

Republic of Macedonia
Ministry of Finance

Q3 2014

QUARTERLY ECONOMIC REPORT

Q3/2014

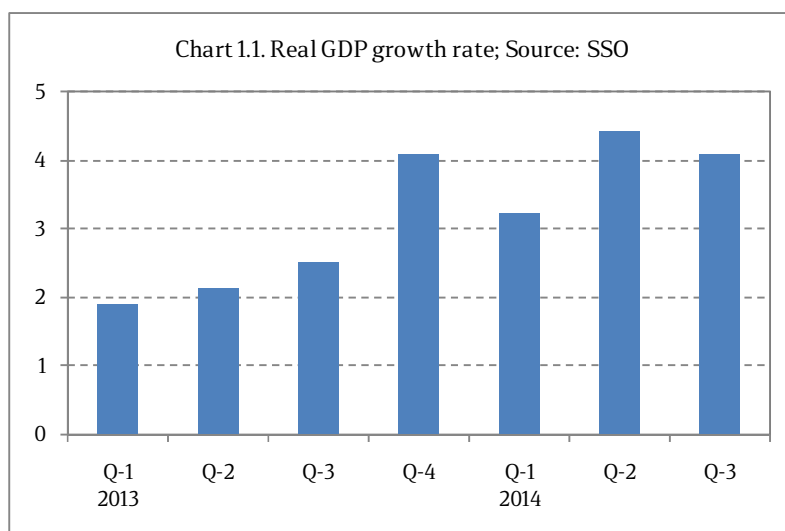
Summary

- **GDP** in Q3 2014 compared to the same quarter in the previous year experienced **real growth** of 4.1%.
- **Number of employed** persons in Q3 2014 was higher by 1.2% compared to the same quarter in the previous year. **Number of unemployed persons** dropped by 2.7% on annual basis, which resulted in reduction of **unemployment rate** to 27.9% in Q3 2014;
- **Inflation rate** in Q3 2014 experienced drop of 0.3% compared to the same quarter in 2013, measured according to the Consumer Price Index;
- Average **gross salary** in Q3 2014 amounted to Denar 31,165 and compared to the gross salary in Q3 2013, it was higher by 0.8% in nominal terms and by 1.1% in real terms;
- Total **budget revenues** were lower by 2.6% in Q3 2014, and total **budget expenditures** dropped by 0.6% compared to the same quarter in 2013;
- Total **deposit potential** of banks increased by 3.6% in Q3 2014 on quarterly basis;
- **Credit activity** of banks to non-government sector in Q3 2014 grew by 1.4% on quarterly basis;
- **Macedonian Stock Exchange Index MSEI-10** in September 2014 increased by 4.9% compared to June 2014, while total turnover realized on the Stock Exchange decreased by 42.2%;
- In Q3 2014, **export increased** by 19.1%, while **import** surged by 16.0%, on annual basis (Q/Q-4), whereby total **foreign trade**, expressed in euros, increased by 17.2%;

1. Macroeconomic Trends and Real Sector

In Q3 2014, compared to the same quarter of 2013, **GDP** showed real growth of 4.1%, by which the GDP growth in the first three quarters of 2014 accounted for 3.9%¹. Nominal GDP growth in Q3 2014 accounted for 2.8% compared to the same quarter last year, implying that GDP deflator amounted to -1.3%.

Analyzed according to the **production side of GDP**, in Q3 2014, positive performance was observed in all sectors. Industrial production continued its positive trends, registering



5.8% growth in Q3 2014, as a result of the growth in the manufacturing industry, experiencing high growth of 16.6%. Services sector experienced 3.5% growth in Q3. As for services, the trade, transport and catering sector contributed the most to the growth of economic activity, experiencing 2.9% growth, followed by the sectors real estate activities (2.8%), financial and insurance activities (7.5%), professional, scientific and technical activities (8.2%), other service activities (11.6%), information and communication (4%) and public administration and defense (0.8%). Construction in Q3 2014 grew by 2.6%, followed by the 0.5% growth in the previous quarter. Real growth rate in agriculture accounted for 0.3%.

Growth of **industry** in Q3 2014 according to the monthly data on industrial production, accounted for 5.4%, being a result of the realized positive rates at: manufacture of other transport equipment (37.3%), manufacture of tobacco products (35%), manufacture of electrical equipment (24.7%), manufacture of paper and paper products (23.1%), manufacture of fabricated metal products (20.5%), manufacture of machinery and equipment (16.7%), manufacture of basic pharmaceutical products (15.3%), manufacture of food products (13.3%), manufacture of basic metals (10.1%), manufacture of beverages (4.4%), other mining and quarrying (3.4%), manufacture of wearing apparel (2.7%), manufacture of rubber and plastic products (2%), manufacture of motor vehicles² and other manufacturing (46.4%). Hence, annual positive growth was registered at 14, comprising 63.7% of the industrial production.

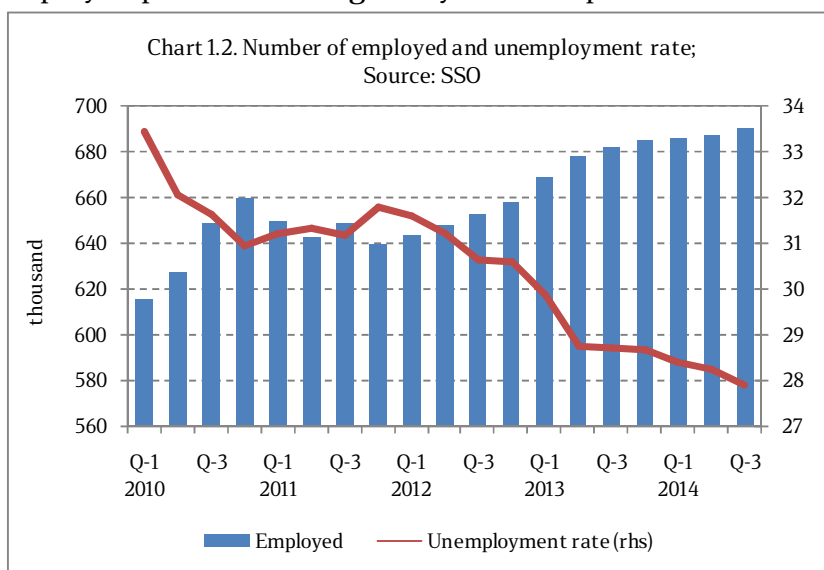
¹ State Statistical Office revised the GDP real growth rates in Q1 and Q2 2014. Thus, GDP growth in Q1 2014 was revised to 3.2% from the previous 3.5%, while the growth in Q2 2014 was revised to 4.4% from the previous 4.3%.

² Index in this activity is higher than 1000.

Drop was seen at: manufacture of coke and refined petroleum products (75%), electricity, gas, steam and air conditioning supply (23.4%), repair and installation of machinery and equipment (13.2%), printing and reproduction of recorded media (12.6%), mining of coal and lignite (10.5%), manufacture of furniture (8.4%), mining of metal ores (5.9%), manufacture of textile (5.4%), manufacture of wood and products of wood and cork (1.7%), manufacture of other non-metallic mineral products (1.7%), manufacture of chemicals and chemical products (1.6%) and manufacture of leather and related products (1.2%).

Analyzed according to the **expenditure side of GDP**, in Q3 2014, growth was driven by gross investments and export. Annual real growth of gross investments accounted for 17%, as a result of the investments in the construction and the growth of import of investment goods. Export of goods and services in Q3 2014 increased by 15.4% in real terms, mainly as a result of the growth of export of companies in the technological industrial development zones, as well as the industrial zones. Import of goods and services surged by 14%. Final consumption in Q3 2014 grew by 1%, being a result of the increase of personal consumption by 2.5%, while public consumption dropped by 5.2%. Growth of personal consumption was mainly a result of the increase of employment and higher growth of crediting to households in this quarter.

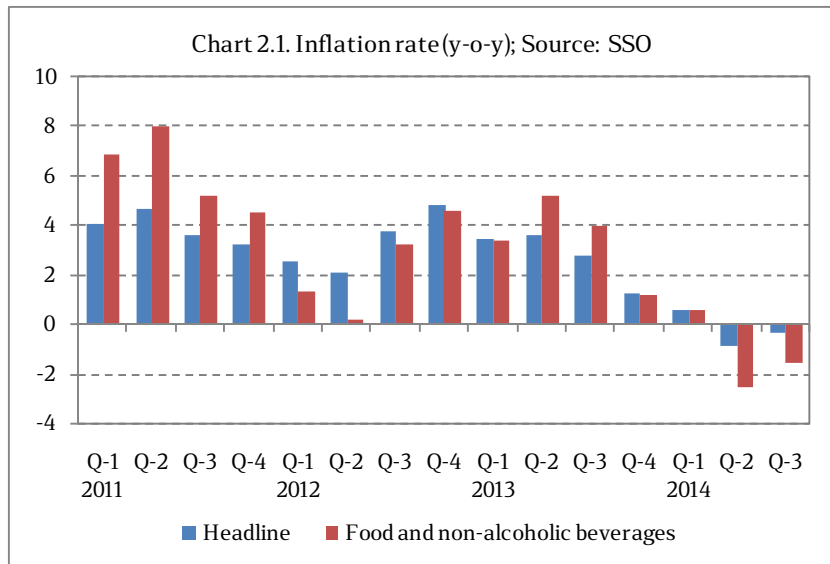
Positive trends continued on the labour market in Q3 2014. According to the **Labour Force Survey**, number of employed persons was higher by 1.2% compared to the same quarter in the previous year. Increase of employment was accompanied by the drop of the number of unemployed persons, decreasing by 2.7% on annual basis. Number of active population in Q3 2014 was higher by 0.1% on annual basis. Such trends on the labour market caused for the unemployment rate in



Q3 2014 to reduce to 27.9%, i.e. by 0.8 percentage points (p.p). compared to the same quarter of the previous year. Employment rate in Q3 amounted to 41.3%, being higher by 0.5 p.p. compared to the same quarter in the previous year. Active population in Q3 2014 accounted for 57.3% of total working-age population, being at the same level compared to Q3 in the previous year.

2. Prices, Costs and Productivity

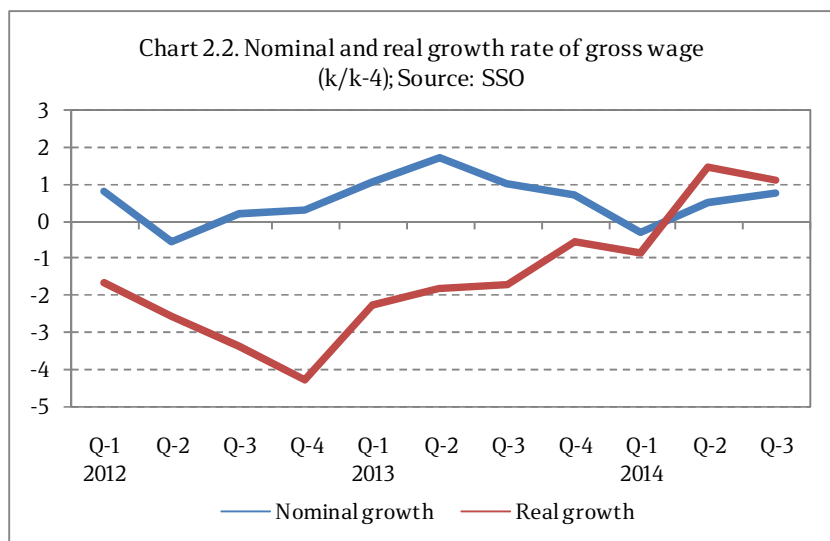
Inflation, in Q3 2014 experienced drop of 0.3% compared to the same quarter in 2013, following the 0.9% drop, measured according to the Consumer Price Index. Price decrease was a result of the reduced prices in many categories: recreation and culture by 5.4%, communication by 2.9%, furnishings, households equipment and routine maintenance of the house by 2.4%, food and non-alcoholic beverages by 1.6%, restaurants and hotels by 1.3% and transport by 0.3%. Highest growth of consumer prices in Q3 2014 was recorded in the category health by 7.7%, followed by the following



categories: alcoholic beverages and tobacco by 3.9%, housing, water, electricity, gas and other fuels by 1.7%, miscellaneous goods and services by 1.4%, clothing and footwear by 0.9% and education by 0.2%.

Retail prices in Q3 2014 decreased by 0.9% compared to the same quarter in 2013, following the 1.2% drop observed in the previous quarter. Drop of retail prices in this period was due to the decreased prices in the category services, being lower by 2.2% on annual basis. Prices remained the same in the goods category. Thereby, drop of prices was seen at agricultural products by 0.9%, while prices of industrial products surged by 0.1% as a result of the increase of the retail price of tobacco by 4.4%, the increase of the retail price of beverages by 0.4%, as well as the growth of the retail price of non-food industrial products by 0.3%. Retail prices of food industrial products dropped by 1.3%.

Average **net salary** in Q3 2014 amounted to Denar 21,282, being higher by 1.1% in nominal terms compared to net salary in Q3 2013. Net salary grew by 1.4% in real terms. Average **gross salary** amounted to



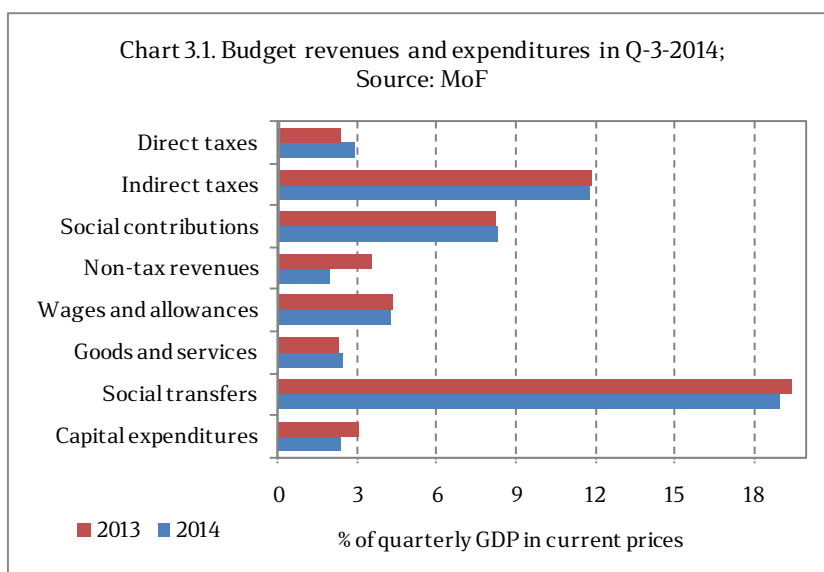
Denar 31,165, increasing by 0.8% in nominal terms, i.e. surging by 1.1% in real terms, compared to the gross salary in Q3 2013.

Growth of economic activity in Q3 2014 was also accompanied by the increase of the number of employees. Thereby, economic growth was higher than employment, also resulting in growth of **labour production** of 2.8%, by which the positive growth of productivity continues.

3. Fiscal Sector

Lower performance of total budget revenues by 2.6% was observed in the third quarter of 2014, compared to same quarter in 2013, accompanied by lower budget expenditures by 0.6%. **Budget deficit** was in the amount of Denar 2,696 million in Q3 2014 or 2.0% of GDP realized in this quarter (central budget deficit amounted to Denar 2,633 million, i.e. 2.0% of GDP).

Total **budget revenues** participated with 27.0% of the realized quarterly GDP, being lower by 2.6% compared to the same quarter in 2013, being mostly due to the lower performance of non-tax revenues by 41.8%, higher tax revenues by 2.7%, as well as higher contributions by 3.6%. Thereby, as for tax revenues, higher collection was recorded at excise duties, value added tax, personal income tax and profit tax, while only customs duties and other taxes experienced lower collection.



VAT revenues dominated, accounting for 52.0% of the total tax

revenues, surging by 1.0% in Q3 2014, compared to the same quarter in 2013. As for gross VAT revenues, gross collection was higher by insignificant 0.1%, while VAT refund was higher by 14.3% compared to the same period in 2013.

As for VAT structure, VAT share was the biggest when importing, increasing by 4.2%, while VAT on the basis of sales in the country grew by 4.5%, while share of VAT grants and interest was insignificant (0.9%). Excise revenues were higher by 5.4% compared to the same quarter of 2013. As for direct taxes, personal income tax increased by 21.4%, revenues on the basis of profit tax increased by 27.5% compared to the same quarter of the previous year, whereby one should take into account that the revenues for this tax

is mainly a result of the tax collected on the basis of monthly advance payments and paid dividends and other distribution of profit and withheld tax paid to foreign legal entities.

From the point of view of structural share in GDP, direct taxes on annual basis increased their share in GDP by 0.5 p.p. (2.9% of GDP), while the share of indirect taxes was identical (11.8% of GDP).

Collection of social contributions was higher by 3.6%, whereby higher collection was recorded at all contributions, i.e. pension insurance contributions - 3.1%, health insurance contributions - 4.7% and employment contributions - 4.0%. Non-tax revenues, accounting for 2.0% of total quarterly GDP, were lower by 41.8% compared to the same period in 2013.

Capital revenues in Q3 2014 were lower by 56.1% on annual basis (these revenues include revenues on the basis of lease of construction land, sale of flats, as well as revenues on the basis of dividends). Revenues on the basis of grants were lower by 24.0%, compared to Q3 2013.

In Q3 2014, total **budget expenditures** participating with 29.0% in the quarterly GDP, were lower by 0.6% compared to the same quarter in 2013. Current expenditures, accounting for 26.7% of quarterly GDP, participating with 91.9% in the total expenditures, were realized by 1.6% more on annual basis. As for current expenditures, expenditures for goods and services increased by 8.1%, while expenditures related to salaries and allowances surged by 1.5% compared to the same quarter last year. Funds for transfers, which participated with 2/3 in the total expenditures (65.5%), were higher by 0.5% on annual basis. Social transfers surged by 1.7%, accounting for 49.7% in the total expenditures. Transfers to the Pension and Disability Insurance Fund, accounting for the most in the social transfers, surged by 8.7%, participating with 31.7% in the total expenditures. Category other transfers, which includes transfers to local government units, accounted for 15.3% in the total expenditures, i.e. they dropped by 1.6% compared to the same period in 2013. Block grants to local government units reduced by 5.9%, while subsidies and transfers were higher by 2.3%.

Expenditures for interest payments surged by 9.6% on annual basis, while compared to Q2 2014 they were lower by 29.6 p.p.. Expenditures on the basis of interests on domestic debt grew by 16.5% on annual basis, while interests on foreign debt grew by 4.1% on annual basis, while compared to Q2 2014, they were lower by 8.2%.

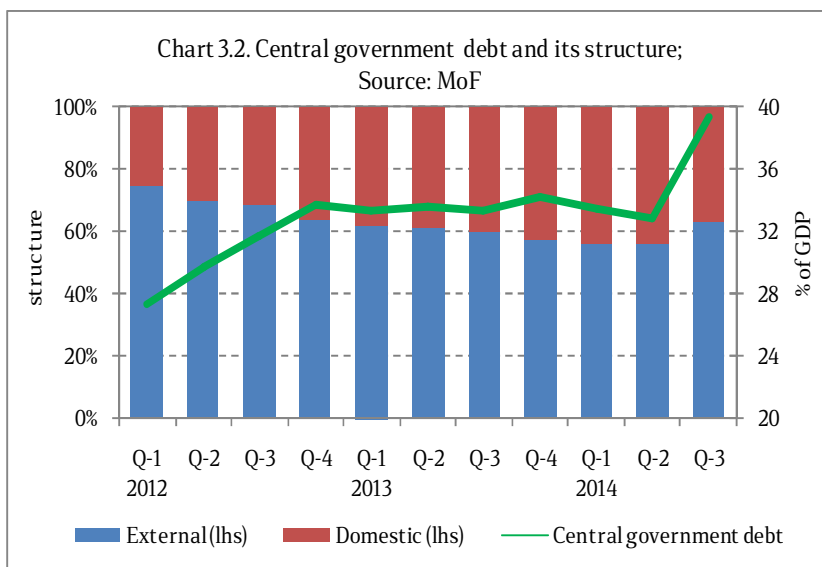
Capital expenditures accounting for 2.4% of quarterly GDP, compared to the same quarter in 2013, were lower by 20.4%, i.e. they participated with 8.1% in the total expenditures.

Fiscal burden, measured as participation of the budget revenues³ in relation to nominal GDP, was 24.2% in Q3 2014, being an identical amount of burdening in relation to Q2

³ It includes tax revenues, social contributions and administrative fees and duties.

2014. Total budget expenditures accounted for 29.0% of quarterly GDP, which was by 1.0 p.p. lower compared to Q2 2014, decreasing by 1.0 p.p. on annual basis.

Total **central government debt**, at the end of Q3 2014 experienced increase of its share in GDP by 6.4 p.p., compared to Q2 2014. Share of central government external debt in the total central government debt increased by 6.4 p.p. compared to Q2 2014, while share of central government domestic debt in the total central government debt decreased by the same amount of percentage points. Hence, share of central government domestic debt decreased to 37.2% of the total central government debt.



4. Monetary and Financial Trends

As for the third quarter of 2014, NBRM assessed the monetary position as adequate to the economic and financial conditions, retaining the reference interest rate at the same level of 3.25%. Interest rate on available 7-day deposits remained the same, accounting for 1.25%.

Primary money⁴ in Q3 2014 registered intensified quarterly growth of 2.9% (accounting for 2.5% in Q2 2014) in conditions of growth of total liquidity of banks by 2.1% and cash in circulation by 3.9%. Compared to September 2013, primary money increased by 7.5% (compared to 2.2% growth in Q2 2014), as a result of the increase of cash in circulation by 9.6% and total liquidity of banks by 5.7%.

During the third quarter of 2014, narrowest money supply **M1** experienced quarterly growth of 5.2% compared to Q2 2014. **Monetary aggregate M2**, in Q3 2014 surged by 3.3%, while the widest **monetary aggregate M4** increased by 3.7%.

Total deposit potential⁵ of banks in Q3 2014 surged by 3.6% on quarterly basis, being accelerated growth compared to the previous quarter, when 0.4% growth was recorded. From the sectoral structure aspect, the increased deposit potential was due to the

⁴It includes ready money in circulation (including cash in hand of banks), denar and foreign currency reserve requirement and the surplus of liquid assets over the reserve requirement (in denars).

⁵Deposits also include calculated interest.

increase of deposits of private enterprises by 8.8%. At the same time, deposits of households experienced quarterly growth of 1.9%.

Analyzed by currency, Denar deposits increased by 4.1%, while foreign currency deposits grew by 2.9% compared to the previous quarter. Level of euroization measured through the share of foreign currency deposits in the total deposit potential reduced by 0.2 p.p., i.e. to 42.4%.

Analyzed by maturity, in the past period, there was continuous growth of share of long-term deposits in total deposit potential, reaching 26.6% in Q3 2014, being in line with the quarterly increase of long-term deposits by 4.7% (3.3% in Q2 2014). Short-term deposits grew by 2.3% in the analyzed period.

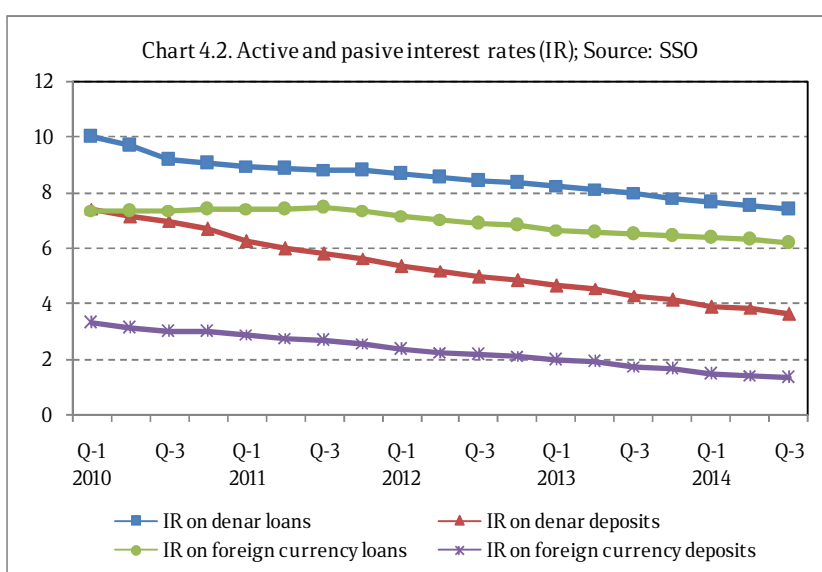
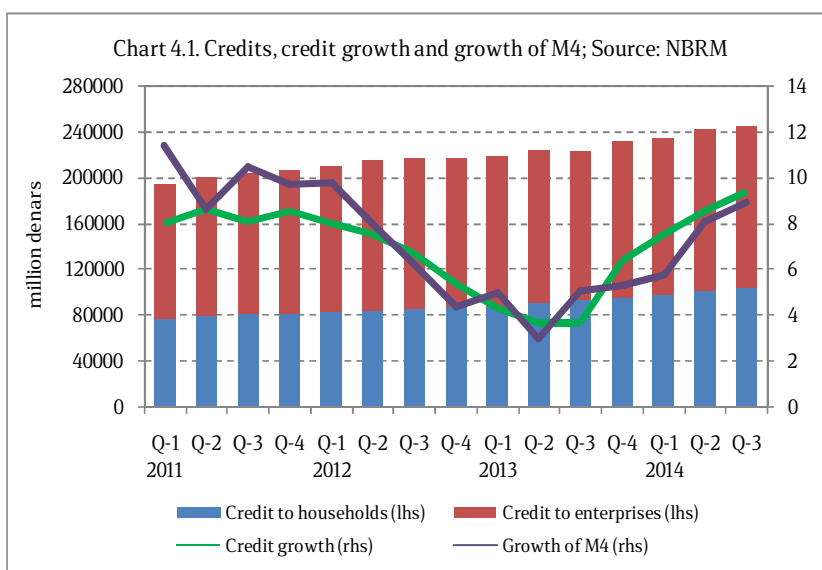
Credit activity of banks to non-government sector

in Q3 2014 experienced growth of 1.4% on quarterly basis (compared to the 2.9% growth in the previous quarter), in conditions of growth of credits to households by 2.9%, and growth of credits to private enterprises by 0.4%. Analyzed by currency, Denar credits

were driving force of the increase of total credits, increasing by 1.7% on quarterly basis, while foreign currency credits in Q3 2014 registered quarterly growth of 0.4%.

Analyzed by maturity, long-term credits in Q3 2014 experienced quarterly growth of 1.4%, while short-term credits were lower by 0.2%.

In the third quarter of 2014, NBRM retained the **interest rate on CB bills** at 3.25%. Interest rates of deposit banks in Q3 2014 also experienced downward swings on quarterly basis. In fact,

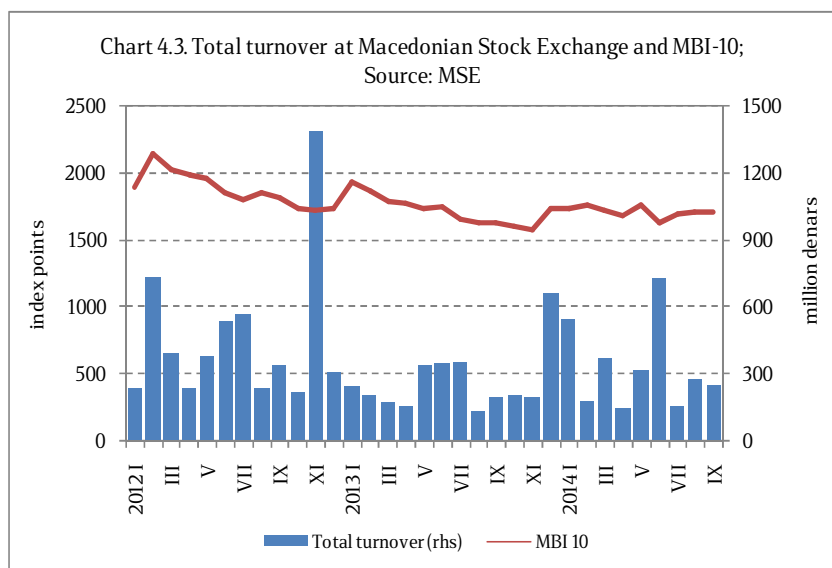


interest rate on Denar credits reduced by 0.1 p.p. compared to the previous quarter, amounting to 7.4%. Thus, the downward trend of this interest rate, which started at the beginning of 2010, continued. Interest rate on foreign currency credits reduced from 6.3% in Q2 2014 to 6.2% in Q3 2014. Interest rate on Denar deposits in Q3 2014 accounted for 3.7%, being lower by 0.2 p.p. compared to the previous quarter, while the interest rate on foreign currency deposits decreased by 0.1 p.p., amounting to 1.3% in Q3 2014.

Interest rate on newly approved Denar credits in Q3 2014 reduced by 0.1 p.p., on quarterly basis, amounting to 6.6%, while interest rate on newly approved foreign currency credits reduced from 0.2 p.p. to 5.9%. Interest rate on newly received Denar deposits dropped by 0.1 p.p., accounting for 2.0%, while interest rate on newly received foreign currency deposits amounted to 0.4%, remaining the same compared to the previous quarter.

On the **capital market**, in the third quarter of the year, total turnover of the Stock Exchange experienced drop of 42.2% compared to the previous quarter, being a result of the reduced amount of block transactions. Turnover realized through traditional trading grew by 1.3%.

Compared to the same quarter in the previous year, total turnover grew by 0.6% in conditions of increased traditional trading turnover. Turnover realized through traditional trading grew by 33.5% on annual basis.



Macedonian Stock Exchange Index MSEI -10, as aggregate indicator of stock exchange trends at the end of the third quarter amounted to 1,713.44 index points, increasing by 4.9% compared to June 2014, while compared to September 2013, the index was higher by 4.8%.

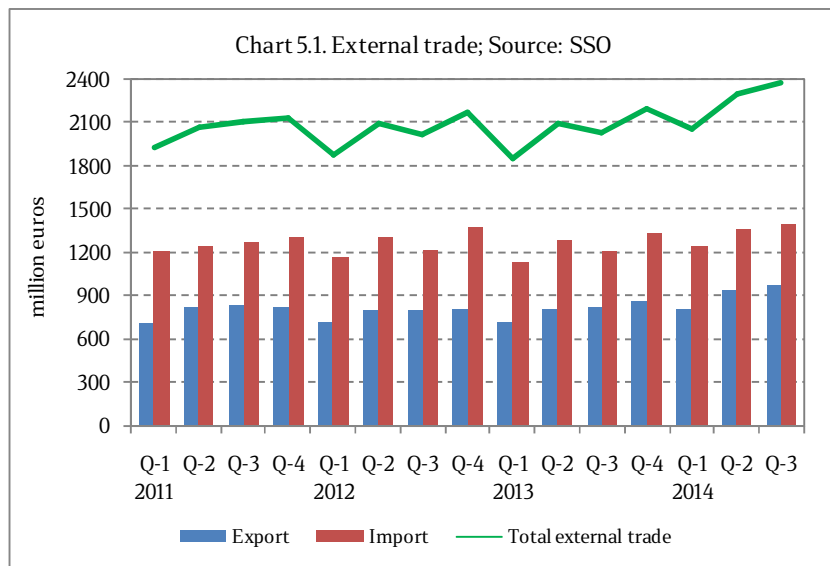
5. External Sector

5.1. Foreign Trade

According to the data of the State Statistical Office in Q3 2014, total foreign trade amounted to EUR 2,384.0 million, increasing by 17.2% compared to the same quarter in 2013.

In Q3 2014, **export** of goods amounted to EUR 982.9 million and, compared to the same quarter in the previous year, it surged by 19.1%, while compared to the previous quarter, it increased by 4.7%.

Analyzed by **SITC sectors** (Standard International Trade Classification), positive trends in the **export** in



Q3 2014 compared to the same quarter in 2013 were registered at the following:

- machines and transport equipment surged by almost two times (within which the following categories experienced increase: electrical machines, devices and spare parts by more than two times or EUR 51.4 million; industrial machines and spare parts by 52.2% or EUR 29.5 million; and road vehicles by almost three times or EUR 12.8 million);
- chemical products by 28.8% (chemical materials and products increased by 40.8% or EUR 46.8 million);
- various finished goods by 10.8% (within which the following categories increased: furniture and parts thereof, bed linen, mattresses and similar by almost two times or EUR 10.7 million, clothing by 5.8% or EUR 7.0 million);
- food products by 8.0% (within which the following categories increased: fruit and vegetables by 10.7% or EUR 5.0 million; cereals and cereal preparations by 11.7% or EUR 1.4 million; and
- raw materials except fuel by 2.0% (raw manure and minerals grew by 17.1% or EUR 1.2 million).

On the other hand, negative export trends are seen at:

- beverages and tobacco by 9.1% (tobacco and tobacco products by 12.3% or EUR 4.8 million);
- mineral oils and lubricants by 12.4% (oil and oil products decreased by 13.6% or EUR 2.8 million); and
- products classified by the material by 0.3% (iron and steel decreased by 0.6% or EUR 0.8 million).

In Q3 2014, observed by **economic purpose**, the following products have the largest share in export: goods for industrial procurement (47.8%), followed by consumer goods (19.8%), products for investments without transport equipment (12.0%), food and beverages (10.1%), transport equipment (8.4%) and fuels and lubricants (1.7%).

Import of goods in Q3 2014 amounted to EUR 1,401.1 million, increasing by 16.0% compared to Q3 2013, while in relation to the previous quarter, it increased by 2.5%.

Analyzed by **SITC sectors**, most positive movement of import in Q3 2014, compared to Q3 2013, was seen at:

- products classified according to the material by 28.2% (whereby increase was seen at the following categories: non-ferrous metals by 68.3% or EUR 72.4 million; iron and steel by 28.1% or EUR 17.2 million);
- machines and transport equipment by 24.4% (electrical machines, devices and spare parts by 51.3% or EUR 26.2 million; and road vehicles by 23.7% or EUR 11.6 million);
- raw materials, except fuel by 65.4% (metal ore and metal scrap surged by more than two times or EUR 21.3 million);
- chemical products by 5.0% (inorganic chemical products by almost two times or EUR 10.2 million); and
- mineral oils and lubricants by 0.5% (electricity by 35.3% or EUR 9.1 million);
- food products by 2.1% (cereals and cereal preparations by 26.6% or EUR 3.8 million);
- various finished goods by 12.2% (clothing by 24.0% or EUR 3.2 million; and furniture and parts thereof, bed linen, mattresses and similar by 19.2% or EUR 1.7 million);

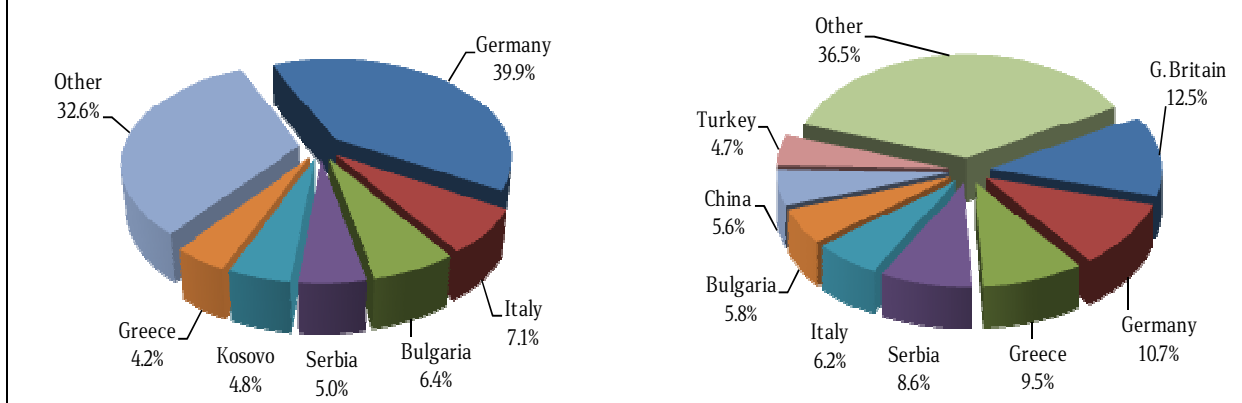
Highest decline of import was seen at the following:

- beverages and tobacco by 9.6% (whereby decline was seen at the following category: tobacco and tobacco products by 14.5% or EUR 1.1million).

Observed by **economic purpose** in Q3 2014, the following products have the largest share in import: goods for industrial procurement (48.0%), followed by fuels and lubricants (14.7%) investment goods without transport equipment (11.9%), consumer goods (10.1%), food and beverages (9.9%), and transport equipment (5.4%).

In Q3 2014, foreign trade of the Republic of Macedonia with the European Union (EU 27), in relation to Q3 2013, surged by 20.2%, whereby share of trade with EU in the total foreign trade increased by 0.7 p.p. compared to the third quarter in 2013, accounting for 68.1%. Export of goods participated with 74.5%, while import of goods with 63.5%.

Chart 5.2. Countries having the highest share in export (left) and import (right) in Q3 2014
Source: MoF calculation based on SSO data

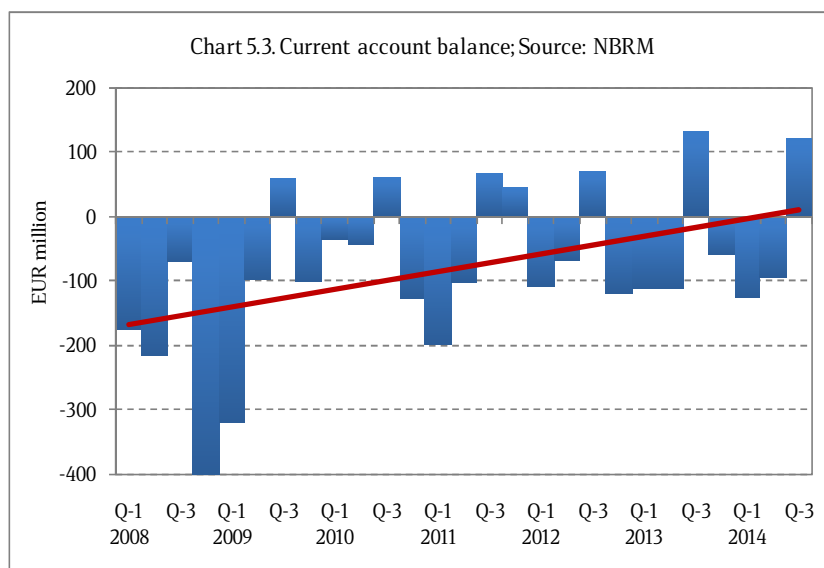


As a result of the structural changes in the trade with abroad, in the third quarter of 2014, 94.9% of the trade deficit of the country was a result of the trade deficit with Great Britain, Greece, Serbia and China, while the rest of the deficit was a result of the trade with: Turkey, Romania, Slovenia, Austria, Bulgaria, Russia, Italy and others. Surplus was realized in the trade with Germany, Kosovo, Belgium and Bosnia and Herzegovina.

5.2. Balance of payments

According to the data from the National Bank of the Republic of Macedonia on the payment of balance developments, current account surplus of EUR 120.6 million was registered in the third quarter of 2014, accounting for 5.6% of GDP⁶ and compared to the same quarter in 2013, it narrowed by 0,2 p.p.

On annual basis, the current account surplus in Q3 2014 decreased by 9.3%, whereby the deepening of the deficit of the goods account by 2.9% (contribution of -9.7 p.p.) and widened negative balance of the primary income account by 13.9% (contribution of -5.5 p.p.) contributed the most thereto. On the other hand, the increase of the surplus of services



⁶ Calculation also included GDP for the third quarter for 2014, announced by the State Statistics Office.

account by 2.1% (contribution of 2.4 p.p.) and the increased surplus of the secondary income account by 1% (contribution of 3,5 p.p.) acted in opposite direction.

In conditions of greater absolute increase of import compared to export of goods, **trade deficit** in Q3 2014 deepened by 2.9% on annual basis (or EUR 13 million), amounting to 20.9% of quarterly GDP.

In Q3 2014, in conditions of greater absolute increase of export compared to import of services, the balance of **services account** increased by 2.1% on annual basis.

Trade openness of the Republic of Macedonia in Q3 2014 amounted to 115.4%, being higher by 9.8 p.p. compared to the same quarter in 2013.

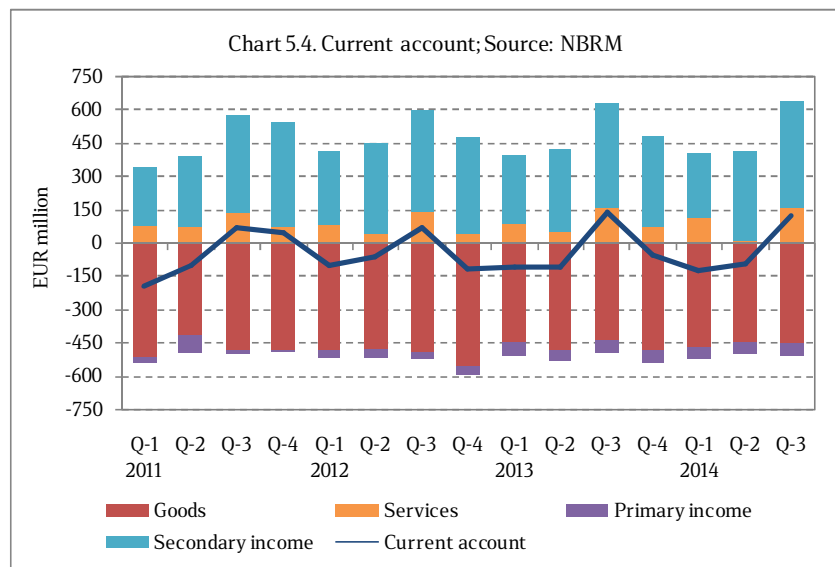
Primary income account in Q3 2014 had negative contribution of 5.5 p.p. in the current account development when registering net outflow of EUR 59.9 million and deepening by 14% on annual basis.

Inflows on the **secondary income** account in Q3 2014 amount to EUR 476.2 million, slightly

increasing on annual basis (1%). Growth was a result of the 3.8% increase of the incomes of the "financial corporations, non-financial corporations, households, and NPISHs"⁷, participating with 98.6% in the secondary income account, while the reduction of the incomes of the general government by 65.2% acted in opposite direction, participating with 1.4% in the secondary income account.

Capital account balance in Q3 2014 was negative, amounting to EUR-0.2 million, being unfavourable trend compared to Q3 2013, when surplus of EUR 1.6 million was realized.

Direct investments in the country in Q3 2014 amounted to EUR 53.2 million, reducing by 31.8% on annual basis (or by EUR 24.8 million) mainly due to the outflows/negative balance on the basis of re-invested profit (negative contribution of -66.3 p.p.) amounting to EUR -26.4 million in Q3 2014. Reduced inflow on the basis of equity (reduction by



⁷Secondary income account includes the incomes from the 1. General government and 2. Financial corporations, non-financial corporations, households and NPISHs, including 2.1/ Personal transfers (current transfers between resident and non-resident households) and 2.2/ Other current transfers.

11.4% in Q3 2014) acted in the same direction, while the inflow of funds on the basis of debt instruments (increase by 74% or EUR 28.5 million) acted in opposite direction.

Portfolio investments in Q3 2014 are negative, amounting to EUR -496.2 million, reducing by EUR 502.6 million on annual basis, mainly due

to the increase of debt securities, i.e. net liabilities of the general government increased due to the issued Eurobond in July 2014.

Other investments in Q3 2014 amounted to EUR 133.5 million, dropping by 29.1% on annual basis. As for the category other investments, currencies and deposits increased by 5.9%, while the loans were reduced by almost seven times.

Stock of foreign currency reserves at the end of the third quarter of 2014 amounted to EUR 2,435 million.

