, the loans (net), after being positive for several years, were negative in 2006. This mainly indicated the increased repayment of loans from foreign creditors, whereby the outflow exceeded the inflow, mainly regarding the medium- and long-term loans.

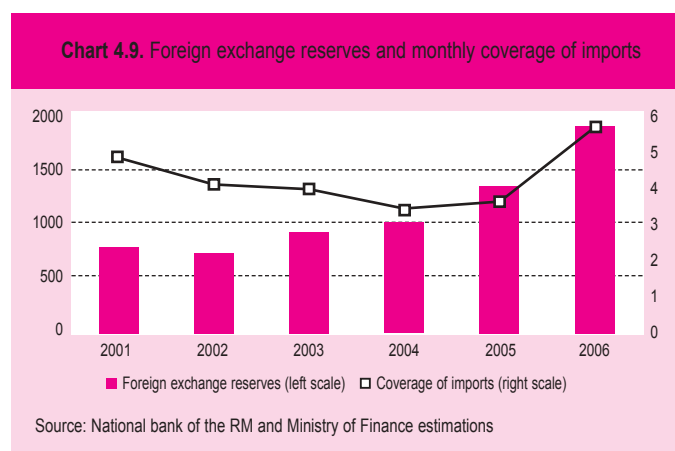
Loans most used were the ones from the commercial creditors, whereby there was no new borrowing from the London Club of Creditors in 2006. Regarding the group of multilateral creditors, borrowing towards which was in the amount of US\$ 73 million in 2006, the biggest borrowing was from EBRD and EIB, and IBRD, EIB and IMF disbursed most funds on the basis of repayment of loans.

Currencies and deposits had significant negative amount, which suggested significant outflow of funds in 2006 regarding currencies and deposits. If the structure is analysed in detail, over 80% of currencies and deposits was used by the households, and the remaining part was kept by the banks and the Central Bank.

#### 4.1.3. Foreign exchange reserves

In conditions of de facto fixed exchange rate regime, foreign currency reserves are the first defensive line of the exchange rate targeted level. Thus, regarding BOP, foreign currency reserves cover the difference between the current account and the capital account, and they are shown as a decrease or increase in the respective year.

In 2006, NBRM purchased foreign currencies on net basis on the foreign exchange market in the amount of US\$ 376 million, thus increasing the level of foreign currency reserves for the respective amount. From cumulative point of view, gross foreign currency reserves in the Republic of Macedonia were continuously increasing and amounted to US\$ 1,866 million in 2006. This figure corresponded to 5.5-month import coverage, which is a greatest coverage of monthly import of goods with the foreign currency reserves since the Republic of Macedonia gained its independence. It should be emphasised that significant part of the increase of foreign currency reserves in 2006 was due to the sale of ESM Distribution to a foreign strategic partner.

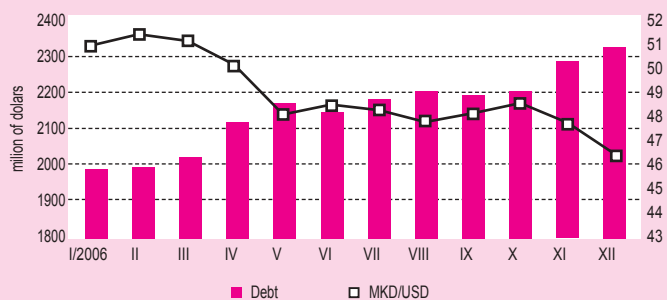


In 2006, although being relatively low, the item - errors and omissions - had positive sign and it amounted to around US\$ 10 million. It mainly referred to the unidentified inflow of foreign currencies in 2006, which was assumed to originate mainly from the private transfers that were part of the current account, but remained unregistered.

#### 4.2. External debt

Total external debt of the Republic of Macedonia on the basis of used short-term and long-term credits amounted to US\$ 2,434 million in 2006. From the point of view of maturity, long-term loans dominated with 96.1%. Long-term component of the foreign debt of the Republic of Macedonia (used long-term credits and loans) amounted to US\$ 2,315 million, which, compared to 2005, increased by US\$ 147 million. Increase of the external debt was mostly due to the positive exchange rate differences, as a

**Chart 4.10. External debt and exchange rate MKD/USD**



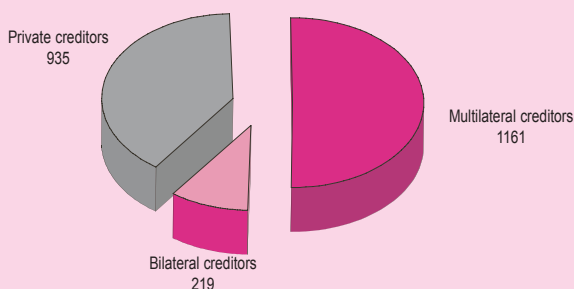
Source: National bank of the RM

result of the US dollar depreciation in relation to the euro and the other currencies.

From the point of view of debtors, public sector external debt amounted to US\$ 1,614.4 million and compared to 2005, it declined by US\$ 92 million. Within the public sector debt, central government debt and Central Bank debt decreased compared to 2005, while the debt of the public funds and public enterprises showed an increase.

Debt structure by creditors was almost unchanged compared to 2005. Thus, multilateral creditors (50.2%) accounted for more than half of the debt, while bilateral creditors participated with 9.5%, and private creditors participated with 40.4%.

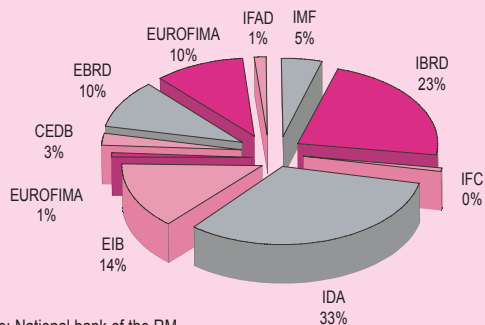
**Chart 4.11. Structure of debt by creditors**



Source: National bank of the RM

With regard to the multilateral creditors, International Development Agency (credits of which are with concessional conditions) and International Bank for Reconstruction and Development were the biggest individual creditors. 28% of the total external debt of the Republic of Macedonia was towards these two international institutions. Regarding the private creditors, 21.1% of the debt was on the basis of eurobonds, while the rest of the debt was towards private banks, financial institutions and enterprises.

**Chart 4.12. Structure of debt by multilateral creditors**



Source: National bank of the RM

With regard to the debt currency structure, which includes only the debt principal, majority of the debt was euro-indexed with around 43%, followed by the US dollar with around 30%, and the special drawing rights with 24%, while the other currencies had an insignificant share.

Regarding the structure of the external debt by debtors, central government liabilities accounted for 80.3%, followed by the liabilities of the public enterprises (12.7%), public funds (3.5%) and the Central Bank (3.5%).

On the basis of already approved credits, funds in the amount of US\$ 350 million were disbursed from the foreign creditors in 2006.

Regarding the multilateral creditors, most funds were disbursed from the European Investment Bank (EIB) and the European Bank for Reconstruction and Development in the amount of US\$ 45 million.

Funds from bilateral creditors in the form of credit lines, in the amount of US\$ 33 million, were mostly used as support to small- and medium-sized enterprises.

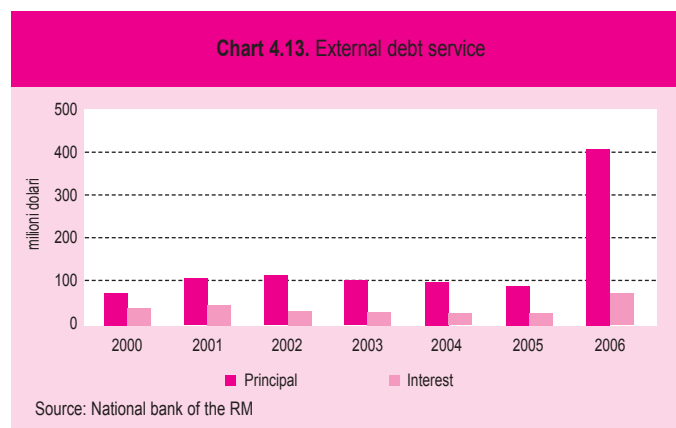
In 2006, US\$ 243.5 million was disbursed from private banks, financial institutions and non-financial private sector, which compared to 2005, was a decrease by 28.5%.

In 2006, new credits and loans were concluded in the amount of US\$ 481 million, mostly under concessional conditions. Funds from the newly concluded credits will be mainly used in the coming years. Newly concluded credits with multilateral creditors were from the European Bank for Reconstruction and Development (EBRD) in the amount of US\$ 79 million, and from the International Bank for Reconstruction and Development (IBRD), in the amount of US\$ 60 million. New credits and loans were also concluded with bilateral creditors in the amount of US\$ 16.5 million and with private banks, financial institutions and non-financial private sector in the amount of US\$ 312 million.

**Servicing of liabilities towards foreign creditors.** Debt servicing continued the trend of constant increasing, whereby servicing of liabilities in 2006 followed the envisaged dynamics. In 2006, liabilities towards foreign creditors were paid in the amount of US\$ 481.5 million, US\$ 403.8 million out of which was on the basis of paid debt principal, and US\$ 77.7 million was on the basis of interest payment. Funds in the amount of US\$ 76.2 million were paid to the multilateral creditors, most out of which towards IBRD (US\$ 21.1 million), towards EIB (US\$ 15.9 million) and towards EBRD (US\$ 11.6 million).

Funds in the amount of US\$ 39.3 million were paid towards bilateral creditors, US\$ 366 million towards private creditors, US\$ 324 million out of which as principal. Within this framework, debt towards the London Club of Creditors was paid in full amount of US\$ 227.5 million.

In particular, funds acquired from the Eurobond issued at the end of 2005 were used to fully buy back the debt towards the London Club in 2006 and partially for strengthening the position of foreign currency reserves. Many positive effects were achieved with the buy back of the debt towards the London Club, in particular improvement of the public debt interest structure and high amount of savings in the Budget in the coming years, improvement of the debt portfolio profile and of the debt maturity, etc.



**Level of indebtedness.** According to the international ranking standards of countries according to the level of indebtedness, the Republic of Macedonia is ranked in the group of middle to modest indebted economies. The most relevant indicator for this was the share of the total external debt (long-term and short-term) in the gross domestic product (average from the last three years), which amounted to 37.2% in 2006.

Regarding the other criteria, Republic of Macedonia was ranked in the group of low-indebted countries. In particular, the ratio between the external debt and the export of goods and services (average from the last three years) was 91.6%, the ratio between the total debt servicing and the export of goods and services (average from the last three years) was 19.0%, and the ratio between the interest payments and the export was 0.3%. Accordingly, the level of indebtedness in the Republic of Macedonia ranged within tolerant framework. However, when monitoring the indebtedness through the export indicators, certain features of the export of goods and services should be taken into consideration. In fact, most of the export was related to export of finishing products, hence the real value of the effective foreign exchange inflow is significantly smaller than the export of goods and services. Also, significant part of the claims is usually settled on the basis of compensation. Hence the level of indebtedness would be higher if calculated only with the effective foreign exchange inflow from the export of goods and services.

#### Box 4.2. Level of indebtedness in the Republic of Macedonia according to several criteria

	31.12.2004	31.12.2005*	31.12.2006
Total external debt/ GDP	36.8	44.2	37.2
Total external debt/export of goods and services	107.1	97.5	91.6
Debt servicing/export of goods and services	14.1	15.7	19.0
Debt payment/export of goods and services	3.0	2.2	0.3

\*Higher level of indebtedness in 2005 was a result of the public sector indebtedness on the basis of the issuance of Eurobonds at the end 2005, which funds were immediately used to fully repay the debt towards the London Club of Creditors in January 2006.

Source: National bank of the RM

*Standards on defining the level of indebtedness and classifying the country in a certain group of countries, are defined in the following way:*

*- Total external debt to the average of the gross domestic product in the last three years: high indebtedness exceeding 50%; modest indebtedness is 60% of the marginal value (50%), though not reaching the critical level, i.e. the interval between 30-50%; and lower indebtedness below 30%.*


*- Total external debt to the average of the export of goods and services in the last three years: high indebtedness exceeding 275%; modest indebtedness is 60% of the marginal value (275%), but not reaching the critical level, being an interval between 165-275%; and lower indebtedness below 165%.*

*- Servicing the debt to the average of the export of goods and services in the last three years: high indebtedness exceeding 30%; modest indebtedness is 60% of the marginal value (30%), but not reaching the critical level, i.e. the interval between 18-30%; and lower indebtedness below 18%.*

*- Interest payments to the average of the export of goods and services in the last three years: high indebtedness exceeding 20%; modest indebtedness is 60% of the marginal value (20%), but without reaching the critical level, i.e. the interval between 12-20%; and lower indebtedness below 12%.*

*According to the recommendations of the World Bank, if three out of the fourth indicators are included in a given interval, the country is classified in the respective group of countries. However, it should be mentioned that approaching the critical level, i.e. marginal value of certain indicator, should be interpreted with caution, taking into consideration the fact that when moving from one to another group of countries, the movement in the past period, not only in the current period, should be taken into consideration.*

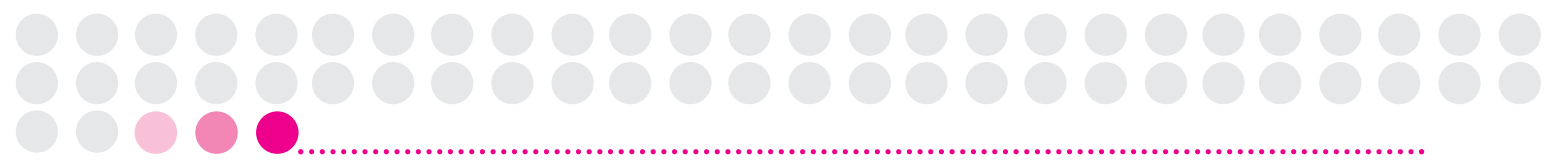
In 2006, level of indebtedness of the CEE countries amounted to around 55% (as ratio between GDP and external debt) and 104.5% as ratio between the debt and the export of goods and services. Analysed by country, Croatia had a highest level of indebtedness in 2006, or 78% (GDP/debt), and 112% (debt/export of goods and services), mainly attributed to the increase of the borrowing by the commercial banks and the decline of the US dollar value. In Serbia and Montenegro, after the debt reprogramming in 2001 and write-off of the debt with the London Club of Creditors in 2004, the debt was reduced to 63% of GDP, while the debt in relation to the export of goods and services was still significantly high (244%). In Bulgaria, share of the external debt in GDP amounted to 67%, while the debt in relation to the export of goods and services amounted to 112%. Romania, according to the level of indebtedness, which amounted to 33%, as



ratio between the debt and GDP, and in relation to the export of goods and services, which amounted to 98%, belonged to the category of middle-indebted countries.

In 2006, short-term debt of the Republic of Macedonia amounted to US\$ 118.8 million, and compared to 2005, it grew by US\$ 30 million. The short-term debt is solely a debt of the private sector in the economy, i.e. the debt of private banks and enterprises, taking into account the fact that there was no short-term borrowing in the public sector.

From the point of view of the structure of short-term debt by types of credits, the trend of predominantly short-term borrowing through financial credits continued, accounting for 99.8%, while the share of the commercial credits was insignificant.





## 5. FISCAL SECTOR

### 5.1. Central Budget revenues

In 2006, actual central budget revenues amounted Denar 63,555 million, financed by the revenues realised in the amount of Denar 62,955 million. Detailed review of the central budget is given in Table B2.

In 2006, total revenues of the Central Budget of the Republic of Macedonia, compared to last year, were higher by 7.1%. Tax revenues reached the level of Denar 58,914 million, participating with 93.6% in the total budget revenues in 2006.

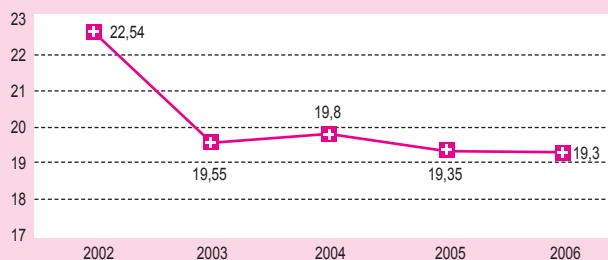
As shown in Chart 5.2., the share of the value added tax (VAT) in the structure of total tax revenues was 47.5%, the share of excises was 20.1%, personal income tax participated with 14.7%, customs duties and other import duties with 9.5% and profit tax with 8.2%.

In 2006, revenues on the basis of personal income tax amounted to Denar 8,414 million, which is by 3.8% higher compared to last year. Regarding the structure of these revenues, as usual most of them were realised on the basis of the payroll tax - 75.3%, as well as on the basis of tax on income received from contractual agreements (9.5%), while the share of revenues on other basis was relatively low. Chart 5.3. shows actual budget revenues on the basis of direct taxes.

Collected revenues on the basis of profit tax in 2006 amounted to Denar 4,708 million, which is by 66% higher compared with the profit tax revenues in 2005. High growth of revenues in 2006 was due to the better performance in the economy and significantly increased profitability (29.7% in 2006 relative to 2005), as well as due to the reduction of the profit tax exemptions from 50% to 30% in 2006.

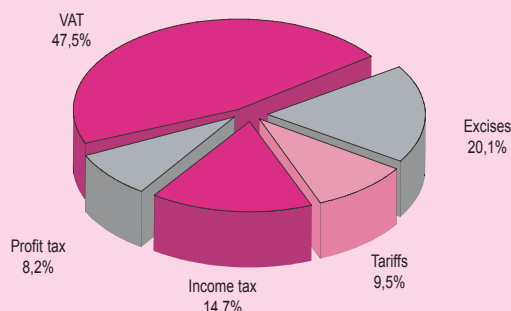
Domestic taxes on goods and services (VAT and excises) as usual had the highest share in the structure of total revenues or 61.6%.

Chart 5.1. Tax revenues, % of GDP



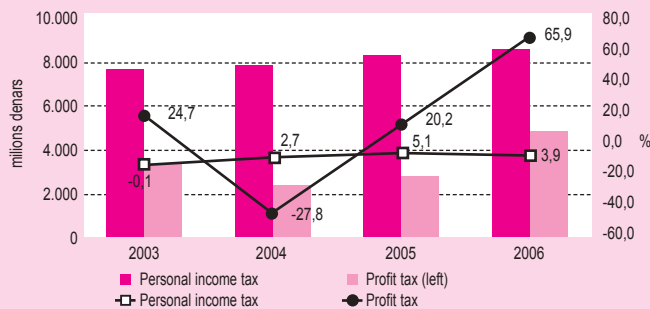
Source: Ministry of Finance

Chart 5.2. Tax revenue structure



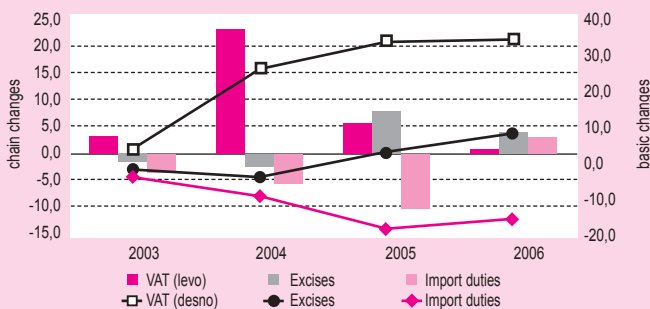
Source: Ministry of Finance

**Chart 5.3. Direct taxes - amount and percentage of annual change**



Source: Ministry of Finance

**Chart 5.4. Indirect taxes - chain rates of changes and basic rates of changes compared to 2002**



Source: Ministry of Finance

VAT revenues in 2006 equalled Denar 27,239 million which is slightly higher compared to last year (0.6%), though they under-performed projected revenues in the Supplementary Budget by 4.5%. This can be explained by the new Customs Law, regulating the deferred payment of the customs debt and the reduction of VAT tax rate from 18% to 5% for agricultural products, in force from 1st October 2006. Collected VAT on imported goods in the country amounted to Denar 26,385 million, and compared to last year, increased by 12.0%.

Excise revenues grew by 3.9% in 2006 compared to 2005, while they exceeded the projected level in the supplementary budget plan by 4.6%. This increase of excise revenues was mainly due to increased revenues on the basis of excise on tobacco processing - by Denar 306 million, the sale of passenger vehicles - by Denar 109 million and revenues on the basis of excise on oil derivatives - by Denar 52 million.

Other tax revenues in the amount of Denar 1,620 million grew by almost 2.5 times on annual level. This increase was due to the inclusion of the fees, introduced in 2006 pursuant to the Law on Environment Protection, Law on Tobacco and the Law on Health Care.

Non-tax revenues dropped by almost 2 times in 2006 compared to 2005, mainly due to the unpaid dividend by AD Macedonian Telecommunications.

Capital revenues amounted to Denar 948 million in 2006, being an increase by 1.6% compared to 2005. Capital revenues were mainly received by the sale of construction land.

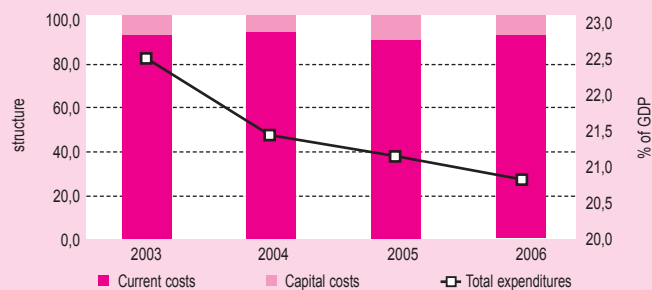
Revenues on the basis of donations amounted to Denar 550 million in 2006, and the main donor was the EU with Denar 120 million, intended to finance development projects, and the Kingdom of the Netherlands with Denar 430 million as support to the implementation of PDPL 2 Arrangement.

## 5.2. Central Budget expenditures

In 2006, total central budget expenditures amounted to Denar 63,555 million, being an increase of 5.8% compared to the last year which was achieved by the increase of almost all expenditure items.

Costs for wages and salaries and allowances amounted to Denar 22,223 million in 2006, being an increase of 2.6% compared to 2005. The increase was mainly due to application of the collective agreements regarding the salary-related expenditures, because of the salary decompression, as well as the continuity of the principle of adequate and equitable

**Chart 5.5. Trend of total expenditures (as % of GDP) and share of current and capital costs in total expenditures \***



\*In 2003, in addition to the mentioned categories, crisis-related costs existed with a share of 0.73% in the total expenditures

Source: Ministry of Finance

representation in public administration of representatives from ethnic communities. Still, costs related to salaries, wages and allowances as percent of the total expenditures were lower by 1.1 percentage point compared to 2005.

Regarding goods and services, Denar 7,922 million was spent in 2006, i.e. 9.2% more compared to last year.

Funds for transfers, which include subsidies, current transfers and social benefits, were realised in the amount of Denar 24.491 million in 2006, which is an increase of 13.3% compared to 2006. This increase in 2006 was mainly due to the higher benefit payments to the Pension and Disability Insurance Fund (by 13.7% compared to the last year) to cover the transitional deficit

of the Fund regarding the introduction of the second pillar.

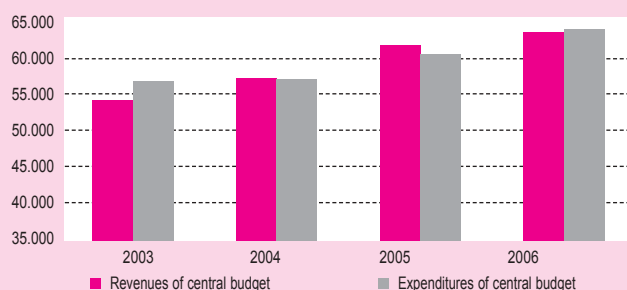
In 2006, Denar 2,862 million were spent for social programmes, which, compared to 2005, was a drop by 5.0%. Transfers for child allowance remained almost the same (an increase by only 0.9%).

Regarding the reforms in the Ministry of Defense, Denar 211 million was spent, which is by 55.2% more than in 2005.

Within the public administration reforms, Denar 501 million was spent in 2006, or 3.3% more compared to 2005.

Regarding interest payments, there was an increase by 21.0% in 2006 compared to 2005. The increase was mainly a result of the increased payments on the basis of interest on external debt by Denar 480 million or by 21.0% compared to last year. Interest payments on the basis of domestic debt remained almost stable.

**Chart 5.6. Budget revenues and expenditures (mil. denars)**



Source: Ministry of Finance

Capital costs reached the amount of Denar 5,721 million or 9% of the total budget expenditures in 2006. This was by 3 percentage points lower compared to the performance in 2005. Major part of the capital expenditures (93.9%) was related to costs for purchasing capital funds and for capital transfers.

### 5.3. Central Budget deficit

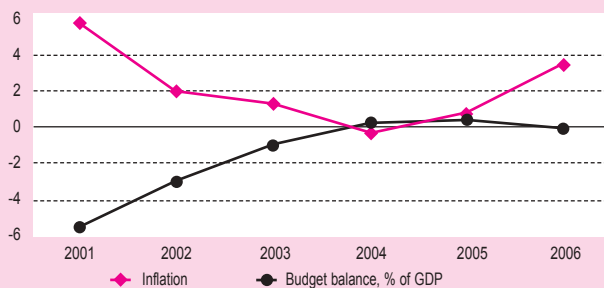
In 2006, central budget was almost balanced, i.e. budget deficit amounted to Denar 600 million or 0.2% of GDP.

Realised budget deficit in 2006 was lower than the envisaged one in the Supplementary Budget by Denar 408 million.

Budget deficit of the consolidated budget amounted to Denar 1,710 million, or 0.6% of GDP.

Budget deficit financing in 2006 and regular servicing of liabilities on the basis of the both domestic and foreign debt

**Chart 5.7** Connection between Central budget balance and inflation



Source: Ministry of Finance

were fully provided from domestic sources, mainly from the privatisation proceeds and the issuance of government securities. In fact, inflows from the sale of the majority capital of ESM contributed around 75% to the total privatisation revenues. In addition, there were inflows from the sale of the state capital in AD Macedonian Telecommunications, banks and other institutions.

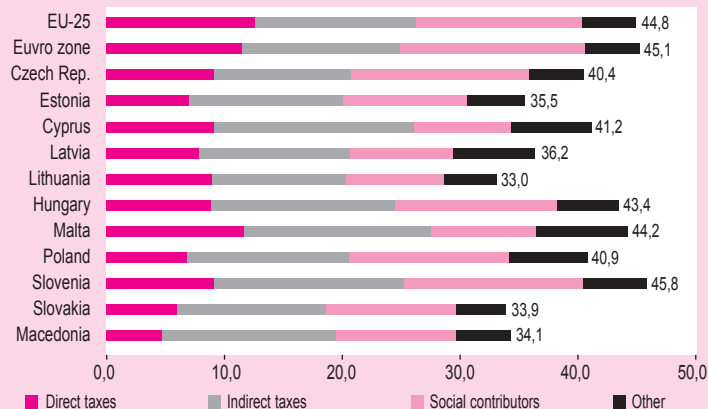
### Box 5.1. Fiscal burden in the Republic of Macedonia

*Analysis of the fiscal burden covers general rather than central government budget, in order to include fiscal duties in this calculation. In fact, in addition to the tax revenues and the administrative fees on all levels of government, social insurance contributions are also necessary for calculation of fiscal burden on economic entities.*

*The results from the calculations showed that in 2006 the fiscal burden amounted to 30.2% of GDP, almost stable compared to the fiscal burden in 2005. In fact, downward tendency could be observed, which will remain in future, taking into consideration the pension and tax system reforms. However, compared to 2005, there were no differences even in the structure.*

*In order to determine the share of GDP distributed to the public sector, we will show the general government revenues as percentage of GDP. In 2006, this amount accounted for 34.1%, whereby, compared to last year, it was by 1.4 percentage points lower. In order to get better picture of the share of the public sector in GDP, Chart 5.8. shows the relative size of this proportion in the Republic of Macedonia and several other countries.*

**Chart 5.8.** Percentage share of the total budget revenues in GDP



The data for the EU countries are for the fiscal year 2005  
Source: Eurostat

*the relative size of this proportion in the Republic of Macedonia and several other countries.*

*A general observation from the above comparison with the European Union is that distribution of GDP for public financing is relatively low in Macedonia, taking into account the smaller share of the budget revenues in GDP by around 10 percentage points.*

*As we can see from the Chart, the analysed indicator regarding the EU - 10<sup>6</sup> is lower than 40% only in Latvia, Estonia, Slovakia and Lithuania. On the other hand, the highest percent of 45.8 was registered in Slovenia.*

6) These countries became EU members in 2004.

Within the EU, the share of budget revenues in GDP is usually the highest in the Scandinavian countries: Sweden (59.1%), Denmark (57.9%) and Finland (52.6%). The structure in Denmark is specific, where the tax revenues only participate with 49.2% in GDP.

Distribution of the fiscal burden in relation to the revenue sources is similar to the one in the EU - 25 and EU - 10. In Macedonia, 57.2% of the budget revenues are from the taxes, which is by 2 percentage points less compared to the EU - 25, while social contributions participate with 29.6% in the budget revenues, a 1.5 percentage points less compared to their share in the EU - 25. However, there are differences in the tax revenue structure. In fact, in Macedonia, 3/4 of the tax revenues are collected on the basis of indirect taxes, while the rest (25%) on the basis of direct taxes.<sup>7</sup> On the other hand, indirect taxes participate with 50.8% in total tax revenues in the EU - 25. Thus, the spread of these categories of taxes is 2.6 percentage points, whereas in Macedonia that spread amounts to around 50 percentage points. The difference is smaller compared to the average of the EU - 10 countries, where the ratio is 62% to 38% in favour of the indirect taxes.

#### 5.4. Public debt

Public debt of the Republic of Macedonia comprises the government debt and all financial liabilities incurred on the basis of borrowing by the municipalities and the City of Skopje, as well as by the public enterprises and companies which are fully or predominantly owned by the state. According to this definition, the Government of the Republic of Macedonia, municipalities and the City of Skopje, public enterprises and companies fully or predominantly owned by the state can be public debt issuers.

Public debt portfolio of the Republic of Macedonia includes debts inherited by ex-Yugoslavia, borrowings from international financial institutions and international financial markets, as well as borrowing on the domestic financial market.

Analysis of the public debt trends according the national methodology which includes the stock of the debt on the basis of treasury bills issued for monetary purposes in addition to the other components of the GFS methodology, shows a reduction of the public debt by EUR 161.9 million in the period from December 2005 to December 2006. In fact, public debt stock in the amount of EUR 1,992.2 million in December 2005 was reduced to EUR 1,830.26 million in December 2006, or 36.8% of GDP.

During 2006, in order to restructure the debt, in addition to the regular servicing, debt towards the London Club of Creditors was early repaid in the amount of EUR 184.3 million, as well as the Continuous Bond no. 2 in 2005 in the amount of EUR 11.7 million.

Regarding the relation between the external and the internal debt, since 1999 domestic debt increases relative to the external one. As of 31st December 2006 inclusive, the share of the external debt and domestic debt in the total public

Table 5.1. Public debt stock in EUR million

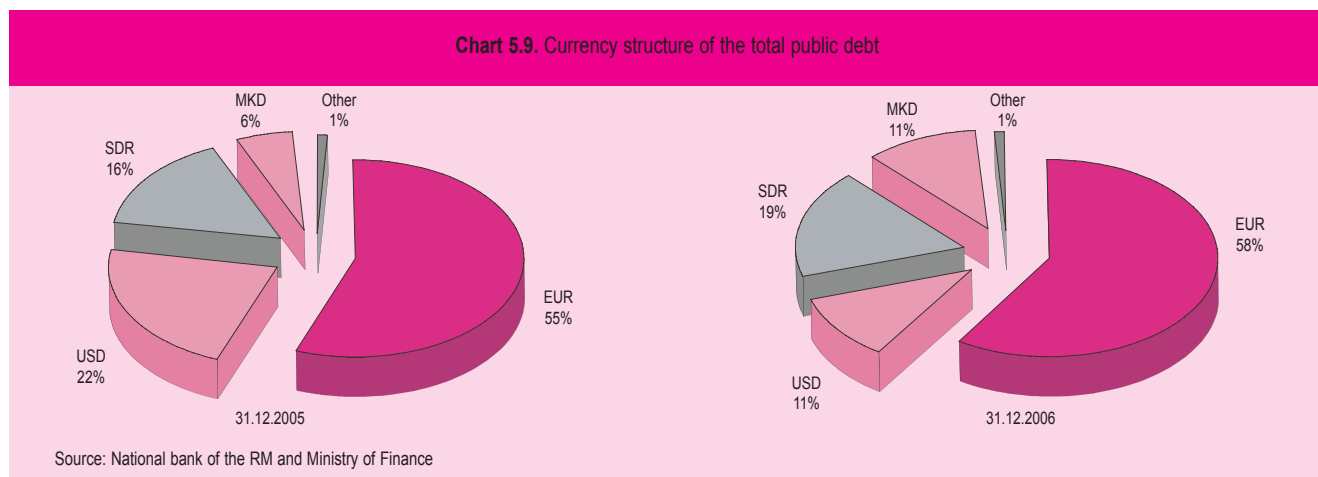
	date	
	31/12/2005	31/12/2006
<b>EXTERNAL PUBLIC DEBT</b>	<b>1441.2</b>	<b>1223.0</b>
General government debt	1245.4	1025.2
Central government	52.7	42.4
Public enterprises	143.2	155.4
<b>DOMESTIC PUBLIC DEBT</b>	<b>750.4</b>	<b>804.9</b>
General government debt	603.7	648.4
Treasury bills for monetary purposes	0.0	75.9
Central Bank	146.7	155.3
Public enterprises	N/A	1.2
<b>TOTAL PUBLIC DEBT - GFS</b>	<b>2191.6</b>	<b>2027.9</b>
Total public debt as % of GDP	47.2	40.7
<b>General government debt - GFS</b>	<b>1849.0</b>	<b>1673.6</b>
General government debt as % of GDP	39.8	33.6
<b>Total public debt calculated pursuant to the Law on Public Debt</b>	<b>1992.2</b>	<b>1830.3</b>
Total public debt as % of GDP	42.9	36.8

Source: Ministry of Finance and National bank of the RM

7) Indirect taxes participated with 14.7% in GDP, while the share of direct taxes was 4.8%.

debt amounted to 64.5% and 35.5%, respectively where the share of the domestic public debt grew by 5.2 percentage points from 2005. This change was mainly due to the development of the domestic financial market, as well as the issuance of treasury bills for monetary purposes, which the Ministry of Finance started in March 2006.

With regard to the interest structure, favourable changes in the total public debt were observed in the course of 2006. In fact, pursuing the goal of the Public Debt Management Strategy, external public debt with fixed interest rate increased as a result of the buyback of the debt towards the London Club of Creditors in January 2006 (debt with floating interest rate) by issuing Eurobond (debt with fixed interest rate). Thus, the share of the debt with fixed interest rate in the total public debt grew from 50.5% at the end of 2005 to 58.6% on 31st December 2006.



Positive changes were also registered in the currency structure of the public debt (shown on Chart 5.9.) aimed at increasing the share of the public debt in domestic currency and the Euro-denominated debt. Thus, as a result of the buy-back and increased issuance of government securities and treasury bills for monetary purposes by the end of 2006, Euro- and Denar-denominated debt grew by 3.2 and 5.3 percentage points, respectively, compared to 2005.

**Box 5.2. Foreign exchange exposure of the public debt of the Republic of Macedonia**

*Public debt in each country is denominated in several currencies, whereby it is expected that the currency of the main trade partner of the country will have the dominant share in the public debt. Analysis of the foreign exchange exposure of the public debt is important for the economic policymakers since it provides information on the level of indebtedness of the country (less or more indebted), if one or several currencies in which the public debt is denominated depreciate/appreciate.*

*Total public debt, observed according to the currency structure, can be expressed in the following way:*

$$p_i = \sum \text{nom}_j * e_{ij} \quad (1)$$

*where  $p_i$  stands for the public debt denominated in domestic currency,  $\text{nom}_j$  is the nominal value of the debt in currency  $j$ , and  $e_{ij}$  is the exchange rate of the domestic currency in relation to the currency in which the debt is*

denominated. Interest rate is excluded from the calculation, in order to emphasise the foreign exchange rather than the interest rate exposure of the public debt of the country. Alternatively, in the equation above, the nominal value can be substituted by the share of the public debt ( $s_j$ ), denominated in the respective currency.

$$p_i = \sum s_j * e_{ij} \quad (2)$$

Having the above-mentioned elaboration as a starting point, currency structure of the public debt of the Republic of Macedonia can be expressed in the following manner:

$$p_{MK} = s_{\epsilon} * e_{MKD/\epsilon} + s_{\$} * e_{MKD/\$} + s_{SDR} * e_{MKD/SDR} + s_{MKD} \quad (3)$$

Taking into consideration that analysing the foreign exchange exposure means how much the value of the public debt is responsive to the exchange rate change, the equation (3) should take into consideration changes of the included variables. That can be achieved with differentiation by both parts, and the following is obtained:

$$\Delta p_{MK} = s_{\epsilon} * \Delta e_{MKD/\epsilon} + s_{\$} * \Delta e_{MKD/\$} + s_{SDR} * \Delta e_{MKD/SDR} + s_{MKD} \quad (4)$$

The equation clearly shows that if one of the foreign currencies included in the public debt structure in the Republic of Macedonia depreciates, public debt of the Republic of Macedonia will decrease in proportion to the share of that currency in the public debt structure, and vice versa.

If the shares of the different currencies in the public debt structure in 2006 are inputted in this equation, the following will be obtained:

$$\Delta p_{MK} = 0,5882 * \Delta e_{MKD/\epsilon} + 0,1082 * \Delta e_{MKD/\$} + 0,1851 * e_{MKD/SDR} + 0,1104 \quad (5)$$

Due to the de facto fixed Denar exchange rate in relation to the Euro, as well as the currency composition of SDR, equation (5) can be expressed in the following form:

$$\Delta p_{MK} = 0,1082 * \Delta e_{MKD/\$} + 0,1851 * \Delta e_{MKD/SDR} \quad (6)$$

which points out that the foreign exchange exposure of the public debt in the Republic of Macedonia refers to the value of the US dollar and the SDR. If one takes into consideration that the SDR draw their value from the US dollar, Japanese yen, pound sterling and euro, than the following equations can be obtained:

$$\Delta p_{MK} = 0,1082 * \Delta e_{MKD/\$} + 0,1851 * \Delta e_{\$/SDR} * \Delta e_{MKD/\$} \quad (7)$$

$$\Delta p_{MK} = 0,1082 * \Delta e_{MKD/\$} + 0,1851 * (0,41 \Delta e_{\$/\epsilon} + 18,4 * \Delta e_{\$/\square} + 0,0903 * \Delta e_{\$/\square} + 0,6323 * \Delta e_{\$/\$}) * \Delta e_{MKD/\$} \quad (8)$$

$$\Delta p_{MK} = 0,1082 * \Delta e_{MKD/\$} + 0,0759 * \Delta e_{MKD/\epsilon} + 3,4058 * \Delta e_{MKD/\square} + 0,01671 * \Delta e_{MKD/\square} + 0,117 * \Delta e_{MKD/\$} \quad (9)$$

We exclude the euro term again, and the following equation is obtained:

$$\Delta p_{MK} = 0,2252 * \Delta e_{MKD/\$} + 3,4058 * \Delta e_{MKD/\square} + 0,01671 * \Delta e_{MKD/\square} \quad (10)$$

This is the final representation of the currency exposure of the public debt of the Republic of Macedonia with a structure as of 31st December 2006. The equation should serve to calculate how much the country would have to pay if the value of the currencies on the global foreign exchange market changes.

For instance, if the value of the US dollar in relation to the Denar drops (depreciates) by Denar 1 (i.e. the value of 46.4496 on 31st December 2006 depreciates to 45.4496 on 31st December 2007), under the assumption that the value of the yen and the pound in this period remains unchanged, and assuming that the structure of the public debt remains unchanged, the value of the public debt would be reduced by:

$$\Delta p_{MK} = 0,2252 * (46,4496 - 45,4496) / 46,4496$$

$$\Delta p_{MK} = 0,2252 * (-0,02153)$$

$$\Delta p_{MK} = -0,004848556$$

$$\Delta p_{MK} = -0,48\%$$

The SDR structure, as well as the shares of the individual currencies when deriving the value of SDR, are taken from [www.imf.org](http://www.imf.org).

Sovereign guarantee is a contingent liability of the country for a payment undertaken on behalf of the public debt issuer, for the account of which the guarantee is being issued. Stock of guaranteed public debt as of 31st December 2006 inclusive amounted to EUR 144.6 million, i.e. 2.9% of GDP and 7.9% in relation to total public debt. The debt slightly increased by 5.55% compared to December 2005. ELEM (72.88%), MBDP (12.42%), MEPSO (8.73%) and Macedonian Railways (4.6%) accounted for the most in the guaranteed public debt.

Issuance of government securities related to public debt was carried out on the basis of certain criteria, whereby special attention was paid to the public enterprises, which often faced liquidity problems.

Total new borrowing amounted to EUR 153.2 million in 2006, and when compared to 2005, it declined by 45.16%. Such decline was mainly due to the issuance of the Eurobond in the amount of EUR 150 million at the end of 2005, but also to the stipulation of the maximum amount for new borrowings pursuant to the Public Debt Strategy.

On the basis of domestic public debt, the new net borrowing amounted to EUR 67 million in 2006, which was due to the increase of the debt on the basis of issued structural bonds (fifth issue of denationalisation bonds) and increased issuance of continuous securities. Regarding maturity, Table 5.2. shows decrease of the borrowing only for the three-month treasury bills by EUR 12.5 million, while regarding the longer-term securities, the borrowing increased, in line with the goals in the Strategy to increase both the domestic public debt maturity and Denar-denominated borrowing.

**Table 5.2.** Net issuance of continuous government securities and structural bonds (EUR million) in 2006

	Jan-06	Feb-06	Mar-06	Apr-06	May-06	Jun-06	Jul-06	Aug-06	Sep-06	Oct-06	Nov-06	Dec-06	Total 2006
Total issued													
government securities	2.25	2.78	32.40	-4.61	8.31	3.20	-4.80	-2.83	8.33	11.73	4.46	5.86	67.08
3-month TB	-0.67	0.58	-5.58	-3.18	0.30	-1.60	-5.61	-4.82	4.02	2.41	-0.81	2.41	-12.54
6-month TB	2.92	2.20	3.18	-1.43	3.96	1.60	0.81	1.99	-0.19	4.46	0.80	1.57	21.87
12-month TB			5.25			3.19			4.50			1.88	14.82
2-year GB					4.05					4.86			8.91
3-year GB											4.47		4.47
5th issue of denationalisation bond				29.55									29.55

Source: Ministry of Finance

Regarding the external debt, total of EUR 86.1 million was disbursed on the basis of concluded credits in 2006, EUR 48.6 million out of which were general government debt, and EUR 32.5 million were debt of the public enterprises. Most of the disbursements by the general government or 77% were from multilateral creditors (mainly EBRD and MBDP), while the rest of the disbursements were from bilateral creditors (Italian credit line for import of equipment, Bank of Bilbao, ICO-Spain, JIBC-Japan and KFW-Germany). Most of the disbursements by the public enterprises were from the private creditor DERNA Bank to AD ELEM (65%), and 35% were from multilateral creditors.

**Government securities.** Comparative analysis of the fluctuations of the interest rates on government securities (GS) in 2005 and 2006 points to a downward trend of interest rates at all maturities (see Chart 5.10.). Illustratively, weighted interest



**Table 5.3.** Disbursements on the basis of concluded credits in 2006 (EUR million)

	Realized	Realized	Realized	Realized	Total 2006	Projected	Difference (projected- actual)
	disbursements	disbursements	disbursements	disbursements		disbursements according	
	Q-1	Q-2	Q-3	Q-4		to Public debt Management Strategy	
Public sector	8.3	15.2	29.5	33.1	86.1	131.7	45.6
Government of the Republic of Macedonia	4.3	15.1	18.0	11.2	48.6	91.9	43.4
Multilateral creditors	2.7	11.9	14.6	7.961	37.2	68.5	31.3
IBRD/IDA	1.2	4.9	3.6	2.23	12.0	30.3	18.3
CEDB	0.0	1.7	0.0	0.0	1.7	3.5	1.8
EIB	0.0	0.0	5.0	0.0	5.0	13.7	8.7
EBRD	1.3	4.8	4.8	5.3	16.2	13.1	-3.2
EU	0.0	0.0	0.0	0.0	0.0	0.0	0.0
IFAD	0.2	0.5	1.1	0.5	2.3	2.0	-0.3
Bilateral creditors	1.6	3.2	3.4	3.3	11.4	23.5	12.1
Private creditors	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Public enterprises	4.0	0.1	11.6	21.9	32.5	39.8	7.3
Multilateral creditors	4.0	0.1	2.8	9.578	11.5	29.5	18.0
IBRD	0.0	0.1	1.0	0.12	1.3	3.2	1.9
EIB	4.0	0.0	0.0	3.5	7.5	3.3	-4.2
CEDB	0.0	0.0	0.0	5.0	5.0	3.5	-1.5
EBRD	0.0	0.0	1.8	1.0	2.8	23.0	20.2
Bilateral creditors	0.0	0.0	0.0	0.0	0.0	7.7	7.7
Private creditors	0.0	0.0	8.7	12.3	21.0	2.6	18.4

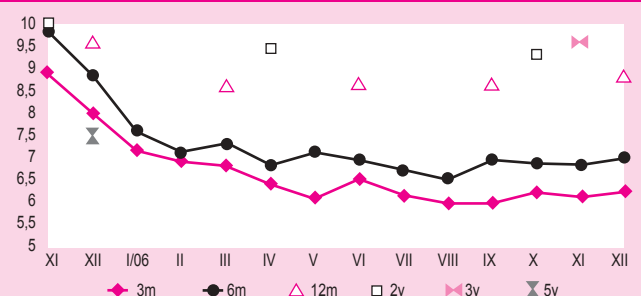
Source: Ministry of Finance and National bank of the RM

rate on 3-month treasury bills on the auctions in December 2005 amounted to 8.00%, while the interest rate on the auctions the same month in 2006 amounted to 6.26%. The trend of fluctuation of interest rates was identical at the other GS.

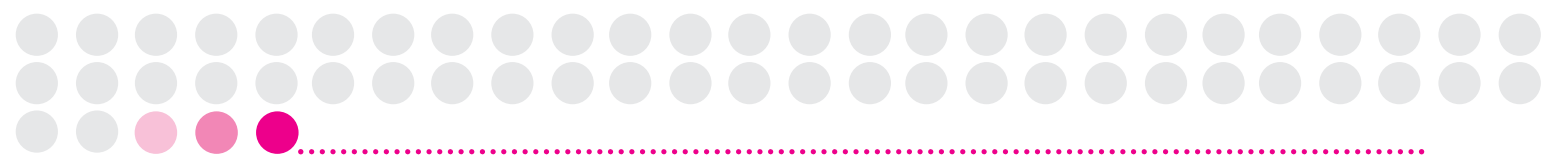
On 23rd November 2006, the Ministry of Finance issued a three-year government bond for the first time, whereby weighted yield of 9.621% was attained on the auction. Such weighted yield was by 0.30 percentage point higher than the one on the 2-year government bond. Regarding the ownership structure, banks had a dominant share of 80%, while the non-banking entities, with significant share of the pension companies in the realised part of the auction, accounted for the rest.

Ownership structure of the continuous government securities shows an increase in the share of banks by 41% at the end of 2005, and by 78% at the end of 2006. This increase was mainly due to the commencement of the issuance of treasury bills for monetary purpose.

**Chart 5.10.** Weighted interest rates achieved at auctions of government securities



Source: Ministry of Finance





## 6. MONETARY SECTOR

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### 6.1. Monetary trends

The monetary policy in 2006 was aimed at maintaining the stability of the Denar exchange rate in relation to the euro, in conditions of significant excess of supply of foreign currencies on the foreign exchange market. In fact, upward trend of foreign currency inflows continued, which combined with the banks' policy for more active usage of foreign currencies on the domestic market, enabled significant net purchase of foreign currencies on the foreign exchange market by the NBRM.

In 2006, monetary policy was also based on active coordination with the other segments of the macroeconomic policy, contributing to the maintenance of consistent macroeconomic framework. Reforms aimed at stimulation of transactions among the banks and further development of the financial market continued, thus improving the monetary transmission function. The NBRM reduced the frequency of the auctions of central bank bills from twice to once a week, reducing its participation on the primary market. This measure is compatible with the introduction of the three-month treasury bills for monetary purposes, which should gradually crowd out the treasury bills.

At the end of 2006, total liquid assets of the banks amounted to Denar 8,685 million and were higher by 44% on annual basis. Dynamics of the primary money was influenced by the demand for cash and the total liquidity in the banking system. Level of primary money amounted to Denar 31,264 million at the end of 2006, being an increase by 21.3% compared to 2005.

Trend of primary money in the course of the year depended on the seasonal effects, i.e. the increased demand for cash during the holiday and the summer vacations, their exhaustion on the basis of the decreased demand for cash in certain period of the year, as well as the dynamics, i.e. the increase and the decrease of the level of liquidity in the banking system.

In 2006, dynamics of the monetary growth was under the influence of strengthened economic activity, further growth of the foreign exchange inflows and the downward trend of the interest rates. M1 money supply amounted to Denar 34,733 million and it increased by 17% on annual level. Lower annual increase of ready money in circulation in relation to deposit money resulted in positive deviations in the structure of M1 money supply. Thus, the share of ready money in circulation in the money supply amounted to 46.6% at the end of 2006, being an annual drop of 2.1 percentage points.

In the course of the year, trends of the cash were in line with the regular seasonal dynamics, and at the end of 2006, the cash showed an increase by 12.2% compared to 2005.

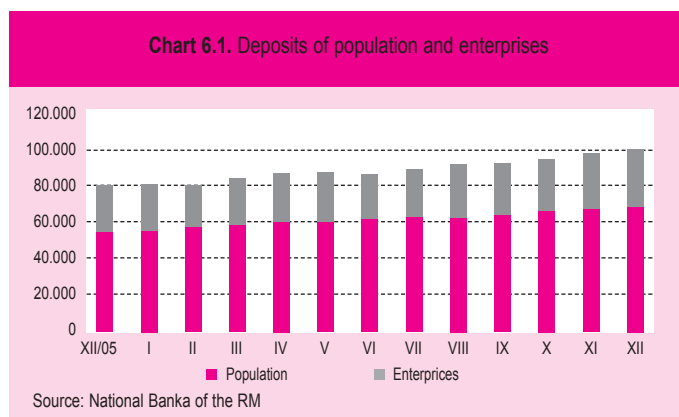
Total deposit money (current and giro accounts) increased by 21.1% at the end of 2006, in conditions of simultaneous increase of the deposit money of the enterprises and the population. From structural point of view, share of the deposit money of enterprises in the total deposit money amounted to 69.5% at the end of 2006, being an increase by 2.8 percentage points on annual basis.

Trend of the broader monetary aggregates was determined by an increase in the M1 monetary aggregate as well as of the total deposit potential of the banks.

M2 money supply amounted to Denar 128,479 million at the end of 2006, being an annual increase by 24.5%. Thereby, the Denar component of M2 money supply increased by 49%, mostly determined by the higher level of short-term deposits in domestic currency. M4 monetary aggregate (M2 money supply, limited and long-term time deposits) increased by 24.9%, and reached the level of Denar 136,117 million at the end of the year.

## 6.2. Total deposits

Total deposits of the non-government sector (sight deposits up one year and over one year) showed permanent increase, due to the strengthened saving orientation of the economic entities. Total deposits in the banking sector reached the level of Denar 100,384 million at the end of 2006, being an annual increase by 27.8%.



From currency point of view, increase was registered in Denar and foreign exchange deposits, and their dynamics was generated by the oscillations of the short-term deposit potential. Denar deposits increased on annual level by 45.6%, along with the increase of the short-term and long-term deposits by 49.1% and 18.7% respectively.

Regarding the sectoral structure, shifts were registered in terms of increasing the share of enterprises in line with the possibility for free disposal of foreign currencies by the legal entities, and declining share of household deposits. At the end of 2006, the share of household deposits in total deposits amounted to 67.1%.

Total deposits of enterprises increased with an annual rate of 38.5%, reaching the level of Denar 15,269 million, whereas Denar deposits followed the same growth of 38.5%.

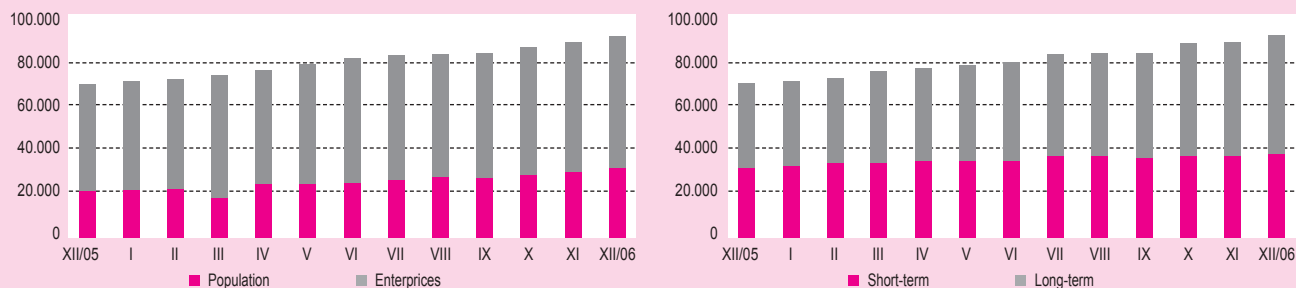
## 6.3. Credits of banks

Under conditions of intensified crediting to private sector both in domestic and foreign currency, total credits of the banks to the private sector reached the level of Denar 89,780 million at the end of 2006, which, compared to 2005, was an increase by 30.5%. Total Denar credits towards the private sector increased by 28.5% compared to 2005 reaching the level of Denar 66,413 million, while the foreign currency credits realised an increase of 36.6% and equalled Denar 23,366 million. This increase was generated by the more intensified crediting to the enterprises and the enforced banks' orientation towards short-term and long-term crediting to the households. This caused shifts in the maturity structure of the Denar credits, to the end of increase of the share of the approved long-term credits by 36.9%. Long-term Denar credits on average increased by 46.1%, specifically, long-term crediting to enterprises increased by 50.5% and to households by 36.2%.

Annual increase of approved short-term credits was more modest and amounted to 7.3%, though their share in the maturity structure of the Denar credits continued to be dominant and amounted to 63.1%.

Regarding the maturity structure of Denar credits to enterprises, long-term credits (73%) kept their dominant position, while with respect to Denar credits approved to enterprises, short-term credits accounted for most (61.6%).

Chart 6.2. Credits by purpose and maturity



Source: National bank of the RM

## 6.4. Interest rates

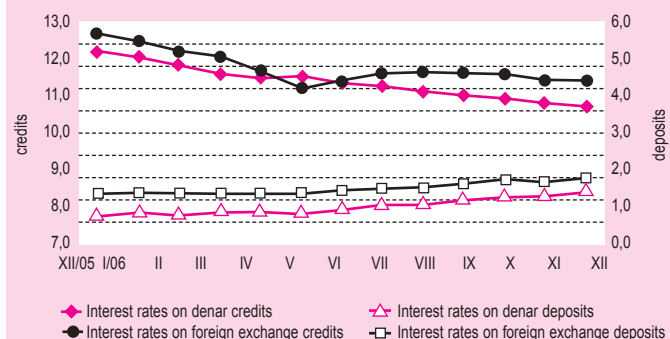
In the course of 2006, several changes in the position of the auctions of the treasury bills were made, which caused decline of the weighted interest rate on treasury bills, being the reference interest rate in the national economy. Interest rate on the CB bills amounted 5.7% at the end 2006, which was by 3.3 percentage points lower than the level at the end 2005.

Weighted interest rates on Denar credits showed continuous decline and they amounted to 10.7% at the end of 2006, compared to 12.1% in 2005, whereas interest rates on foreign exchange credits amounted to 8.5% at the end of 2006. Interest rates on Denar deposits amounted to 4.4% at the end of 2006, i.e. declined by 1.6 percentage points compared to the end of 2005, while interest rates on foreign exchange deposits amounted to 1.8%.

At the same time, in 2006, Central Bank interest policy was aimed at continuous decline of interest rates. Multiple declines of interest rates on Lombard credits were carried out. Thus, discount rate remained the same as in 2005 and amounted to 6.5% whereas the interest rate on Lombard credits was reduced to 9.5% from 13.0% in 2005.

Positive trend in terms of reduction of interest rates of banks reflected the favourable effects from the reform process in the banking sector and indicated a gradual movement of the monetary policy transmission canal through interest rates.

Chart 6.3. Interest rates of commercial banks



Source: National bank of the RM

### Box 6.1. Republic of Macedonia and the criteria for acceptance of euro as a part of EMU

Republic of Macedonia is a small and open economy with a de facto fixed foreign exchange rate in relation to the euro. The result from the strategy of targeting the exchange rate is the established and maintained macroeconomic stability in the economy, expressed through low inflation, stable level of exchange rate and trend of decline of interest rates (so-called convergence of interest rates in the Republic of Macedonia with those from the Euro zone). Also, these trends were supplemented with a disciplined fiscal policy.

An analysis of the fulfilment of the criteria for acceptance of the euro as part of the European Economic and Monetary Union (EMU) is of great importance for the economic policy in Macedonia. Economic convergence of an EU member state regarding the acceptance of the euro is assessed by four criteria: price stability, sound fiscal position, exchange rate stability and converging interest rates. In particular, the country, which is in the process of monetary integration with the Eurozone, should have:

- sustainable price stability, meaning its average annual inflation rate not to exceed 1.5 percentage point over the average rate of the three countries with the lowest inflation;
- sustainable fiscal position, meaning planned or current fiscal deficit that does not exceed 3% of GDP;
- public debt that does not exceed 60% of GDP;
- exchange rate stability (ensured through membership in ERM II), in a period of at least 2 years prior to the membership in EMU, without pressures for devaluation of the domestic currency in relation to the euro or any other currency of a member state;
- converging long-term interest rates, as a result of the membership in ERM II, defined as an average nominal interest rate of 5- or 10-year government or corporate bond that does not exceed 2 percentage points compared to the one of the three EMU member states with the lowest inflation.

On the basis of such defined economic criteria, analysis of fulfilment of the criteria by the Republic of Macedonia is given in the table below:

Criterion	Met
1. Price stability	
- three countries with the lowest inflation in 2006	
Finland 1.3%	
Austria 1.7%	
The Netherlands 1.7%	
average 1.6% + 1.5 p.p. = 3.1%	
- inflation rate in the Republic of Macedonia in 2006 was 3.2%	X
2. Fiscal position	
- fiscal deficit/GDP = 0.5%	
- public debt/GDP = 36.8%	✓

3. Exchange rate

- pegged to the euro (Deutsche mark) since October 1995



4. Long-term interest rate

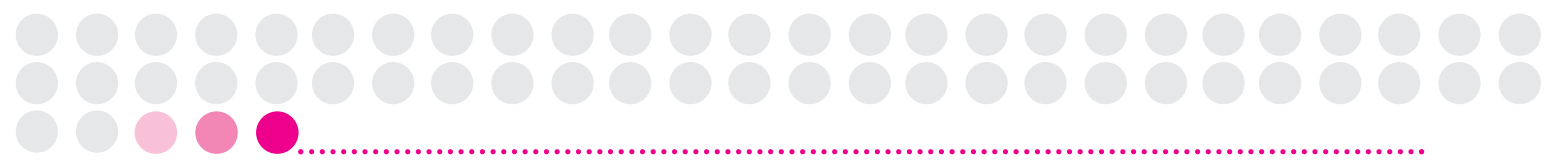
- long-term government bond (10-year) - average rate in the three countries

with the lowest inflation -  $3.9\% + 2 \text{ p.p.} = 5.9\%$

- long-term government bond (3-year)\* - Republic of Macedonia 9.6%



\* Bond with the longest maturity period issued in 2006 was with a 3-year maturity. Hence, the comparison is partly inappropriate.





## 7. FINANCIAL SYSTEM

### 7.1. Banking

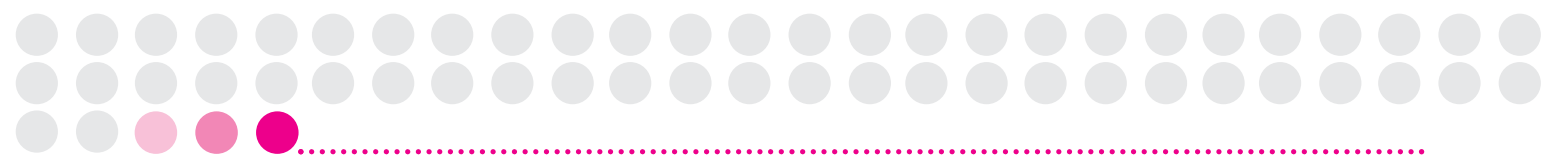
Taking into consideration that the banks dominate the financial sector in the Republic of Macedonia and that they represent the largest source of credits in the economy, the restructuring of the banking sector is priority in the financial reforms. The sector underwent deep changes in the last years in order to adjust to the competitive market conditions. Unlike many countries in transition, which faced banking crises in the second half of the 90s, the Republic of Macedonia avoided them successfully. Crises were also avoided in the recent past, when the country was affected by strong non-economic shocks, such as the Kosovo crisis in 1999 and the crisis caused by the internal conflict in 2001.

On 31st December 2006, banking sector in the Republic of Macedonia composed 18 universal private banks, one state-owned bank having specific functions as a result of which it is not a competition to the commercial banks, and 12 saving houses. From the ownership structure point of view, share of state-owned banks was below 5% in the total capital of the banking system, while foreign capital was present in 17 banks. In 8 banks out of these 17 banks, foreign owners presented the shareholder majority; their share amounted to 50.0% in the total capital i.e. 53.2% in the total assets of the banking sector. Four out of these 8 banks were branch offices of foreign banks. During 2005 and 2006, there was increased interest by certain eminent international banks to enter certain banks in the Republic of Macedonia.

On 31st December 2006, the level of financial intermediation, that is the ratio between total assets, gross credits and total deposits and GDP of the Republic of Macedonia, increased and amounted to 57.4%, 29.6% and 41.4%, respectively. For comparison purposes, on 31st December 2005, these indicators amounted to 49.4%, 24.2% and 34.5%, respectively. However, the level of banking intermediation in the country is still very low, if compared to the level in Central European countries, which recently became EU member state. On 31st December 2005, financial intermediation, calculated as ratio between total assets and GDP, amounted to 95.4% in Slovenia, 62.5% in Poland and 106.6% in the Czech Republic. Though, on 31st December 2006, the level of financial intermediation (expressed as ratio between assets and GDP) in the Republic of Macedonia was higher than the respective level in Romania (51.2%), which became an EU member state in 2007. As of 31st December 2006 inclusive, total assets of the banks in the Republic of Macedonia amounted to Denar 174.1 billion, while their capital amounted to Denar 22.3 billion.

Performance of the banking sector in the Republic of Macedonia was quite favourable showing an upward trend. Confidence in the banking sector increased, which reflected in an increase of savings and total deposits in the banks. At the end of 2006, deposit base in the banks reached the amount of Denar 125.3 billion and increased by 27.9% compared to the 31st December 2005. Positive performance of the Macedonian banking sector also reflected in its profitability indicators. For instance, in 2006, the sector achieved positive financial results in the total amount of Denar 2.8 million, with a rate of return on assets (ROA) of 1.8% and rate of return on equity (ROE) of 12.3%.

Strengthening of the banking supervision capacity had an important role in the increase of the banking sector stability. The NBRM, as an authority authorised for licensing and supervision of banks, executes its role on the basis of



the provisions prescribed in the Law on National Bank and the Banking Law. Activities of the National Bank in the area of strengthening the banking supervision were aimed at implementing the new Banking Law, which, will be adopted in the first half of 2007, as well as at successful implementation of the adopted Plan for Risk-Oriented Supervision. The new Banking Law will contribute to further strengthening of the shareholders criteria (prior approval for acquiring qualified participation in a bank, envisaging the possibility for the NBRM to revoke the previously given approval, as well as introducing the possibility for the National bank to sell the shares of a shareholder who does not meet the shareholders criteria anymore or who acquired qualified participation without prior approval by the NBRM); strengthening of the safeguarding measures which the NBRM can undertake towards a bank; and increasing the efficiency of the procedure for the exit of a bank from the banking system. The Law will also provide for further strengthening of prudent standards, promotion of the corporate management of banks through strengthening the role and the responsibilities of the management bodies, internal control systems, the role of the external auditor, greater transparency when performing financial activities, strengthening the accounting standards, etc. The new Law will specify the types of risks which the banks are exposed to, and it will provide for a step forward towards approaching the New Basel Accord through the provisions on strengthening the market discipline of the banks, as well as the provisions on risk management according to the type and the scope of the bank's activities.

Although the quality of the assets and the financial results of the Macedonian banks significantly improved during the recent years, still the banking sector in the country faces numerous actual and potential challenges. What is common for the banks is that they lack activities for restructuring of the banks, which are necessary for their effective adjustment to the challenges related to the EU accession, and in general, to the challenges from the global liberalisation of the financial services. In addition to competitiveness, further improvements are also necessary in the area of deepening the banking sector. Apart from the progress during the past years, the sector should additionally develop when compared with the Central and Eastern European countries that have recently become an EU member states.

On 31st December 2006, the share of monetary aggregates M1 (short definition) and M2 (broad definition of the money supply) in GDP amounted to 11.5% and 42.4%, respectively. When compared to last year, the share of money supply M1 increased by one percentage point, which indicates a relatively stable level of transactional money demand, while the share of the broader money supply increased by around 6 percentage points, showing gradual deepening of the economy monetisation level. For comparison purposes, average share of monetary aggregates M1 and M2 in GDP regarding the ten new EU member states amounted to 34.1% and 67.2%, respectively at the end of 2005 (last available data). However, the two new member states joining the EU in 2007 - Bulgaria and Romania had lower average share, which amounted to 19.2% and 45.3% for M1 and M2, respectively.

On 31st December 2004, most of the credits to enterprises were short-term with a share of 40.2% in the gross credits to enterprises, while the share of long-term credits to enterprises amounted to 36.7%. However, starting 30th June 2005, long-term credits to enterprises became dominant category participating with 41.6% in the gross credits to enterprises, while the share of short-term credits amounted to 37.9%. On 31st December 2006, long-term credits to enterprises remained on and kept their dominant position, participating with 51.1% in the gross credits to enterprises, while the share of the short-term credits amounted to 32.6%.



## 7.2. Leasing

Since the adoption of the Law on Leasing in February 2002, the Ministry of Finance issued licenses for performing financial leasing to 10 companies. Only 3 out of the companies having obtained this license were active in 2006, whereby the following data cover 2 companies, taking into consideration the fact that the third active company for financial leasing began its activities on 30th November 2006. Total assets of the active leasing companies on the basis of audited financial statements as of 31st December 2005 amounted to Denar 2,275,518,000, while the total capital on the basis of audited financial statements amounted to Denar 121,577,000. There were 4,947 active agreements on financial leasing as of 12th September 2006, with the total amount of Denar 4,744,910,000.

The share of leasing companies in the total assets of financial institutions, as well as in the gross domestic product, was below 1%, which reflects their marginal role on the market.

## 7.3. Capital market

Autonomous and independent body regulating and performing supervision on all participants on the Macedonian capital market is the Securities and Exchange Commission, established in 1992, which is a member of the International Organisation of Securities Commission (IOSCO) since 1994. Securities and Exchange Commission is responsible for the efficient operations of the capital market, protection of investors' rights and promotion of capital market confidence.

Trading realised on the Macedonian Stock Exchange on 31st December 2006, excluding the trading through block transactions and the government auctions, amounted to EUR 176.4 million or Denar 10,794 million, which, compared to 2005, was an increase of 61.1%. This increase was due to the increased interest of foreign investors for investing in securities, increased transparency in the public announcement of financial data of the listed companies, the sale of shares of part of the listed companies below their nominal value, and increased public interest of the domestic population in investments in shares.

At the end of 2006, trading realised through sale of government bonds for the old foreign exchange saving and denationalisation amounted to Denar 2,229 million or EUR 36.4 million, being an increase of 8.4% compared to the realised trading of government bonds in 2005.

As of 31st December 2006, 43 companies were listed on the Macedonian Stock Exchange, with market capitalisation of EUR 833.7 million, being an increase of 53.8% compared to 2005.

At the end of 2006, total market capitalisation of shares, government bonds and publicly owned companies amounted to EUR 1.7 billion, being an annual increase of 46.4%.

Macedonian stock exchange index (MSEI-10) amounted to Denar 3,702.54 or EUR 61 on 31st December 2006, i.e. an annual increase of 61.5%.

The average share of foreign investors in the trading realised during buying on the Macedonian Stock Exchange amounted to 28.7% in 2006, while their average share in the trading realised during selling on the Macedonian Stock Exchange amounted to 6.6%.



## 7.4. Foreign exchange system

The Law on Foreign Exchange Operations and bylaws thereof regulate foreign exchange operations between residents and non-residents, current transactions, as well as the regime of the capital movement. The Law is fully in line with the Stabilisation and Association Agreement (SAA) with the European Union, i.e. it incorporates the time framework on capital liberalisation. In fact, current transaction between residents and non-residents are fully liberalised, which is in line with the SAA. The Law enables for full liberalisation of capital transactions envisaged in the first stage of SAA implementation (direct investments, commercial credits and financial loans with a maturity period of over 1 year). The Law also provides for liberalisation of financial credits with a maturity period shorter than 1 year, which should be implemented in the second stage of the SAA implementation. Portfolio investments are partially liberalised, while their full liberalisation is envisaged after completion of the first stage of the SAA. In addition, liberalisation of investments in the real estate of residents living abroad should follow after the first stage. Regarding deposit activities, non-residents can open foreign exchange and Denar accounts with Macedonian banks and they can freely manage the funds, while the domestic enterprises and the citizens can freely open foreign exchange accounts with foreign banks after the second stage of SAA is completed. Transfer of profit and invested capital at direct investments are free, provided that non-residents have registered the direct investments pursuant to the Law and settled all legal liabilities on the basis of taxes and contributions.


Intention of the Law on Foreign Exchange Operations is to stimulate economic entities towards a larger volume of transfer of foreign exchange inflows in the domestic banks, better competitive position of enterprises on the foreign markets, simplification of the procedures for conclusion of credit-related operations and performing payment operations with abroad, as well as of transfer of funds from and abroad. At the same time, the Law provides for greater safety and transparency for foreign investors and increases their interest in investing in direct investments and in domestic securities.

## 7.5. Insurance

At the end of 2006, insurance market in the Republic of Macedonia consisted of 10 insurance companies, eight out of which performed activities of non-life insurance, one performed activities of non-life insurance and reinsurance, and one performed activities in the group of life insurance. 5 insurance brokerage companies operated on the insurance market, which performed activities related to the insurance intermediation. At the end of 2006, the share of foreign capital (legal persons) in total equity capital of insurance companies amounted to 62.5%. Four insurance companies were fully established with foreign capital.

Total gross calculated premium amounted to Denar 5,445 million in 2006. Market concentration, measured according to the share of the three largest insurance companies in the total gross calculated premium, was constantly declining and it amounted to 66.2% at the end of 2006. Life insurance participated with only 2.12% in the total written premium.

Increase in the number of entities on the insurance market in the period from 2002 to date, through increased competition, did not significantly influenced the enlargement of the offer of insurance products, improvement of the premium structure and improvement of the quality of insurance services. Measured according to the EU standards, insurance remained relatively underdeveloped, both in terms of premium and in terms of its structure. This was confirmed



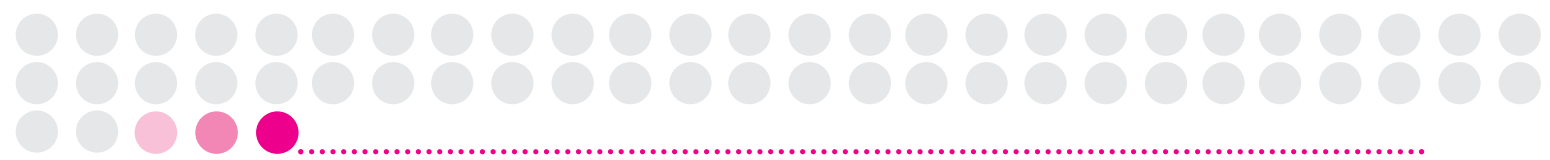
by the fact that the share of the motor TPL insurance (compulsory insurance) amounted to 46% in the totally calculated premium, followed by the property insurance participating with 24% in the total premium.

Basic legal framework that regulates the terms and conditions and the manner of performing insurance activities, carrying out supervision over the operation of insurance companies, insurance brokerage companies and the National Insurance Bureau comprises the Law on Insurance Supervision (Official Gazette of the Republic of Macedonia, no. 27/02, 84/02, 98/02 and 33/04) and the Law on Compulsory Insurance in Traffic (Official Gazette of the Republic of Macedonia, no. 88/05).

Ministry of Finance of the Republic of Macedonia is a body in charge of the adoption of legal regulations in the field of insurance and carrying out supervision over the operations of insurance companies, insurance brokerage companies and the National Insurance Bureau.

Ministry of Finance puts ever stronger accent on larger and more efficient implementation of the legal regulation in order to provide financially stable and sustainable development of the insurance market on the long run in the country, which will enable efficient integration of domestic insurance entities in the European market in 2006 and in the course of 2007, by the means of:

- establishment of a supervisory body in the insurance area, as well as an independent and autonomous surveillance institution with public authorisations delegated by law, in line with the principles and standards of the International Association of Insurance Supervisors (IAIS);
- adoption of bylaws arising from the Law on Insurance Supervision, aimed at detailed regulation of risk management measures, as well as of the methods and procedures of carrying out supervision;
- promotion of the methods and procedures of carrying out supervision to the end of developing a modern supervision and control system, aimed at permanent monitoring of the operations of insurance companies, from the point of view of their exposure to risks and undertaking preventive and corrective measures, as well as transfer from supervision based on compliance with the regulations to risk-based supervision.
- strengthening the administrative capacity of the supervisory body through permanent education of supervisors and the insurance industry, to the end of full understanding of the process of risk management and application of adequate corporate governance.



## 8. SOCIAL SECTOR

### 8.1. Labour market

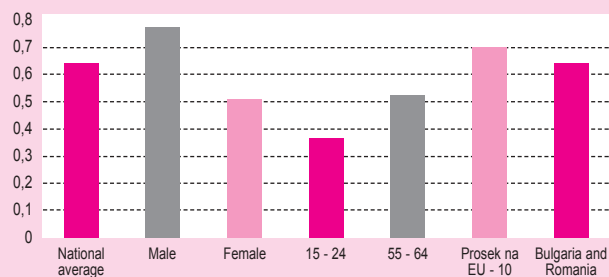
General characteristics of the labour market in the Republic of Macedonia include low rate of activity, high and persistent unemployment, as well as relatively low employment rate. Although in 2006 there was a slight improvement of the labour market situation, the Republic of Macedonia, with an unemployment rate of 36% in 2006, remains a country with the highest unemployment among all Central and Eastern European countries, except Bosnia. (Data on the labour market in the Report are from the Labour Force Survey (LFS), if not otherwise indicated). Detailed analysis of the labour market in the Republic of Macedonia, i.e. analysis of certain characteristics of employment and unemployment (for instance, age structure, gender, duration of unemployment, education structure, etc.) points out that the poor performance of the labour market is caused by structural, rather than transitional factors. Certainly, this has implications on the policies necessary for resolving the unemployment problem. In fact, coordination of different policies is necessary, starting from the core employment policy or active labour market policies, to the broader macro and micro policies and reforms to be aimed at acceleration of the growth and employment encouragement.

#### 8.1.1. Activity

Relatively low activity or participation in the labour market in the Republic of Macedonia (62.2% in 2006)<sup>8</sup> reflects the very low level of employment in the country, which is only partially offset with the high unemployment. Despite the increase of the activity in the Republic of Macedonia in 2006 (1.5 percentage points compared to 2005), it was by 12 percentage points lower than the EU - 10 and by 6 percentage points lower than in Romania and Bulgaria.

Participation rate of women in Macedonia was lower than the one for men (see Chart 8.1.) due to the traditional role of the women in the society, especially of women from the ethnic minorities, such as the Albanians and Roma. Gender gap in the activity in Macedonia was 25.8 percentage points in 2006, which was much above the average gap in the

Chart 8.1. Participation rate in 2006



Source: State Statistical Office and Eurostat

<sup>8</sup> Working-age population is defined as population at the age of 15-64, which is in line with the definition of the International Labour Organisation (ILO). This definition differs from the national one, according to which working-age population is defined as the population at the age of 15 and above. This analysis presents data on the basis of ILO standards so as to ensure comparison at international level. However, only part of the data in LFS publications can be calculated for the population at the age between 15-64, so part of the indicators are calculated according to the national definition, to be pointed out in the text.

countries of Central and Eastern Europe of around 12% and 16% in EU - 15. However, gender gap reduces with the level of education, and on tertiary level of education, women have higher participation rate compared to men.

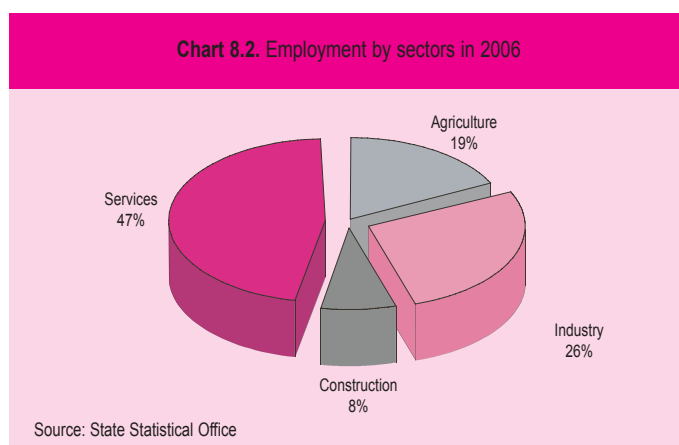
Labour market activity of young workers decreased during the transition period because of the difficulties in finding first employment after the completed education and because of the fact that the increasing number of young people decided to continue their studies in view of increasing returns to (investment in) education. However, certain progress was achieved in 2006, i.e. growth of the activity of young people from 32.9% in 2005 to 33.7% in 2006.

### 8.1.2. Employment

Gender, age and educational features of employment. Employment rate in the Republic of Macedonia was 39.6% in 2006, which was by 1.3 percentage point higher than in 2005. However, employment in the Republic of Macedonia was by around 17 percentage points lower than the lowest employment rates in the EU member states (in Poland and Malta).

In 2006, gender gap regarding employment in the Republic of Macedonia was 17.6 percentage points, which was close to the average in the EU - 25 (first quarter in 2006). Again, the difference in the employment rates between genders decreases with education, so that in 2006 (the last available data), women with higher education showed higher rates of employment compared to men.


In the age groups that are ten years below and above the central age group (25-54), only 14 persons out of one hundred young people worked in 2006, and 28 persons out of one hundred people at the age of 55-64. Very low employment rate among the young people in Macedonia, one third of the total employment rate, could be ascribed to the late employment due to difficulties in finding first employment.



Employment by sectors and type of contract. Employment structure in the Republic of Macedonia is similar to the one in Bulgaria, Croatia, Lithuania and Romania, where the share of employment in the agriculture in the total employment increased or remained on relatively high level during the transition period. The reason was that agriculture absorbed the laid-off workers from the restructured companies, and/or provided existence, mainly for the workers with lower education. In 2006, agriculture accounted for 20% of the total employment, industry accounted for 25%, and construction with 8% (see Chart 8.2). Services were the main "employer", accounting for 47% of the total employment. Although, unlike the developed countries, jobs in the service sector in the Republic of Macedonia are with low quality in terms of stability, salary and working conditions (in personal services and household services), rather than being high-quality jobs in the service sector, as for instance, in the information technology.

There was a positive change in the employment structure in the last year in terms of the economic status, i.e. increase of the share of self-employment and employers. The share of self-employed persons increased by 12.4% in 2006, while the share of employers increased to 6% (see Table D.1.). Self-employment, as a form of employment, is of especial importance due to its potential for reducing unemployment in an environment of low job creation, like that in the Republic of Macedonia. With regard to the ownership, 66% of all employed persons in 2006 worked in private companies.





An important issue for analysis is part-time employment since net increase of part-time jobs creates additional possibilities for employment, mainly for young people and women, and can help the employers to quickly adjust to changing aggregate demand. In 2005, 5.0% of the employees in the Republic of Macedonia (last available data) worked under such employment contracts. There were two regulatory barriers to greater application of part-time employment contracts: (1) base for the payment of social contributions was prescribed monthly, rather than by working hour; (2) health insurance contribution was calculated for full-time employment, rather than on hour basis, which increased the labour force costs for the workers with part-time jobs. Like in all Central and Eastern European countries, women use more the part-time employment (6.1%), as well as the young persons (10.4% of the employed young persons in 2005).

Temporary employment is a precautionary measure for the employers in unfavourable economic conditions, although it implies certain level of insecurity for the employees. Relatively high level of employees on the basis of temporary employment contracts is characteristic for the Republic of Macedonia. Share of temporary employment in the total employment ranged from 10% to 13%, and it increased to 17.7% in 2003, according to the last published data. Regarding age groups, this type of engagement was more common for the young workers, which suggests further disadvantaged position of young workers on the labour market, in terms of access to permanent employment/full-time employment, as well in terms of on-the-job training and possibility for promotion of young persons.

The application of civil-low contracts<sup>9</sup> was broadly used in the Republic of Macedonia until 2006, whereby the persons being engaged on the basis of these agreements considered and declared themselves as unemployed persons. Hence, in 2006, pursuant to the Law on Agencies for Temporary Employment, a new form of employment was introduced, temporary employment, which crowded out the civil-low contracts, the main objective being increase of labour market flexibility. In fact, Agencies for Temporary Employment provide flexibility to the employers since they can engage workers for a limited period of time, in line with the economic conditions, without significant costs for employment and dismissal. Moreover, Agencies for Temporary Employment provide a certain job and income security for workers. Hence, they can minimise one of the main conflicts of interest on the labour markets, the conflict between the safety in terms of keeping the job, important for the workers and job flexibility, important for the employers.

Eighteen Agencies for Temporary Employment were registered at the end of 2006, which signed 3,210 employment contracts.

### **8.1.3. Unemployment**

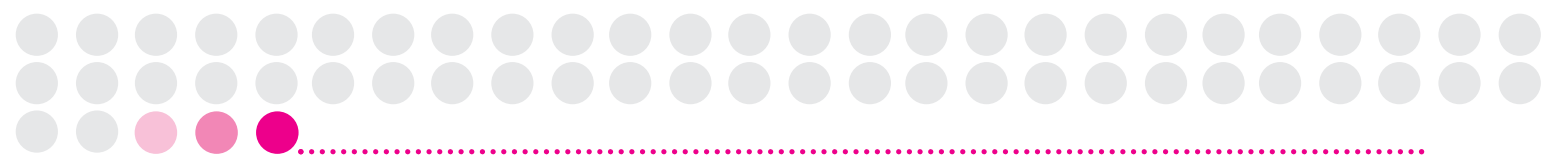
Age, gender and educational features of employment. Unemployment rate in the Republic of Macedonia declined to 36.3% in 2006 (by 1.3 percentage point compared to 2005), although it is still on an unacceptably high level (see table E.1.).

Unemployment rate of women was 37.5% in 2006, which is only 1.9 percentage points higher than the unemployment rate of men. Unemployment rates were the highest for young labour force at the age of 15-24, and gradually decrease with the age. As in other countries, possibility is higher for young persons to be unemployed: their unemployment rate is by 1.7 time higher than the national average.

Long-term unemployment, i.e. unemployment for more than one year, is an important characteristic of the labour market situation because the depreciation of knowledge, qualifications and working experience leads to a negative

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9) Civil-low contracts were used in most of Central and Eastern European countries and were regulated pursuant to the national laws on obligations and acts, i.e. they were not employment contracts. As a result, payments, i.e. salaries, were subject only to personal income tax, and no social contributions were paid, thus reducing the labour force costs.



dependence between the duration of unemployment and the possibility of finding a job, so the longer the people are unemployed, the lower their chances to find a job. Around 80% of the total unemployment in the Republic of Macedonia is characterised as long-term, which is above the average of the EU - 25 and the new member states by 43.3% and 55.7% in the first quarter of 2006, respectively. This shows the stagnant nature of the Macedonian labour market where (almost all) unemployed persons have difficulties in finding a job.

Persons with primary education are more likely to be unemployed than those with secondary education, especially compared to those with higher education. Unemployment rate of persons with higher education was around half of the national average. Relatively low unemployment rate of those with incomplete primary education indicate that they were probably oriented towards agriculture as a survival strategy, i.e. they accepted to work as unpaid family workers, and/or that the workers with completed primary and secondary education had high reference wage (minimum salary at which they would accept a job offer).

## 8.2. Social protection

Government policy in the field of social protection in 2006 was designed on the following strategic documents: 2006 Macroeconomic Policy, 2006 Operational Programme of the Government of the Republic of Macedonia; 2006 - 2010 Employment Strategy, 2006 - 2008 National Employment Action Plan, thereby observing the fiscal guidelines determined in the 2006-2008 Fiscal Strategy and the 2006 Budget of the Republic of Macedonia.

In addition, international conventions and recommendations have an important role, among which the following: Strategy for Social Cohesion of the European Committee for Social Cohesion, UN Millennium Development Goals regarding the first development goal: poverty reduction, as well as other recommendations on the basis of which gradual accession toward the EU legislation is carried out.

To the end of social inclusion of socially excluded persons, as a measure in dealing with the poverty, the Ministry of Labour and Social Policy prepares a Joint Inclusion Memorandum, being a mandatory document for each country that acquires the status of an EU candidate country. This document will contribute to building the capacities of the country and all other participants in the fight against poverty (non-governmental sector, local and national authorities, science, etc.), and will be the basis for determining the national plan and strategy for dealing with poverty and social exclusion.

Within the available funds of the 2006 Budget of the Republic of Macedonia and the 2006 Programme for Receiving Social protection, pursuant to the Law on Social Protection and the government Decision on determining the criteria, the manner and the procedure for exercising the right to a pecuniary allowance, as well as providing resources for the unemployed, regular payment of pecuniary allowance was provided, ensuring a minimum social safety.

Social protection policy was aimed at promoting the non-institutional protection, as well as enlarging the number and the type of daily centres as more adequate forms of sheltering. Further strengthening of the capacities of the social protection centres and other institutions was made through training of the professional staff.

The cooperation on "Municipal Development Project", supported by the World Bank, continued in the de-institutionalisation process, which provided for construction and equipping of daily centres for people with mental disabilities and for elder people in the rural and urban municipalities in the Republic of Macedonia.

Following the completion of the first stage of decentralisation process in the area of social protection in 2005, according to which the old people's homes were transferred to the municipalities, implementation of the municipalities' obligation to

organise and provide social protection tailored to the specific needs of the citizens was emphasized in 2006. To that end, a Programme for cooperation and monitoring of social protection in municipalities in the Republic of Macedonia was prepared. This programme also regulated the closer cooperation in the field of social protection between the central government, presented by the Ministry of Labour and Social Policy, and centres for social work with the local government.

The implementation of the Social Protection Implementation Project (SPIL Project<sup>10</sup>) - social protection program support - continued in 2006, the basic goal of which is to improve effectiveness and efficiency of the social protection system by improving its administration.

According to the information from the Ministry of Labour and Social Policy (MoLSP), in December 2006, 66,540 households were recorded as social welfare beneficiaries, which, compared to the same month last year, dropped by 0.8% (see Chart 8.3.). Thereby, around Denar 144.4 million was paid on the basis of social welfare or 3.1% less compared to December 2005.

Social welfare is paid to households in which certain members are working able, but unsecured in terms of income.

In 2006, 5,183 beneficiaries exercised the right to a permanent pecuniary assistance. The regular assistance is paid to persons incapable to work, who cannot provide an existence on their own or through other regulations.

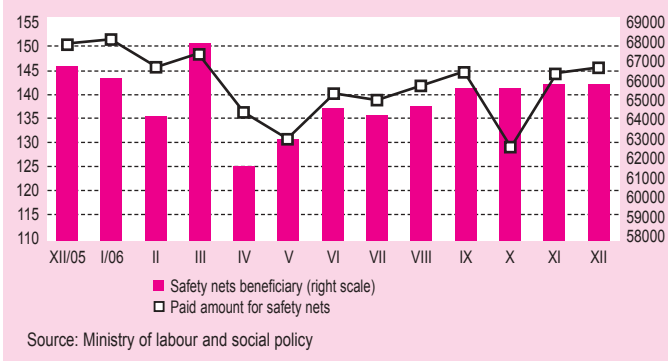
On the basis of allowance for support and care, as of December 2006 inclusive, 21,807 beneficiaries acquired this right. Pecuniary allowance for support and care is paid to persons who are not able to perform the basic life activities without the help of other person, as well as to person with severe and most severe mental disabilities over the age of 26.

In addition to these groups, pecuniary assistance was also used by:

- internally-displaced families and families of refugees from other countries;
- persons who, by the age of 18, have the status of a child without parents and parental care;
- persons who have part-time job, because of a care for their disabled children;
- foster families; and
- persons beneficiaries of one-off pecuniary allowance and in-kind allowance.

To the end of improving the economic and social position of Roma population, international initiative "Decade of Roma Inclusion" begun to be applied in Europe. It sets clear guidelines, at national level, for progress, constant monitoring of the achievements with respect to these guidelines, as well as exchange of information, as priority areas. The initiative is closely related to two current initiatives: Millennium Development Goals and the EU Social Inclusion Programme, defining the following as priority areas: education, employment, health and housing.

Chart 8.3. Beneficiaries of welfare and paid funds



10) SPIL Project is financed by the World Bank loan. In addition to the social protection reforms, it also includes pension system reforms.

Pension and disability insurance. Under SPIL, in addition to the reforms in the social protection system, reforms in the pension system are envisaged. Therefore, during 2006, many procurements of hardware and software for the needs of the Pension and Disability Insurance Fund (PDF) and the Pension Supervision Agency (MAPAS) were carried for the establishment of a new system for monthly registration of individual pension contributions and collection of contributions for the state and private pension funds. An uniformed manner of collecting PDF contribution for the first and the second pillar was established in 2006.

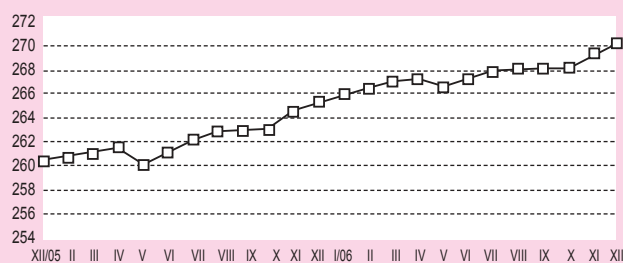
The unfavourable upward trend regarding the number of pensioners also continued in 2006, which was consistent with the demographic trend of the aging of the population in the Republic of Macedonia. Thus, in December 2006, 269,681 persons in total were registered as pensioners.

Compared to December 2005, this was an increase of 4,529 persons, i.e. 1.7%, in total, creating additional pressure on the public finances.

Average pension amounted to Denar 7,684 in 2006, which, compared to December 2005, increased by 3.0% in real terms. Within the average pension, the highest amount or Denar 8,492 was paid on the basis of old-age pension, average disability pension amounted to Denar 6,509 and average family pension amounted to Denar 6,023.

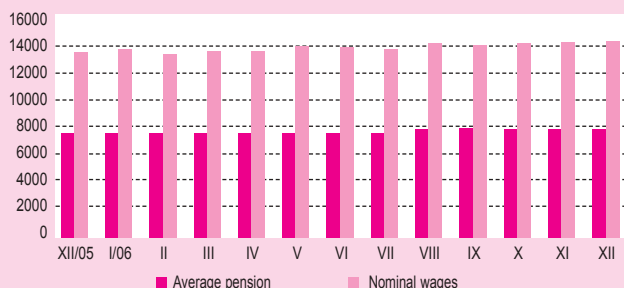
In December 2006, Denar 2,025 million was spent on the basis of payment of pensions. From the structural point of view, old-age pension beneficiaries accounted the most, i.e. 146,852 beneficiaries or 54.5%, followed by family pension beneficiaries - 73,465 or 27.2% and disability pension beneficiaries - 49,364 or 18.3%. Ratio between the average pension in 2006 and the total average salary in the country in 2006 was 56% (see Chart 8.5.).

**Chart 8.4.** Number of pensioners (in thousands)

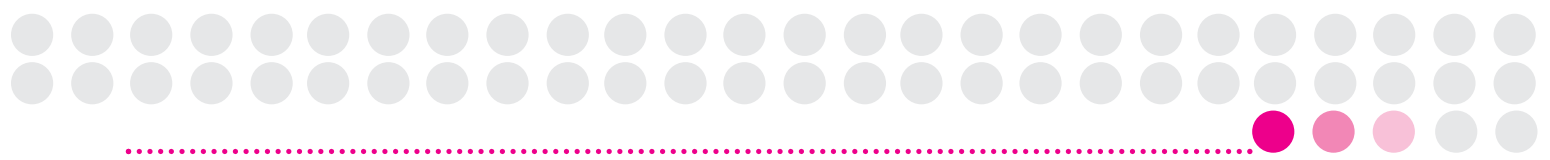


Source: Ministry of labour and social policy

**Chart 8.5.** Trends in average pensions and salary

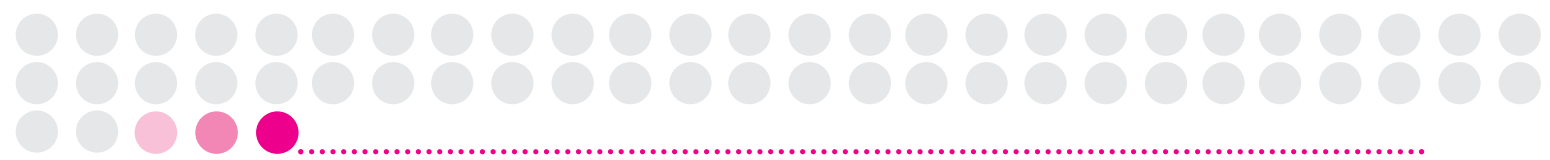


Source: State Statistical Office and Pension and Disability insurance FundInsurance



# APPENDICES





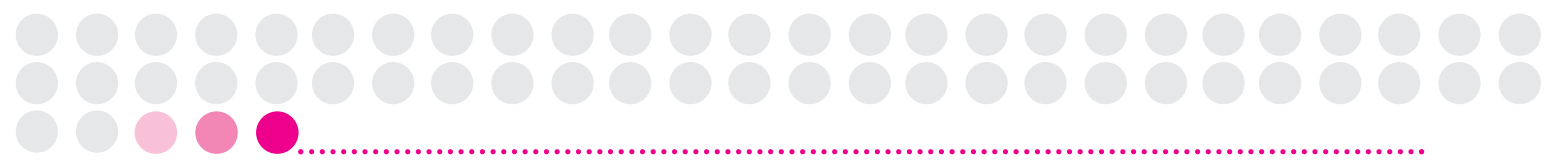
## □. REAL SECTOR

Table A.1. Macroeconomic Indicators

	1998	1999	2000	2001	2002	2003	2004	2005	2006
<b>Real sector</b>									
Gross domestic product									
- real growth rate	3.4	4.3	4.5	-4.5	0.9	2.8	4.1	3.8	4.0
- current prices, Denar million	194,979	209,010	236,390	233,841	243,970	251,486	265,257	284,423	305,265
- US dollar million (nominal)	3,581	3,674	3,588	3,437	3,769	4,631	5,368	5,770	6,257
- US dollar million (PARE methodology)	3,575	3,730	3,899	3,723	3,872	4,119	4,928	4,519	-
- EUR million (nominal)			3,893	3,839	4,001	4,105	4,325	4,640	4,989
Inflation (costs of living, average)	-0.1	-0.7	5.8	5.5	1.8	1.2	-0.4	0.5	3.2
GDP Deflator	1.4	2.7	8.2	3.6	3.4	0.3	1.3	3.3	3.2
Salaries (monthly average, net)									
- nominal growth	3.7	2.9	5.5	3.5	6.9	4.8	4.0	4.0	7.3
- real growth	3.8	3.6	-0.3	-2.0	5.1	3.6	4.4	3.5	4.1
Employment growth (%)	5.4	1.0	0.8	9.0	-6.3	-2.9	-4.1	1.5	4.3
<b>External sector</b>									
Import (f.o.b.), US dollar million	1,292	1,190	1,321	1,155	1,112	1,362	1,672	2,040	2,400
Import (f.o.b.), US dollar million	1,807	1,686	2,011	1,682	1,916	2,211	2,784	3,097	3,681
Trade balance (US dollar million)	-515	-496	-690	-527	-804	-849	-1,112	-1,057	-1,281
Trade balance (f.o.b.) (% of GDP)	-14.4	-13.5	-19.2	-15.3	-21.3	-18.3	-20.7	-18.3	-20.5
Current account deficit (US dollar million)	-270	-33	-72	-244	-358	-149	-415	-81	-24
Current account deficit (% of GDP)	-7.5	-0.9	-2.0	-7.1	-9.5	-3.2	-7.7	-1.4	-0.4
Foreign direct investments (dollar million)	128	32	176	441	78	96	156	97	350
- % of GDP	3.6	0.9	4.9	12.8	2.1	2.1	2.9	1.7	5.6
External sector (growth rates)									
Export (f.o.b.)	4.4	-7.9	11.0	-12.6	-3.7	22.5	22.8	22.0	17.6
Import (f.o.b.)	11.3	-6.7	19.3	-16.4	13.9	15.4	25.9	11.2	18.9
<b>Fiscal sector</b>									
General government budget deficit (% of GDP)	1.7	0.0	1.8	-7.2	-5.7	-0.6	0.4	0.3	-0.5

Table A.2. Wages

	2001	2002	2003	2004	2005	2006
Prose~na mese~na neto-plata (vo denari)	10.551	11.279	11.828	12.298	12.597	13.517
Nominalni plati -stapki	3,5	6,9	4,8	4,0	2,5	7,3
Realni plati -stapki	-1,9	5,0	3,6	4,4	2,0	4,0





## B. EXTERNAL SECTOR

Table B.1. Balance of Payments of the Republic of Macedonia

	2002	2003	2004	2005	K1	K2	K3	K4	2006
<b>CURRENT TRANSACTIONS</b>	<b>-357.81</b>	<b>-152.28</b>	<b>-414.82</b>	<b>-81.48</b>	<b>-44.46</b>	<b>-64.11</b>	<b>133.46</b>	<b>-48.61</b>	<b>-23.73</b>
Goods, net	-804.34	-851.48	-1,112.08	-1,057.47	-266.83	-367.20	-261.39	-389.82	-1,285.24
Export, f.o.b.	1,112.15	1,359.04	1,672.43	2,039.64	449.87	586.05	699.82	660.51	2,396.26
Import, f.o.b. 2	-1,916.49	-2,210.52	-2,784.51	-3,097.11	-716.70	-953.26	-961.21	-1,050.33	-3,681.49
Services, net	-22.13	-2.56	-54.39	-33.87	-6.18	-5.60	30.02	6.96	25.20
Income, net	-29.78	-32.33	-39.23	-54.99	5.89	-1.88	-11.88	4.78	-3.09
out of which: interest, net	-18.64	-31.88	-26.22	-25.95	-9.38	-3.60	-6.70	-4.66	-24.34
Current transfers, net	498.45	734.09	790.88	1,064.85	222.66	310.57	376.71	329.47	1,239.40
Official	100.50	103.36	70.07	64.39	16.93	19.73	17.83	19.26	73.75
Private	397.95	630.73	720.81	1,000.47	205.73	290.84	358.88	310.21	1,165.66
<b>CAPITAL AND FINANCIAL ACCOUNT</b>	<b>376.87</b>	<b>169.97</b>	<b>407.01</b>	<b>94.67</b>	<b>42.00</b>	<b>58.71</b>	<b>-135.45</b>	<b>48.60</b>	<b>13.87</b>
Capital account, net	8.26	-6.69	-4.61	-2.01	0.44	-0.54	-0.26	-0.76	-1.11
Capital transfers, net	9.92	-6.60	-4.61	-2.01	0.44	-0.54	-0.26	-0.76	-1.11
Official	9.92	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Others	0.00	-6.60	-4.61	-2.01	0.44	-0.54	-0.26	-0.76	-1.11
Acquisition/availability of non-production/non-financial assets	-1.66	-0.09	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Financial account, net	368.62	176.66	411.62	96.68	41.56	59.24	-135.19	49.37	14.98
Direct investments, net	77.72	94.26	155.85	97.08	290.53	21.61	11.97	26.22	350.33
Portfolio investments, net	0.35	3.39	14.82	235.11	14.19	31.53	8.96	28.63	83.31
Other investments, net	159.98	129.97	260.42	179.56	-229.63	118.90	11.67	56.21	-42.84
Trade credits, net	83.1	82.95	170.05	24.60	7.18	40.11	-57.21	51.09	41.17
Loans, net	8.19	23.47	59.82	153.94	-161.58	70.55	31.56	40.27	-19.20
Currencies and deposits, net	44.69	2.85	-3.66	-24.77	-81.16	-3.88	29.43	-48.14	-103.75
out of which: monetary authority, net	68.79	17.77	26.44	0.77	-68.78	0.00	65.66	-0.14	-3.26
commercial banks, net	112.17	-54.59	-105.08	26.57	7.02	24.63	-22.48	-24.74	-15.58
population, net	-136.27	39.68	74.97	-52.10	-19.40	-28.50	-13.74	-23.25	-84.90
Others, net	24.00	20.69	34.22	25.79	5.93	12.12	7.89	12.99	38.94
Gross official reserves ("-" means increase) <sup>3</sup>	130.57	-50.96	-19.47	-415.07	-33.53	-112.80	-167.80	-61.69	-375.82
<b>ERRORS AND OMISSIONS</b>	<b>-19.07</b>	<b>-17.70</b>	<b>7.81</b>	<b>-13.19</b>	<b>2.46</b>	<b>5.40</b>	<b>1.99</b>	<b>0.00</b>	<b>9.86</b>

Table B.2. Foreign trade

	2000	2001	2002	2003	2004	2005*)	2006*)		2000	2001	2002	2003	2004	2005*)	2006*)
Export	1.323	1.158	1.116	1.367	1.675	2.041	2.400	Export	1.323	1.158	1.116	1.367	1.675	2.041	2.400
Import	2.094	1.694	1.995	2.306	2.931	3.227	3.762	- regular	679	603	589	756	1.035	1.385	1.767
Deficit	-771	-536	-879	-939	-1.256	-1.186	-1.362	- temporary import	644	555	527	611	640	656	633
								Import	2.094	1.694	1.995	2.036	2.931	3.227	3.762
								- regular	1.584	1.308	1.611	1.591	2.473	2.766	3.296
								- temporary import	510	386	384	445	458	461	466

\*) Preliminary data

Source: State Statistical Office

**Table B.3. Export and import by groups of countries**

US dollar million	2000	2001	2002	2003	2004	2005*)	2006*)
<b>EXPORT</b>	<b>1,323</b>	<b>1,158</b>	<b>1,116</b>	<b>1,367</b>	<b>1,675</b>	<b>2,041</b>	<b>2,400</b>
Developed countries	792	721	692	883	1,099	1,278	1,373
European Union	566	566	570	747	956	1,083	1,326
EFTA	36	39	28	19	7	8	10
Other developed countries	190	116	94	116	136	186	**)
Central and Eastern European countries and former USSR countries	60	561	59	68	100	134	**)
Undeveloped countries	2	3	2	1	2	2	**)
Developing countries	34	14	17	28	12	35	**)
Former Yugoslav countries	432	363	345	386	460	591	**)
Other countries	3	1	0	0	0	0	**)
<b>IMPORT</b>	<b>2,094</b>	<b>1,694</b>	<b>1,995</b>	<b>2,306</b>	<b>2,931</b>	<b>3,227</b>	<b>3,762</b>
Developed countries	1,010	880	1,089	1,220	1,711	1,769	1,893
European Union	801	719	894	1,009	1,460	1,467	1,650
EFTA	30	26	31	29	46	65	61
Other developed countries	180	135	164	182	203	236	**)
Central and Eastern European countries and former USSR countries	583	394	405	518	679	825	**)
Undeveloped countries	1	2	3	3	1	1	**)
Developing countries	101	90	113	137	214	268	**)
Former Yugoslav countries	398	327	384	427	325	363	**)
Other countries	0	0	0	0	0	0	**)

\*) Preliminary data

\*\*) Due to the change in the groups of countries and the methodology of calculation, 2006 data are not comparable with those from the previous years.

Source: State Statistical Office

**Po novata metodologija od 2006 godina**

US dollars million	2005**)	2006**)
<b>EXPORT*)</b>	<b>2,041</b>	<b>2,400</b>
Developed countries	1,234	1,373
European Union	1,083	1,326
EFTA	8	10
Other developed countries	143	37
Undeveloped countries	4	2
Developing countries	184	236
Western Balkan	618	787
Other countries	0	0
<b>IMPORT*)</b>	<b>3,227</b>	<b>3,762</b>
Developed countries	1,693	1,893
European Union	1,467	1,650
EFTA	65	61
Other developed countries	160	181
Undeveloped countries	23	26
Developing countries	1,139	1,442
Western Balkans	372	400
Other countries	0	0

\*) Preliminary data

Source: State Statistical Office

**Table B.4. Export and import by main trading partners**

	US dollar million							structure in %						
	2000	2001	2002	2003	2004	2005*)	2006*)	2000	2001	2002	2003	2004	2005*)	2006*)
<b>EXPORT</b>	<b>1.323</b>	<b>1.158</b>	<b>1.116</b>	<b>1.367</b>	<b>1.675</b>	<b>2.041</b>	<b>2.400</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>
Main trading partners:	75.49	82.47	82.09	78.64	77.01	78.44	80.25							
Serbia and Montenegro	335	267	246	275	347	459	557	25.33	23.06	22.04	20.12	20.72	22.49	23.21
Germany	257	238	234	280	317	364	375	19.46	20.55	20.97	20.48	18.93	17.83	15.63
Italy	91	91	82	95	134	169	236	6.86	7.86	7.33	6.95	8.00	8.28	9.83
Greece	84	101	117	180	228	312	361	6.36	8.72	10.47	13.17	13.61	15.29	15.04
USA	84	99	77	72	72	44	22	6.36	8.55	6.94	5.27	4.30	2.16	0.92
Croatia	48	58	59	66	80	81	124	3.61	5.01	5.29	4.83	4.78	3.97	5.17
The Netherlands	36	45	44	47	47	44	55	2.72	3.89	3.94	3.44	2.81	2.16	2.29
Bulgaria	27	21	21	26	19	76	130	2.03	1.81	1.88	1.90	1.13	3.72	5.42
Slovenia	26	21	22	21	27	31	41	2.00	1.81	1.94	1.54	1.61	1.52	1.71
Russia	10	14	14	13	19	21	25	0.78	1.21	1.29	0.95	1.13	1.03	1.04
<b>IMPORT</b>	<b>2,094</b>	<b>1,694</b>	<b>1,995</b>	<b>2,306</b>	<b>2,931</b>	<b>3,227</b>	<b>3,762</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>	<b>100</b>
Main trading partners:								65.71	68.89	68.80	68.21	63.12	63.37	61.78
Germany	253	215	285	304	368	334	369	12.09	12.69	14.29	13.18	12.56	10.35	9.81
Serbia and Montenegro	190	158	185	212	243	264	282	9.09	9.33	9.27	9.19	8.29	8.18	7.50
Greece	202	184	238	300	282	296	319	9.63	10.86	11.93	13.01	9.62	9.17	8.48
Italy	111	107	118	123	168	193	227	5.31	6.32	5.91	5.33	5.73	5.98	6.03
Russia	192	139	125	178	271	424	569	9.16	8.21	6.27	7.72	9.25	13.14	15.12
USA	83	51	58	56	47	45	41	3.97	3.01	2.91	2.43	1.60	1.39	1.09
Slovenia	144	119	130	139	140	127	129	6.88	7.02	6.50	6.03	4.78	3.94	3.43
Bulgaria	98	103	128	149	209	234	250	4.66	6.08	6.42	6.46	7.13	7.25	6.65
Croatia	58	46	55	63	65	75	79	2.76	2.72	2.76	2.73	2.22	2.32	2.10
The Netherlands	45	45	51	49	57	53	59	2.16	2.66	2.56	2.12	1.94	1.64	1.57

\*) Preliminary data  
Source: State Statistical Office

**Table B.5. Export and import by economic purpose**

US dollar million	2000	2001	2002	2003	2004	2005*)	2006*)
<b>EXPORT</b>	<b>1.323</b>	<b>1.158</b>	<b>1.116</b>	<b>1.367</b>	<b>1.675</b>	<b>2.041</b>	<b>2.400</b>
Reproduction materials	719	573	510	669	816	1.110	1.393
Operating assets	33	29	27	22	30	39	51
Consumer goods	564	554	574	674	827	890	954
Undistributed	4	1	2	1	1	1	1
<b>IMPORT</b>	<b>2.094</b>	<b>1.694</b>	<b>1.995</b>	<b>2.306</b>	<b>2.931</b>	<b>3.227</b>	<b>3.762</b>
Reproduction materials	1.416	1.124	1.266	1.492	1.904	2.095	2.453
Operating assets	263	209	253	285	312	348	419
Consumer goods	408	355	471	525	711	782	886
Undistributed	5	4	4	2	2	2	3

\*) Preliminary data  
Source: State Statistical Office

**Table B.6. Export and import by level of processing**

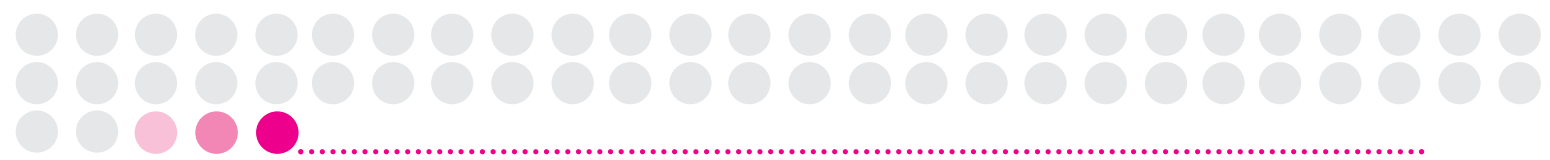
US dollar million	2000	2001	2002	2003	2004	2005*)	2006*)
<b>EXPORT</b>	<b>1.323</b>	<b>1.158</b>	<b>1.116</b>	<b>1.367</b>	<b>1.675</b>	<b>2.041</b>	<b>2.400</b>
Unprocessed products	109	104	117	140	143	215	264
General-level processing products	522	391	322	455	600	845	1.085
High-level processing products	686	660	673	770	930	979	1.049
Undistributed	4	0	2	1	1	1	1
<b>IMPORT</b>	<b>2.094</b>	<b>1.694</b>	<b>1.995</b>	<b>2.306</b>	<b>2.931</b>	<b>3.227</b>	<b>3.762</b>
Unprocessed products	281	211	201	310	398	573	752
General-level processing products	385	330	447	462	803	914	1.032
High-level processing products	1.421	1.147	1.342	1.529	1.727	1.738	1.974
Undistributed	5	4	4	2	2	2	3

\*) Preliminary data  
Source: State Statistical Office

**Table B.7. External debt of the Republic of Macedonia**

(US dollar million)	31.12.1999	31.12.2000	31.12.2001	31.12.2002	31.12.2003	31.12.2004	31.12.2005	31.12.2006
<b>Official creditors</b>	<b>870</b>	<b>1.052</b>	<b>973</b>	<b>1.034</b>	<b>1.193</b>	<b>1.314</b>	<b>1.257</b>	<b>1.380</b>
Multilateral	521	720	689	757	922	1.062	1.052	1.161
IMF	99	82	71	67	68	63	62	56
IBRD	92	123	124	145	181	223	248	264
IFC	1	57	33	18	13	9	6	4
IDA	145	250	255	296	358	389	362	2.384
EIB	37	69	75	102	116	148	140	165
EUROFIMA	25	17	14	12	8	8	7	6
CEDB	5	7	6	15	17	23	20	30
EBRD	88	74	62	32	40	65	87	116
EU	27	37	44	65	112	122	106	118
IFAD	0	3	4	5	7	11	13	16
EAR	0	1	1	1	1	1	0	0
Bilateral	349	332	284	277	271	252	205	219
<b>Private creditors</b>	<b>261</b>	<b>443</b>	<b>456</b>	<b>543</b>	<b>605</b>	<b>694</b>	<b>924</b>	<b>935</b>
London Club	234	253	262	254	243,3	233	222	0
Eurobond		0	0	0	0	0	177	197
Others	27	191	194	289	362	461	525	738
Banks and financial institutions	16	136	131	205	202,25	238	265	374
Enterprises	11	55	63	85	159,68	223	260	363
<b>TOTAL</b>	<b>1.131</b>	<b>1.495</b>	<b>1.429</b>	<b>1.577</b>	<b>1.799</b>	<b>2.008</b>	<b>2.181</b>	<b>2.315</b>

\*) Preliminary data  
Source: State Statistical Office



## C. FISCAL SECTOR

Table C.1. General government budget

	Q1	Q2	Q3	Q4	Total	Q1	Q2	Q3	Q4	Total
	2005	2005	2005	2005	2005	2006	2006	2006	2006	2006
<b>TOTAL REVENUES</b>	<b>21.732</b>	<b>24.627</b>	<b>27.928</b>	<b>26.641</b>	<b>100.928</b>	<b>23.069</b>	<b>26.306</b>	<b>26.222</b>	<b>28.504</b>	<b>104.101</b>
Tax revenues and contributions	18.972	21.172	21.285	23.152	84.581	19.848	22.782	23.080	24.888	90.598
Tax revenues (special revenue account)	68	75	70	91	304	79	50	35	35	199
Taxes	12.314	13.944	14.107	15.316	55.681	12.658	15.097	15.460	16.360	59.575
Personal income tax	1.834	2.052	1.951	2.260	8.097	1.933	2.098	2.025	2.358	8.414
Profit tax	1,080	600	623	534	2,837	1,725	914	950	1,119	4,708
VAT	5,745	6,767	6,652	7,918	27,082	5,228	7,342	7,155	7,534	27,259
Excises	2,461	2,937	3,385	2,965	11,748	2,542	2,839	3,374	3,419	12,174
Import duties	1,026	1,441	1,335	1,464	5,266	993	1,494	1,982	3,243	7,712
Other taxes	168	147	161	175	651	237	410	390	176	1,213
Contributions	6,590	7,153	7,108	7,745	28,596	7,111	7,635	7,586	8,493	30,825
Pension and Disability Insurance Fund	4,230	4,569	4,553	4,948	18,300	4,619	4,969	4,893	5,467	19,948
Employment Agency	312	325	322	353	1,312	322	336	337	375	1,370
Health Insurance Fund	2,048	2,259	2,233	2,442	8,982	2,170	2,330	2,356	2,651	9,507
Non-tax revenues	2.495	3.088	5.284	2.951	13.818	2.306	2.721	2.627	2.826	10.480
Non-tax revenues (special revenue account)	1,414	1,673	1,549	1,676	6,312	1,234	1,117	1,496	1,656	5,503
Profit from public financial institutions	83	260	2,837	139	3,319	103	406	56	258	823
Administrative fees	387	459	358	453	1,657	395	426	308	364	1,493
Co-payment for health services	127	122	70	115	434	80	76	65	22	243
Other administrative fees	58	69	55	64	246	65	70	59	26	220
Other non-tax revenues	87	52	53	72	264	109	176	209	125	619
Road Fund Contributions	340	441	462	432	1,675	321	452	434	374	1,581
Capital revenues	112	107	587	127	933	143	390	143	272	948
Foreign donations	152	259	672	411	1,494	727	299	166	231	1,423
Income on the basis of loan repayment	1	1	0	0	2	45	74	153	288	560
<b>TOTAL REVENUES</b>	<b>22.766</b>	<b>23.875</b>	<b>24.482</b>	<b>29.096</b>	<b>100.219</b>	<b>23.538</b>	<b>26.265</b>	<b>25.085</b>	<b>30.871</b>	<b>105.759</b>
Current costs	21.657	22.180	21.707	24.482	90.026	22.475	24.145	22.335	27.569	96.524
Salaries and allowances	5,640	5,736	5,566	5,894	22,836	5,750	5,878	5,707	6,086	23,421
Goods and services	3,197	3,140	2,620	4,028	12,985	2,856	3,264	2,655	4,128	12,903
Transfers	12,252	12,639	12,795	13,911	51,597	13,080	14,265	13,167	16,163	56,675
Transfers (special revenue account)	160	220	192	341	913	167	209	165	240	781
Social transfers	11,582	11,670	11,533	12,085	46,870	11,566	12,726	12,072	12,466	48,830
Pension and Disability Fund	6,294	6,241	6,151	6,285	24,971	6,396	6,640	6,751	6,947	26,734
Employment Agency	783	767	715	675	2,940	659	521	487	450	2,117
Social welfare	965	1,026	1,113	1,034	4,138	948	945	1,114	1,090	4,097
Structural reforms	0	0	0	0	0	0	0	0	0	0
Public Administration Reforms	0	0	0	0	0	0	0	0	0	0
Health care	3,539	3,637	3,557	4,092	14,825	3,561	4,621	3,718	3,979	15,879
Other transfers	487	704	1,037	1,453	3,681	1,326	1,308	911	3,451	6,996

(continued from page 71)

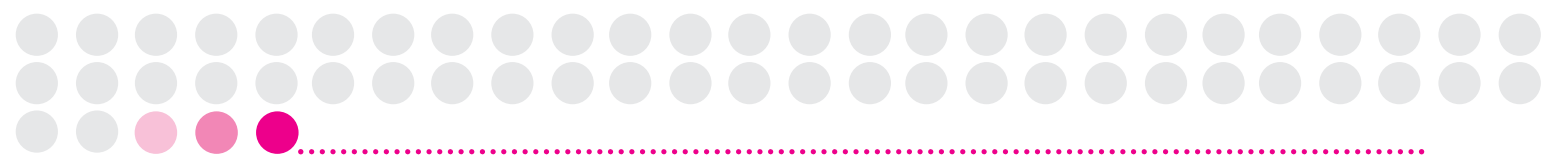
Table C.1. General government budget

	Q1	Q2	Q3	Q4	Vkupno	Q1	Q2	Q3	Q4	Vkupno
	2005	2005	2005	2005	2005	2006	2006	2006	2006	2006
Refugee-related costs	24	45	33	33	135	21	22	20	7	70
Interest payments	569	666	727	648	2,610	790	736	418	1,193	3,137
Interest on domestic debt	116	433	163	362	1,074	140	444	79	419	1,082
Interest on external debt	453	233	564	286	1,536	650	292	339	774	2,055
Guarantees	0	0	0	0	0	0	0	387	0	387
Capital expenditures	1.108	1.695	2.775	4.613	10.191	1.063	2.120	2.751	3.301	9.235
<b>Budget balance</b>	<b>-1.034</b>	<b>752</b>	<b>3.446</b>	<b>-2.455</b>	<b>709</b>	<b>-469</b>	<b>2</b>	<b>1.083</b>	<b>-2.365</b>	<b>-1.749</b>
<b>Financing</b>	<b>1.034</b>	<b>-752</b>	<b>-3.446</b>	<b>2.455</b>	<b>-709</b>	<b>469</b>	<b>-2</b>	<b>-1.083</b>	<b>2.355</b>	<b>1.739</b>
<b>Inflow</b>	<b>2.458</b>	<b>2.015</b>	<b>-1.964</b>	<b>4.554</b>	<b>7.063</b>	<b>9.759</b>	<b>3.097</b>	<b>-166</b>	<b>5.390</b>	<b>18.080</b>
Privatisation revenues	265	231	147	740	1.383	13.928	3.846	0	0	17.774
Foreign donations	0	0	0	0	0	0	0	0	0	0
Foreign loans	139	1,219	838	11,717	13,913	159	496	484	534	1,673
Deposits	1,532	-343	-3,398	-7,588	-9,797	-4,835	-4,101	-695	3,741	-5,890
Treasury bills	521	905	427	-315	1,538	484	422	43	1,070	2,019
Sale of shares	1	3	24	1	29	24	2,433	2	0	2,459
<b>Outflow</b>	<b>1.425</b>	<b>2.765</b>	<b>1.483</b>	<b>2.099</b>	<b>7.772</b>	<b>9.290</b>	<b>3.099</b>	<b>917</b>	<b>3.025</b>	<b>16.331</b>
Principal repayment	1.425	2.765	1.483	2.099	7.772	9.290	3.099	917	3.025	16.331
External debt	1.255	331	1.305	404	3.295	9.159	381	917	487	10.944
Domestic debt	170	2.435	178	1.695	4.478	131	2.718	0	2.538	5.387



**Table C.2. Central Government Budget of the Republic of Macedonia**

000 000 denars	2002	2003	2004	2005	2006
<b>TOTAL REVENUES</b>	<b>71,981</b>	<b>68,406</b>	<b>68,258</b>	<b>76,993</b>	<b>81,749</b>
GENUINE REVENUES	58,896	56,784	56,534	58,462	59,940
TAX REVENUES	54,389	49,166	52,527	53,184	56,840
Income tax, profit tax and capital gain tax	10,137	10,772	10,069	10,668	11,236
Personal income tax	7,513	7,502	7,707	8,097	8,051
Profit tax	2,624	3,270	2,362	2,571	3,185
Domestic taxes on goods and services	31,235	31,741	36,093	37,082	40,136
Sales tax and VAT (from 1st April 2000)	20,521	21,175	25,757	26,325	28,334
Excises	10,714	10,565	10,336	10,757	11,802
International trade and transactions tax	6,336	6,141	5,815	4,867	4,848
Import duties	5,230	4,909	4,598	3,861	3,817
Other import duties and fees	1,105	1,232	1,217	1,006	1,031
Other taxes	0	0	0	0	0
Taxes from specific services	3	4	5	0	0
Fees for usage and licenses for performing an activity	340	475	546	567	620
Financial transactions tax	6,335	31	0	-	-
NON-TAX REVENUES	4,506	7,617	4,007	5,278	3,100
Entrepreneur income and property income	931	1,963	1,752	3,388	1,100
Fees and allowances	1,091	1,366	1,465	1,390	1,500
Other government services	205	370	257	300	300
Other non-tax revenues	2,277	3,917	532	200	200
CAPITAL REVENUES	7,193	4,081	3,342	1,120	16,227
Sale of capital assets	6,244	4,002	3,159	920	16,027
Sale of land and non-tangible investments	949	78	183	200	200
TREANSFERS AND DONATIONS	3,808	3,651	4,933	1,213	540
Transfers from other levels of government	1,167	1,136	3,889	397	0
Donations from abroad	2,641	2,515	1,044	816	540
DOMESTIC BORROWING	480		1,909	3,229	300
BORROWIN ABROAD	1,584	3,766	1,530	12,969	2,042
INCOME FROM REPAYMENT (collection) OF LOANS	18	123	11	0	0
<b>TOTAL EXPENDITURES</b>	<b>71,700</b>	<b>64,463</b>	<b>63,744</b>	<b>77,127</b>	<b>81,749</b>
CURRENT EXPENDITURES	56,314	51,105	51,668	46,616	49,295
Salaries, wages and allowances	18,337	20,234	20,943	21,861	22,669
Goods and other services	13,991	7,326	6,833	7,503	7,327
Current transfers	20,586	21,102	21,839	1,410	14,603
Current transfers to the local government units	-	-	-	813	1,819
Interest payments	3,398	2,444	2,053	2,335	2,877
SUBSIDIES AND TRANSFERS	-	-	-	2,885	2,111
SOCIAL BENEFITS	-	-	-	4,058	3,633
CAPITAL EXPENDITURES	8,366	4,688	4,867	16,376	12,543
LENDING, SHARE IN					
SECURITIES AND PRINCIPAL REPAYMENT	7,019	8,670	7,209	7,191	14,166
Lending and share in securities	931	637	76	0	0
Amortisation (principal repayment)	6,088	8,033	7,132	7,191	14,166



## D. MONETARY SECTOR

Table D.1. Monetary review

	XII.05	III.06	VI.06	IX.06	XII.06 <sup>1)</sup>
<b>I. Net foreign currency assets</b>	<b>89,738</b>	<b>96,611</b>	<b>100,288</b>	<b>105,619</b>	<b>108,042</b>
National bank	66,282	71,907	77,256	82,064	85,116
Assets	69,504	75,076	80,181	84,956	87,761
Liabilities	3,222	3,169	2,925	2,892	2,645
Deposit banks	23,456	24,704	23,032	23,555	22,926
Assets	37,786	36,669	35,526	36,867	39,707
Liabilities	14,330	11,965	12,494	13,312	16,781
<b>II. Net domestic assets</b>	<b>19,545</b>	<b>16,577</b>	<b>18,220</b>	<b>19,219</b>	<b>28,288</b>
<b>1. Domestic credits</b>	<b>62,382</b>	<b>62,714</b>	<b>65,763</b>	<b>65,575</b>	<b>77,176</b>
out of which: claims from the Government	-11,791	-15,747	-19,421	-21,017	-17,184
a) Deposit banks	81,371	88,476	96,610	99,729	107,866
- Denar	64,186	69,847	75,954	77,855	84,368
Government	7,118	9,930	11,340	12,998	13,377
Credits	7,115	9,927	11,317	12,974	13,355
Calculated outstanding interest	3	3	23	24	22
Non-government sector	57,068				
59,917	64,614	64,857	70,991		
Credits	51,672	54,473	58,993	60,349	66,410
out of which: outstanding claims	9,807	10,146	10,538	9,682	9,810
Calculated outstanding interest	5,396	5,444	5,621	4,508	4,581
- foreign currency	17,185	18,629	20,656	21,874	23,498
Government	80	85	86	139	129
out of which: outstanding claims	0	0	0	0	0
Non-government sector	17,105	18,544	20,570	21,735	23,369
out of which: outstanding claims	1,748	1,444	1,693	1,532	1,650
b) Claims by the National Bank from the Government	-18,989	-25,762	-30,847	-34,154	-30,690
<b>2. Other items, net</b>	<b>-42,837</b>	<b>-46,137</b>	<b>-47,543</b>	<b>-46,356</b>	<b>-48,888</b>
out of which: claims from the Government					
for frozen foreign currency saving deposits	0	0	0	0	0
Calculated outstanding interest	-5,399	-5,447	-5,644	-4,532	-4,603
Other	-37,438	-40,690	-41,899	-41,824	-44,285
<b>M4 Total</b>	<b>109,283</b>	<b>113,188</b>	<b>118,508</b>	<b>124,838</b>	<b>136,330</b>
<b>M4 (non-government sector)</b>	<b>108,174</b>	<b>111,912</b>	<b>117,333</b>	<b>123,869</b>	<b>135,131</b>

(continued from page 75)

Table D.1. Monetary review

	XII.05	III.06	VI.06	IX.06	XII.06 <sup>1)</sup>
<b>M1 (Total)</b>	<b>30,034</b>	<b>28,431</b>	<b>31,201</b>	<b>32,419</b>	<b>35,436</b>
<b>M1 (non-government sector)</b>	<b>29,663</b>	<b>27,962</b>	<b>30,768</b>	<b>32,090</b>	<b>34,747</b>
<b>Ready money in circulation</b>	<b>14,439</b>	<b>13,700</b>	<b>14,580</b>	<b>14,810</b>	<b>16,206</b>
<b>Deposit money (total)</b>	<b>15,595</b>	<b>14,731</b>	<b>16,621</b>	<b>17,609</b>	<b>19,230</b>
<b>Deposit money (non-government sector)</b>	<b>15,224</b>	<b>14,262</b>	<b>16,188</b>	<b>17,280</b>	<b>18,541</b>
Deposit banks	15,577	14,519	16,509	17,482	19,207
Deposit money of non-government sector	15,206	14,050	16,076	17,153	18,518
Deposit money of the Government	371	469	433	329	689
a) Budget and Ministries	236	132	158	92	551
b) Funds	135	323	275	236	138
c) Central government institutions: courts, etc.	0	14	0	1	0
National Bank - deposit money of non-government sector	18	212	112	127	23
<b>M2 (Total)</b>	<b>104,195</b>	<b>107,835</b>	<b>112,772</b>	<b>118,872</b>	<b>129,644</b>
<b>M2 (non-government sector)</b>	<b>103,134</b>	<b>106,607</b>	<b>111,645</b>	<b>117,952</b>	<b>128,494</b>
<b>Quasi -deposits (total)</b>	<b>74,161</b>	<b>79,404</b>	<b>81,571</b>	<b>86,453</b>	<b>94,208</b>
<b>Quasi -deposits (non-government sector)</b>	<b>73,471</b>	<b>78,645</b>	<b>80,877</b>	<b>85,862</b>	<b>93,747</b>
Deposit banks	74,161	79,404	81,571	86,453	94,208
Non-government sector	73,471	78,645	80,877	85,862	93,747
Denar	24,364	27,889	28,062	30,638	36,317
Foreign currency	49,107	50,756	52,815	55,224	57,430
Government deposits	690	759	694	591	461
Denar	689	759	694	590	460
Foreign currency	1	0	0	1	1
NBRM - quasi-deposits	0	0	0	0	0
<b>Non - monetary (total)</b>	<b>5,088</b>	<b>5,353</b>	<b>5,736</b>	<b>5,966</b>	<b>6,686</b>
Denar non-monetary deposits (total)	3,105	3,171	3,303	3,292	3,678
Non-monetary deposits in foreign currency (total)	1,983	2,182	2,433	2,674	3,008
<b>Non-monetary deposits (non-government sector)</b>	<b>5,040</b>	<b>5,305</b>	<b>5,688</b>	<b>5,917</b>	<b>6,637</b>
Denar non-monetary deposits (non-government sector)	3,057	3,123	3,255	3,243	3,629
Non-monetary deposits in foreign currency (non-government sector)	1,983	2,182	2,433	2,674	3,008
- Deposit banks	5,088	5,353	5,736	5,966	6,686
Denar non-monetary deposits - non-government sector	3,057	3,123	3,255	3,243	3,629
Non-monetary deposits in foreign currency - non-government sector	1,983	2,182	2,433	2,674	3,008
Denar non-monetary deposits - government	48	48	48	49	49
Non-monetary deposits in foreign currency - government	0	0	0	0	0
- NBM non-monetary deposits (non-government sector)	0	0	0	0	0
Denars	0	0	0	0	0
Foreign currency	0	0	0	0	0
<b>Total deposits</b>	<b>94,844</b>	<b>99,488</b>	<b>103,928</b>	<b>110,028</b>	<b>120,124</b>
<b>Total deposits (non-government sector)</b>	<b>93,735</b>	<b>98,212</b>	<b>102,753</b>	<b>109,059</b>	<b>118,925</b>

1) Final data

## E. SOCIAL SECTOR

**Table E.1.** Employment and unemployment rates (2003-2006)

	Employment rate				Unemployment rate			
	2003	2004	2005	2006	2003	2004	2005	2006
<b>Total</b>	<b>38,5</b>	<b>36,8</b>	<b>37,9</b>	<b>39,6</b>	<b>37,1</b>	<b>37,4</b>	<b>37,6</b>	<b>36,3</b>
Men	45.6	44.4	45.4	48.3	37.4	37.1	36.9	35.6
Women	31.3	28.9	30.1	30.7	36.7	38.0	38.8	37.5
15-24	12.1	11.5	12.3	14.4	66.1	67.6	62.6	59.9
55-64	28.1	24.0	26.2	36.4	18.8	25.2	27.9	28.4
Primary	20.7	18.1	19.9	-	45.1	46.1	43.3	41.8
Secondary	43.9	41.5	42.0	-	36.2	37.6	38.6	36.9
Higher education	63.5	65.5	64.0	-	19.4	18.3	20.5	21.3

**Table E.2.** Employed persons according to the economic status, sectors and property (age 15-80)

	2003	2004	2005	2006
Employment according to the economic status				
Employees	72.7	75.4	71.8	70.8
Employers	7.6	5.9	5.7	5.9
Self-employees	8.2	10.2	12.0	12.4
Unpaid family workers	11.4	8.5	10.4	10.9
Employment by sectors				
Agriculture	22.1	16.8	19.5	18.5
Industry	27.3	25.8	25.8	26.4
Construction	6.6	7.0	6.5	7.6
Services	44.0	50.4	48.2	47.5
Employees according to the ownership of business entity				
Private ownership	54.4	56.7	62.4	65.8
Other ownership (social, mixed, cooperative, state)	45.6	43.3	37.6	34.2

**Table E.3. Pension beneficiaries**

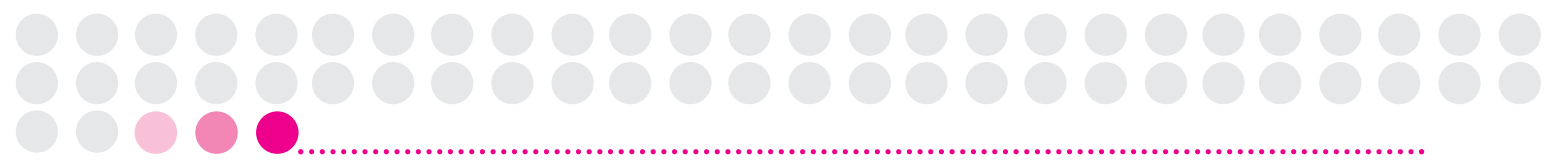
	2001	2002	2003	2004	2005	2006
I	241.364	247.094	249.583	254.723	260.364	265.686
II	241.863	247.419	249.858	255.279	260.591	266.125
III	242.157	247.615	250.355	254.333	260.879	266.615
IV	242.625	247.911	250.492	255.143	261.447	266.840
V	243.110	248.218	250.802	256.274	259.985	266.242
VI	244.125	247.594	251.166	256.917	261.005	266.842
VII	244.751	247.807	251.284	257.294	261.975	267.426
VIII	244.972	248.671	251.471	257.688	262.641	267.686
IX	244.596	248.178	251.589	258.360	262.833	267.636
X	245.158	248.522	251.614	257.014	262.855	267.711
XI	246.499	249.561	253.367	259.124	264.366	268.936
XII	247.200	249.421	254.267	260.075	265.152	269.681
<b>Average I - XII</b>	<b>244.035</b>	<b>248.168</b>	<b>251.321</b>	<b>256.852</b>	<b>262.008</b>	<b>267.286</b>

**Table E.4. Number of households receiving welfare**

	2001	2002	2003	2004	2005	2006
I	77.642	79.790	58.024	59.213	66.243	65.949
II	78.098	80.905	59.997	64.032	68.080	64.094
III	78.226	82.099	60.954	64.584	69.667	67.629
IV	75.728	77.247	60.311	64.163	63.442	61.676
V	76.939	80.569	61.707	64.832	66.604	63.030
VI	76.808	80.839	62.739	64.594	68.011	64.402
VII	76.057	79.690	61.847	65.026	66.328	64.054
VIII	75.407	82.633	62.963	65.681	67.736	64.553
IX	76.722	82.556	63.173	65.960	68.517	65.380
X	77.161	81.433	62.330	65.218	66.532	65.382
XI	78.747	81.885	63.256	66.402	67.094	65.620
XII	80.160	82.673	64.453	66.940	66.485	65.540
<b>Average I - XII</b>	<b>77.308</b>	<b>81.027</b>	<b>61.813</b>	<b>64.720</b>	<b>67.062</b>	<b>64.776</b>

**Table E.5. Number of beneficiaries of unemployment benefit**

	2001	2002	2003	2004	2005	2006
I	36.214	41.618	45.314	49.307	46.928	39.850
II	37.025	41.698	44.521	50.882	46.059	39.171
III	36.815	43.639	44.125	53.273	44.230	36.982
IV	36.768	43.696	44.058	51.304	44.267	36.228
V	36.618	44.782	45.436	51.509	43.968	35.024
VI	36.413	46.718	45.484	51.221	43.570	36.184
VII	36.403	48.134	44.599	49.691	42.878	33.843
VIII	35.379	48.514	44.175	48.821	43.075	33.761
IX	36.908	47.705	44.596	48.189	41.412	33.196
X	36.638	48.267	44.970	46.299	41.462	32.349
XI	37.129	47.330	45.891	45.652	40.767	31.400
XII	41.375	46.772	47.324	45.867	40.124	30.572
<b>Average I - XII</b>	<b>36.974</b>	<b>45.740</b>	<b>41.097</b>	<b>49.335</b>	<b>43.228</b>	<b>34.880</b>



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