

MACEDONIAN ECONOMIC OUTLOOK¹



Quarterly

(Reference period: January – March 2012)

Center for Economic Analyses (CEA)

Skopje, 2012

1 Supported by: Open Society Institute Think Tank Fund Budapest

General information about CEA

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1. Recent economic developments and current political environment

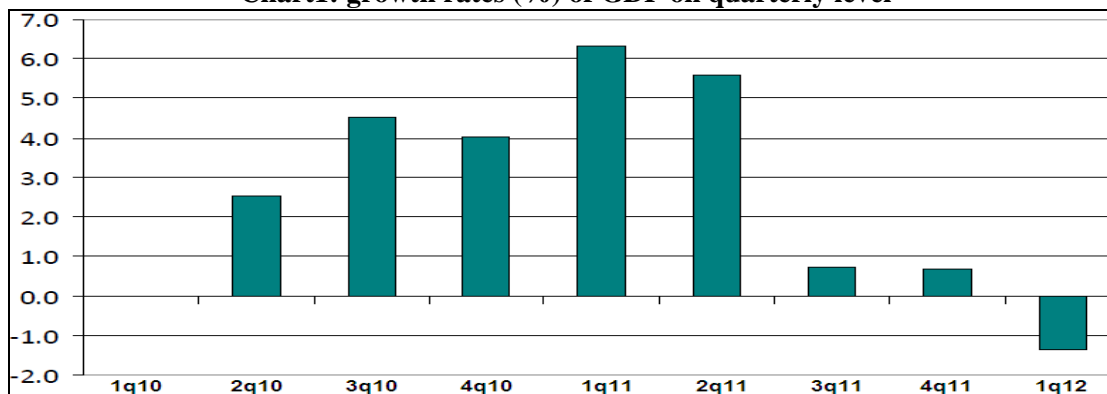
As a result of the expected trends in the EU (the most important trade partner of Macedonia) economic growth in the period 2011-2013 is expected to be on average up to 4.5%². In 2011 realized economic growth was under this projection reaching the level of 3%. It is expected that recovery of domestic economic activity will be with lower intensity, whereas it is estimated that economic growth will be maintained below it's potential trend by the end of 2013. The beginning of 2012 was marked with record multiple increase of the price of fuel.

From March 2012 Macedonia officially launched High dialogue with the European Union. In the report from 2011 the European Commission noted good progress in the reforms of the chapter "Statistics", however, failed Census of Population led to negative reviews in 2012. Despite the remarks for the failed Census of Population, the following additional remarks were given to Macedonia: *protection of intellectual property, de-politicization and functioning of a market economy (primarily the Agency for Electronic Communications (AEC) and the Broadcasting Council (BC) must become independent), competitiveness and good business climate for small and medium-sized enterprises.*

2. GDP developments

In the first quarter of 2012 the downward trend of GDP growth rate which begun in the second quarter of 2011 maintain its trend. The available data for economic activity indicate reduced production activity and external exchange. Hence, according to the State Statistical Office of Macedonia, the growth rate of GDP in this period of time was -1.4%.

Chart1: growth rates (%) of GDP on quarterly level



Source: State Statistical Office of Macedonia

² Pre-Accession Economic Programme 2011-2013

This slowdown in GDP growth rate was mainly driven by the reduced economic activity in **Construction sector** by 9.8% in comparison with 21.2% in the first quarter of 2011, reduced activity in sector of **Mining and quarrying, Manufacturing and Electricity, gas and water** by 9.6%³ and the sector of **Transport, storage and communications** which decreased by 0.1%. Also, in this period of time, there is a very significant slowdown in the **Retail sector** from 11.7% in the last quarter of 2011 to 0.7%. Economic growth is registered only in the sectors of **financial intermediations and real estate business** by 3%, in **agriculture sector** by 1% and **public administration, education and health** by 2.3%.⁴

In January 2012 the trend of annual growth of both components of the exchange was interrupted. For the first time in two years, there is a deeper decline in the **imports** of goods by 24.5% on an annual basis, compared with a decline in the **exports** by 13.9%. On a quarterly basis, in the first quarter of 2012, exports of goods and services decline by 3.7% in nominal terms, while the imports of goods and services nominally decline by 4.6%.⁵ The reduction in the export is mainly driven by the lower export of iron and steel, chemical materials and products, clothing and tobacco, while growth is noticed in the export of machinery (automotive parts). Main factors that contributed to the reduction of the import of goods and services are slower import of chemical products, ferrous metals and metal ores. Increase is registered in the imports of electricity, oil, textile and textile products, nonferrous, road vehicles, gas and others⁶.

Final consumption of households, including the non-profit institutions, in the first quarter of 2012 compared to the same period in 2011 nominally increased by 2%, and its share in the structure of GDP amounted to 78.6%. Available data for the first quarter of 2012 shows weaker investment activity. Thus, in this period of time, the gross investments decreased to 19.1% in comparison with 65.6% in the first quarter last year. This is mainly driven by the lower industrial production, reduced construction activities and lower foreign direct investments in the period from January to February.⁷

³ State Statistical Office of the Republic of Macedonia

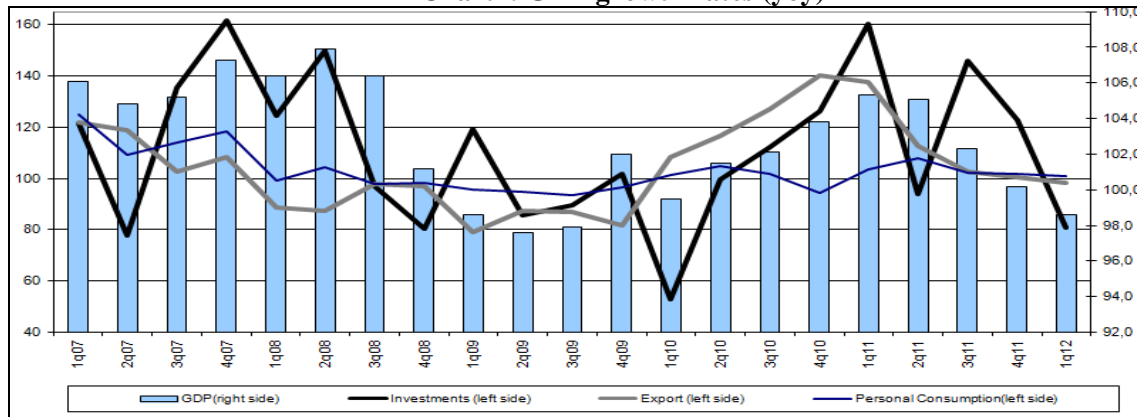
⁴ State Statistical Office of the Republic of Macedonia

⁵ National Bank of the Republic of Macedonia

⁶ Ministry of Finance of the Republic of Macedonia

⁷ Ministry of Finance of the Republic of Macedonia

Chart2: GDP growth rates (yoy)



Source: State Statistical Office of Macedonia

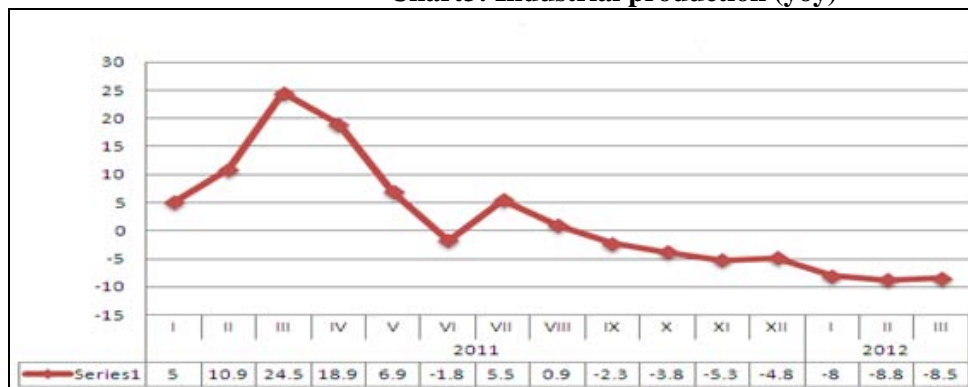
3. Real sector

A further slowdown in the industrial production...

In January 2012, the industrial output registered monthly fall mainly driven by the seasonal factors. On annual basis, industrial output noticed 8% fall. The reduced production of electricity had the largest negative contribution, due to the lower hydro energy potential and the lower production of oil derivatives, which registered a decrease for four consecutive months.⁸ The industrial production volume index in the Republic of Macedonia in March 2012 compared to March 2011 (124.5) was 91.5. The industrial production dropped by 8.5% in March 2012 in comparison with March 2011.⁹ Such a drop was a result of the high basis and also a result of the reduced production activity in the following sectors:

- Manufacturing industry declined by 6.0%.
- Mining and quarrying decreased by 4.7%.
- Electricity, gas, steam and air conditioning supply dropped by 23.8%.¹⁰

Chart3: Industrial production (yoy)



⁸ National Bank of the Republic of Macedonia

⁹ Ministry of finance of the Republic of Macedonia

¹⁰ State Statistical Office of the Republic of Macedonia

Source: State Statistical Office of the Republic of Macedonia

Construction sector

According to the issued building permits, in March 2012, the total value of the constructions was estimated 3,570,055 thousands Denars, which was 74.2% more than the same month of the previous year.¹¹ The total number of issued building permits in comparison with March 2011, increased by 20.7%.¹²

Tourism

In the period January-March 2012, the number of tourists, compared to the same period of the last year, increased by 2.5%, the number of domestic tourists decreased by 1.5%, while that of foreign tourists increased by 5.7%. The number of spent nights in the first quarter in 2012 compared to the same period from the last year, increased by 0.2%.

The number of tourists in March 2012 was 32,092, and the number of spent nights by tourists was 66,486. Compared to March 2011, the number of tourist in March 2012 increased by 0.4%, while the number of spent night dropped by 3.2%. Specifically, the number of domestic tourists in March 2012 compared to the same period in 2011 increased by 2.5%, while the number of foreign tourists decreased by 1%. The nights spent by domestic tourists in the same period increased by 2.4%, whereas the number of nights spent by foreign tourists decreased by 7.4%.

4. External sector

Continuing the trend of steady decline in exports...

In the first three months of 2012, total foreign trade dropped by 4.7% compared to the same period of the last year. In the first quarter of 2012, physical output of export dropped by 12.2% compared with the same period of 2011. Decreasing value of exported goods by 1.8% was mainly a result of the less exported iron and steel, chemical materials and products, clothing. Observed by economic purpose, the following products were most exported: goods for industrial production (51.7%), followed by personal consumption goods (32.2%), investment goods (9.3%) and energy (6.9%).

Imported quantities of goods in the first quarter of 2012 decline by 8.9%, compared to the same period in the previous year, while their value amounted to EUR 1,133.6 million, which is a reduction of 6.4%. It is important to mention that import of electricity increased by EUR 29 million, compared to the same period in 2011, being a result of the increased consumption for heating end use due to the lower seasonal temperatures.

¹¹ State Statistical Office of the Republic of Macedonia

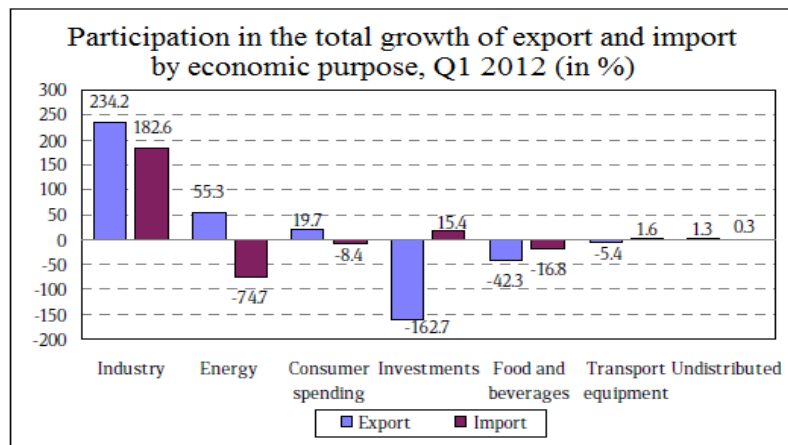
¹² Ministry of finance of the Republic of Macedonia

Chart4: Foreign trade comparison Q1 2012 and Q1 2011



Source: State Statistical Office of the Republic of Macedonia

Chart5: Export and import in Q1 2012



Source: SOS and calculation of Ministry of finance

From surplus in Q4 2011 to deficit on current account in Q1 2012...

In the first quarter of 2012, due to the higher absolute drop of import than export, trade deficit narrowed by EUR 65 million or 13.0% compared to the same period last year. The increased current account deficit is mostly due to the deterioration of the energy trade balance which contributed a deeper negative balance of foreign trade experience exchange. Analyzed according to economic groups of countries - 48.6% of the trade deficit of the country was realized during the trade with Russia and Greece, followed by: Great Britain, Serbia, China, Turkey, Switzerland, Bulgaria, Ukraine and others. Surplus were realized during the trade with Germany, Kosovo, Bosnia and Herzegovina and the Netherlands.

Public debt at the end of the first quarter of 2012 amounted to 4,918 billion Euros. Indeed, increasing the gross external debt was due to the rapid pace of growth of the public debt i.e. debt of the state. In terms of its level in March last year when it was 1,662 billion Euros for one year the public debt increased by enormous 465 million Euros.

5. Labor market

According to the State Statistical Office of the Republic of Macedonia, in the first quarter of 2012 the number of employed persons was 643,668 while 297,351 were unemployed. Employment rate in this quarter compared with the first quarter of 2011 (39.3%) decreased by 0.7 p.p. and it is 38.6%. Also the activity rate dropped to 56.4% in comparison with 57.1% in the first quarter of 2011. Within the unemployment rate, there is a small increase to 31.6% in comparison with the first quarter of 2011 (31.2%).

Chart 6: Number of employees and unemployed in R. Macedonia



Source: State Statistical Office of the Republic of Macedonia

The number of workers in the industry in March 2012 compared to March 2011 decreased by 0.7%. The sector analysis shows that there is an increase of the number of workers in the sector of mining and quarrying by 1.2%, in the sector for electricity, gas and steam by 0.6%, while processing industry registered reduction of the number of workers by 1.0% on annual basis.¹³

On cumulative basis, in the first three months of 2012, the average gross salary increased by 0.8% in nominal terms, while it was lower by 1.6% in real terms, in comparison with

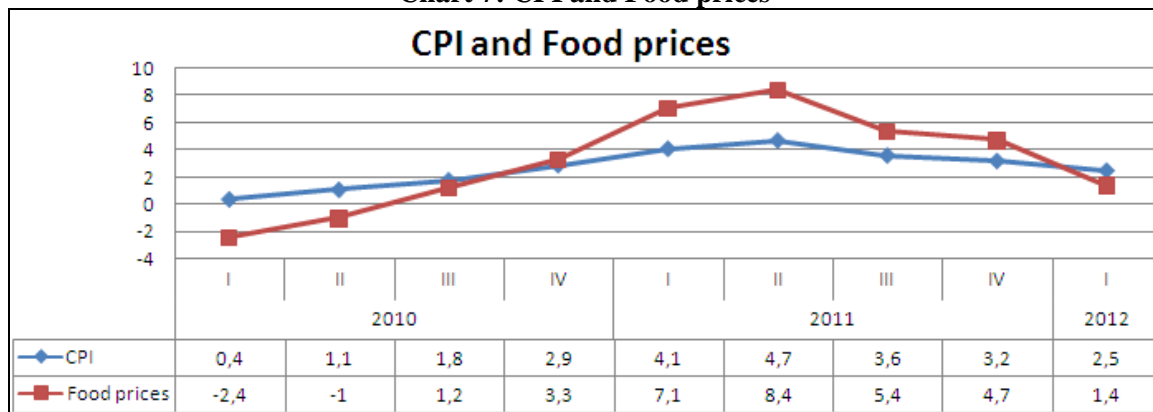
¹³ Ministry of Finance of the Republic of Macedonia

the same period last year. Average net salary in the same months, was higher by 1% in nominal terms, but in real terms was lower by 1.4%.¹⁴

6. Monetary developments

Inflation rate in the first quarter of 2012 compared with the last quarter in 2011, declined by 3.2%; and 2.5% (yoy). This slowdown in the inflation rate is mainly driven by the reduced contribution of food prices from 4.7% in the last quarter of 2011 to 1.4% in the first quarter of 2012¹⁵. In this period of time, the domestic prices increased by 1.9% on a quarterly basis. Thus, the trend of quarterly growth in inflation that began in the previous quarter continues. This dynamic of inflation is a result to the increased world oil prices by 7.7% on a quarterly basis, and increased prices of electricity and thermal energy by 4.9%.¹⁶

Chart 7: CPI and Food prices



Source: National Bank of the Republic of Macedonia

Narrow money (M1) in the first three months of 2012 registered a decline in comparison with the previous quarter, when they grow by 6.6% on a quarterly basis. Thus, in March 2012 M1 declined by 3.6%, as a result of the decline of the currency in circulation and total liquidity of the banks.¹⁷ Broadest money supply (M4) continue to grow in the first quarter in 2012. Hence, the broad money (M4) in March has increased by 9.8%, but in comparison with January 2012 (10%) there is a decline of 0.2 p.p.

Increase of total deposit potential of the banks continue to intensify in the beginning of the year as well. Hence, the total deposits in February registered an annual growth of 9.2% and in March increased to 9.5%. The savings in March 2012 mainly arises from the

¹⁴ Ministry of Finance of the Republic of Macedonia

¹⁵ National Bank of the Republic of Macedonia

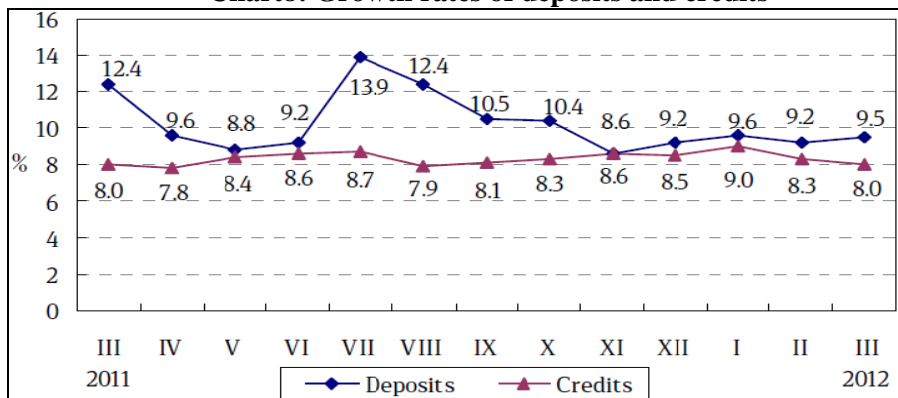
¹⁶ National Bank of the Republic of Macedonia

¹⁷ National Bank of the Republic of Macedonia

increased savings of households by 12%, while deposits of private enterprises were higher by 6.2%.

In the first three months of 2012 a slower credit activity of the Banks was registered - credit growth from 9% in January decline to 8.3% in February to 8.3%. In March there was a decline by 8% with slower lending growth of enterprises and households by 8.3% and 7.4% respectively, compared with 9.1% and 6.6% in March 2011 respectively.¹⁸

Chart8: Growth rates of deposits and credits



Source: Ministry of Finance of the Republic of Macedonia

At the end of 2011 foreign exchange reserves reached historically highest level and they have continued to grow during the first quarter of 2012. In the first three months of the year, foreign exchange reserves are almost unchanged compared to the end of 2011 and they amounted to 2,067 million Euros. By comparison, in 2010 they were 1,715 million Euros¹⁹. In this period of time, with lower inflation pressures and favorable macroeconomics situation National Bank retained basic interest rate to 4%.

7. Fiscal sector

Budget revenues

In the first quarter of 2012 the total budget revenues amounted to 31,800 million Denars, and they have increased by 1.2% in comparison with the same months in 2011. The tax revenues in the first three months amounted to 18,217 million, being higher by 1.2% compared to the first quarter in the previous year. The value added tax amounted to 9,798 million Denars, whereby the share of VAT in the total tax revenues in March 2012 was dominant, amounting to 53.8%.²⁰

Observed by certain categories of taxes, the personal income tax revenues were realized in the amount of 2,298 million Denars, increasing by 2.5% on annual basis. Compared to the same months in 2011, the revenues from the profit tax surged by 4.8% as result of the tax collected for advance payments on monthly basis and on the basis of paid dividend

¹⁸ Ministry of Finance of the Republic of Macedonia

¹⁹ National Bank of the Republic of Macedonia

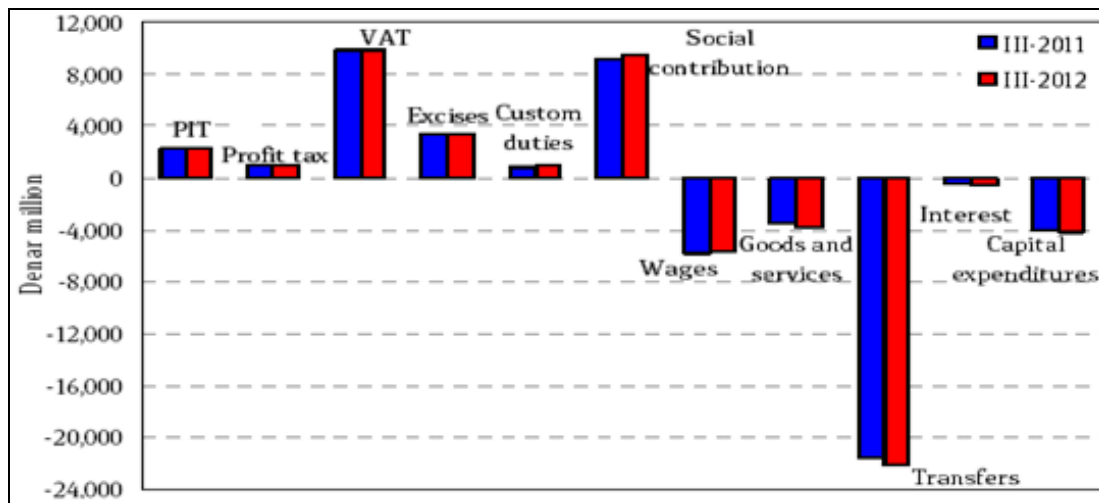
²⁰ Ministry of finance of the Republic of Macedonia

and other profit distribution. The VAT revenues dropped by 0.4%, while the excises declined by 0.7%.²¹ The non- tax revenues dropped by 7% and the capital revenues have increased by 40.2% compared with the same period in 2011. The collection of social contributions amounted to 9,445 million, being higher by 3.4%, whereby the collection of pension insurance increased by 3% compared with the same period.

Budget expenditures

In the period January – March 2012, the total budget expenditures amounted to 36,328 million Denars, which was higher by 3.4% compared to the same period in 2011. In March 2012 the Transfers increased by 3% compared to March 2011 and they participated with 61% in the total expenditures. The social transfers amounted to 17,013 million Denars and have increased by 6.6% with participation of 46.8% in the total expenditures. Such increase was mainly due to the payments of due interest on the basis of foreign borrowing.²² In the first quarter in 2012, the budget deficit reached the amount of 4,528 million, while the central budget deficit amounted to 3,475 million Denars.

Chart 9: Separate categories of revenues and expenditures



Source: Ministry of finance of the Republic of Macedonia

8. Uncertainties and risk to projection

Downward revision of capital inflows in 2012, with lower debt and lower foreign investment...²³

Recent macroeconomic projections indicate a relatively unstable environment. It is expected that the unfavorable external environment will lead to slower growth in export demand, but also will cause a slower recovery of domestic demand and lower pressure on

²¹ Ministry of finance of the Republic of Macedonia

²² Ministry of finance of the Republic of Macedonia

²³ Pre-accession Economic Programme 2012-2014, Ministry of finance of the Republic of Macedonia

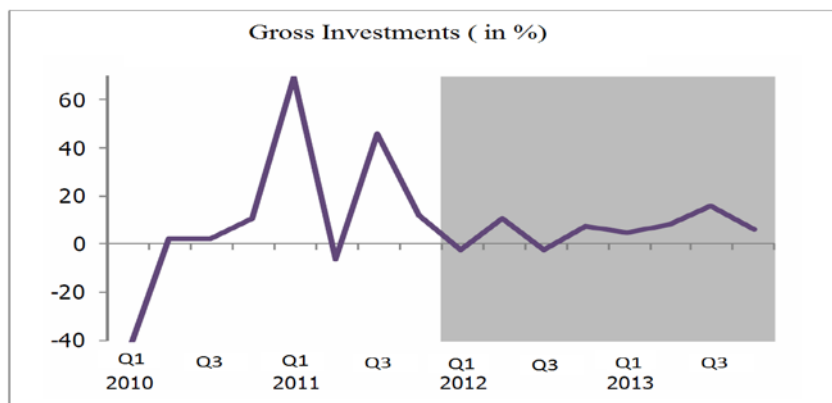
imports. Current macroeconomic scenario until the end of 2012 does not signal the appearance of greater imbalance in the domestic foreign exchange market and pressures on the exchange rate. Net capital inflows are expected to be lower mainly due to servicing the government debt. The risk around this scenario mainly arising from the dynamic of foreign demand which is evaluated in a downward direction. There is additional risk about the oil prices, with possibility that they will be higher.

Although macroeconomic and fiscal projections on paper shows very good results, in practice there is no positive impact on solving the main problem-the high rate of unemployment in the country that contributes to significant rate of poverty.

Efforts to increase investment in the country...

Expectations in 2012 are related to the maintenance of a small current account deficit. The assumptions of lower expected growth of the foreign effective demand indicate slowing growth in investment activity and reduced exports. Reduced investment in the country forced the government representatives to begin visits of foreign countries in order to attract new investment. Governmental visit were conducted in Qatar and visits were announced in India and Turkey.

Chart 10 Gross investments



Source: National Bank of the Republic of Macedonia

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About CEA

CEA is established in 2003 as an independent research think tank - first think tank of this kind on the Macedonian market and served as role model for others as well. Thus, CEA attracted attention, started different type of public debate.

CEA was established by young Macedonian economists who have received their professional education and training through studying at western universities, attending seminars and courses organized by international financial institutions and international organizations, and/or working in an international environment. They share common vision of the Republic of Macedonia as a new emerging economy integrated with regional and world markets. They devote their time, efforts and knowledge to help make this vision become a reality.

CEA is organized on a non-profit base (the legal form is a citizens' associations) and is open for membership to all economists operating in Macedonia and sharing the same vision. The core members and founders of CEA are successful young professionals working in banks, audit firms, international consulting companies, universities and government. Their expertise ranges from econometrics, macroeconomics, microeconomic modeling and economic policy analyses to financial analyses strategies for local economic and rural development, Public-Private Partnerships and business planning. CEA members are also widely present in Government working groups as experts for preparation of legal framework.

Mission statement of CEA

The Mission of CEA is to continuously research economic development and public policy in the Republic of Macedonia and to offer recommendations, suggestions and measures to the government and non-governmental institutions.

CEA members share a common vision of the Republic of Macedonia as a new emerging economy integrated with regional and world markets. They devote their time, efforts and knowledge to help make this vision become a reality.

The goal is to institute a sustainable think tank that provides outstanding intellectual capacities and resources, and to create a demand for those services that ensures Macedonia has the capability to properly support policy analysis.

The main Goals of the organization:

1. To provide quality policy analyses;
2. To support viable economic policy in Macedonia;
3. To help foster an environment that brings about higher investment, accelerated development and growth of the Macedonian economy, and EU accession;
4. To achieve financial sustainability;
5. To encourage regional cooperation and collaboration in the Balkans;
6. To strengthen civil society, social capital and trust.

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