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Macedonia Business Forecast Report Q2 2014

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Abstracts

Core Views

Macedonia's economic recovery will gradually shift into a higher gear as stronger industrial activity increases demand for labour and household consumption growth accelerates. For the time being, there is little to suggest that stronger external demand for Macedonian manufactured goods is driving fixed investment into productive capacity, preventing a more robust recovery.

Macedonia's coalition government looks set to fall apart over the nomination of a presidential candidate for elections in April, and the dissolution is likely to trigger an early general election. We have long suggested that an early election looked likely; however, we do not expect it to destabilise the country politically.

With low borrowing costs and a favourable maturity profile, we believe that Macedonia's public debt position is sustainable, with limited risks of instability over the coming years.

Major Forecast Changes

We have revised up our real GDP growth forecast for 2014 from 2.0% to 2.6%, and have lowered our 2013 growth estimate from 3.0% to 2.4%.

We have modified our current account forecast and now expect a deficit of 1.5% in 2014, from a previous projection for a 3.0% deficit.

Key Risks To Outlook

Deflationary risks in the eurozone could derail the ongoing economic recovery and significantly curtail demand for Macedonian export goods. In turn, this could slow the

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gradual improvement in domestic demand conditions, preventing higher fixed investment into productive capacity and slowing the recovery in household consumption. Should political tensions escalate and an early parliamentary election over the coming months lead to a legislative deadlock, investors could be spooked, and the fixed investment outlook could prove to be worse than we are already projecting this year.

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for Macedonian manufactured goods is driving fixed investment into productive capacity, preventing a more robust recovery. Greater political clarity following what could be an early parliamentary election could see business confidence rise and fixed investment increase. We forecast real GDP growth of 2.6% in 2014 and 2.8% in 2015.

Table: GDP BY EXPENDITURE

Fiscal Policy

Fiscal Improvement Ensures Longer-Term Stability

A sharper-than-expected drop in expenditure in late 2013 saw Macedonia's nominal budget deficit narrow significantly, to 4.0% of GDP, and we believe that stronger economic growth this year and next will see the deficit continue to shrink. With low borrowing costs and a favourable maturity profile, we believe that Macedonia's public debt position is sustainable, with limited risks of instability over the coming years.

Table: FISCAL POLICY

Balance Of Payments

Improving Export Performance Points To Continued External Adjustment

The adjustment in Macedonia's current account has been more pronounced than expected, and an increasingly promising export outlook has encouraged us to reduce our current account deficit forecasts for the coming years. Although stronger import growth over the next few years could derail the narrowing of the country's current account deficit, we believe increased remittance flows will mitigate this impact.

Table: BALANCE OF PAYMENTS

Regional Exchange Rate Policy

Monetary Policy Decoupling Will Weaken The Euro

We expect euro strength against the US dollar and on a trade-weighted basis to persist in H114. However, we continue to argue that the economic and monetary policy cycles in the eurozone are lagging further behind peers in the US and UK, which will trigger a re-pricing of the euro towards the end of 2014. We believe that weak eurozone economic growth and lingering deflationary risks will spur the European Central Bank to loosen monetary policy further.

Table: BMI Eurozone Currency Forecast

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The Macedonian Economy To 2023

Reform Agenda Will Support Steady Return To Growth

Macedonia's reformist trajectory looks set to generate solid GDP growth through to 2023 amid steady convergence to EU political and economic standards. Nevertheless, we caution that political uncertainties could yet pose risks to the longer-term outlook.

Table: Long-Term Macroeconomic Forecasts

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