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## **Macedonia: policy stance eases**

In the last couple of years growth has returned to Macedonia. In the first half of this year, growth prospects seem good as well. In part this is the consequence of increased inflows of transfers and investments from abroad, but the other part can be attributed to a somewhat eased monetary and fiscal policy stances, in particular in the second half of last year.

The main easing has come from the side of monetary policy. Interest rates have declined after years of a very restrictive stance. In the previous period the central bank argued that a more accommodative monetary policy would destabilize the exchange rate. However, the current easing has had no such consequences. In fact, at least judging by the development of foreign currency reserves, the stability of the denar has if anything been strengthened. This has been supported by the marked improvement of the current account last year, and this trend seems to be continuing this year too. Most of this is the result of the large increase in inflows of private transfers, though it is arguable that some of that inflow should be put in the capital account. It is not altogether clear how much of this is a real shift in financial flows and how much is due to statistical reasons. As the inflows of remittances do not tend to swing so wildly, and given that the level of foreign debt has been more or less the same for a long time now, it is quite possible that the current account has not run such deficits as was reported in the previous years. The easing of the monetary policy has not led to significant changes in the commercial banks' lending behaviour either. Unlike in most of the region, the credit boom is not all that pronounced in Macedonia. This is certainly because growth has been rather unimpressive even after the recent improvement.

There has been a change in fiscal policy too. After a period of fiscal consolidation following the large fiscal imbalances that had developed after the violent conflict in 2001, last year and this year too, a small fiscal deficit is being planned. Whether it will turn out to be 0.6% of GDP this year, as planned, or a bit higher, it will certainly contribute to the continuation of GDP growth. With all that, growth rates are still modest compared to those that are characteristic of recovering economies in transition. This is mostly because domestic demand is recovering only slowly while foreign demand is traditionally not very strong. This year imports are growing faster than exports, as in the region as a whole. Also, foreign investments are not increasing, if the one time items, such as the sale of the distribution part of the electricity company, are excluded.

On the supply side, industrial production is faltering again in the first half of this year. There is very little in the way of reindustrialization to speak of in Macedonia, so the ups and downs of industrial production are driven by what is happening in one or the other of the

larger companies. Services are not posting high growth rates either. Construction is doing well, as in the region as a whole. This is where much of the inflows of remittances go and this should be expected to continue. The political and social situation is stabilizing and this is helping investments in private housing and also in the communal infrastructure.

In early July parliamentary elections will be held. Those are important because they are seen as a test of the stabilization of democracy after the adoption and implementation of the law on decentralization that gave greater autonomy to local governments. If the elections are held in a free and fair atmosphere, as expected, and if the new government takes over smoothly, as is also expected, these proofs that democratization has matured in Macedonia should be a strong argument for the EU to start negotiations for membership with Macedonia. If that were to happen by the end of this year, it would add to the stability of this country and should help improve its economic prospects.

Table MK

## Macedonia: Selected economic indicators

	2001	2002	2003	2004	2005 <sup>1)</sup>	2005 1st quarter	2006	2006 forecast	2007
Population, th pers., mid-year <sup>2)</sup>	2034.9	2020.2	2026.8	2032.0	2035.0	.	.	.	.
Gross domestic product, MKD mn, nom.	233841	243970	251486	265257	284027	.	.	302800	324300
annual change in % (real) <sup>3)</sup>	-4.5	0.9	2.8	4.1	3.6	2.9	.	3.5	4
GDP/capita (EUR at exchange rate)	1887	1981	2025	2130	2280	.	.	.	.
GDP/capita (EUR at PPP - wiiw)	5000	5210	5350	5690	6000	.	.	.	.
Gross industrial production									
annual change in % (real) <sup>4)</sup>	-2.9	-4.8	4.1	-2.2	7.0	4.9	0.5	3	5
Gross agricultural production									
annual change in % (real)	-10.2	-2.3	4.5	6.8	2.2	.	.	.	.
Construction output, value added									
annual change in % (real)	-14.4	0.6	13.3	7.2	.	.	.	.	.
Consumption of households, MKD mn, nom.	163788	188179	191873	206610	.	.	.	.	.
annual change in % (real)	-11.6	12.4	-1.5	.	.	.	.	.	.
Gross fixed capital form., MKD mn, nom.	34716	40448	42110	47286	.	.	.	.	.
annual change in % (real)	-8.6	17.6	1.1	.	.	.	.	.	.
LFS - employed persons, th. avg.	599.3	561.3	545.1	523.0	545.3	507.4	.	.	.
annual change in %	9.0	-6.3	-2.9	-4.1	4.3	-2.4	.	.	.
Reg. employees in industry, th pers., avg.	122.5	110.9	106.7	101.5	97.6	98.2	94.0	.	.
annual change in % <sup>4)</sup>	-4.8	-9.5	-3.8	-4.9	-3.9	-4.8	-4.3	.	.
LFS - unemployed, th pers., average	263.2	263.5	315.9	309.3	323.9	320.0	.	.	.
LFS - unemployment rate in %, average	30.5	31.9	36.7	37.2	37.3	38.7	.	37	37
Reg. unemployment rate in %, end of period	.	.	.	.	.	.	.	.	.
Average gross monthly wages, MKD	17886	19025	19950	20771	21330	20965	22558	.	.
real growth rate, % (net wages)	-1.9	5.0	3.6	4.4	2.2	3.5	4.8	.	.
Consumer prices, % p.a.	5.5	1.8	1.2	-0.4	0.5	-0.4	2.7	3	3
Producer prices in industry, % p.a.	2.0	-0.9	-0.3	0.9	3.2	1.9	5.6	4	4
General governm. budget, nat.def., % GDP <sup>5)</sup>									
Revenues	34.4	34.9	33.4	33.2	32.7	.	.	.	.
Expenditures	40.8	40.0	34.5	33.2	32.5	.	.	.	.
Deficit (-) / surplus (+), % GDP	-6.3	-5.0	-1.1	0.0	0.2	.	.	.	.
Public debt in % of GDP	.	.	.	.	.	.	.	.	.
Discount rate, % p.a., end of period	10.7	10.7	6.5	6.5	6.5	6.5	6.5	.	.
Current account, EUR mn <sup>6)7)</sup>	-272.1	-379.9	-132.1	-334.2	-65.5	-21.0	-18.5	-150	-150
Current account in % of GDP	-7.1	-9.5	-3.2	-7.7	-1.4	.	.	-3.1	-2.9
Gross reserves of NB, excl. gold, EUR mn	845.5	692.8	718.4	665.2	1041.4	634.4 <sup>III)</sup>	798.3 <sup>III)</sup>	.	.
Gross external debt, EUR mn <sup>8)</sup>	1621.4	1513.2	1439.4	1475.7	1849.1	1515.9	1670.6	.	.
FDI inflow, EUR mn <sup>7)</sup>	493.2	82.6	85.4	126.5	80.3	.	.	.	.
FDI outflow, EUR mn <sup>7)</sup>	1.0	0.1	0.3	0.9	2.2	.	.	.	.
Exports of goods, BOP, EUR mn <sup>7)</sup>	1291	1181	1208	1347	1640	482	450	1700	1800
annual growth rate in %	-9.9	-8.5	2.3	11.5	21.7	31.9	-6.7	4	6
Imports of goods, BOP, EUR mn <sup>7)</sup>	1879	2035	1959	2243	2491	672	689	2700	2800
annual growth rate in %	-13.9	8.3	-3.7	14.5	11.0	13.9	2.4	8	4
Exports of services, BOP, EUR mn <sup>7)</sup>	273	269	290	329	379	.	.	.	.
annual growth rate in %	-20.5	-1.6	7.8	13.4	15.4	.	.	.	.
Imports of services, BOP, EUR mn <sup>7)</sup>	295	292	299	372	407	.	.	.	.
annual growth rate in %	1.3	-0.8	2.2	24.7	9.2	.	.	.	.
Average exchange rate MKD/USD	68.04	64.74	54.30	49.41	49.29	.	.	.	.
Average exchange rate MKD/EUR (ECU)	60.91	60.98	61.26	61.34	61.30	46.80	51.07	62	62
Purchasing power parity MKD/USD, wiiw	19.67	20.00	19.67	19.42	19.54	61.40	61.23	.	.
Purchasing power parity MKD/EUR, wiiw	22.97	23.18	23.18	22.96	23.26	.	.	.	.

Notes: 1) Preliminary. - 2) From 2002 according to census November 2002; 2005 wiiw estimate. - 3) According to the Ministry of Finance GDP in 2005 is 3.8%. - 4) Excluding small enterprises, from 2004 new methodology. - 5) Revenues excluding privatization incomes, expenditures excluding financing items. 2005 data projected. - 6) Including grants. - 7) Converted from USD. - 8) Medium- and long-term debt.

Source: wiiw Database incorporating national statistics; wiiw forecasts.