January 2010
IMF Country Report No. 10/19

Former Yugoslav Republic of Macedonia: Staff Report for the 2009 Article IV Consultation—Staff Report; Staff Statement; Public Information Notice on the Executive Board Discussion; and Statement by the Executive Director for the Former Yugoslav Republic of Macedonia

Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. In the context of the 2009 Article IV consultation with the former Yugoslav Republic of Macedonia, the following documents have been released and are included in this package:

- The staff report, prepared by a staff team of the IMF, following discussions that ended on October 27, 2009, with the officials of the former Yugoslav Republic of Macedonia on economic developments and policies. Based on information available at the time of these discussions, the staff report was completed on November 24, 2009. The views expressed in the staff report are those of the staff team and do not necessarily reflect the views of the Executive Board of the IMF.
- A staff statement of December 11, 2009.
- A Public Information Notice (PIN) summarizing the views of the Executive Board as expressed during its December 11, 2009 discussion of the staff report that concluded the Article IV consultation.
- A statement by the Executive Director for the former Yugoslav Republic of Macedonia.

The document listed below has been separately released.

Selected Issues

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

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INTERNATIONAL MONETARY FUND

FORMER YUGOSLAV REPUBLIC OF MACEDONIA

Staff Report for the 2009 Article IV Consultation

Prepared by Staff Representatives for the 2009 Consultation with
Former Yugoslav Republic of Macedonia

Approved by Adam Bennett and Michele Shannon

November 24, 2009

Discussions. Skopje, October 15−27, 2009. The mission met with Finance Minister and Deputy Prime Minister Stavreski; Deputy Prime Minister Peshevski; Economy Minister Besimi; NBRM Governor Goshev; other officials; members of the opposition parties; the private sector; and others. At the conclusion of the mission a joint press conference was held with the finance minister and NBRM governor.

Team: Mr. McGrew (head), Ms. Chen (EUR), Mr. Gottlieb (EUR), Ms. Dobrescu (FAD), Mr. Salman (SPR), and Mr. Tieman (Resident Representative).

Consultation focus: The discussions focused on the impact of the global crisis and the policy mix needed to support economic stability and a resumption of growth in the context of the exchange rate peg.

Political developments and EU accession: The government holds a majority in parliament and the next elections are not due until 2012. The ruling VMRO party won the presidency and most municipal elections in March−April 2009. FYR Macedonia is an EU candidate country, and in October 2009 the European Commission recommended the start of accession talks. However, the opening of negotiations requires a unanimous decision by EU members, and Greece is seen as unlikely to agree until a long-standing dispute on the country's name is resolved.

Publication intentions: The authorities have not yet indicated whether they will agree to publication.

Exchange rate arrangement and Article VIII status: The *de jure* exchange rate regime is managed floating; the *de facto* regime is a stabilized arrangement against the euro. Macedonia has accepted the obligations of Article VIII, sections 2, 3, and 4.

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Boxes

I. Executive Summary and Staff Appraisal

1. **Macedonia's main vulnerability at the outset of the global crisis was its large current account deficit in the context of the exchange rate peg to the euro.** At the same time it benefited from a small fiscal deficit, modest public debt, significant international reserve buffers, and a small banking system with limited reliance on external financing—which provided room for maneuver and limited its exposure to global financial conditions.

2. **The crisis hit Macedonia at the end of 2008 through a collapse in export demand and loss of external financing.** These factors caused a sharp slowdown in the economy and a decline in tax revenues. They also forced a rapid sell-off of central bank foreign exchange reserves, and raised uncertainties about the sustainability of the exchange rate peg. Currency substitution and cash outflows by residents added to pressures on reserves, while elections in spring 2009 created additional uncertainties. By May 2009 central bank reserves had fallen below €1.2 billion (75 percent of short-term debt), 30 percent down from the October 2008 peak.

3. **The National Bank of Macedonia (NBRM) responded to reserve outflows by raising its policy rate from 7 to 9 percent (even as inflation fell to zero) and tightening bank reserve and liquidity requirements.** These actions helped to slow credit growth and contain the loss of reserves.

4. **The government curtailed planned spending increases under the 2009 budget to preserve its 2.8 percent of GDP deficit target in the face of declining revenues.** It also issued an €175 million Eurobond (at 9⅞ percent) in July, which bolstered reserves and ensured sufficient budget financing.

5. **By the second half of 2009 the situation had stabilized and confidence had improved.** Indicators of activity flattened out or turned positive, external financing pressures eased, and by November reserves had recouped 70 percent of their earlier losses. In the banking sector nonperforming loans rose and profits fell, but capital adequacy ratios remained high and no significant liquidity pressures emerged. For the year as a whole, staff expect GDP to decline 1.3 percent, less than most countries in the region, and slight deflation.

6. **Looking ahead, the slow pace of recovery in trading partners and continued tightness in external financing conditions will weigh on the economy.** As a result, staff and the authorities expect only a moderate recovery to 2 percent growth in 2010. The current account deficit is expected to narrow from 13 percent of GDP in 2008 to 9½ percent in 2009 and 8 percent in 2010, while reserves are expected to finish 2009 at 90 percent of short-term debt and remain near that ratio over the medium term.

7. **The NBRM's response to the crisis has been appropriate in light of its commitment to protect the exchange rate peg.** The pegged regime has served Macedonia

well by providing a stable policy framework that is supportive of steady growth and low inflation. Moreover, staff analysis does not show significant exchange rate misalignment. Nonetheless, maintaining policies supportive of the exchange rate anchor is critical and the high interest rates currently prevailing are one of the tradeoffs associated with the exchange rate anchor. At this stage, further tightening does not appear warranted, given the underlying improvement in the balance of payments, weak credit growth and economic activity, and modest deflation. On the other hand, an easing of monetary conditions, which would translate into faster growth and less current account adjustment, should await greater certainty that reserves are on an underlying upward path.

8. **The government's 2009 fiscal stance is appropriate in the current circumstances.** The targeted deficit (equivalent to 2.8 percent of GDP) reflects the operation of automatic stabilizers, is fully financed, and is consistent with medium-term sustainability. While a tighter stance would have helped contain the current account deficit and protect reserves and the peg, it would likely have been at the cost of lost output and employment.

9. **The government has set a target of 2.5 percent of GDP for the fiscal deficit in 2010 and 2 percent of GDP or lower for the medium term.** Staff view the 2010 target, which is modestly contractionary in cyclically adjusted terms, as appropriate in light of financing constraints and the need to strike a balance between supporting growth and containing external imbalances. Over the medium term, staff advise a fiscal deficit of below 1.5 percent of GDP in order to maintain debt at moderate levels that will support policy flexibility under the peg.

10. **Looking forward, Macedonia's key risks arise from its still sizable current account deficit, in the context of the exchange rate peg.** The failure of exports and FDI to recover as expected, or persistent global financial strains, could put renewed pressures on foreign exchange reserves. On the upside, progress towards EU accession could bolster foreign investment and ease external financing pressures.

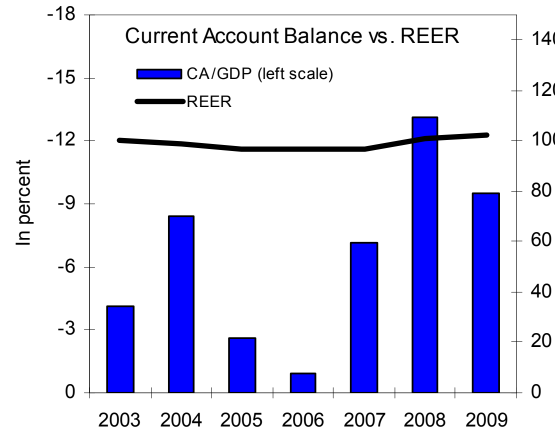
11. **The authorities have indicated that they do not intend to seek Fund support at this time but are prepared to do so if needed in the future.** The government has said it views the Fund as a possible option for financing in the event of future balance of payments pressures.

12. **It is proposed to hold the next Article IV consultation on a 12-month cycle.**

II. Impact of Crisis and Policy Response

A. Context: Macrofinancial Vulnerabilities and Strengths

13. **Macedonia's main vulnerabilities on entering the crisis were its external imbalances in the context of an exchange rate peg.** The current account had widened from near-balance in 2006 to a deficit of 13 percent of GDP in 2008 despite little movement in the real exchange rate, due to rapid import growth (partly related to FDI) and a worsening terms of trade. The exchange rate regime reduced flexibility to adjust to external shocks, and the economy was highly euroized. Meanwhile, elections scheduled for spring 2009 added an element of uncertainty.

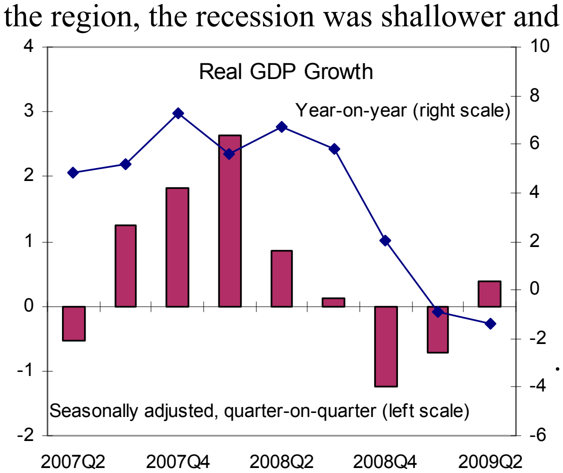


Source: WEO, INS and IMF Staff Estimates

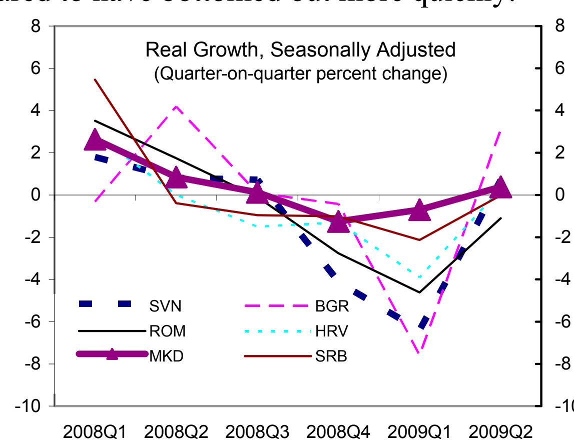
14. **Macedonia benefited from a broadly sound banking system, a low level of public debt, and a significant foreign exchange reserve buffer.** The banking system was relatively small and well capitalized, and relied on domestic deposits rather than external sources for funding. Public debt was a little over 20 percent of GDP, half of which was long-term loans from official lenders. Meanwhile, €1.7 billion of foreign exchange reserves (115 percent of short-term debt) at end-September 2008 provided a significant buffer.

B. Impact of Global Crisis

15. **Growth, which had already been slowing, turned negative in the last quarter of 2008, driven by an abrupt fall in exports and industrial production.**[1] However, by the second quarter of 2009 initial signs of stabilization were evident in production, exports and retail sales, and quarterly GDP growth (seasonally adjusted) turned positive. Compared to other countries in the region, the recession was shallower and appeared to have bottomed out more quickly.



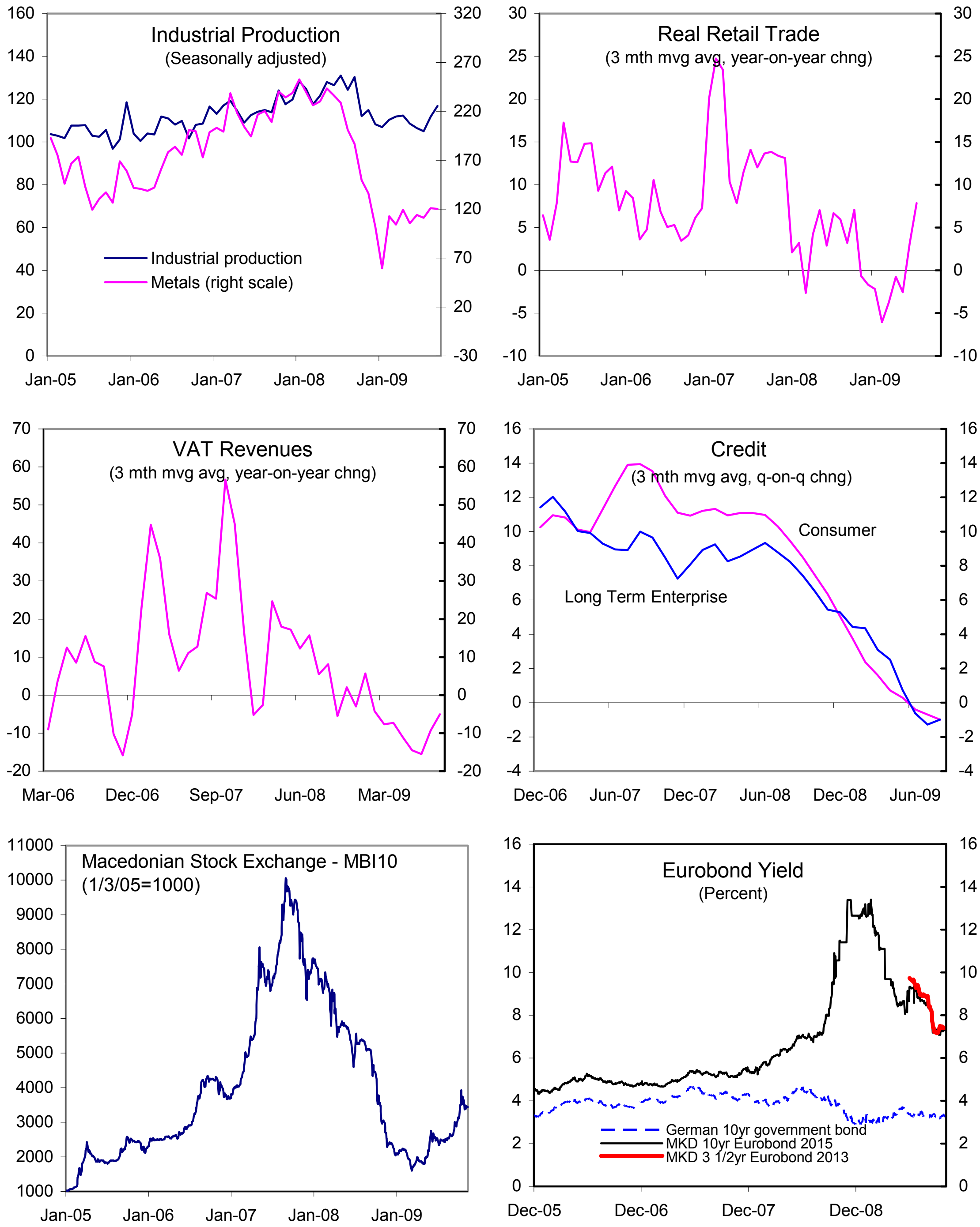
Sources: SSO; and IMF staff estimates.



Sources: Respective statistical offices; and IMF staff estimates.

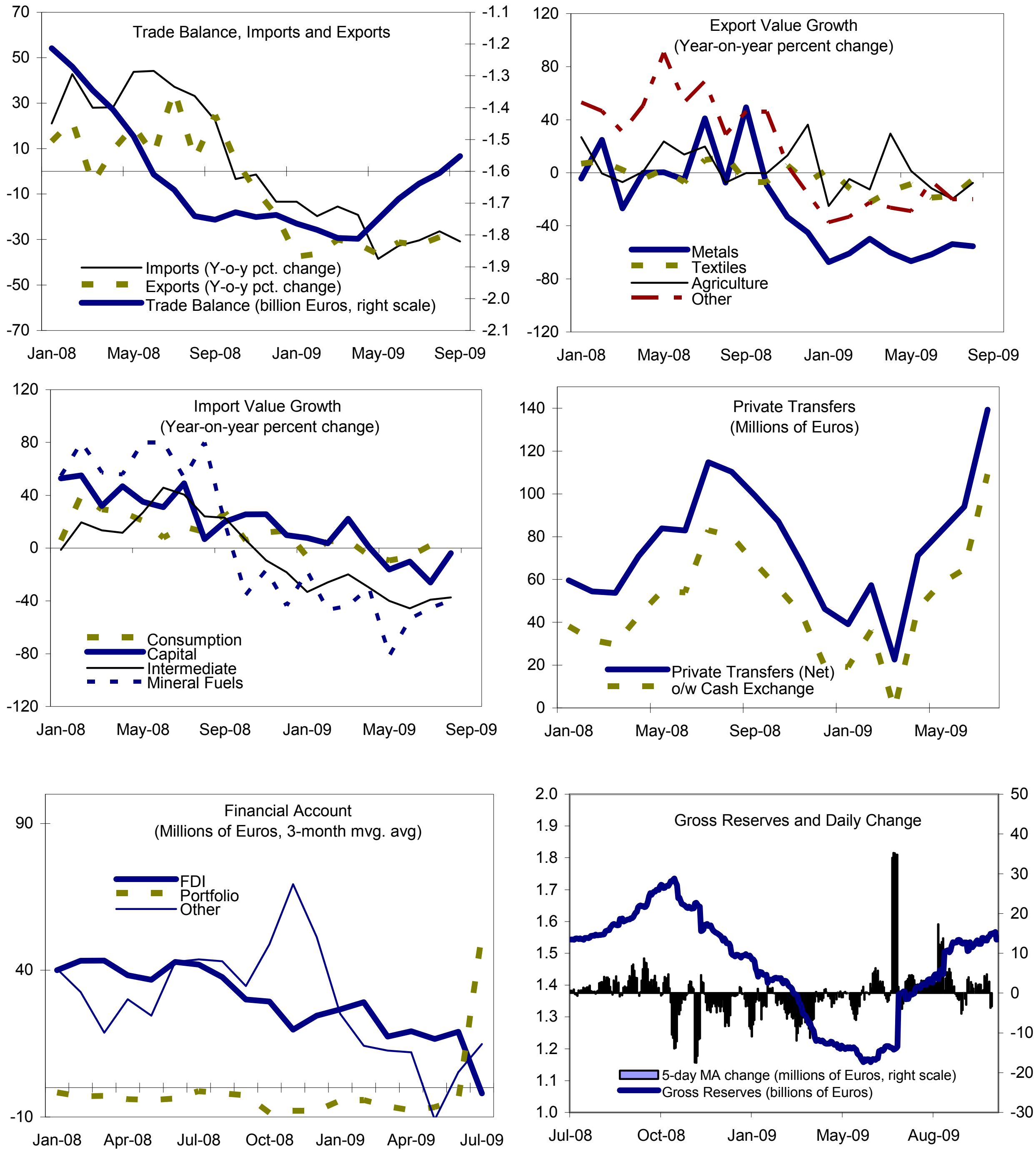
[1] These GDP growth trends are on a seasonally adjusted basis. Due to a relatively short series and structural breaks, the seasonal adjustments are subject to uncertainty.

Figure 1. FYR Macedonia: Recent Economic Developments



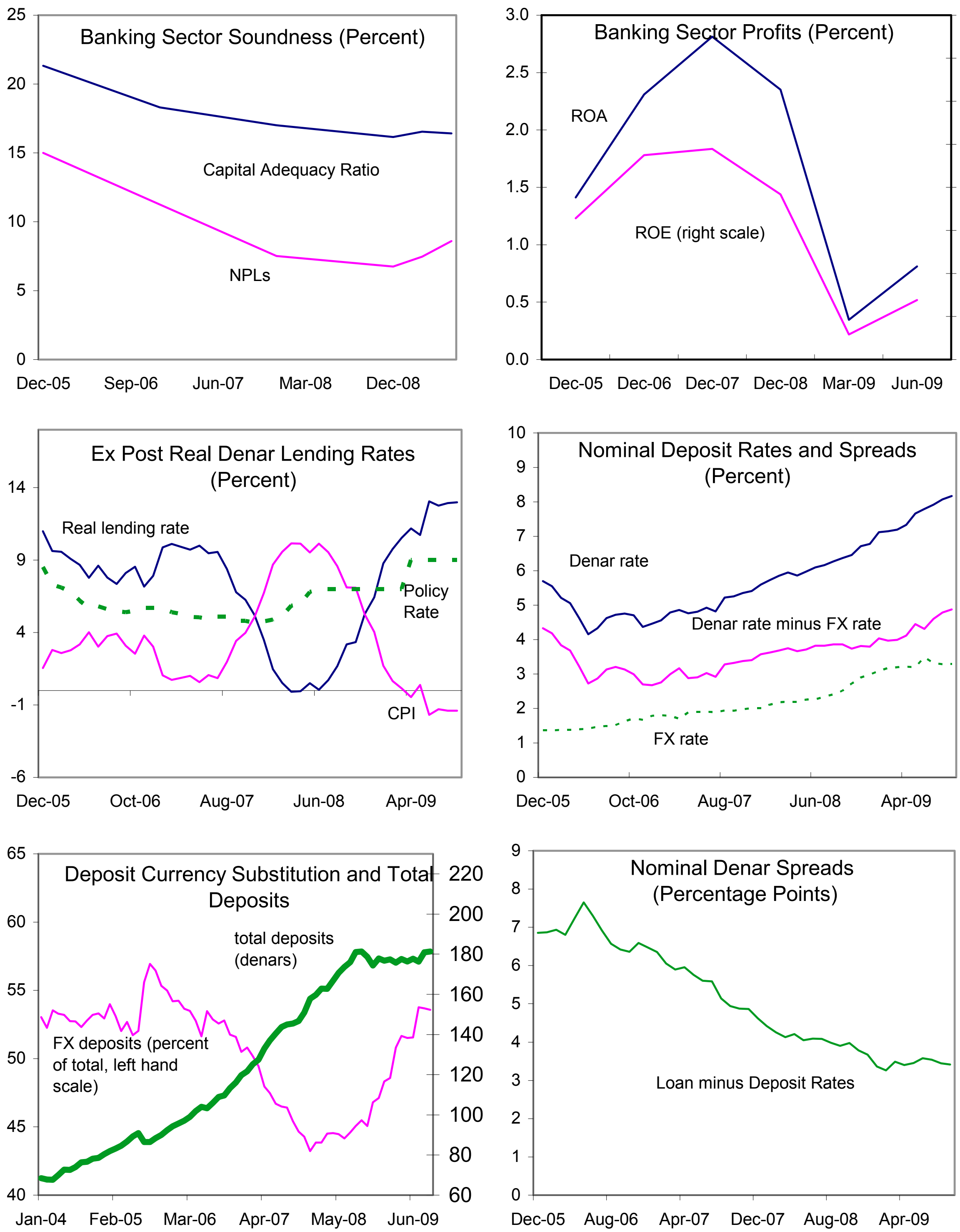
Sources: NBRM; SSO; and IMF staff estimates.

Figure 2: FYR Macedonia: External Sector Developments, (2008-09)



Sources: NBRM; and IMF staff estimates.

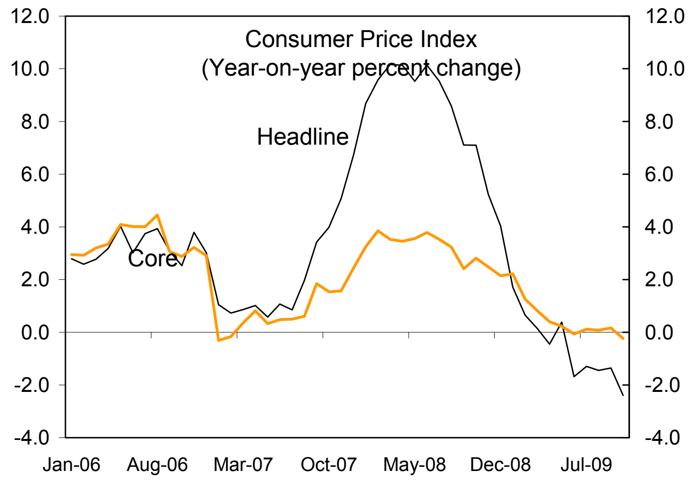
Figure 3: FYR Macedonia: Banking Sector Developments



Sources: NBRM, and IMF staff estimates.

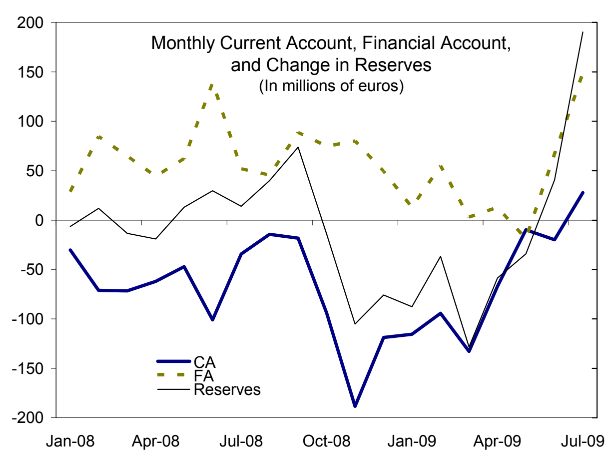
16. **Inflation started falling in late 2008 due to the decline in food and energy prices and to slowing growth.** By October 2009 headline inflation was -2.4 percent and core inflation (excluding food and energy) was near zero.

17. **The current account deficit initially widened, but started to adjust in the second quarter of 2009.** Adjustment was delayed because exports were hit quickly but imports initially remained high, while net private transfers fell as a result of cash exchange house outflows.[2] By the second quarter imports began to contract sharply at the same time as the decline in exports leveled off. Meanwhile, private transfers bottomed out and began to rebound in the second quarter, helped by the successful resolution of election uncertainties.



Sources: SSO and IMF staff estimates.

18. **International reserves fell 30 percent through mid-year before subsequently recouping most of their losses.** A sharp decline in financial inflows, coupled with the lagged current account adjustment, forced the NBRM to intervene heavily to protect the peg. FDI fell sharply, while banks increased their foreign assets, in part reflecting the switch of depositors from denar to euro deposits. Altogether, the NBRM sold some €500 million from October through May, when gross reserves reached a low of under €1.2 billion (75 percent of short-term debt). Starting in June inflows improved, with the government's €175 million Eurobond issue, a reversal of commercial bank foreign asset accumulation, and the SDR allocation of €60 million (which the authorities have used to augment NBRM reserves). By end-October reserves had risen to above €1.5 billion (94 percent of short-term debt), recovering most of their losses of the previous year.



Source: IMF staff estimates.

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[2] Cash exchange houses are small shops where individuals can buy and sell foreign currency. They account for a large share of private transfers. Part of their transactions are thought to be remittances and another part reflects households' cash management and risk hedging activities (often referred to as "mattress money").

Box 1. Banking Sector Stability

Macedonia experienced a considerable credit boom prior to the global crisis, similar to other European emerging markets although somewhat later and on a smaller scale. Bank loan growth averaged 30 percent annually between 2004−08. Nonetheless, the sector remains relatively small with assets at 62 percent of GDP. The sector's small size, substantial liquidity, and high capital adequacy have allowed it to absorb the effects of the global economic crisis well.

A key strength of the sector is a reasonably conservative business model. Bank assets are primarily loans (62 percent of total) and highly liquid assets like Central Bank bills, accounts with foreign banks and short term Treasury bills (15 percent of total), rather than riskier (and potentially illiquid) trading securities. On the liability side, funding sources are stable: resident deposits account for 76 percent of total liabilities versus foreign liabilities at 9 percent, a third of which is subordinated debt.

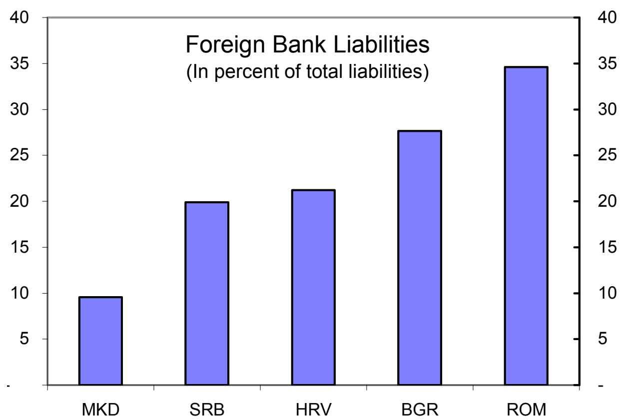
The recession and tighter monetary policy nonetheless weighed on the banking system. Between September 2008 and September 2009, deposit growth fell from 25 percent yoy to 0 percent and lending growth fell from 29 percent to 6 percent. From June 2008 to June 2009, nonperforming loans rose from 6.9 percent to 8.6 percent of total loans, return on equity fell from 19.1 to 4.3 percent (on the back of higher provisioning), and foreign exchange deposits rose from 53 percent to 61 percent of total deposits.

Despite these adverse development, risks appear contained.

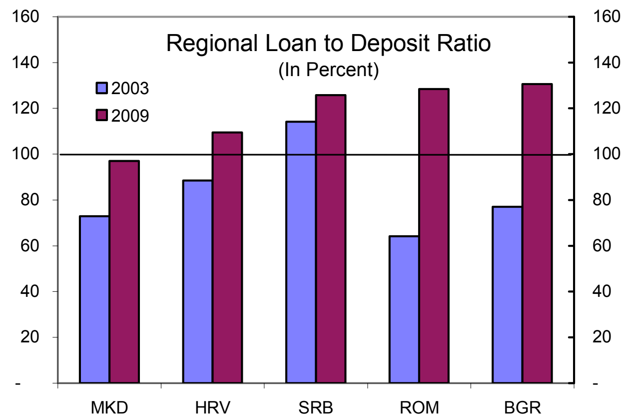
- ***Liquidity Risk*** – The loan to deposit ratio is 97 percent as of June 2009, suggesting a stable source of funding. Ample liquidity means that, in aggregate, banks could cover a sudden loss of 23 percent of short-term liabilities with highly liquid assets.
- ***Interest Rate Risk*** – Direct exposure to rate risk via higher funding costs is low because 87 percent of bank loans to households are adjustable rate as of end-2008. However, there is indirect credit risk via the impact of higher rates on borrower capacity to repay.
- ***Exchange Rate Risk*** **–** The aggregate banking sector has a net neutral foreign exchange position (and each bank's net open foreign exchange position is limited to 30 percent of own funds). However, indirect credit risk arises because 57 percent of loans as of June 2009 are foreign exchange denominated or indexed, most of which appears to be unhedged.
- ***Buffers***. The system's capital adequacy ratio remained stable at 16 percent in June 2009, compared to the legal minimum of 8 percent and the NBRM's recommended 12 percent. Nonperforming loans are 67 percent provisioned as of June 2009. Meanwhile, required reserves at the NBRM are 10 percent on denar deposits, 13 percent on foreign exchange deposits, and 20 percent on foreign exchange indexed deposits, providing another buffer.

The central bank conducts quarterly stress tests and the system remains solvent even under extreme adverse scenarios (an increase in NPLs of 50 percent, a 20 percent depreciation, and a 5 percentage point rise in interest rates). The NBRM also conducts on-site examination of asset quality and lending practices at the three largest banks, which account for 66 percent of assets.

19. **The banking system absorbed the crisis without significant pressures on capital or liquidity, despite a rise in non-performing loans and lower profitability.** Due to their relative insulation from the global financial system, banks were affected by the crisis mainly through its impact on the real economy, and through the NBRM's tightening measures in response to the crisis, rather than directly from external funding pressures. Overall, risks in the banking sector appear to be contained (Box 1).



Sources: Respective central banks and IMF staff estimates.



Sources: Respective banking supervision departments and IMF staff estimates.

C. Policy Response

20. **The Government curtailed planned spending increases to achieve its 2.8 percent fiscal target for 2009 in the face of revenue shortfalls resulting from the economic slowdown** (Box 2). Overall real expenditure is expected to decline 0.8 percent relative to 2008. Compared to other countries in the region, the spending cuts in Macedonia are relatively modest. Staff believe the revised revenue projections remain optimistic. However, the government is committed to underexecution of spending as necessary to achieve the deficit target of 2.8 percent of GDP for 2009.

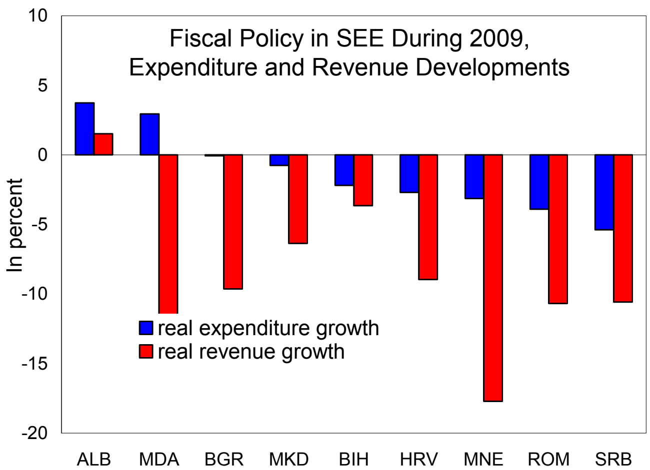
Box 2. Macedonia's Response to Past IMF Advice

At the time of the 2008 Article IV consultations (concluded in December 2008), Directors welcomed Macedonia's strong economic growth and improved business climate. But they expressed concern about increasing macroeconomic and external vulnerabilities, highlighting the widening current account deficit and the increase in public sector wages. In this context they expressed concerns about plans to increase the fiscal deficit from 1.1 percent of GDP in 2008 to 2.8 percent in 2009 and stressed that the priority of monetary policy should be to protect the exchange rate. At the time of these recommendations, 2009 growth was expected to be 4 percent and the current account deficit to be 13.3 percent of GDP.

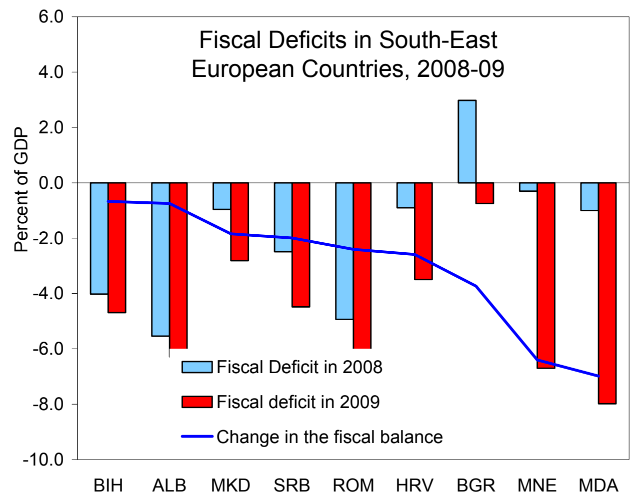
Events unfolded differently than anticipated in December 2008, as the global crisis spilled onto Macedonia's economy, leading to a mild recession. Meanwhile, the current account began to adjust and is projected to fall to 9.5 percent of GDP in 2009 and to be on a downward path over the medium term.

The government largely allowed automatic stabilizers to work, while cutting public spending in response to declining revenues, including a freeze on public sector wages and employment. The end result was a budget that staff expect to be roughly neutral in cyclically adjusted terms. Meanwhile, the central bank tightened monetary policy through higher interest rates and tighter prudential requirements in order to arrest the loss of foreign exchange deposits and protect the exchange rate peg. In light of the economic downturn, these policy responses appear to be broadly consistent with the underlying advice of Directors.

21. **The budget deficit is expected to be financed fully from external sources (mainly the Eurobond).** There will be no net domestic financing, as expected net issuance of T-bills and T-bonds of some denar 5.4 billion (1.4 percent of GDP) is offset by repayment of structural bonds.[3] In mid-2009 the Treasury began to issue foreign exchange linked T-bills to reduce its financing costs, and these now account for close to 90 percent of the T-bill stock (which totals some 3 percent of GDP). This likely contributed to the recovery of reserves by providing banks with liquid domestic foreign exchange assets. It also shifted foreign exchange risk to the government.



Source: WEO Data, Oct. 2009
Note: Countries ordered descreasingly with the real expenditure



Source: WEO Data, Oct. 2009.
Note: Countries ordered by the change in the fiscal balance.

22. **The NBRM took several steps to stop the outflow of foreign exchange reserves by tightening credit conditions.** First, it imposed liquidity requirements in January, with banks given a timetable for coming into compliance. Second, it hiked its policy rate (one-month central bank bills) by 200 basis points in April. Third, it raised reserve requirements on bank deposits in June. These measures helped to rebuild reserves both directly (banks brought back assets held abroad to meet higher reserve requirements) and indirectly by slowing bank lending. Macedonia's monetary tightening stood out among the countries in the region, which generally reduced interest rates and relaxed reserve requirements. This tighter stance was required due to the need to protect the peg in the face of declining reserves, and it was feasible because bank balance sheets were sufficiently healthy to absorb these measures.

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[3] Structural bonds, which amount to 5 percent of GDP, are long-term bonds issued to cover historic liabilities (primarily related to denationalization, pre-independence frozen currency deposits, and Stopanska Bank privatization).

Monetary Policy: September 2008–June 2009

	De Facto Exchange Rate Regime	Interest Rate Movement	Reserve Requirement Movement
Albania	Floating	Loosened	Neutral
Bosnia and Herzegovina 1/	Currency Board	Loosened	Loosened
Bulgaria 1/	Currency Board	Loosened	Loosened
Croatia	Other Managed Float	Tightened	Loosened
Macedonia	Stabilized Arrangement	Tightened	Tightened
Romania	Floating	Loosened	Loosened
Serbia	Floating	Loosened	Loosened

Sources: Respective Central Banks; and IMF staff.

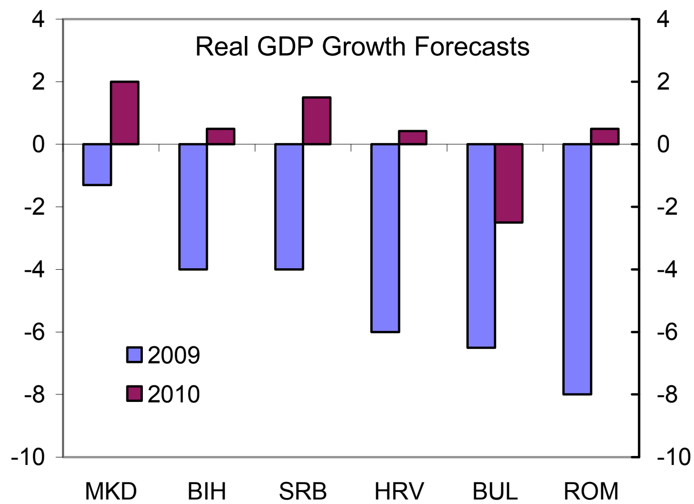
1/ For the currency board countries, interest rate movement refers to market rather than policy rates.

III. MACROECONOMIC OUTLOOK

23. **Output is projected to contract 1.3 percent in 2009 and expand 2 percent in 2010.**

- The 2009 outlook is based on the presumed stabilization of activity in the second half of the year—as suggested by economic indicators of production, sales, and confidence—and on improved global economic prospects. Compared to other countries in the region, the projected downturn is mild.

- The 2010 outlook is based on the recent signs of revived momentum in the economy, the modest recovery expected in trading partners, improved conditions for external financing, and the contained impact of the crisis on the banking sector in Macedonia.



Sources: WEO and IMF staff estimates.

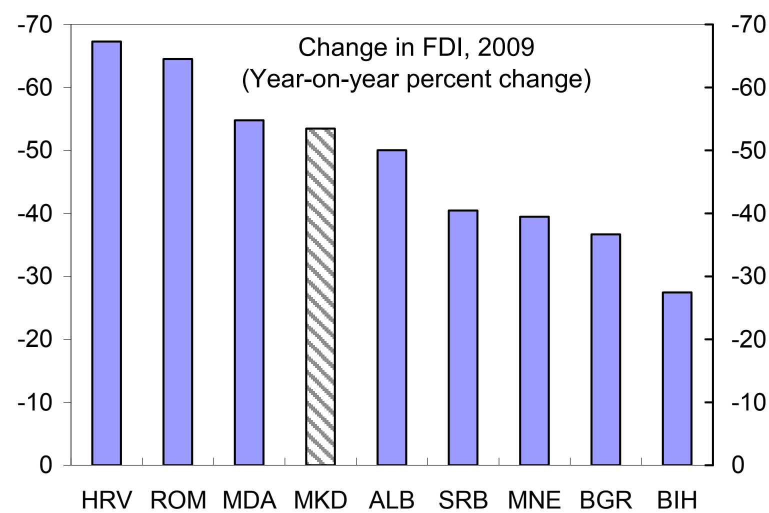
- The government expects a smaller contraction of 0.6 percent in 2009, while the NBRM expects a 1.6 percent contraction. The government shares the staff's outlook for 2010.

24. **Inflation is expected to be -0.8 percent in 2009.** Core inflation (excluding food and energy) is expected to be close to zero. Prices are expected to rise somewhat over 1 percent in 2010 as the effects of food and energy fade and economic growth resumes.

25. **The current account deficit is expected to narrow in 2009 and continue to do so over the medium term.** FDI should recover towards pre-crisis levels, and foreign exchange reserves are expected to stabilize near 90 percent of short-term debt.

- The current account deficit appears on track to fall from 13 percent of GDP in 2008 to 9½ percent of GDP in 2009, on the back of declining trade deficits and stable private remittances and other transfers. For 2010 and over the medium term exports are expected to recover further, supported by resumed growth in trading partners, a rebound in metals prices from the lows of early 2009, and ongoing structural reforms that are improving the business climate. Meanwhile import growth is expected to be contained due to modest growth of output and credit in Macedonia, and to restrained fiscal policies. The current account deficit is projected to narrow to 8 percent of GDP in 2010 and to 5 percent by 2014.

- Foreign direct investment is projected to fall by more than 50 percent this year, in line with other countries in the region. This is partly compensated by portfolio inflows (the Eurobond) and the SDR allocation, but net financial inflows are still expected to fall some €300 million below last year's levels. International reserves are projected to decline €100 million this year, to €1.4 billion or 88 percent of ST debt. In 2010 and over the medium term FDI is expected to bounce back towards (but still below) the peak levels of 2007-08, supported by continued structural reforms and, potentially, progress towards EU accession. Together with disbursement of an €100 million EIB loan and further adjustment of the current account, this is expected to support a modest increase in reserves, which would remain near 90 percent of short-term debt in 2010 and over the medium term.



Sources: WEO and IMF staff estimates

IV. Policy discussions

A. Fiscal Policy

26. **Staff viewed the authorities' fiscal targets for 2009 (2.8 percent of GDP) and 2010 (2.5 percent of GDP) as appropriate.** The authorities felt that such deficits were needed to support growth and protect public investment. Staff's view that these deficit targets are appropriate is based on the following considerations**.**

- These deficits mainly reflect the operation of automatic stabilizers. The moderate contraction in adjusted terms in 2009 and 2010 is appropriate in light of financing constraints and the need to contain the current account.

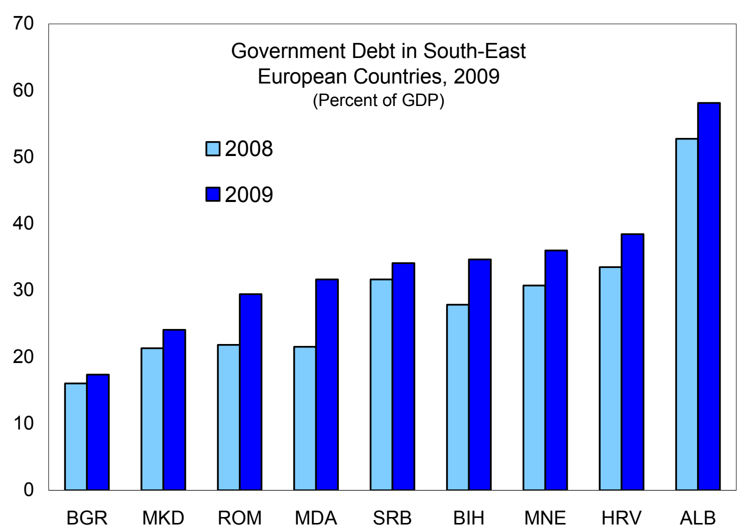
FYR Macedonia: Cyclically-adjusted Fiscal Balances

	2006	2007	2008	2009	2010
Primary fiscal balance	0.5	1.5	-0.4	-2.2	-1.6
Overall fiscal balance	-0.5	0.6	-1.0	-2.8	-2.5
Output gap	-1.2	-0.2	4.6	-0.4	-1.8
Absorption gap	-3.2	3.9	14.8	5.9	3.2
Cyclical balance	-0.7	0.5	2.8	0.7	0.1
Cyclically-adjusted primary balance	1.2	1.0	-3.2	-2.9	-1.8
Cyclically-adjusted overall balace	0.2	0.2	-3.9	-3.5	-2.7
Automatic stabilizers	-0.5	1.2	2.3	-2.1	-0.6
Fiscal impulse (primary balance)	-0.2	-0.2	-4.2	0.3	1.1
Fiscal impulse (overall balance)	-0.3	0.0	-4.1	0.4	0.9

Source: IMF staff estimates.
Note: Automatic stabilizers are the difference in the cyclical balance between the current and the previous year. The fiscal impulse is the difference in the cyclically-adjusted balance between the current and the previous year (a positive fiscal impulse means a cyclically-adjusted contraction). Cyclical adjustment of fiscal balances is done with respect to both output and absorption gaps as described in the Selected Issues Paper, Ch. 3.

- Given the modest levels of public debt, fiscal deficits on this scale do not threaten fiscal sustainability.

- The government has already secured financing for 2009 through the Eurobond issue.



Source: WEO data, October 2009

27. **The 2010 budget may be somewhat optimistic in its revenue assumptions**. The budget, released in mid-November, is based on the same 2 percent growth assumption as projected by staff. However, it assumes 0.9 percent of GDP more buoyancy on tax and non-tax revenues than expected by staff. If revenues fall short of budgeted levels, staff expect the authorities will underexecute spending (primarily capital outlays) in order to meet the 2.5 percent of GDP deficit target. Revenues will be affected by a 1.5 percentage point cut in social contribution rates and changes in the corporate income tax, with a combined impact estimated at -0.3 percent of GDP.[4] The government's announced freeze on public sector employment and wages for a second consecutive year and strict control over goods and services outlays will help to contain expenditures.

FYR Macedonia: 2010 Budget Revenue Assumptions Compared to Preliminary Staff Projections
(In percent of GDP)

	Budget vs. preliminary staff projections
Total	0.9
Personal Income Tax	0.1
Corporate Income Tax	0.1
Social Contributions	0.3
Indirect Taxes	0.2
Non-tax revenues	0.3

Sources: IMF staff estimates.

28. **Securing financing for the 2010 fiscal deficit target may be a challenge**. Domestic financing sources are limited due to the small domestic debt market. The government is reluctant to borrow too much from this market, lest private lending be crowded out. Foreign official financing from development banks[5] and bilateral donors will provide valuable support. In addition it will likely be necessary to seek private external financing (possibly another Eurobond), provided market conditions are sufficiently favorable. While some further accumulation of private external debt may be appropriate, Eurobonds create rollover risks that need to be managed. In the medium term the public sector will need to carefully manage the build-up of external market debt, including through a strengthening of its debt

Central Government Financing
(In millions of euros)

	2009	2010
CG Deficit Target (percent of GDP)	2.8	2.5
Total Financing Requirement	313.5	300.5
Deficit	181.1	166.7
Gross Amortizations	132.4	133.9
Domestic State Bonds	93.5	90.2
External	38.9	43.6
Total Financing Sources	313.5	300.5
Domestic T-Bills Issuance (net)	86.7	95.5
External	226.7	205.0
Official	51.7	80.0
Private (incl. Eurobond)	175.0	125.0

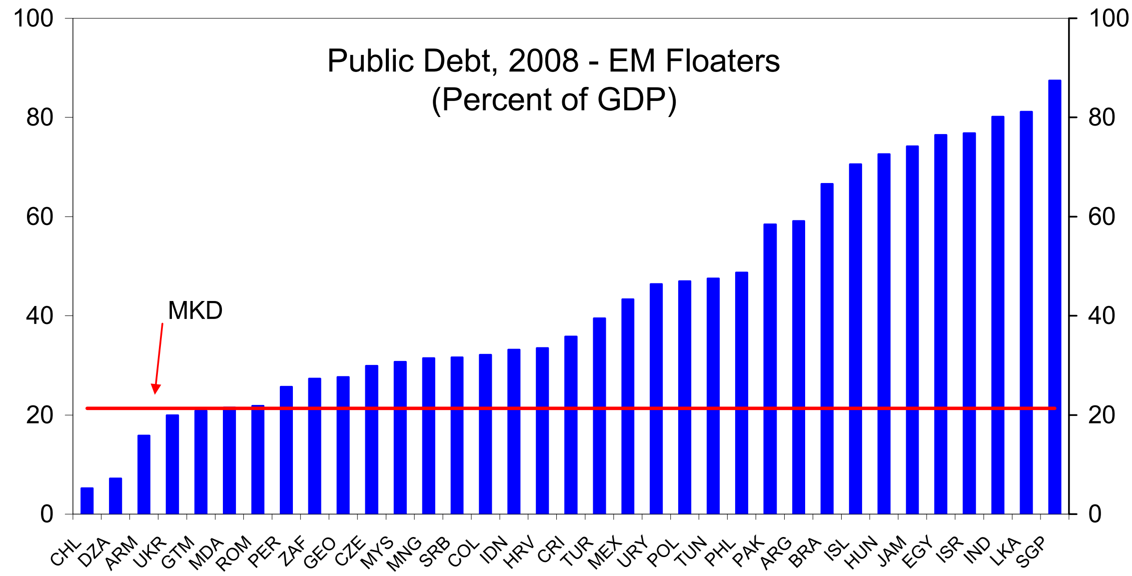
Sources: MoF; and IMF staff estimates.

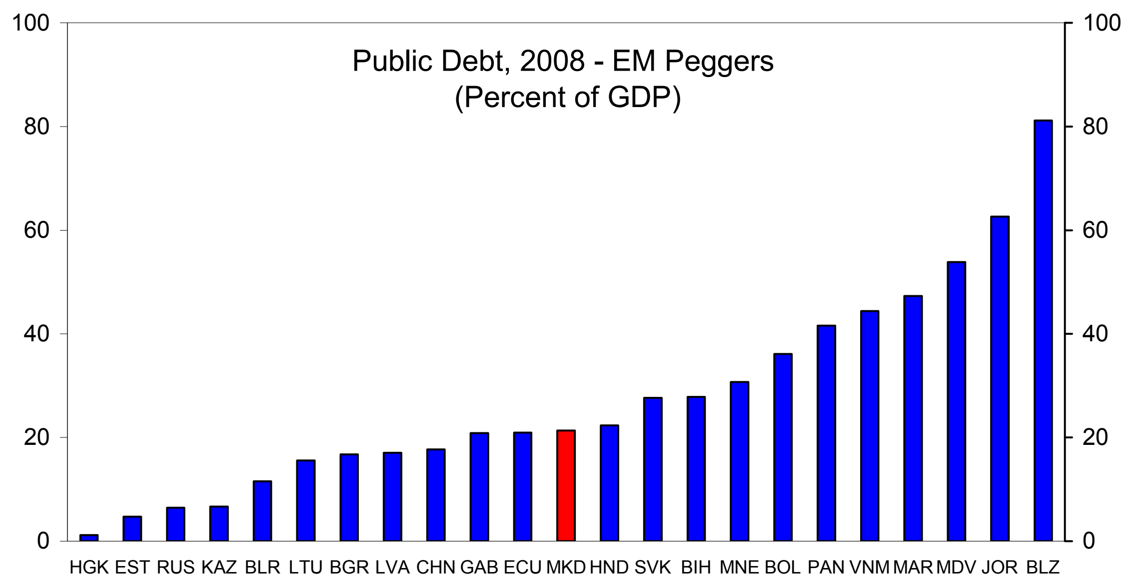
[4] The social contributions rate (pension, health, and unemployment) was scheduled to be cut from 27.9 percent in 2009 to 24.7 percent in 2010 (and 22 percent in 2011). The government announced in November that it would implement the cuts over a longer period, with a smaller reduction to 26.5 percent in 2010.

[5] The government is seeking to borrow up toUS$60 million from the World Bank through two DPL loans for 2010 budget support, half in 2009 and half in 2010.

management infrastructure, with official financing expected to continue to be important and the domestic debt markets potentially playing an increased role over time.

29. **Staff recommended that fiscal deficits be limited to below 1.5 percent of GDP in the medium term.** A 1.5 percent ceiling would maintain debt ratios at moderate levels (well below the median for emerging markets and near the median of emerging market countries with exchange rate pegs) and provide flexibility to follow countercyclical policy over the business cycle (Box 3). The government agreed with the need to reduce deficits over the medium term, but felt a ceiling of 2 percent of GDP would be more feasible in light of the need to increase investment spending.





Source: WEO, September 2009.

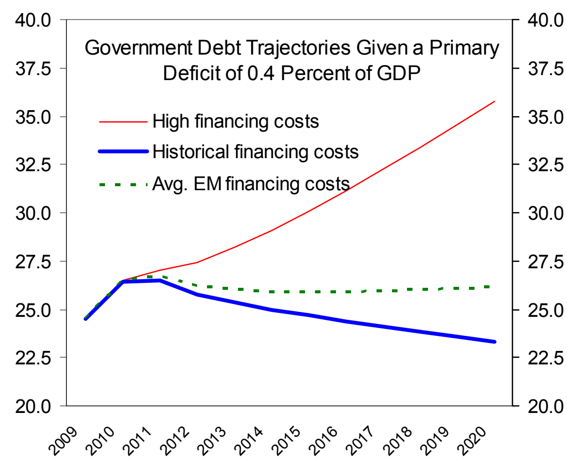
Box 3. Debt-Sustainability Guidance for Medium-Term Fiscal Targets

This box assesses the appropriate public debt ratio for Macedonia and the associated annual fiscal targets (Selected Issues Paper, Chapter 3). Medium-term fiscal targets should be consistent with a sustainable debt path. One approach to assessing an appropriate public debt ratio is to look at the empirical relationship between debt ratios and the vulnerability of countries to crisis. Another approach is to view debt as sustainable if sufficient future primary surpluses can feasibly be generated to service it.

These approaches suggest a prudent public debt ratio for Macedonia would be around 25 percent of GDP based on the following considerations:

- While there is no consensus in the academic literature on the appropriate debt target for emerging markets, it is generally accepted that emerging markets can sustain lower levels of debt than advanced economies. IMF Vulnerability Studies find a higher probability of a debt crisis in emerging economies when the public debt ratio surpasses a threshold of around 25 percent of GDP.
- Although Macedonia's projected end-2009 debt ratio (24 percent of GDP) is low compared to its regional peers, it is at the median among emerging markets with fixed exchange rate regimes. Constrained policies and increased vulnerability to sudden stops suggest lower debt ratios are prudent in fixed exchange rate regime countries.
- A model-based approach to debt sustainability indicates that debt levels much above 20 percent of GDP would be imprudent in Macedonia's case. This model imposes the requirement that the government can credibly service its debt in all circumstances and therefore that it should contain debt to the level it can sustain in the case of a negative shock to revenues.
- The prudent level of debt also depends on interest costs. The average interest rate paid on Macedonian public debt is likely to increase from the historical 3.4 percent as the share of market financing in overall borrowing increases. The chart below shows that for a given primary balance, higher financing costs can lead to unsustainable debt dynamics. Alternatively, for a given debt level, higher interest payments raise the debt-stabilizing primary balance. (The average financing costs line assumes 30 percent of new debt is at historical costs of 3.4 percent and 70 percent is at the EM average of 7 percent. The high cost line assumes 30 percent at historical costs and 70 percent at a 9 percent rate.)

Stabilizing debt at 25 percent of GDP in the medium-term implies running annual primary fiscal deficits of around 0.4 percent of GDP (overall fiscal deficits of around 1.5 percent of GDP) from 2012 onwards, given baseline growth and interest rate projections.



Source: IMF staff estimates.

B. Monetary and Exchange Rate Policy

30. **The NBRM measures to tighten monetary policy in the first half of 2009 were driven by its commitment to ensure the stability of the exchange rate peg.** In its view, it is necessary to protect reserve buffers, and it is too early to relax its stance in light of the still large current account deficit and the potential for further reserve losses. Staff share this assessment and believe that more evidence of external stabilization would be desirable before easing. Once external adjustment progresses and reserves approach desired levels, there will be room to begin loosening policy (Boxes 4 and 5).

31. **The government believes that the NBRM stance is too cautious and that it should begin easing now.** It acknowledges the risk of future reserve losses but believes current reserve levels provide an adequate buffer against that contingency. In its view, the present stance will not allow the resumption in bank lending required to stimulate a return to growth. Further, monetary policy acts with a lag, so incremental easing should begin now to support growth in 2010. Moreover, if risks materialize, both monetary and fiscal policies can respond to protect exchange rate stability. Nonetheless, the government affirmed that it respects the autonomy of the NBRM in setting monetary policy. Staff noted that maintenance of the exchange rate peg involved tensions between the goal of protecting reserves through tighter monetary policy, and the goal of supporting growth and employment through easier credit policies. Premature easing might need to be reversed, which could harm NBRM credibility as well as damage confidence.

32. **The authorities remain fully committed to the exchange rate peg, which they believe has served Macedonia well, including during the crisis, and which has deep public support.** They recognize the tradeoffs and reduced flexibility associated with the peg but believe it is an essential anchor for monetary policy and for safeguarding stability. Staff agreed that the exchange rate system should, with supportive policies, anchor the authorities' objectives of stable growth and low inflation, as it has in the past. In staff's view policies have been supportive of the exchange rate and the costs of the policies needed to protect the peg do not appear to have been excessive to date. In particular, despite high interest rates and tight monetary conditions, the economic downturn has been modest compared to other countries in the region, and the banking sector seems to have weathered the crisis in overall healthy shape. Further, the exchange rate does not appear significantly overvalued (Box 6).

Box 4. FYR Macedonia: Assessment of Reserve Adequacy

This box seeks to assess the desired level of foreign exchange reserves in Macedonia (based on Selected Issues Paper, Chapter 1). The adequacy of reserves is a key consideration in setting the stance of monetary policy. A variety of methods including popular rules of thumb, comparisons with other emerging countries (EMs), and model based estimates suggest a target range of €1.5–2 billion.

Popular benchmarks:

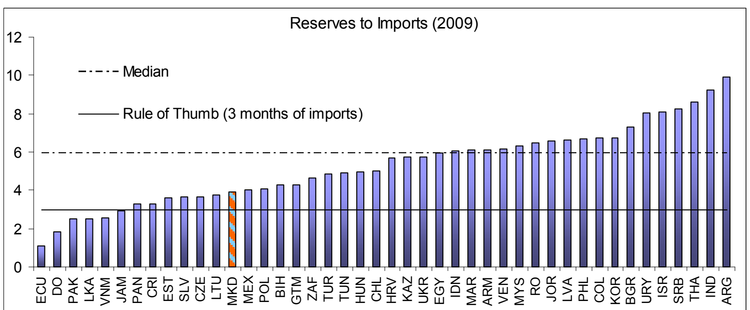
- Maintaining reserves at 3 months of imports would require €1.1 billion.
- The Greenspan-Guidotti rule of 100 percent cover of short-term debt (remaining maturity) would require €1.6 billion.

Comparison with the medians of 51 EM countries (a comparison with 22 EM pegged regimes gives similar results).

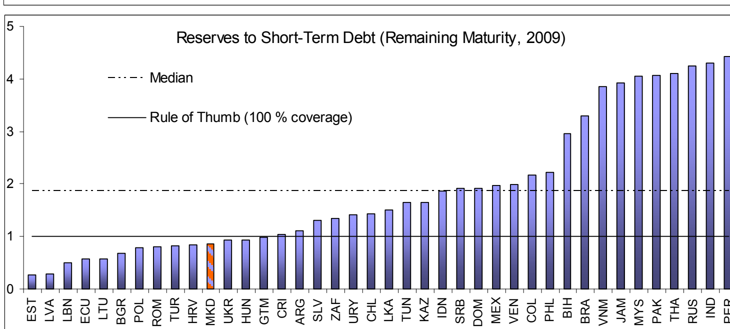
- To be at the median of the broad money to GDP ratio would require €1.1 billion.
- To be at the median in term of months of imports would require €2.0 billion.
- To be at the median reserve to short-term debt ratio would require €2.6 billion.

Model-based approach:

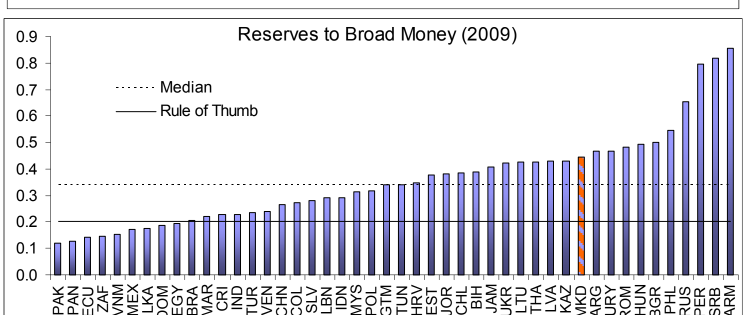
Based on Jean and Ranciere's (2006) model, the optimal level of reserves for Macedonia is calibrated to be €1.8 billion. In this model, the economy is vulnerable to sudden stops of capital flows; reserves are used to smooth domestic absorption in case of a sudden stop; and reserves yield a lower return than other assets in the economy.



Source: IMF Staff Calculations
1\ Except Peru, Lebanon, Iceland, Brazil, Russia, China, Algeria (ratio over 10).



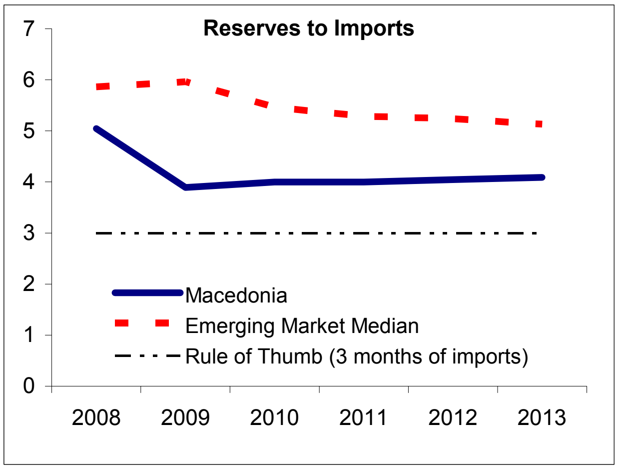
Source: IMF Staff Calculations
1\ Except Egypt, Morocco, Panama, Jordan, Armenia, China, Algeria (ratio over 5).

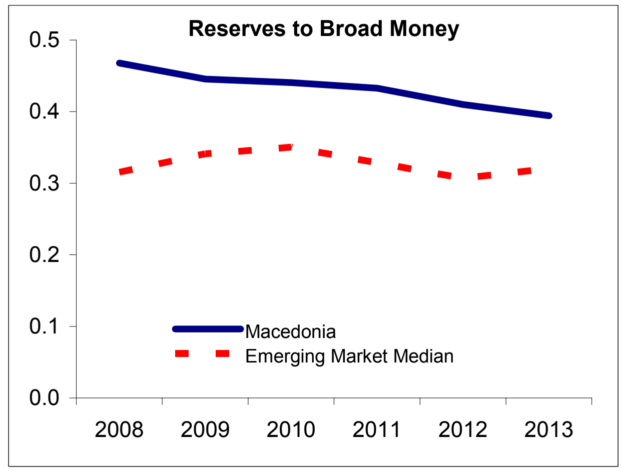


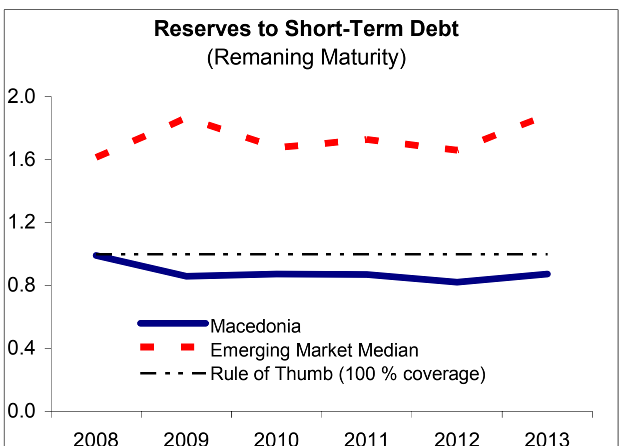
Source: IMF Staff Calculations
1\ Except Algeria

Box 4. FYR Macedonia: Assessment of Reserve Adequacy (concluded)

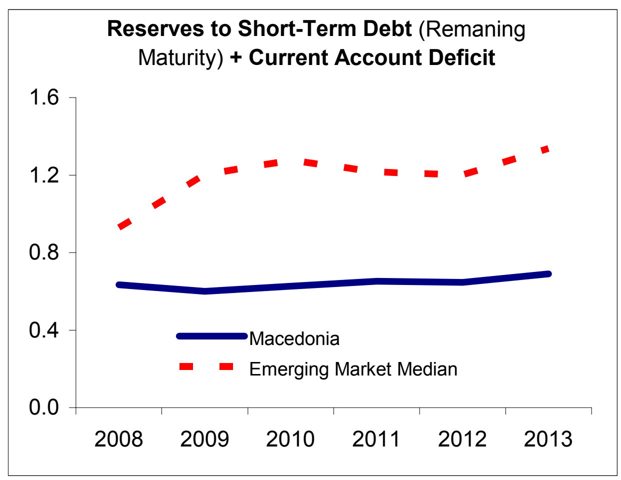
In addition to the above estimates of reserve adequacy, the recent experience is illustrative. Entering the crisis in the fall of 2008, Macedonia had reserves of €1.7 billion. By May 2009 reserves had fallen to a low point of below €1.2 billion as the central bank sold €500 million to defend the peg. If the NBRM had not entered the crisis with such a buffer, reserves would have fallen below the 3 months of imports benchmark, which may have intensified uncertainties and put greater pressure on the peg.





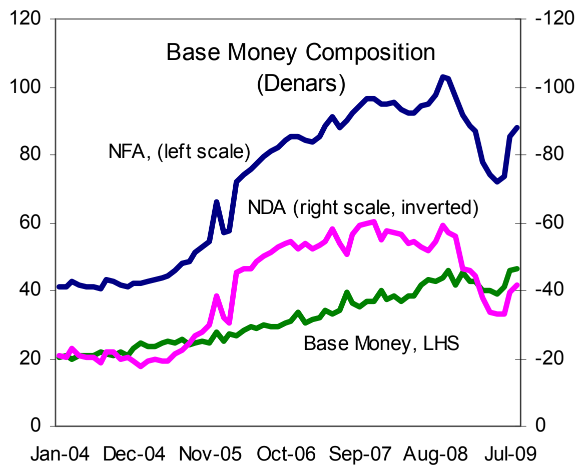


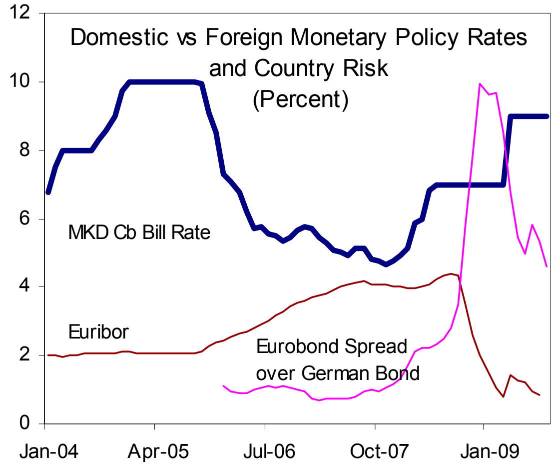
Source: WEO and IMF Staff Calculations



Box 5. Framework for Assessing Monetary Policy

This box (drawn from Selected Issues Paper, Chapter 2) seeks to provide a framework for assessing the appropriate stance of monetary policy in Macedonia given its de facto peg to the euro (formally the peg serves as an intermediate target to help the NBRM meet its primary goal of price stability). The peg ultimately constrains monetary policy through the flow of international reserves. However, a range of policies could be sustainable in the short term, even if not in the longer run, due to imperfect capital market integration and lags between monetary policy actions and the balance of payments. This creates uncertainty in the near term about the appropriate policy stance.





Sources: NBRM; IMF staff estimates.

This degree of latitude in the short term can be seen in two ways. First, base money growth tends to grow relatively smoothly despite foreign exchange intervention purchases and sales—i.e., such intervention is sterilized rather than allowing money to move with foreign exchange intervention as might be expected in a "pure" peg. Second, domestic interest rates move independently of foreign interest rates in ways that do not appear to be fully accounted for by risk premia.

While this short-run uncertainty complicates monetary policy, sustainability of the exchange rate peg requires a policy stance that ensures adequate foreign exchange reserves to defend the peg. Thus both the level of reserves and their underlying trend need to be supportive of the peg. For example, if reserves are low and falling, policy needs to be tightened in order to 1) limit import demand, supporting a correction in the current account; and 2) attract financial inflows via arbitrage to support an improvement in the capital account. At the other extreme, if reserves are high and rising, there is room for easing monetary policy.

Change in Reserves		Level of Reserves: Low	Level of Reserves: High
	Faling	Low, Falling	High, Falling
	Rising	"MKD" Low, Rising	High, Rising

In staff's view, it remains early to loosen. First, staff would advise reserve levels between €1.5 and €2 billion (Box 4), and the current level is at the bottom of that range. Second, the recent reserve increase was due in part to one-off factors and the underlying balance of payments flows are not yet clearly positive. And third, a current account deficit near 10 percent of GDP leaves the country exposed to changes in external conditions, suggesting extra caution. However, as the external adjustment process progresses and reserves approach desired levels, there will be room to begin loosening policy.

Box 6. Exchange Rate Assessment

Staff analysis does not show significant exchange rate misalignment. This conclusion is consistent with that of the December 2008 Article IV report. Standard CGER analysis estimates overvaluation in the range of 6-11 percent, albeit with wide uncertainty bands in these estimates. The weak historical relationship between the real exchange rate and the current account complicates assessment of the exchange rate in the case of Macedonia. A significant current account adjustment, reversing the rapid build-up in deficits in the past two years, is now underway, albeit at a slower pace than regional comparators. While external developments are subject to substantial uncertainty in the current context, the competitiveness benefits of ongoing structural reforms and prospective EU accession, supported by the resumption of foreign direct investment (albeit at lower levels than the pre-crisis period), are expected to result in a further moderation of current account deficits.

Macedonia: Estimated REER Misalignment

Approach	Magnitude of Misalignment	
	Elasticity	
	Baseline (-0.25)	-0.34
Macroeconomic Balance	6.9	5.6
Equilibrium REER 1/	10.8	…
External Stability	8.7	7.1
Overall Assessment	No Significant Misalignment	

Source: IMF staff estimates.

1/ Equilibrium REER measure does not depend on elasticity.

Three complementary CGER methodologies were examined:

- **Under the *macroeconomic balance* (MB) approach, the current account norm is estimated to be around -3.0 percent of GDP.** Depending on the assumptions used for elasticity of the current account with respect to the REER (real exchange rate), the REER needs to adjust by 6 to 7 percent to close the gap between the norm and the underlying current account in the medium run.

- **The *equilibrium real effective exchange rate* (ERER) approach suggests overvaluation of 11 percent.**

- **The *external sustainability* (ES) approach points to similar overvaluation as the MB approach.** In ES, the current account norm is estimated to be 2.6 percent deficit, with a real exchange rate depreciation of 7−9 percent needed to stabilize NFA.

The macro balance and external sustainability approaches both rely on a projected improvement in the current account based on export growth. This is subject to risks on both sides. On the positive side, the improvements in the business climate and the high FDI of recent years should help boost competitiveness. Further, progress towards EU accession would likely attract more foreign investment as well as improve competitiveness through regulatory harmonization. On the negative side, continued efforts are needed to address a shortage of skilled workers, infrastructure needs in roads, railroads and electricity, and regulatory and judicial shortcomings.

C. Financial Sector and Structural Reform

33. **The quality of banking supervision and regulation has contributed to the stability of the banking sector.** Regular on-site examinations of bank credit portfolios and stress tests have played an important role in this regard. Recent progress in implementing arrangements for crisis coordination between relevant agencies (as recommended in the 2008 FSAP update) is welcome. The NBRM agreed with the FSAP recommendations to undertake legal changes to allow it to intervene troubled banks without being subject to court challenge and to remove bank management who do not meet appropriate standards of integrity. The NBRM is working with the justice and finance ministries on the necessary legislation. Staff also encouraged the NBRM and finance ministry to find a solution that will enhance lender of last resort facilities through acceptance of a broader set of collateral, with appropriate Treasury indemnities. The creation of an insurance supervisory body is a positive development, and the authorities should move forward swiftly to make it fully operational.

34. **Macedonia has made significant progress in improving its business climate**, improving property rights through development of the cadastre, and reducing the labor tax burden.[6] The authorities' priority areas for reform in the future include further improvement in property rights; investment in the electricity sector; administrative reform aimed at streamlining and improving efficiency; and judicial reform to improve the speed, consistency and predictability of judicial processes.

V. Risks

35. **Macedonia's large current account deficit, in the context of the exchange rate peg, makes it dependent on continued external financing.** The failure of export demand to recover as expected, renewed weakness of metals prices, or stronger than expected domestic demand and imports could cause the current account deficit to widen once more. Moreover, financial inflows could be lower than anticipated if global financial conditions fail to normalize. Such developments would put renewed pressures on foreign exchange reserves and the exchange rate peg and would also weigh on the banking sector. On the upside, rapid progress towards EU accession would improve prospects for foreign investment, which would likely ease external financing pressures and bolster reserves and the peg.

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[6] As a result of reforms in the business environment, Macedonia climbed from 69th to 32nd place in the Ease of Doing Business category of the most recent World Bank Doing Business ranking. It made particular progress in conditions for starting a business, where it climbed to 6th place, although it lagged behind at 115th place in closing a business.

Table 1. FYR Macedonia: Macroeconomic Framework, 2006–14

(Percentage change, unless otherwise indicated)

	2006	2007	2008	2009	2010	2011	2012	2013	2014
				Projections					
Real GDP	4.0	5.9	4.8	-1.3	2.0	5.0	5.0	4.0	4.0
Real domestic demand	5.9	9.0	9.3	-2.6	1.2	3.8	3.6	3.2	3.1
Consumption	5.2	8.0	7.4	-1.1	1.0	3.7	3.2	3.5	3.4
Private	6.0	9.8	6.9	0.5	0.8	6.0	2.9	3.4	3.2
Public	1.8	0.4	9.7	-8.4	2.2	-7.7	5.1	4.2	4.2
Gross investment	9.6	13.3	18.3	-10.7	2.4	5.6	6.5	2.4	2.4
of which: Private	13.1	10.1	9.8	-9.0	1.6	7.5	6.8	2.0	2.0
of which: Public	-1.6	33.4	39.8	-17.0	5.9	-1.8	5.1	4.2	4.2
Exports (volume)	8.4	14.3	-4.3	-12.0	2.8	5.2	7.2	8.3	9.1
Imports (volume)	11.0	17.4	5.8	-10.9	1.1	3.0	4.0	5.7	6.2
Contributions to growth	4.0	5.9	4.8	-1.3	2.0	5.0	5.0	4.0	4.0
Domestic demand	6.9	10.6	11.2	-3.2	1.4	4.6	4.3	3.8	3.6
Net exports	-2.8	-4.4	-5.8	1.9	0.6	0.4	0.7	0.2	0.4
Statistical discrepancy	0.1	0.3	0.6	-1.1	-0.1	-0.3	-0.3	-0.2	-0.2
Central government operations (percent of GDP)									
Revenues	32.9	34.3	33.5	31.4	33.2	32.7	32.4	32.6	32.8
Expenditures	33.4	33.7	34.5	34.3	35.7	34.7	33.9	34.1	34.3
Of which: capital	3.0	4.0	5.0	3.4	4.4	4.0	4.0	4.3	4.5
Balance	-0.5	0.6	-1.0	-2.8	-2.5	-2.0	-1.5	-1.5	-1.5
Savings and investment (percent of GDP)									
Domestic saving	21.0	17.1	14.6	15.4	16.8	17.6	18.7	18.8	18.9
Of which: public	2.6	4.5	4.1	1.2	1.7	1.9	2.4	2.4	2.4
private	18.5	12.5	10.6	14.2	15.1	15.7	16.3	16.3	16.5
Foreign saving 1/	0.9	7.2	13.1	9.5	8.2	7.3	6.2	5.6	5.0
Gross investment	21.9	24.2	27.7	24.9	24.9	24.9	24.9	24.4	23.9
Fixed investment	18.2	20.2	23.7	20.4	20.6	20.7	20.9	20.6	20.2
Private	15.1	16.3	18.7	16.4	16.4	16.8	17.0	16.6	16.3
Public	3.1	3.9	5.0	4.0	4.2	3.9	3.9	3.9	3.9
Change in stocks	3.7	4.0	4.0	4.5	4.4	4.2	4.0	3.8	3.7
Consumer prices									
Period average	3.2	2.3	8.3	-0.8	0.8	2.5	3.0	3.0	3.0
End-period	3.0	6.7	4.0	-1.7	2.0	3.0	3.0	3.0	3.0
Memorandum items:									
Current account balance (in percent of GDP)	-0.9	-7.2	-13.1	-9.5	-8.2	-7.3	-6.2	-5.6	-5.0
Gross official reserves (in millions of euros)	1,417	1,524	1,495	1,415	1,514	1,589	1,740	1,927	2,159
Gross official reserves (in months of imports)	4.1	3.6	4.6	3.8	3.9	3.9	3.9	4.0	4.1
Gross central government debt (in billions of denars)	97.8	82.9	85.0	97.1	107.3	116.1	123.3	131.0	139.3
Central government gross debt (in percent of GDP)	31.5	23.4	21.3	24.5	26.2	26.3	25.7	25.4	25.2
Foreign direct investment (percent of GDP)	6.8	8.8	6.5	2.5	5.3	5.3	5.3	5.3	5.3
External debt (in percent of GDP)	49.1	48.9	51.0	56.4	59.8	59.3	58.2	57.6	56.8
Nominal GDP (in billions of denars)	310.9	354.3	398.5	396.4	409.4	441.7	479.6	514.8	552.4
Nominal GDP (in millions of euros)	5,081	5,791	6,504	6,465	6,678	7,205	7,822	8,397	9,011

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

1/ Current account deficit.

Table 2. FYR Macedonia: Central Government Operations, 2006−10

	2006	2007	2008	2009 Budget	2009 Proj.	2010 Budget	2010 Proj.
	(In billion denars)						
Total revenue	102.3	117.5	133.7	135.4	124.6	140.2	135.9
Tax revenue	89.2	101.3	112.7	110.1	106.0	115.4	112.3
Personal Income Tax	8.4	8.9	8.7	9.0	8.8	9.7	9.3
Corporate Income Tax	4.7	5.9	8.6	5.1	5.0	4.5	4.2
VAT	27.2	33.0	36.2	36.1	33.6	37.9	37.0
Excises	12.2	13.3	14.3	15.0	14.6	15.7	15.7
Custom Duties	5.4	6.2	6.3	5.4	5.3	6.2	5.8
Other taxes	1.8	2.5	2.9	3.4	2.9	3.5	3.5
Social contributions (total)	29.4	31.6	35.8	36.1	35.8	38.0	36.8
Pension contributions	18.6	20.1	23.1	23.3	23.3	24.7	24.0
Unemployment contributions	1.4	1.5	1.8	1.8	1.8	1.7	1.7
Health contributions	9.4	10.0	10.9	10.9	10.7	11.6	11.1
Non Tax revenue	9.9	10.4	12.8	17.2	12.2	15.1	14.7
Capital Revenue	1.8	4.9	6.9	5.4	5.0	7.0	6.1
Of which: Telecom dividend	0.0	2.9	3.8	2.4	2.4	2.4	2.4
Grants	1.4	0.9	1.3	2.7	1.3	2.7	2.7
Total expenditure	104.0	115.4	137.6	146.6	135.8	150.7	146.1
Current expenditure	94.8	101.8	117.7	127.4	122.7	128.3	128.3
Wages and salaries	23.4	23.6	20.8	23.5	23.0	22.8	22.8
Goods and services	12.9	14.8	18.7	19.1	16.4	17.2	17.2
Transfers	55.3	60.5	75.5	82.3	80.8	84.6	84.6
Pensions	25.4	26.3	30.9	34.0	33.5	34.9	34.9
Health	15.8	16.1	19.1	18.7	18.7	18.9	18.9
Local governments	2.1	3.7	10.5	12.8	12.6	12.9	12.9
Other	12.0	14.4	15.0	16.8	15.9	17.9	17.9
Interest	3.1	2.9	2.6	2.5	2.5	3.6	3.6
Capital expenditure	9.3	13.7	20.1	19.4	13.3	22.5	17.9
Lending minus repayment	0.0	-0.2	-0.2	-0.2	-0.2	-0.2	-0.2
Fiscal Balance	-1.7	2.2	-3.9	-11.1	-11.3	-10.5	-10.2
Financing	1.1	-3.7	2.4	11.1	11.3	10.5	10.2
Domestic	-9.8	7.5	-0.1	-1.3	-0.2	-1.6	-0.1
Central Bank	-7.2	12.7	3.2	0.0	0.0	0.0	0.0
Other domestic financing	-2.6	-5.2	-3.3	-1.3	-0.2	-1.6	-0.1
Privatization receipts	20.3	-0.7	1.7	0.0	0.0	0.4	0.4
Foreign	-9.4	-10.5	0.8	12.4	11.5	11.6	9.9
Official	…	…	…	…	0.8	3.1	2.2
Private	…	…	…	…	10.7	8.6	7.7
Memo items:							
Contributions to second pillar pensions	1.3	1.9	2.5	2.9	2.9	2.9	2.9
Unexplained measures	-0.6	-1.5	-1.4	0.0	0.0	0.0	0.0
Gross debt (as share of GDP)	31.5	23.4	21.5	24.5	24.5	26.2	26.2

Sources: IMF Staff and MoF estimates.

Note: Central government refers to the core government, plus consolidated extra-budgetary funds.

Table 2. FYR Macedonia: Central Government Operations, 2006–10 (concluded)

	2006	2007	2008	2009		2010	
				Budget	Proj.	Budget	Proj.
	(as share of GDP)						
Total revenue	32.9	33.2	33.5	34.2	31.4	34.1	33.2
Tax revenue	28.7	28.6	28.3	27.8	26.7	28.0	27.4
Personal Income Tax	2.7	2.5	2.2	2.3	2.2	2.4	2.3
Corporate Income Tax	1.5	1.7	2.2	1.3	1.3	1.1	1.0
VAT	8.8	9.3	9.1	9.1	8.5	9.2	9.0
Excises	3.9	3.7	3.6	3.8	3.7	3.8	3.8
Custom Duties	1.7	1.7	1.6	1.4	1.3	1.5	1.4
Other taxes	0.6	0.7	0.7	0.9	0.7	0.9	0.9
Social contributions (total)	9.5	8.9	9.0	9.1	9.0	9.2	9.0
Pension contributions	6.0	5.7	5.8	5.9	5.9	6.0	5.9
Unemployment contributions	0.4	0.4	0.5	0.5	0.5	0.4	0.4
Health contributions	3.0	2.8	2.7	2.7	2.7	2.8	2.7
Non Tax revenue	3.2	2.9	3.2	4.3	3.1	3.7	3.6
Capital Revenue	0.6	1.4	1.7	1.4	1.3	1.7	1.5
Of which: Telecom dividend	0.0	0.8	0.9	0.6	0.6	0.6	0.6
Grants	0.5	0.3	0.3	0.7	0.3	0.7	0.7
Total expenditure	33.4	32.6	34.5	37.0	34.3	36.6	35.7
Current expenditure	30.5	28.7	29.5	32.1	30.9	31.2	31.3
Wages and salaries	7.5	6.7	5.2	5.9	5.8	5.6	5.6
Goods and services	4.2	4.2	4.7	4.8	4.1	4.2	4.2
Transfers	17.8	17.1	18.9	20.8	20.4	20.6	20.7
Pensions	8.2	7.4	7.7	8.6	8.5	8.5	8.5
Health	5.1	4.5	4.8	4.7	4.7	4.6	4.6
Local governments	0.7	1.0	2.6	3.2	3.2	3.1	3.1
Other	3.8	4.1	3.8	4.2	4.0	4.4	4.4
Interest	1.0	0.8	0.7	0.6	0.6	0.9	0.9
Capital expenditure	3.0	3.9	5.0	4.9	3.4	5.5	4.4
Lending minus repayment	0.0	-0.1	0.0	0.0	0.0	0.0	0.0
Fiscal Balance	-0.5	0.6	-1.0	-2.8	-2.8	-2.5	-2.5
Financing	0.4	-1.0	0.6	2.8	2.8	2.5	2.5
Domestic	-3.2	2.1	0.0	-0.3	-0.1	-0.4	0.0
Central Bank	-2.3	3.6	0.8	0.0	0.0	0.0	0.0
Other domestic financing	-0.9	-1.5	-0.8	-0.3	-0.1	-0.4	0.0
Privatization receipts	6.5	-0.2	0.4	0.0	0.0	0.1	0.1
Foreign	-3.0	-3.0	0.2	3.1	2.9	2.8	2.4
Official	…	…	…	…	0.2	0.8	0.5
Private	…	…	…	…	2.7	2.1	1.9
Memo items:							
Contributions to second pillar pensions	0.4	0.5	0.6	0.7	0.7	0.7	0.7
Unexplained measures	-0.2	-0.4	-0.4	0.0	0.0	0.0	0.0
Gross debt (as share of GDP)	31.5	23.4	21.5	24.5	24.5	26.2	26.2

Sources: IMF Staff and MoF estimates.

Note: Central government refers to the core government, plus consolidated extra-budgetary funds.

Table 3. Macedonia: Balance of Payments (Baseline), 2006–14 1/

(Millions of Euros)

	2006	2007	2008	2009	2010	2011	2012	2013	2014
				Projection					
Current account	-45	-415	-853	-613	-547	-526	-482	-472	-450
(excluding official transfers)	-104	-439	-901	-653	-587	-566	-522	-512	-490
Trade balance (fob)	-1,020	-1,175	-1,751	-1,494	-1,504	-1,493	-1,474	-1,501	-1,514
Exports	1,903	2,441	2,684	1,977	2,266	2,468	2,719	3,009	3,360
Imports	-2,923	-3,616	-4,435	-3,471	-3,770	-3,961	-4,193	-4,510	-4,875
Services (net)	22	26	4	5	19	21	17	23	25
Income (net; including net interest) /2	-28	-278	-91	-111	-98	-136	-144	-141	-141
Of which: Telecom Dividend	0	-47	-60	-78	-40	-40	-40	-40	-40
Transfers (net)	982	1,012	984	987	1,036	1,082	1,118	1,148	1,180
Official	59	24	48	40	40	40	40	40	40
Private	923	988	936	947	996	1,042	1,078	1,108	1,140
Of which: cash exchange	649	695	631	660	679	693	707	721	735
Capital and financial account	343	533	784	461	646	601	635	660	683
Capital account (net)	-1	4	-12	0	0	0	0	0	0
Financial account	344	529	796	461	646	601	635	660	683
Net disbursements	-36	-96	283	51	97	48	49	49	31
Disbursements	240	272	441	240	300	240	255	272	289
Amortization	-276	-368	-157	-189	-203	-192	-206	-223	-258
Of which: prepayments 3/	167	170	0	0	0	0	0	0	0
Direct and portfolio investment (net)	418	621	359	298	506	514	552	587	624
Direct investment	345	507	409	161	351	379	412	442	474
Of which: nonprivatization related FDI	120	519	387	161	351	379	412	442	474
Portfolio investment	73	114	-51	138	155	135	140	145	150
Of which: Eurobond (net)	0	0	0	175	125	100	100	100	150
Currency and deposits (net)	-78	6	191	45	0	0	0	0	0
Of which: commercial banks	-10	68	235	4	0	0	0	0	0
Other credits (net)	40	-2	-38	67	42	39	34	24	27
Of whcich: trade credits	3	-29	-16	55	37	32	27	16	17
Errors and omissions	7	-33	2	11	0	0	0	0	0
Overall balance	305	85	-68	-152	99	75	153	188	232
Financing	-305	-85	68	152	-99	-75	-153	-188	-232
Net foreign assets (flows)	-311	-144	61	152	-99	-75	-153	-188	-232
Valuation effects on the stock of NFA (increase: -)	4	-6	-15	0	0	0	0	0	0
Change in the stock of NFA (increase:-)	-307	-149	45	152	-99	-75	-153	-188	-232
Change in gross foreign reserves (increase:-)	-294	-108	29	79	-99	-75	-153	-188	-232
IMF (net)	-8	-42	0	0	0	0	0	0	0
Other (net)	-6	0	16	62	0	0	0	0	0
Change in arrears 4/	6	58	7	0	0	0	0	0	0

Sources: Data provided by the authorities; and IMF staff estimates and projections.

1/ NBRM issued revised BOP statistics in November 2008, based on new surveys and other sources.

2/ For 2008 and beyond, the figures include accrued interest on reserves.

3/ Amortization payments include prepayment of London Club debt in 2006 and Paris Club debt in 2007.

4/ Private sector arrears.

5/ GIR in percent of S-T debt (residual basis) plus current account deficit (0 if surplus)

6/ Revised debt series completed end-2007 resulted in upward revisions in debt stock beginning 2004.

7/ Debt service due including IMF as percent of exports of goods and services. Excludes rollover of trade credits.

8/ Including IMF.

Table 3: FYR Macedonia: Medium-Term Balance of Payments (Baseline), 2006?14, (concluded) 1/

(In percent of GDP, unless otherwise noted)

	2006	2007	2008	2009	2010	2011	2012	2013	2014
				Projections					
Memorandum items:									
Current account	-0.9	-7.2	-13.1	-9.5	-8.2	-7.3	-6.2	-5.6	-5.0
Trade balance	-20.1	-20.3	-26.9	-23.1	-22.5	-20.7	-18.8	-17.9	-16.8
Exports f.o.b.	37.4	42.2	41.3	30.6	33.9	34.3	34.8	35.8	37.3
Imports, f.o.b.	57.5	62.4	68.2	53.7	56.5	55.0	53.6	53.7	54.1
Non-energy trade balance	-11.1	-10.7	-16.1	-14.1	-11.4	-10.7	-9.4	-8.9	-8.3
Of which: vehicles	-2.9	-3.7	-4.4	---	---	---	---	---	---
food	-3.4	-3.8	-3.7	---	---	---	---	---	---
iron & steel	3.5	7.3	2.0	---	---	---	---	---	---
Energy trade balance	-9.0	-9.6	-10.8	-9.0	-11.2	-10.0	-9.5	-9.0	-8.5
Of which: electricity	-1.6	-3.1	-3.6	---	---	---	---	---	---
Export growth (value, fob)	15.8	28.3	9.9	-26.3	14.6	8.9	10.1	10.7	11.7
Import growth (value, fob)	16.9	23.7	22.6	-21.7	8.6	5.1	5.9	7.6	8.1
Export growth rate (volumes)	8.4	14.3	-4.3	-14.0	2.8	6.8	8.0	8.5	9.5
Import growth rate (volumes)	11.0	17.4	5.8	-9.5	1.1	3.0	3.8	5.5	6.0
Export price increase	6.8	12.2	14.9	-14.5	11.5	2.0	2.0	2.0	2.0
Import price increase	5.3	5.4	15.9	-13.7	7.5	2.0	2.0	2.0	2.0
Terms of trade	102.9	109.6	108.6	107.6	111.6	111.6	111.6	111.6	111.6
Nickel prices (in thousands of Euros/metric tonne)	19.2	27.1	14.4	10.6	11.4	12.1	11.5	10.9	10.3
Oil prices (USD per barrel)	64	71	97	62	77	80	81	83	85
Oil prices (Euro per barrel)	51	52	66	45	54	57	58	60	62
Food prices (world), % change (Euro-based index)	9.6	5.6	14.9	-8.8	-1.3	0.6	1.3	1.8	1.9
Net income	-0.6	-4.8	-1.4	-1.7	-1.5	-1.9	-1.8	-1.7	-1.6
Private transfers, net	18.2	17.1	14.4	14.6	14.9	14.5	13.8	13.2	12.7
Of which: cash exchange	12.8	12.0	9.7	10.2	10.2	9.6	9.0	8.6	8.2
formal remittances	2.8	2.7	2.5	2.4	2.6	2.5	2.4	2.4	2.3
other private transfers	2.5	2.3	2.2	2.0	2.2	2.3	2.3	2.2	2.2
Net FDI	6.8	8.8	6.3	2.5	5.3	5.3	5.3	5.3	5.3
Of which: nonprivatization related FDI	2.4	9.0	5.9	2.5	5.3	5.3	5.3	5.3	5.3
Gross reserves (in millions of Euros)	1,417	1,524	1,495	1,415	1,514	1,590	1,742	1,930	2,163
In months of following year's imports of G&S	4.1	3.6	4.4	3.9	3.9	3.9	3.9	4.0	4.1
In percent of short-term debt residual maturity	130.8	119.2	99.1	88.2	89.7	88.4	82.6	87.4	93.0
Reserve cover 5/	132.1	95.4	65.9	67.0	68.9	68.2	72.1	77.0	82.7
External debt service ratio (in percent) 6/ 7/	22.6	35.1	25.1	38.7	37.3	37.4	37.2	36.6	35.8
External debt to GDP ratio (in percent) 6/ 8/	49.1	48.9	51.0	56.4	59.4	58.9	57.9	57.3	56.5
Medium and long term (in percent of GDP)	35.0	29.5	30.7	34.7	37.0	36.8	36.3	36.1	35.7
Short term (in percent of GDP)	14.1	19.4	20.3	21.7	22.4	22.1	21.6	21.2	20.8
Of which: Intercompany lending (direct investment)	3.2	3.7	5.0	5.4	6.0	6.4	6.6	7.0	7.3
Nominal GDP (in millions of euros)	5,081	5,791	6,504	6,465	6,678	7,205	7,822	8,397	9,011

Sources: Data provided by the authorities; and IMF staff estimates and projections.

1/ NBRM issued revised BOP statistics in November 2008, based on new surveys and other sources.
2/ For 2008 and beyond, the figures include accrued interest on reserves.
3/ Amortization payments include prepayment of London Club debt in 2006 and Paris Club debt in 2007.
4/ Private sector arrears.
5/ GIR in percent of S-T debt (residual basis) plus current account deficit (0 if surplus)
6/ Revised debt series completed end-2007 resulted in upward revisions in debt stock beginning 2004.
7/ Debt service due including IMF as percent of exports of goods and services. Excludes rollover of trade credits.
8/ Including IMF.

Table 4: FYR Macedonia: External Financing Requirements and Sources, 2006–14

(In millions of euros)

	2006	2007	2008	2009	2010	2011	2012	2013	2014
	Actual			Projections					
I. Gross financing requirement	1,079	1,563	2,180	2,162	2,191	2,254	2,320	2,597	2,625
External current account deficit (excl. official transfers)	104	439	901	653	587	566	522	512	490
Debt amortization (MLT) 1/	284	409	157	189	203	192	206	398	358
Public	187	244	85	61	69	51	58	242	194
Private	97	165	72	128	134	141	148	156	163
Debt Amortization (ST)	692	716	1,121	1,319	1,401	1,496	1,592	1,687	1,778
II. Identified financing sources	1,373	1,671	2,128	2,082	2,291	2,329	2,474	2,610	2,758
Capital account	-1	4	-12	0	0	0	0	0	0
Financial account Total	344	529	796	461	646	601	635	660	683
Foreign direct investment (net)	345	507	409	161	351	379	412	442	474
Portfolio investments (net)	73	114	-51	138	155	135	140	145	150
Of which: Eurobond (issuance)	0	0	0	175	125	100	100	275	250
MLT Debt disbursement	240	272	443	240	300	240	255	272	289
Public	48	81	211	85	85	85	85	85	85
Private	192	190	232	155	215	155	170	187	204
ST Debt Disbursement	654	719	1,250	1,432	1,444	1,535	1,627	1,711	1,805
Official transfers and grants	59	24	48	40	40	40	40	40	40
Other	3	31	41	73	0	0	0	0	0
Errors and omissions	7	-33	2	11	…	…	…	…	…
Valuation effects	-4	6	15	0	…	…	…	…	…
Other Changes	-6	0	16	62	…	…	…	…	…
Accumulation of arrears 2/	6	58	7	0	…	…	…	…	…
III Financing Gap (1 - 2)	294	108	-52	79	-99	-75	-153	-188	-232
IMF/BIS purchases and disbursements	0	0	0	0	0	0	0	0	0
Gross reserves accumulation (-: increase)	-294	-108	52	79	-99	-75	-153	-188	-232
Memorandum item:									
Reserves	1,417	1,524	1,495	1,415	1,514	1,590	1,742	1,930	2,163

Sources: NBRM and IMF staff estimates and projections.

1/ Excluding the IMF.

2/ Private sector and public enterprise arrears.

Table 5. FYR Macedonia: Central Bank Accounts, 2005–09 (baseline)

(End-period; in billions of denars unless otherwise indicated)

	2004	2005	2006	2007	2008				2009			
	Dec	Dec	Dec	Dec	Mar	June	Sept	Dec	Mar	June	Sept Actual	Dec Proj
	(At current exchange rates)											
Net foreign assets (NFA)	41.4	65.7	84.9	94.4	93.0	93.9	102.4	91.0	77.2	73.2	89.0	81.8
Net domestic assets (NDA)	-18.7	-38.0	-51.5	-54.6	-56.1	-52.3	-58.9	-45.7	-37.4	-32.4	-43.6	-36.4
Banks (net)	-3.7	-8.9	-9.5	-21.0	-21.7	-21.6	-20.1	-17.4	-7.5	-12.5	-15.2	-9.5
Of which: NBRM bills	-4.6	-8.9	-9.5	-21.0	-21.7	-21.6	-20.1	-17.5	-6.9	-9.7	-12.6	-6.9
Of which: FX Deposit Auctions	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	-0.6	-2.8	-2.6	-2.6
Central government (net)	-9.4	-20.5	-32.1	-19.6	-21.7	-17.5	-23.3	-11.0	-13.6	-4.1	-12.2	-11.0
Of which: deposits	-12.9	-24.0	-34.6	-20.8	-22.9	-18.7	-24.6	-12.3	-14.9	-5.4	-13.5	-12.3
Municipalities (net)	0.0	-0.7	-0.6	-1.6	-2.0	-2.6	-2.9	-2.8	-2.7	-3.2	-3.5	-3.5
Other items (net)	-5.6	-8.0	-9.2	-12.4	-10.8	-10.6	-12.6	-14.5	-13.6	-12.5	-12.7	-12.5
Reserve money	22.7	27.7	33.4	39.9	36.9	41.7	43.6	45.2	39.9	40.8	45.4	45.4
Currency	14.2	14.4	16.2	17.9	15.7	16.2	16.5	17.6	14.6	14.2	14.5	14.3
Other	8.5	13.3	17.2	22.0	21.2	25.5	27.0	27.6	25.2	26.6	31.0	31.1
Cash in vaults	0.9	1.4	1.5	2.0	2.1	2.3	2.4	3.2	2.6	2.6	2.7	2.7
Total reserves	6.0	10.3	13.8	18.0	16.7	20.7	21.7	21.6	19.7	20.8	24.9	25.0
On denar deposits	2.7	5.0	7.4	10.7	8.2	11.7	12.0	11.8	9.1	9.6	12.9	0.0
On FX deposits	3.4	5.3	6.4	7.3	8.6	9.0	9.8	9.8	10.6	11.2	12.0	0.0
Other	1.6	1.6	1.9	2.0	2.4	2.5	2.9	2.8	2.9	3.1	3.4	3.4
	(Year-on-year growth rates, percent)											
Net foreign assets	...	58.9	29.1	11.3	9.6	7.2	8.9	-3.7	-16.9	-22.1	-13.1	-10.0
Reserve money	...	22.1	20.5	19.4	24.6	30.0	33.0	13.4	8.2	-2.1	4.2	0.4
Currency	...	1.9	12.2	10.6	4.7	2.1	-1.2	-1.7	-6.8	-12.0	-12.5	-18.8
	(Contribution to year-on-year change in base money)											
Net foreign assets	...	107.4	69.1	28.7	27.4	19.7	25.6	-8.7	-42.6	-49.8	-5.6	-4.5
Net domestic assets	...	-85.3	-48.5	-9.2	-10.8	3.2	-0.7	22.1	50.8	47.7	9.8	4.9
Memorandum items:												
Reserve money/GDP (in percent)	8.6	9.7	10.7	11.3	10.1	11.0	11.2	11.3	10.0	10.2	11.4	11.4
Program exchange rate (denars per euro)	61.3	61.3	61.3	61.3	61.3	61.3	61.3	61.3	61.3	61.3	61.3	61.3

Sources: NBRM, and IMF staff projections.

1/ Measured on a rolling basis as a sum of nominal GDP of four preceding quarters including the last quarter of each period.

Table 6. FYR Macedonia: Monetary Survey, 2005–09 (baseline)

(End-period; in billions of denars unless otherwise indicated)

	2005	2006	2007	2008				2009			
	Dec	Dec	Dec	Mar	June	Sept	Dec	Mar	June	Sep Actual	Dec Proj
						(At current exchange rates)					
Net foreign assets (NFA)	88.9	107.5	109.1	104.8	104.2	111.0	91.0	80.9	77.5	92.2	85.0
NBRM	65.7	84.9	94.4	93.0	93.9	102.4	91.0	77.2	73.2	89.0	81.8
Domestic money banks (DMBs)	23.2	22.7	14.6	11.8	10.2	8.6	0.0	3.7	4.3	3.2	3.2
Net domestic assets (NDA)	19.8	28.4	66.7	73.7	85.6	86.9	104.5	109.4	114.5	103.6	111.3
Credit to the government	-16.0	-21.9	-10.5	-16.1	-15.6	-21.2	-8.4	-6.7	-2.2	-10.8	-9.6
Banks	5.2	10.9	10.6	7.6	4.4	4.9	5.5	9.5	5.2	4.9	4.9
NBRM (net)	-21.2	-32.8	-21.2	-23.6	-20.0	-26.2	-13.9	-16.2	-7.4	-15.7	-14.5
Of which: municipalities	-0.7	-0.6	-1.6	-2.0	-2.6	-2.9	-2.8	-2.7	-3.2	-3.5	-3.5
Credit to the private sector	72.0	93.8	130.4	143.0	155.7	167.0	174.8	177.8	176.7	176.7	176.7
In denars 1/	54.5	70.0	99.4	110.7	120.7	128.5	136.0	138.9	138.8	139.0	139.0
Of which: foreign exchange indexed											
In foreign currency	17.4	23.8	31.0	32.4	35.0	38.6	38.8	38.9	37.9	37.7	37.7
Other items (net)	-36.2	-43.5	-53.1	-53.2	-54.5	-58.9	-61.9	-61.6	-60.1	-62.4	-55.8
Broad money (M3)	108.7	135.9	175.8	178.5	189.7	197.9	195.5	190.4	191.9	195.7	196.3
Currency in circulation	14.4	16.2	17.9	15.7	16.2	16.5	17.6	14.6	14.2	14.5	14.7
Total	94.3	119.7	157.9	162.8	173.6	181.4	177.9	175.7	177.7	181.3	181.5
Private denar deposits 1/ 2/	43.2	59.3	89.6	90.4	96.9	98.9	94.1	86.4	86.1	84.2	84.5
Of which: foreign exchange indexed											
Private foreign currency deposits	51.1	60.5	68.3	72.5	76.7	82.5	83.8	89.3	91.6	97.1	97.1
						(Year-on-year growth rates, percent)					
NFA domestic money banks	-11.9	-2.3	-35.4	-48.6	-46.5	-47.9	-99.8	-68.7	-57.8	-63.1	11656.2
Credit to the private sector	22.7	30.3	39.0	42.1	42.0	38.5	34.1	24.3	13.5	5.8	1.1
Denar credit	15.9	28.3	42.0	46.7	46.8	40.8	36.9	25.5	15.0	8.2	2.2
Foreign currency credit	50.7	36.7	30.2	28.2	27.6	31.4	25.1	20.3	8.4	-2.2	-2.8
Broad Money	15.0	25.0	29.3	25.3	21.4	22.0	11.2	6.6	1.2	-1.1	0.4
Total Deposits	17.3	27.0	31.9	27.8	23.6	24.7	12.7	7.9	2.4	-0.1	2.0
Private denar deposits	14.2	37.2	51.2	40.2	29.5	24.5	5.0	-4.3	-11.1	-14.9	-10.2
Private foreign currency deposits	20.1	18.3	12.9	15.0	16.9	24.9	22.8	23.2	19.5	17.7	15.8
Memorandum items:											
M3/GDP (in percent)	37.9	43.7	49.6	47.3	47.6	50.8	49.0	47.6	48.0	49.6	49.6
GDP/M3	2.6	2.3	2.0	2.1	2.1	2.0	2.0	2.1	2.1	2.0	2.0
Broad money multiplier (M3/reserve money)	3.9	4.1	4.4	4.8	4.6	4.5	4.3	4.8	4.7	4.3	4.3
NFA of DMBs/forex deposits (percent)	55.8	48.0	32.1	28.1	25.1	22.3	11.7	16.0	17.0	15.6	3.3
Private credit (percent of GDP)	25.1	30.2	36.8	37.9	39.1	42.8	43.8	44.5	44.2	44.7	44.6
Nominal GDP (yearly total) 3/	286.6	310.9	354.3	377.8	398.6	389.9	398.6	399.7	400.3	395.0	396.0

Sources: NBRM, and IMF staff projections.

1/ Includes foreign currency indexed.
2/ Includes municipal and public enterprise accounts.
3/ Measured on a rolling basis as a sum of nominal GDP of four preceding quarters including the last quarter of each period.

Table 7. FYR Macedonia: Financial Soundness Indicators, 2005–09

	2005	2006	2007	2008	2009Q1	2009Q2
Capital adequacy						
Regulatory capital/risk weighted assets	21.3	18.3	17.0	16.2	16.5	16.4
Tier I capital/risk weighted assets 1/	24.3	18.9	15.7	14.0	14.1	14.0
Asset composition and quality						
Structure of loans to nonfinancial entities						
Enterprises (loans to enterprises/total loans to nonfinancial entities)	61.7	59.0	54.9	54.2	59.0	58.3
Households (loans to households/total loans to nonfinancial entities)	30.6	33.4	37.7	38.5	38.5	38.9
Foreign currency lending						
Foreign currency lending/total credit to private sector	25.4	26.3	24.6	22.9	23.1	22.6
Foreign currency indexed lending/total credit to private sector	23.8	26.4	30.1	34.1	31.6	34.2
NPLs						
NPLs / gross loans 2/	15.0	11.2	7.5	6.8	7.5	8.6
NPLs net of provision / capital	2.9	0.7	-5.0	-6.2	-2.6	0.4
Large exposures/capital	189.7	194.7	181.4	118.0	122.5	167.3
Connected lending						
Banking system exposure to shareholders / own funds	4.3	5.2	5.6	3.1	3.5	11.6
Banking system equity investments/own funds	7.0	6.3	4.9	3.9	2.1	2.2
Earning and profitability						
ROAA 3/	1.2	1.8	1.8	1.4	0.2	0.5
ROAE 3/	7.5	12.3	15.0	12.5	1.8	4.3
Interest margin/gross income 4/	53.8	57.1	57.0	58.9	63.1	63.2
Noninterest expenses/gross income 5/	68.1	63.6	60.3	64.0	64.3	66.6
Personnel expenses/noninterest expenses	42.1	41.1	38.4	36.5	36.6	36.8
Interest Rates						
Local currency spreads	6.5	6.3	4.5	3.2	3.3	3.3
Foreign currency spreads	6.5	6.7	6.5	4.2	4.2	4.2
Interbank market interest rate	8.7	4.9	3.1	5.3	5.4	6.4
Liquidity	`					
Highly liquid assets/total assets 6/	14.9	17.7	20.6	16.6	15.6	15.4
Highly liquid assets/total short-term liabilities 7/	22.0	25.6	28.7	24.4	22.9	22.6
Customer deposits/total (noninterbank) loans	142.3	137.1	128.3	107.7	102.3	103.4
Foreign currency deposits/total deposits	55.7	51.8	44.5	48.1	54.0	54.8
Including foreign exchange-indexed 8/	58.5	56.1	51.5	54.8	59.6	61.1
Central bank credit to banks/bank liabilities 9/	0.2	0.2	0.1	0.1	0.0	0.0
Sensitivity to market risk						
Net open foreign exchange position / own funds	51.6	47.0	38.2	25.1	9.6	13.6

Sources: NBRM's Financial Stability, Banking Regulations and Methodology Department.

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

2/ Includes only loans to nonfinancial sector.

3/ Adjusted for unallocated provisions for potential loan losses. Since 31.03.2009 these items have been adjusted for unrecognized impairment.

4/ Interest margin is interest income less interest expense. Gross income includes net interest income, fees and commissions income (gross, not net), dividends, net income regarding securities, net capital income, net FX income and other income excluding extraordinary income.

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

6/ Highly liquid assets are defined as cash and balance with the NBRM, treasury bills, NBRM bills, and correspondent accounts with foreign banks.

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

8/ FX indexed deposits include deposits and other FX indexed liabilities. However FX indexed deposits comprise the majority of these items. Since 31.03.2009 the figure refers only to foreign exchange indexed deposits.

9/ The increase in 2006 is due to loans channeled through NBRM, not NBRM credit to banks.

Table 8. FYR Macedonia: Foreign Exchange Balance Sheet

	FX	FX Indexed	Total	Total
	(In millions of Euros)			In percent of GDP
Banks				
Assets	1,288	1,001	2,289	35
Domestic	…	…	1,834	…
Foreign	455	…	455	…
Liabilities	1,967	250	2,217	34
Domestic	…	…	1,832	…
FX deposits of residents	…	…	1,621	…
Other	…	…	211	…
Foreign	385	…	385	…
ST deposits of nonresidents	154	…	154	…
LT loans from nonresidents	191	…	191	…
Other	40	…	40	…
Banks net	0	…	73	1
Households	0	…	0	…
Assets	1,222	1	1,224	…
Liabilities	67	408	474	…
Households net	0	…	749	11
Firms	0	…	0	…
Assets	0	…	1,045	16
Domestic	289	159	448	…
Foreign	…	…	597	…
Of which: trade credits	…	…	523	…
Liabilities	…	…	3,059	47
Domestic	564	463	1,027	…
External	2,032	…	2,032	…
Intercompany	649	…	649	…
Trade credits	695	…	695	…
Loans	564	…	564	…
Other	…	…	123	…
Firms net	…	…	-2,014	-31
Government				0
Assets	…	…	…	…
Liabilities	…	…	1,274	…
Domestic	326	42	369	…
FX linked bonds	…	42	42	…
Domestic bonds (in Euros)	326	…	326	…
Foreign	905	…	905	…
Foreign bonds and notes	129	…	129	…
Loans	775	…	775	…
Other	1	…	1	…
Government net	…	…	-1,274	-20
Central Bank				0
Assets	…	…	1,206	…
Liabilities	…	…	12	…
Central bank net	…	…	1,194	18
Total (without Central Bank)	…	…	…	-38
Total (with Central Bank)	…	…	…	-20

Source: IMF staff estimates.

Table 9. FYR Macedonia: Fiscal Debt Sustainability Framework, 2004-14 (baseline)

(In percent of GDP, unless otherwise indicated)

	Actual							Projection							
	2004	2005	2006	2007	2008			2009	2010	2011	2012	2013	2014	2015	Debt-stabilizing primary balance 9/
Public sector debt 1/	36.6	39.5	31.5	23.4	21.5			24.5	26.2	26.3	25.7	25.5	25.2	25.0	-0.4
Of which: foreign-currency denominated	27.8	30.8	24.1	17.8	17.1			22.9	24.7	24.8	24.4	23.5	22.7	22.0	
Change in public sector debt	-2.4	3.0	-8.0	-8.1	-1.9			3.0	1.7	0.1	-0.6	-0.3	-0.2	-0.2	
Identified debt-creating flows	-1.5	-1.6	-8.3	-3.2	-1.6			3.0	1.8	0.1	-0.6	-0.3	-0.2	-0.2	
Primary deficit	-1.3	-1.2	-0.5	-1.4	0.3			2.2	1.6	0.9	0.3	0.3	0.3	0.3	
Revenue and grants	36.5	35.2	32.9	33.2	33.6			31.4	31.9	31.4	31.7	32.0	32.2	32.2	
Primary (noninterest) expenditure	35.2	34.0	32.4	31.7	33.9			33.6	33.5	32.2	32.0	32.3	32.4	32.5	
Automatic debt dynamics 2/	-1.1	-1.9	-2.0	-3.0	-1.9			0.7	0.1	-0.8	-0.9	-0.6	-0.5	-0.4	
Contribution from interest rate/growth differential 3/	-1.1	-1.8	-2.1	-3.0	-1.9			0.7	0.1	-0.8	-0.9	-0.6	-0.5	-0.4	
Of which contribution from real interest rate	0.4	-0.4	-0.6	-1.4	-0.9			0.5	0.6	0.4	0.3	0.4	0.4	0.5	
Of which contribution from real GDP growth	-1.5	-1.4	-1.5	-1.6	-1.0			0.3	-0.5	-1.2	-1.2	-1.0	-0.9	-0.9	
Contribution from exchange rate depreciation 4/	0.0	-0.1	0.1	0.0	0.0			0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Other identified debt-creating flows	0.9	1.5	-5.9	1.2	0.0			0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Privatization receipts (negative)	-0.2	-0.2	-6.5	0.2	-0.4			0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Recognition of implicit or contingent liabilities	1.1	1.2	0.7	1.0	0.4			0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Residual	-0.9	4.5	0.3	-4.8	-0.3			0.0	0.0	0.0	0.0	0.0	0.0	0.0	
Public sector debt-to-revenue ratio 1/	100.2	112.3	95.8	70.7	64.1			77.9	82.2	83.8	81.2	79.6	78.4	77.7	
Gross financing need 5/	2.4	1.9	6.0	4.4	2.0			5.2	4.9	4.3	3.4	5.0	4.7	5.6	
in million Euros	103.9	90.9	306.0	253.9	132.9			334.9	326.1	313.4	263.1	417.1	423.6	537.3	
Key Macroeconomic and Fiscal Assumptions						7-Year Historical Average	7-Year Standard Deviation								Projected Average
Real GDP growth (in percent)	4.1	4.1	4.0	5.9	4.8	3.8	1.6	-1.3	2.0	5.0	5.0	4.0	4.0	4.0	3.2
Average nominal interest rate on public debt (in percent) 6/	2.5	2.7	2.8	3.0	3.2	2.8	0.3	2.9	3.8	4.7	4.8	5.0	5.2	5.3	4.5
Average nominal interest rate on forex debt (in percent) 6/	1.9	2.8	2.9	3.1	3.6	2.8	0.5	2.7	3.4	4.9	5.9	6.7	6.5	6.5	5.2
Average real interest rate (nominal rate minus change in GDP deflator, in percent)	1.1	-1.1	-1.5	-4.6	-4.1	-1.2	2.6	2.1	2.5	1.9	1.4	1.8	2.0	2.3	2.0
Nominal appreciation (increase in euro value of local currency, in percent)	0.0	0.2	-0.2	0.0	0.0	-0.1	0.2	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Inflation rate (GDP deflator, in percent)	1.3	3.8	4.3	7.6	7.3	4.0	2.7	0.8	1.3	2.8	3.4	3.2	3.2	3.0	2.5
Growth of real primary spending (deflated by GDP deflator, in percent)	-2.0	0.6	-0.9	3.7	11.8	2.0	4.8	-2.0	1.6	1.0	4.3	4.9	4.5	4.1	2.6
Primary deficit	-1.3	-1.2	-0.5	-1.4	0.3	-0.1	2.0	2.2	1.6	0.9	0.3	0.3	0.3	0.3	0.8

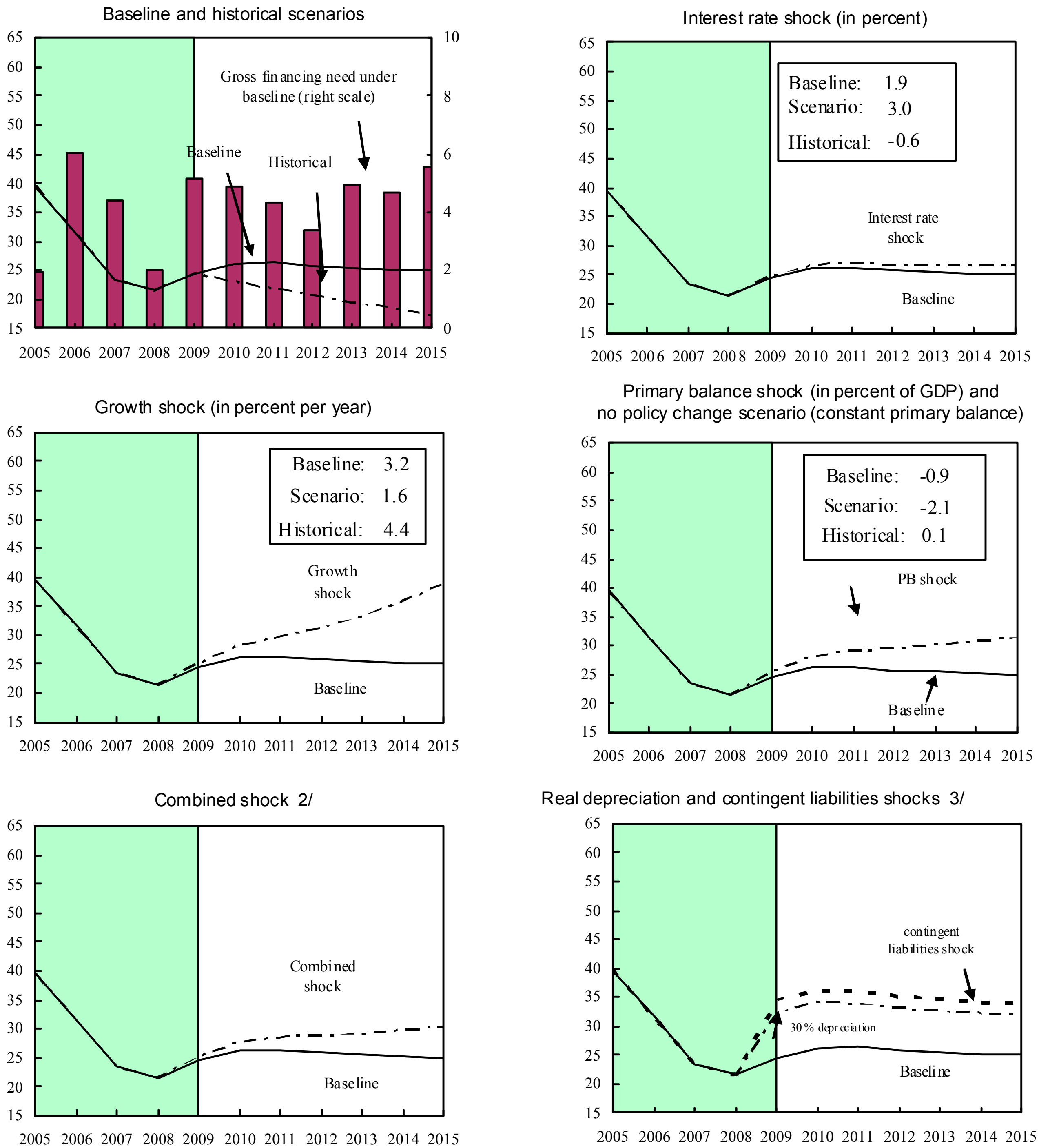
II. Stress Tests for Public Debt Ratio

	2009	2010	2011	2012	2013	2014	2015	Debt-stabilizing primary balance 9/
A. Alternative Scenarios								
A1. Key variables are at their historical averages in 2009-14 7/	24.5	23.1	21.9	20.7	19.6	18.5	17.5	-0.9
A2. No policy change (constant primary balance) in 2008-13	26.1	25.7	24.7	24.3	25.8	28.5	28.5	-1.0
B. Bound Tests								
B1. Real interest rate is at baseline plus one standard deviations	24.8	26.8	27.2	26.9	26.9	27.0	27.1	-0.2
B2. Real GDP growth is at baseline minus one-half standard deviation	24.9	27.4	28.4	29.0	30.2	31.6	33.4	-0.4
B3. Primary balance is at baseline minus one-half standard deviation	25.5	28.2	29.2	29.5	30.1	30.8	31.5	-0.9
B4. Combination of B1-B3 using one-quarter standard deviation shocks	25.2	27.7	28.5	28.6	29.0	29.5	30.0	-0.6
B5. One time 30 percent real depreciation in 2006 8/	32.4	34.1	34.0	33.1	32.7	32.3	32.0	-1.0
B6. 10 percent of GDP increase in other debt-creating flows in 2006	34.5	36.3	36.0	35.1	34.7	34.2	33.9	-1.0

Sources: MoF and IMF Staff estimates.

1/ Consolidated central government gross debt.
2/ Derived as [(r - p(1+g) - g + ae(1+r)]/(1+g+p+gp)) times previous period debt ratio, with r = interest rate; p = growth rate of GDP deflator; g = real GDP growth rate; a = share of foreign-currency denominated debt; and e = nominal exchange rate depreciation (measured by increase in local currency value of euro).
3/ The real interest rate contribution is derived from the denominator in footnote 2/ as r - π (1+g) and the real growth contribution as -g.
4/ The exchange rate contribution is derived from the numerator in footnote 2/ as ae(1+r).
5/ Defined as public sector deficit, plus amortization of medium and long-term public sector debt, plus short-term debt at end of previous period.
6/ Derived as nominal interest expenditure divided by previous period debt stock.
7/ The key variables include real GDP growth; real interest rate; and primary balance in percent of GDP.
8/ The implied change in other key variables under this scenario is discussed in the text.
9/ Assumes that key variables (real GDP growth, real interest rate, and other identified debt-creating flows) remain at the level of the last projection year.

Figure 4. FYR Macedonia: Public Debt Sustainability: Bound Tests 1/
(Public debt in percent of GDP)



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

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

2/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and primary balance.

3/ One-time real depreciation of 30 percent or a 10 percent of GDP shock to contingent liabilities occur in 2009. Real depreciation is defined as nominal depreciation (measured by percentage fall in dollar value of local currency) minus domestic inflation (based on GDP deflator).

Table 10. FYR Macedonia: External Debt Sustainability Framework, 2004?14

(In percent of GDP, unless otherwise indicated)

	Actual					Projections						
	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	Debt-stabilizing non-interest current account 6/
Baseline: External debt	47.9	53.9	49.1	48.9	51.0	**56.9**	**59.8**	**59.2**	**58.1**	**57.4**	**57.0**	**-4.8**
Change in external debt	1.9	6.0	-4.8	-0.2	2.1	5.9	2.9	-0.6	-1.1	-0.7	-0.4	
Identified external debt-creating flows (4+8+9)	0.0	-2.9	-9.0	-5.6	5.1	8.6	3.5	0.9	-0.2	-0.2	-0.8	
Current account deficit, excluding interest payments	7.4	1.5	-0.5	5.7	11.9	8.0	6.0	4.8	3.4	2.7	2.2	
Deficit in balance of goods and services	-22.1	-18.9	-19.6	-19.8	-26.9	-23.4	-22.3	-20.8	-18.8	-17.8	-16.7 #	
Exports	39.5	44.0	46.8	52.4	51.8	40.4	44.9	44.6	45.0	46.3	48.0	
Imports	-61.7	-62.9	-66.5	-72.3	-78.7	-63.8	-67.1	-65.4	-63.8	-64.1	-64.7	
Net non-debt creating capital inflows (negative)	-6.0	-1.9	-5.6	-6.8	-2.9	-1.8	-3.7	-3.7	-3.7	-3.7	-3.7	
Automatic debt dynamics 1/	-1.3	-2.5	-2.9	-4.4	-3.9	2.3	1.2	-0.1	0.1	0.8	0.7	
Contribution from nominal interest rate	1.0	1.1	1.4	1.5	1.3	1.6	2.3	2.6	2.8	3.0	2.8	
Contribution from real GDP growth	-2.1	-1.9	-2.0	-2.6	-2.1	0.7	-1.1	-2.8	-2.7	-2.2	-2.1	
Contribution from price and exchange rate changes 2/	-0.3	-1.7	-2.3	-3.4	-3.0	...	...	...	...	...	...	
Residual, incl. change in gross foreign assets (2-3) 3/	1.9	8.9	4.2	5.4	-3.0	-2.7	-0.6	-1.5	-0.9	-0.5	0.4	
External debt-to-exports ratio (in percent)	121.2	122.3	104.8	93.3	98.5	140.7	133.2	132.8	129.1	123.9	118.7	
Gross external financing need (in billions of Euros) 4/	1025.8	780.8	998.7	1440.4	2027.5	1993.6	2016.9	2073.1	2132.0	2401.1	2421.3	
In percent of GDP	23.7	16.7	19.7	24.9	31.2	31.3	30.7	29.3	27.7	29.1	27.3	
Scenario with key variables at their historical averages 5/	...	...	...	...	...	56.9	54.6	52.4	51.2	50.2	50.2	-6.4
Key Macroeconomic Assumptions Underlying Baseline												
Real GDP growth (in percent)	4.7	4.3	4.0	5.9	4.8	-1.3	2.0	5.0	5.0	4.0	4.0	
GDP deflator in Euros (change in percent)	0.6	3.7	4.4	7.3	6.6	-0.9	1.3	2.8	3.4	3.2	3.2	
Nominal external interest rate (in percent)	2.4	2.5	2.7	3.4	2.9	3.1	4.2	4.8	5.2	5.5	5.3	
Growth of exports (Euro terms, in percent)	11.1	20.5	15.6	27.6	11.0	-23.7	14.6	7.3	9.6	10.4	11.2	
Growth of imports (Euro terms, in percent)	16.1	10.3	14.8	23.9	22.3	-20.7	8.6	5.1	6.0	7.8	8.3	
Current account balance, excluding interest payments	-7.4	-1.5	0.5	-5.7	-11.9	-8.0	-6.0	-4.8	-3.4	-2.7	-2.2	
Net non-debt creating capital inflows	6.0	1.9	5.6	6.8	2.9	1.8	3.7	3.7	3.7	3.7	3.7	

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

2/ The contribution from price and exchange rate changes is defined as [-∈(1+g∈+γ93 (1+r∈φ1+g+∈+g∈) times previous period debt stock. ∈ increases with an appreciating domestic currency (∈> 0) and rising inflation (based on GDP deflator).

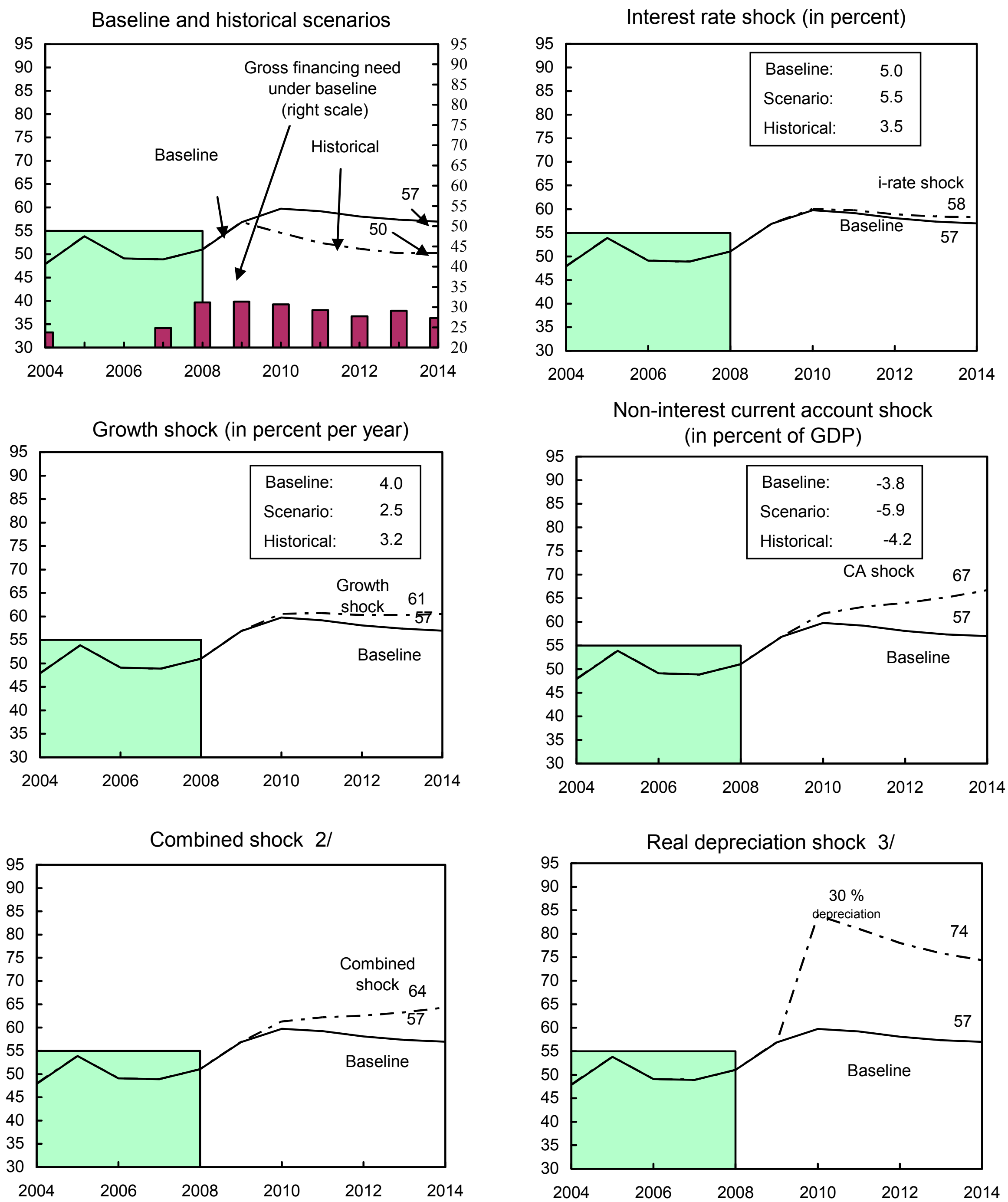
3/ For projection, line includes the impact of price and exchange rate changes.

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

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

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

Figure 5. FYR Macedonia: External Debt Sustainability: Bound Tests 1/
(External debt in percent of GDP)



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

1/ Shaded areas represent actual data. Individual shocks are permanent one-half standard deviation shocks. Figures in the boxes represent average projections for the respective variables in the baseline and scenario being presented. Ten-year historical average for the variable is also shown.
2/ Permanent 1/4 standard deviation shocks applied to real interest rate, growth rate, and current account balance.
3/ One-time real depreciation of 30 percent occurs in 2009.

Table 11. FYR Macedonia: Composition of Central Government Debt

(End of period)

	2008		2009 (projected)	
	(share of GDP)	(share of debt)	(share of GDP)	(share of debt)
External	14.2	65.9	17.1	70.1
Official	11.9	55.2	12.1	49.6
Private	2.3	10.7	5.0	20.5
Domestic	7.3	34.1	7.3	29.9
Structural bonds	5.4	25.0	3.9	16.2
Government securities	2.0	9.1	3.3	13.7
Gross debt	21.5	100.0	24.4	100.0
NBRM deposits	3.1	…	3.1	…
Net debt	18.4	…	21.3	…
Memo Items:				
Foreign currency debt	16.9	78.7	22.2	91.2
Short-term debt	1.9	8.7	3.3	13.4

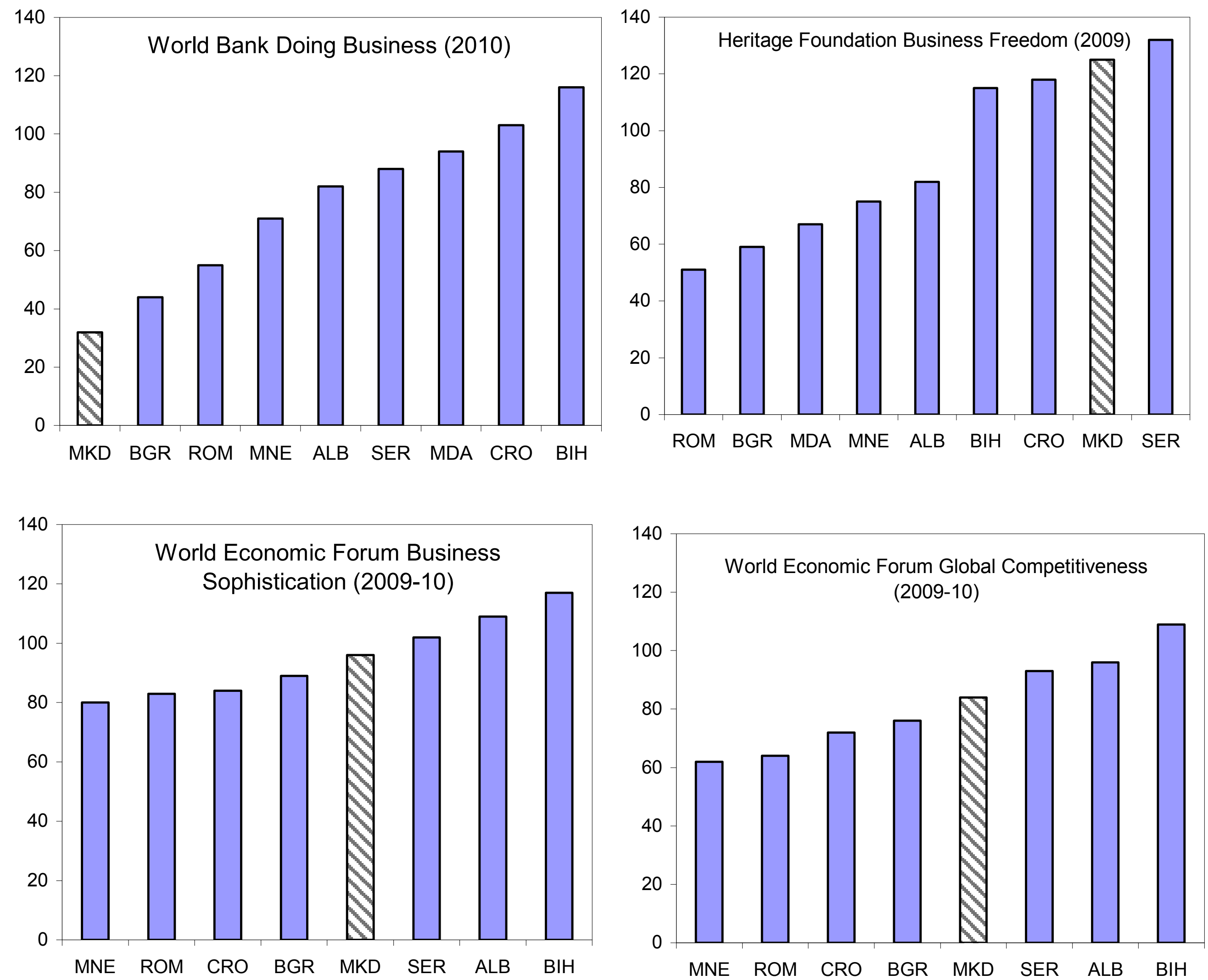
Source: Ministry of finance and IMF staff estimates.

Table 12. FYR Macedonia: External Debt Decomposition

	2008		2009 Q2	
	In millions of Euros	In percent of GDP	In millions of Euros	In percent of GDP
Total external debt	3,318	51.0	3,451	53.2
Total external MLT debt	1,999	30.7	2,106	32.5
Private	1,096	16.9	1,201	18.5
Intecompany loans	325	5.0	388	6.0
Loans	737	11.3	768	11.8
Other	35	0.5	45	0.7
Public	903	14.2	905	14.0
Offical creditors	663	10.2	669	14.0
Private creditors	240	3.7	236	3.6
Total external ST debt	1,319	20.3	1,344	20.7
Private	1,319	20.3	1,344	20.7
Intercompany debt	325	5.0	388	6.0
Trade credits	672	10.3	670	10.3
Other	323	5.0	440	6.8

Source: NBRM and IMF Staff Estimates

Figure 6. Regional Rankings for Competitiveness and Business Environment 2009–10



Source: World Bank, World Economic Forum and Heritage Foundation

INTERNATIONAL MONETARY FUND

FORMER YUGOSLAV REPUBLIC OF MACEDONIA

Staff Report for the 2009 Article IV Consultation

Informational Annexes

Prepared by the European Department
(In consultation with other departments)

November 24, 2009

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Annex I—FYR Macedonia: Statistical Issues

As of November 12, 2009

I. Assessment of Data Adequacy for Surveillance
General: Data provision has some shortcomings, but is broadly adequate for surveillance. Areas that would benefit most from further improvement are national accounts, government finance statistics, and the balance of payments.
National accounts: National accounts statistics are available on an annual basis and quarterly data are available from the first quarter of 2006. Despite recent improvements, GDP statistics continue to have large discrepancies between the official quarterly and annual GDP estimates, the lack of official levels of GDP according to the expenditure side, inconsistencies between the production and the expenditure approaches to GDP, and inconsistencies between GDP subcomponents and the behavior of a variety of indirect economic indicators. Employment data from the company survey continue to be unreliable, and wage data suffer from inconsistencies in definitions as a result of the recent social insurance reform. **Price statistics:** The CPI series are rebased every year and this has caused small discrepancies in historical data.
Government finance statistics: The consolidated central government data are affected by unreliable source data on extra-budgetary funds, hospital arrears, and special revenue accounts, including foreign financed projects. The has resulted in sometimes large discrepancies between the above-the-line and below-the-line items. Data on state enterprises are limited. Macedonia does not report government finance statistics to the Fund for publication in either the *Government Finance Statistics Yearbook* (GFSMY) or the *International Financial Statistics* (*IFS)*.
Monetary sector: EUR receives a monthly electronic report of monetary statistics, covering the balance sheet of the central bank, the commercial banks and other depository corporations. The foreign currency shares of the loans and deposits do not accurately reflect the foreign exchange risk as the bank data do not identify the foreign currency indexed loans or deposits.
External sector: The compilation and coverage of balance of payments statistics have improved in recent years and most of the recommendations from the 2004 ROSC mission and the late 2006 STA mission were implemented. Some areas for improvement remain, including trade credit data which tend not to be consistent with relevant indirect economic indicators. Balance of payments data are compiled on a monthly basis.

II. Data Standards and Quality	
FYR Macedonia participates in the General Data Dissemination System (GDDS).	Data ROSC published on September 29, 2004
III. Reporting to STA (Optional)	
No data are being reported for publication in the *Government Finance Statistics Yearbook* or in the *IFS*.	

FYR MACEDONIA: TABLE OF COMMON INDICATORS REQUIRED FOR SURVEILLANCE

(as of November 12, 2009)

	Date of latest observation	Date received	Frequency of Data[7]	Frequency of Reporting[7]	Frequency of publication[7]	Memo Items: Data Quality – Methodological soundness[8]	Memo Items: Data Quality – Accuracy and reliability[9]
Exchange Rates	Current	11/12/09	D	D	D		
International Reserve Assets and Reserve Liabilities of the Monetary Authorities[1]	11/6/09	11/11/09	D	W	Q		
Reserve/Base Money	Sept. 09	11/3/09	M	M	M	O, LO, LO, O	O, LO, O, O, O
Broad Money	Sept. 09	11/3/09	M	M	M		
Central Bank Balance Sheet	Sept. 09	11/3/09	M	M	M		
Consolidated Balance Sheet of the Banking System	Sept. 09	11/3/09	M	M	M		
Interest Rates[2]	Sept. 09	10/30/09	M	M	M		
Consumer Price Index	Oct. 09	11/03/09	M	M	M	O, O, O, LO	LO, O, LNO, O, LO
Revenue, Expenditure, Balance and Composition of Financing[3] – General Government[4]	Jun. 09	07/09/09	Q	Q	Q	LO, LNO, LO, O	LO, LO, LO, LO, LNO
Revenue, Expenditure, Balance and Composition of Financing[3] – Central Government	Sept. 09	10/06/09	Q	Q	Q		
Stocks of Central Government and Central Government-Guaranteed Debt[5]	Mar. 09	May 09	Q	Q	I		
External Current Account Balance	Aug. 09	11/06/2009	M	M	M	O, LO, O, LO	LO, O, LO, O, LO
Exports and Imports of Goods and Services	Sept. 09	11/11/2009	M	M	M		
GDP/GNP	Jun. 09	09/22/09	Q	Q	Q	O, LO, O, LO	LO, O, LNO, O, O
Gross External Debt	Jun. 09	09/30/2009	Q	Q	Q		
International Investment Position[6]	2007	Dec 2008	A	A	A		

[1] Includes reserve assets pledged or otherwise encumbered as well as net derivative positions.
[2] Both market-based and officially-determined, including discount rates, money market rates, rates on treasury bills, notes and bonds.
[3] Foreign, domestic bank, and domestic nonbank financing.
[4] The general government consists of the central government (budgetary funds, extra budgetary funds, and social security funds) and state and local governments.
[5] Currency and maturity composition is reported only on request.
[6] Includes external gross financial asset and liability positions vis-à-vis nonresidents.
[7] Daily (D), Weekly (W), Monthly (M), Quarterly (Q), Annually (A), Irregular (I); Not Available (NA).
[8] Reflects the assessment provided in the data ROSC or the Substantive Update (published on September 29, 2004, and based on the findings of the mission that took place during February 18 – March 3, 2004) for the dataset corresponding to the variable in each row. The assessment indicates whether international standards concerning concepts and definitions, scope, classification/sectorization, and basis for recording are fully observed (O), largely observed (LO), largely not observed (LNO), or not observed (NO).
[9] Same as footnote 8, except referring to international standards concerning source data, assessment and validation of source data,, statistical techniques, assessment and validation of intermediate data and statistical outputs, and revision studies.

Annex II—FYR Macedonia: Fund Relations
(as of October 31, 2009)

Mission. Skopje, October 15−27, 2009. Concluding statement is available at: http://www.imf.org/external/np/ms/2009/102709.htm

Staff team. Wes McGrew (head), Geoff Gottlieb (EUR), Ferhan Salman (SPR), Gabriela Dobrescu (FAD) and Alexander Tieman (Resident Representative).

Discussions. The staff team met Deputy Prime Minister Peshevski, Deputy Prime Minister and Finance Minister Stavreski, National Bank of the Republic of Macedonia Governor Gošev, other senior officials, and representatives of the banking, business, civil society, political and international communities.

Publication. The Macedonian authorities have not yet decided on publication of this staff report.

I. **Membership Status**: Joined 12/14/92; Article VIII

II. **General Resources Account**:	SDR Million	Percent of Quota
Quota	68.90	100.00
Fund holdings of currency	68.90	100.00
Reserve Position	0.00	0.00

III. **SDR Department**:	SDR Million	Percent of Allocation
Net cumulative allocation	65.62	100.00
Holdings	58.09	88.53

IV. **Outstanding Purchases and Loans:** None

V. **Latest Financial Arrangements**:

Type	Approval Date	Expiration Date	Amount Approved (SDR Million)	Amount Drawn (SDR Million)
Stand-By	08/31/2005	08/30/2008	51.68	10.50
Stand-By	04/30/2003	08/15/2004	20.00	20.00
EFF	11/29/2000	11/22/2001	24.12	1.15

VI. **Projected Payments to the Fund (Expectations Basis)**[1]

(SDR million; based on existing use of resources and present holdings of SDRs):

	Forthcoming				
	2009	2010	2011	2012	2013
Principal					
Charges/Interest	0.01	0.03	0.03	0.03	0.03
Total	0.01	0.03	0.03	0.03	0.03

VII. **Exchange Arrangement**:

The currency of the FYR Macedonia is the denar. FYR Macedonia maintains a managed floating exchange rate system with a de facto stabilized arrangement against the Euro. Households can transact through commercial banks or through foreign exchange bureaus that act as agents of banks; enterprises can transact through the banking system. The reserve requirement on all foreign currency deposits is set at 13 percent.

At end-October 2009, the official exchange rate was 41.38 denars per U.S. dollar and 61.17 denars per Euro. FYR Macedonia has accepted the obligations of Article VIII, Sections 2, 3, and 4 with effect from June 19, 1998.

VIII. **Article IV Consultations**:

The first consultation with FYR Macedonia was concluded in August 1993. The last consultation was concluded on December 1, 2008 (SM/08/329). FYR Macedonia is on the standard 12-month consultation cycle.

IX. **Technical Assistance (since 2005)**:

Purpose	**Department**	**Date**
Tax Administration	FAD	July 2009
National Accounts	STA	June 2009
Contingency Planning and Crisis Preparedness	MCM	February 2009

[1] This schedule presents all currently scheduled payments to the IMF, including repayment expectations and repayment obligations. The IMF Executive Board can extend repayment expectations (within predetermined limits) upon request by the debtor country if its external payments position is not strong enough to meet the expectations without undue hardship or risk.

Government Finance Statistics	STA	October 2008
Balance of Payments Statistics	STA	October 2008
National Accounts Statistics	STA	April 2007, January, May, September, December 2008
Export and Import Deflators	STA	December 2007
GFS 2001	STA	November 2007
Expenditure Rationalization	FAD	July 2007
Central Bank Law	MCM	July 2007
Tax Policy	FAD	June 2007
National Accounts Statistics	STA	April 2007
Liquidity, Cash and Debt Management	MCM	April 2007
Tax Administration	FAD	October 2006
Balance of Payments Statistics	STA	October 2006
Tax Policy	FAD	September 2006
Government Finance Statistics	STA	June 2006
Banking Law	LEG, MCM	June 2006
Banking Reform	MCM	November 2005
Credit Growth	MCM	October 2005
National Accounts	STA	July 2005
BOP Statistics	STA	July 2005
Tax Administration	FAD	May 2005
Reserve Management	MCM	May 2005
Monetary Statistics	STA	

		April 2005

Resident Experts

Banking Supervision	MCM	May 2006-present
Tax Administration	FAD	October 2006-present
Monetary Policies	MCM	October 2004- April 2005

X. FSAP Participation and ROSCs (since 2003)

Purpose	**Department**	**Date**
FSAP update	MCM/WB	March 2008
Fiscal ROSC	FAD	February 2005
Data ROSC	STA	February 2004
FSAP	MCM/WB	May 2003 and June 2003

XI. Resident Representative

The Fund has had a resident representative in Skopje since 1995. Mr. Alexander Tieman has held this position since August 2009.

Annex III—Coordination of IMF and World Bank with Programs on FYR Macedonia

1. **IMF and World Bank country teams for FYR Macedonia agreed that FYR Macedonia faces an environment of significant difficulties including balance of payments pressures, recession, and falling tax revenues.** Against this background Macedonia's main macroeconomic challenges are to achieve balance of payments adjustment without an exchange rate or banking crisis; and to avoid excessively procyclical fiscal or monetary policies while ensuring medium-term fiscal and external sustainability. To meet these challenges will require fiscal and monetary policies that are adequate to maintain the current account deficit at levels that will prevent loss of reserves, and to ensure the fiscal deficit is consistent with near-term financing constraints and medium-term public debt sustainability; and close monitoring of the financial sector.

2. **Based on this shared assessment, the teams identified six areas of structural reform as macrocritical** in light of their importance for fiscal sustainability and financial sector stability.

- **Tax administration.** Continued reforms in this area will help to improve compliance and reduce informality, contributing to a broader and more stable tax base that allows lower tax rates and adequate fiscal financing. Macedonia has already achieved major gains in unifying the collection of social contributions (pension, health, and unemployment) and integrating them with personal income tax collection, resulting in significant improvement in compliance.

- **Pension reform.** Reforms to the system in recent years put the system on a sustainable financial basis, but recently contribution rates were lowered, the pension indexation formula was made more generous, and a discretionary element was added to the rules-based system.

- **Social safety net.** The social safety net is complex, with a large number of overlapping programs that are not well-targeted and fail to reach some of most vulnerable elements in society. Efforts are needed to ensure spending cuts do not weaken the social safety net.

- **Budget planning.** Accurate revenue and expenditure forecasts are needed to ensure realistic budgets and avoid supplementary budgets and under-execution of the budget that result from revenue underperformance or underestimation of spending. Moreover, further expanding the medium-term elements of the fiscal framework would help to anchor fiscal policy around the goal of public debt sustainability.

- **Financial sector**. Stronger financial sector supervision and contingency planning will help to ensure the authorities are able to monitor the health of the system carefully and respond appropriately to problems that emerge. This includes powers of the banking regulator to impose fit and proper requirements on bank owners and to intervene banks that are not viable. A framework for cooperation between the NBRM, the Finance Ministry, and other agencies, along the lines recommended by the February 2009 IMF technical assistance mission, is also important to provide for a quick response to threats.

- **Electricity sector.** It will be important over time to revise the tariff structure to better reflect the costs of service delivery. This will help eliminate hidden and cross-subsidies that are poorly targeted, encourage inefficient patterns of consumption, damage incentives for investment, and impose fiscal or quasi-fiscal costs. New investment in generation capacity is also needed in light of inadequate domestic supplies and the high price of energy imports. In view of financial and environmental considerations, use of PPPs and renewable energy sources should be promoted. Privatization of power generation and reforms to create a more modern and transparent regulatory framework will be helpful in this regard.

3. **The teams agreed on the following division of labor.**

- The Fund, which has a full-time resident advisor in place (funded by the Dutch government) as well as a full program of technical assistance missions, will retain the lead in tax administration reform. Priorities for the coming year include reviewing the progress in modernizing revenue administration and addressing compliance problems that have emerged with the economic slowdown, and coordinating technical assistance with other donors.

- The Bank will support the Government in undertaking an analysis of the recent changes to the pension system and their implications for its financial sustainability and will work with the authorities to make needed adjustments to preserve the system's sustainability and prevent a drain on general tax revenues.

- Social safety net. The Bank will continue to advise the government on measures to consolidate various programs and improve targeting through its Social Protection Implementation Loan (SPIL) and Conditional Cash Transfers (CCT) operations. Future priorities include introduction of a registry of programs and beneficiaries, initiating a conditional cash transfer system to ensure compliance with requirements for mandatory secondary school enrollment, consolidation of benefits, etc. Once implemented, these activities should result in better administration and targeting of social programs.

- Both the Fund and the Bank will encourage the authorities to implement realistic, predictable, and transparent budget procedures. The Fund will also encourage the authorities to anchor fiscal policies in a credible medium-term fiscal framework and are prepared to offer technical assistance for that purpose.

- The Fund and Bank have both been involved in financial sector reform, most recently through the November 2008 FSAA update. The Fund has also provided technical assistance in the area of contingency planning and will provide further assistance in this area as well as in stress testing bank balance sheets. The Bank is also administering a Dutch trust fund providing technical assistance for the implementation of the Supervisory Development Plan, which is supporting the introduction of risk-based bank supervision.

- The Bank has the lead on electricity sector reform. It will continue to encourage the adoption over time of realistic prices of electricity and elimination of subsidized rates for consumers. It is also supporting the preparation of the Energy Sector Strategy and advising the government on promoting use of alternative ways of financing energy sector investments (PPPs) as well as diversifying energy sources (use of gas, renewables, wind etc.). The Bank is also providing technical assistance to strengthen the capacities of the Energy Regulatory Commission, The Bank’s Energy Community of South East Europe Adaptable Programmatic Loan 3 (ECSEE APL3) supports improvements of interconnectivity and the transmission grid. Finally, the GEF project support activities that promote energy efficiency and greater use of renewable sources of energy.

Appendix 1. FYR Macedonia: IMF and World Bank planned activities in macrocritical structural reform areas, June 2009-May 2010

Title	Products	Provisional Timing of Missions	Expected Delivery Date
1. Fund work program	Mission on use of Fund Resources or Article IV consultation	October 2009	December 2009
	Technical assistance to NBRM on stress testing and contingency planning	2009-10, dates TBD	TA report by spring 2010
	Technical assistance to Ministry of Finance on tax compliance and on debt sustainability	Ongoing	TA report by end-2009
	Technical assistance to statistical agency on national income accounts statistics	2009-10, dates TBD	TBD
2. Bank work program	Supervision of CCT and SPIL projects	August 2009	
	Supervision of energy sector activities	July 2009	
	Preparation of potential DPL (to include fiscal framework and social transfers)	August 2009	November 2009
	Technical assistance to NBRM on SDP implementation	Ongoing	December 2009
3. Joint work program	Review of budget projections	Ongoing	

Statement by the IMF Staff Representative on Former Yugoslav Republic of Macedonia Executive Board Meeting December 11, 2009

1. This statement provides information that has become available since the staff report for the 2009 Article IV Consultation was issued. The thrust of the staff appraisal remains unchanged.

2. On November 30 the National Bank of the Republic of Macedonia (NBRM) announced a reduction in its reference rate from 9 to 8½ percent. In explaining this decision, Governor Goshev cited favorable developments in international reserves and faster than expected external adjustment. Reserves were €1.6 billion on December 2, up from €1.55 billion at end-October, while the NBRM now expects the 2009 current account deficit to be 8 percent of GDP, compared to its projection in October of 9.1 percent of GDP.

3. The staff report advised that further evidence of external stabilization would be desirable before easing. Based on the most recent data, reserves are likely to be higher at end-2009 than the €1.4 billion projected in the staff report, which suggests more favorable balance of payments developments over the past two months than projected by staff. In staff's view, the 50 basis point cut by the NBRM is justified based on the improved outlook. However, in light of continued uncertainties, staff would recommend that further easing should be cautious and conditioned on the continuation of favorable trends in reserves and the balance of payments.

4. The NBRM also announced on November 30 that the mandatory reserve requirement imposed when a bank’s consumer loan portfolio grows by more than a prescribed rate would be allowed to expire on January 1, 2010. This requirement, which the 2008 Article IV staff report had recommended eliminating, had limited impact in light of the slow credit growth over the past year.

INTERNATIONAL MONETARY FUND
Public Information Notice
EXTERNAL
RELATIONS
DEPARTMENT

Public Information Notice (PIN) No. 09/140
FOR IMMEDIATE RELEASE
December 28, 2009

International Monetary Fund
700 19th Street, NW
Washington, D. C. 20431 USA

IMF Executive Board Concludes 2009 Article IV Consultation with FYR Macedonia

On December 11, 2009, the Executive Board of the International Monetary Fund (IMF) concluded the Article IV consultation with the Former Yugoslav Republic of Macedonia (FYR).[1]

Background

FYR Macedonia's main vulnerability at the outset of the global crisis was its large current account deficit in the context of the exchange rate peg to the euro. At the same time, it benefited from a small fiscal deficit, modest public debt, significant international reserve buffers, and a small banking system with limited reliance on external financing. These factors provided room for maneuver and limited the country's exposure to global financial conditions.

The crisis hit Macedonia at the end of 2008 through a collapse in export demand and decline in external financing. These factors led to a sharp slowdown in the economy, reduced tax revenues, and a significant loss of central bank foreign exchange reserves.

The National Bank of Macedonia (NBRM) responded to reserve outflows by tightening bank liquidity and reserve requirements and raising its policy rate from 7 to 9 percent. These actions helped to slow credit growth and contain the loss of reserves. The government curtailed planned spending increases to preserve its 2.8

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[1] Under Article IV of the IMF's Articles of Agreement, the IMF holds bilateral discussions with members, usually every year. A staff team visits the country, collects economic and financial information, and discusses with officials the country's economic developments and policies. On return to headquarters, the staff prepares a report, which forms the basis for discussion by the Executive Board. At the conclusion of the discussion, the Managing Director, as Chairman of the Board, summarizes the views of Executive Directors, and this summary is transmitted to the country's authorities.

percent fiscal deficit target in the face of declining tax revenues. It also issued an €175 million Eurobond (at 9⅞ percent) in July, which bolstered reserves and ensured sufficient budget financing.

By the second half of 2009 the situation had stabilized, confidence had improved, and reserve losses from earlier in the year had been recouped. In the banking sector, nonperforming loans rose, but capital adequacy ratios remained high and no significant liquidity pressures emerged. For the year as a whole, GDP is expected to decline 1.3 percent, less than most countries in the region, before returning to 2 percent growth in 2010.

Executive Board Assessment

Executive Directors praised the Macedonian authorities for the conduct of macroeconomic policies, which contributed to a modest downturn in Macedonia's economy relative to other countries in the region. They welcomed the prospect of a return to growth in 2010. Nevertheless, the large—albeit reduced—current account deficit in the context of an exchange rate peg is a source of vulnerability and limits the room for policy maneuver. In the near term, supporting growth while reducing external imbalances will remain a key challenge.

Directors agreed that the exchange rate peg, supported by prudent fiscal and monetary policies, has served Macedonia well. They took note of the staff assessment that there is no significant exchange rate misalignment. They encouraged the authorities to press ahead with structural reforms to boost competitiveness and foster foreign direct investment, particularly administrative and judicial reforms.

Directors observed that the tightening of monetary policy in the first half of 2009 had helped to rebuild international reserves and provided critical support to the exchange rate peg. They supported the recent cut in the policy rate, given more conducive conditions. Going forward, Directors called for cautious monetary easing that should await clear signs of lasting favorable trends in the balance of payments and international reserves.

Directors supported the fiscal stance in 2009 and 2010, which aims to accommodate automatic stabilizers and protect spending from the cyclical shortfall in revenues. Noting that revenue assumptions for 2010 may prove somewhat optimistic, they welcomed the authorities' readiness to take all the necessary measures to meet the deficit target for 2010. They were also reassured by the authorities' commitment to fiscal consolidation over the medium term, and recommended that fiscal targets be guided by debt sustainability considerations.

Directors were encouraged by the broadly healthy condition of the banking system and its low reliance on external funding. They welcomed the authorities' intentions to move forward on the recommendations in the Financial Sector Assessment Program (FSAP) Update, including strengthening crisis response mechanisms, and legal changes enabling the authorities to intervene in troubled banks without being subject to court challenge. They looked forward to early operation of the recently created supervisory body for the insurance sector.

Public Information Notices (PINs) form part of the IMF's efforts to promote transparency of the IMF's views and analysis of economic developments and policies. With the consent of the country (or countries) concerned, PINs are issued after Executive Board discussions of Article IV consultations with member countries, of its surveillance of developments at the regional level, of post-program monitoring, and of ex post assessments of member countries with longer-term program engagements. PINs are also issued after Executive Board discussions of general policy matters, unless otherwise decided by the Executive Board in a particular case.

FYR Macedonia: Selected Social and Economic Indicators

I. Social and Demographic Indicators

GDP (billions of denar, 2008)	398.6	Poverty rate	
US dollars (billions)	9.6	Less than $2 per day, PPP 2003	<1%
Per capita (U.S. dollars)	4,653		
Population characteristics		Income distribution (2003)	
Total (millions, 2008)	2.0	Income share of highest 10%	29.60
Urban population (percent of total, 2007)	66.9	Income share of lowest 20%	6.10
Life expectancy at birth (years, 2006)	74.1	Gini coefficient	0.39

II. Economic Indicators

	2006	2007	2008	2009	2010
	(Annual percentage change, unless otherwise specified)				
National accounts and employment					
Real GDP	4.0	5.9	4.8	-1.3	2.0
Total Domestic demand	5.9	9.0	9.3	-2.6	1.2
Consumption	5.2	8.0	7.4	-1.1	1.0
Private	6.0	9.8	6.9	0.5	0.8
Public	1.8	0.4	9.7	-8.4	2.2
Investment	9.6	13.3	18.3	-10.7	2.4
Private	13.1	10.1	9.8	-9.0	1.6
Public	-1.6	33.4	39.8	-17.0	5.9
Net exports 1/	-2.8	-4.4	-5.8	1.9	0.6
Consumer prices					
End of period	3.0	6.7	4.0	-1.7	2.0
Average	3.2	2.3	8.3	-0.8	0.8
Unemployment rate (annual average)	36.0	34.7	33.5 …		…
	(In percent of GDP)				
External debt and balance of payments					
Current account	-0.9	-7.2	-13.1	-9.5	-8.2
Trade balance	-20.1	-20.3	-26.7	-23.1	-22.5
Exports of goods	37.4	42.2	41.3	30.6	33.9
Imports of goods	57.5	62.4	68.0	53.7	56.4
Gross external debt	49.1	48.9	51.0	59.0	58.0
Public	25	18	17	22	22
Private	24	31	34	37	36
Savings and investment					
Gross domestic investment	21.9	24.2	27.7	24.9	24.9
Public	3.1	3.9	5.0	4.0	4.2
Private	15.1	16.3	18.7	16.4	16.4
National savings	21.0	17.1	14.6	15.4	16.8
Public	2.6	4.5	4.1	1.2	1.7
Private	18.5	12.5	10.6	14.2	15.1
Public sector finance	2006	2007	2008	2009	2010
Public sector gross debt	35.4	26.1	24.5	27.3	29.1
Central government gross debt	31.5	23.4	21.3	24.5	26.2
Central government balance	-0.5	0.6	-1.0	-2.8	-2.5
	(Annual percentage change)				
Terms of trade	1.5	6.5	-0.9	-1.0	3.7

Sources: Ministry of Finance, National Bank of Republic of Macedonia, World Development Indicators 2008, and IMF staff estimates.

1/ Contribution to growth.

Statement by Age Bakker, Executive Director for Former Yugoslav Republic of Macedonia, and Mihai Tanasescu, Advisor to the Executive Director
December 11, 2009

On behalf of the authorities we thank staff for their report and contribution to the policy dialogue and their analysis and recommendations. They appreciate the Fund's advice and the presentation of the topics covered in the Selected Issues report. The authorities value their cooperation with the Fund, and are of the view that the consultation process has worked well and has focused on topics of importance to the Macedonian economy. There is broad agreement between the authorities and staff on fiscal and monetary policies. Some nuances in views remain with regard to fiscal policy in the medium term, but the authorities are of the opinion that the consultations provided a good opportunity to focus on the economic aspects aimed at strengthening macroeconomic stability and intensifying efforts for recovery.

Economic performance and outlook

The current economic crisis hit Macedonia at the end of 2008, but the activity in the domestic economy proved to be relatively resistant to the global shock. For 2009 the authorities expect a moderate contraction of 0.6 percent of GDP, after 1.2 percent of GDP decline in the first half of the year, and a more stable situation in the second half of 2009. This contraction is significantly lower than the economic decline in most of the other economies in the region. The main factors behind the slowdown in the economy were a collapse in export demand and industrial production, and loss of external financing. The latter eased in the second part of 2009 and international reserves have recouped 80 percent of their earlier losses.
For 2010 a moderate recovery to 2 percent growth is expected, which would be triggered primarily by exports and revitalization of investment demand. At the same time, the authorities expect a moderate increase in private consumption, and a slight increase in imports, conditioned by exports recovery and new investments. Risks related to growth projections still exist, however, especially in case of failure of export demand to recover as expected, or renewed weakness of metal prices. On the upside, progress towards EU accession will improve prospects for attracting foreign investment.

Inflation started falling in late 2008 due to decline in import prices, including food and energy, and reduced pressures of domestic demand due to a sharp decline in industrial production. By October 2009 headline inflation was -2.4 percent and core inflation was near zero; by the end of the year inflation is expected to be around -1 percent (y-o-y). In 2010 prices are expected to rise by 1.2 percent due to supply-side factors. However, the administrated prices could be a risk factor, and contribute to an increasing inflation rate at the end of 2010.

The current account deficit initially widened in the first quarter, due to a massive decline in exports, and delayed downward adjustment on imports, but started to adjust in the second quarter, when imports began to contract sharply at the same time as the decline in exports leveled off. Private transfers started to grow on an annual basis, and both the trade and current account deficits began to decrease. The current account deficit is expected to narrow in 2009 at around 9 percent of GDP from 13 percent of GDP in 2008, and continue to do so over the medium term. For 2010 the current account deficit is projected to decrease to 8 percent of GDP and to 5 percent by 2014. The large current account deficit, in the context of the exchange rate peg, makes Macedonia dependent on continued external financing, and the authorities are committed to strengthening both fiscal and monetary policies, if needed, to keep the exchange rate peg, which has served the country well.

Fiscal policy

In recent years the authorities have successfully pursued fiscal consolidation, and this provided room in the current economic crisis to implement some fiscal stimulus in 2009 and to move ahead with improving the infrastructure and to create a positive impact on the output of the private sector in the long run. The fiscal deficit in 2009 would reach 2.8 percent of GDP and both the authorities and staff agreed that this target is appropriate given the modest levels of public debt, and secured financing through an Eurobond issue. The authorities are committed to improving the fiscal stance, and they approved the 2010 budget with a smaller fiscal deficit than in 2009. Staff consider the 2010 budget to be appropriate, although they view its revenue assumptions as somewhat optimistic, due to factors including the cut in social contribution rates and changes in the corporate income tax. Against this background, the authorities are fully committed to keeping the budget deficit under control and will take all necessary measures in order to meet the 2.5 percent of GDP 2010 deficit target, and agreed with staff's recommendations for adjusting the fiscal policy, if needed.

Consistent with their commitment to fiscal consolidation, the authorities agreed with the need to reduce the fiscal deficit over the medium term to 2 percent of GDP, in light of the need to increase investment spending and improve infrastructure. Staff recommended that the fiscal deficit should be limited to a somewhat lower level of 1.5 percent of GDP to keep a prudent public debt ratio which would be around 25 percent of GDP. The authorities acknowledge staff's concerns regarding the fiscal deficit target over the medium term, but are committed to continuing fiscal consolidation which would help contain the current account deficit and protect reserves and the peg.

Monetary policy and financial sector

The National Bank of the Republic of Macedonia (NBRM) continues to play an important role in ensuring the stability of the exchange rate peg. In 2009 the NBRM responded well to reserve outflows by increasing its policy rate by 2 percent from 7 to 9 percent. These measures significantly decelerated both monetary and credit growth and helped to tighten international reserves and keep them at 3 months of imports. After a sharp decline in the first part of the year, reserves recouped much of their losses and had reached the level of 1.6 billion euros at the beginning of December. In response to the recent more favorable external sector developments and more stable prospects for 2010, the NBRM reduced its policy rate by 0.5 percent to 8.5 percent, which signals a more stable environment and a return to growth.

At the same time, with credit growth being subdued and expectations moderate, the NBRM decided not to extend the decision on compulsory deposits that expires at the end of 2009. Moreover, the NBRM is committed to tightening its monetary policy, if needed, in order to protect reserve buffers and to keep a stable exchange rate peg which would continue to be the main nominal anchor for stabilizing market expectations and prices.

The banking sector seems to have weathered the crisis in an overall healthy shape, and the banks are well capitalized and still profitable. At the end of September the capital adequacy ratio was 16.5 percent, higher than the legally prescribed minimum of 8 percent. At the same time, the NBRM agreed to implementing the FSAP recommendations, including undertaking legal changes to allow it to intervene in troubled banks without being subject to court challenge and to remove bank management who do not meet appropriate standards of integrity. At the same time, the quality of banking supervision has improved and contributed to the stability of the banking sector.

Structural reforms

Macedonia has made significant progress on structural reforms, attracting greenfield foreign direct investment, privatizing and restructuring the railway system, liberalizing the telecommunications, and improving the business climate. The recent measures approved by the government to reduce the social contributions rate over the medium term will stimulate employment and encourage lower paid workers to enter the formal economy. The authorities are committed to accelerating the electricity sector reform, by gradually eliminating the existing distortions and improving the companies' capacity to cover their costs, and to focus on the administrative reform, aimed at streamlining and improving efficiency.

Finally, we would like to express the authorities' commitment to continuing to work with the Fund, in pursuing reforms and maintaining a strong policy framework that will help the country to strengthen macroeconomic stability.