



REPUBLIC OF MACEDONIA

GOVERNMENT OF THE REPUBLIC OF MACEDONIA

*FISCAL STRATEGY OF
THE REPUBLIC OF MACEDONIA
2016-2018*

Skopje, October 2015

CONTENTS

I. INTRODUCTION	3
II. CURRENT ECONOMIC TRENDS	4
MACROECONOMIC PERFORMANCE	4
Global Economic Trends.....	4
Economic Trends in the Republic of Macedonia.....	5
2015 FISCAL FRAMEWORK.....	8
Budget of the Republic of Macedonia.....	8
Local Government Budget	11
III. ECONOMIC TRENDS IN THE COMING MEDIUM-TERM PERIOD	12
MEDIUM-TERM MACROECONOMIC SCENARIO	12
MEDIUM-TERM FISCAL FRAMEWORK	14
Budget of the Republic of Macedonia.....	15
Projected Deficit and Its Financing	22
Local Government Budget	23
Improvement of Public Finance Management.....	25
Use of EU Pre-Accession Assistance.....	26
IV. TRENDS OF PUBLIC DEBT OF THE REPUBLIC OF MACEDONIA	32
Currency Structure of Government Debt Denominated in Foreign Currency.....	34
Interest Structure of Government Debt	35
Risk Management Indicators	35
MEASURES TO IMPLEMENT PUBLIC DEBT MANAGEMENT STRATEGY	36
Development of Government Securities Market	36
RISKS IN PUBLIC DEBT MANAGEMENT	37
Sensitivity of Servicing-Related Costs	39

Pursuant to Article 16, paragraph 2 of the Budget Law (“Official Gazette of the Republic of Macedonia”, nos. 64/2005, 04/2008, 103/2008, 156/2009, 95/2010, 180/2011 and 171/2012), Government of the Republic of Macedonia, at its session held on _____, adopted the 2016-2018 Fiscal Strategy of the Republic of Macedonia.

I. INTRODUCTION

Medium-term fiscal framework defines the most important goals and policies, as well as the medium-term macroeconomic and fiscal projections, through which stronger linkage between the defined strategic priorities and the available sources of financing is established. Defined goals for increasing the economic growth and the employment, as precondition for higher living standard of citizens, integration of the Republic of Macedonia in both the EU and NATO, entail successful management of public expenditures and continuous improvement of the quality of public expenditures, contributing to significant share of capital investments in total expenditures.

Sound public finance management is set as one of the top priorities, taking into account the strong economic and social significance of the Budget, especially in conditions of uncertainties and harsh challenges.

Medium-term projections of the main macroeconomic and fiscal parameters impose as an essential element of the professional public finance management, to the end of attaining financial safety and sustainability of public finances.

Guidelines and policies in this document are the basis for medium-term projections of public revenues and expenditures. Stronger fiscal discipline and adequate allocation of available funds, in line with the strategic priorities, are thus ensured. Set guidelines are the first step towards ensuring adequate allocation of budget funds for the purpose of attaining stronger development in the priority areas.

Government of the Republic of Macedonia has identified the most important strategic priorities defined in the Decision on Determining Strategic Priorities, as follows:

- increased economic growth and employment, better standard of living and quality of life of the citizens;
- integration of the Republic of Macedonia in both the European Union and NATO;
- uncompromising fight against corruption and crime and efficient law enforcement;
- maintaining good inter-ethnic relations on the principles on mutual tolerance and respect and equal treatment of all before the law;
- investments in education, innovations and information technology, as key elements for creation of knowledge-based society.

Realization of these strategic priorities and adequate allocation of budget funds will provide for higher growth rates of the Macedonian economy in the

coming period, at the same time contributing to better living standard of the citizens.

Public Debt Management Policy sets the framework for the Government of the Republic of Macedonia to act towards prudent public debt management on the medium term. Main principles taken into account when managing public debt portfolio, as well as when preparing and implementing the public debt management policy, are the following:

- determining the optimal structure of debt portfolio and its compliance with the national macroeconomic policy;
- harmonization of debt portfolio-related costs with the costs set in the state budget for each year separately and in the medium term, and
- limiting and eliminating the risk effects on public debt medium- and long-term sustainability.

II. CURRENT ECONOMIC TRENDS

MACROECONOMIC PERFORMANCE

Macroeconomic policy is aimed at maintaining macroeconomic stability and increasing competitiveness of the economy on a permanent basis, job creation, better standard of living and quality of life of the citizens, by improving the business environment, conducting tax and customs policy aimed at underpinning the development of economic entities, boosting investment activity and attracting foreign direct investments, developing human capital and economic infrastructure in the country.

Fiscal policy is designed to achieve reasonable balance between the two strategic goals of the Government of the Republic of Macedonia, those being maintaining macroeconomic stability and encouraging economic activity by increasing the quality of public finances, above all, through increasing capital expenditures related to improving the infrastructure and strengthening private sector capacities for growth and job creation.

Main objective of the monetary policy is to maintain price stability by keeping Denar exchange rate stable in relation to the euro in order to achieve favorable macroeconomic environment for long-term economic development.

Global Economic Trends

Global economic growth in 2014 reached 3.4%, being similar to the growth rate achieved in 2013. Thereby, growth in the developed economic reached 1.8%, slowing down compared to 1.1% growth in 2013, while growth in the developing countries declined from 5% in 2013 to 4.6% in 2014. Eurozone, where growth reached 0.9% in 2014, compared to 0.3% decline in 2013, significantly contributed to growth boosting in the developed countries, while growth in the EU reached 1.5% in 2014, performing significantly better in relation to 2013, when the ERU economy grew by 0.2%. Growth in the EU was driven by domestic demand, mainly as a result of growth of private consumption in conditions of improved trends on the labour market.

As for the largest economies in the EU, growth in Germany picked up the most, reaching 1.6% compared to 0.4% in 2013, while with respect to Spain, it reached 1.4% in 2014 compared to 1.2% decline in 2013. However, growth in Germany, which was broad based and mostly drive by private consumption and investments, contributed the most to the improvement of the economic situation in the European countries. Great Britain continued its good performance, reaching 3% growth in 2014, while growth in France remained low (0.2%) in 2014. Italy experienced negative growth rate third year in a row, although 0.4% decline in 2014 was weaker compared to the previous years. It is expected to exit recession in the coming period.

EU experienced economic growth of 1.9% in the first half of 2015, while growth in the Eurozone reached 1.5%. With respect to the largest EU economies, Spain reached the highest growth of 3% in the first half of 2015, followed by Great Britain, experiencing 2.6% growth. During the same period, Germany reached 1.4% growth, growth in France accounted for 1%, while it reached 0.6% in Italy.

Global growth is expected to be 3.1% in 2015, picking up to 3.6% in 2016, boosted by further growth pick-up in the developed economies. Main driving force will be the economic growth in the USA, which is expected to reach 2.6% in 2015 and 2.8% in 2016, instigated by the improved trends on the labour market and the increased real income as a result of reduced prices of oil and US dollar strengthening.

Favourable economic trends are expected to continue in the EU, as a result of realization of the new Investment Plan for Europe, monetary easing by ECB, euro depreciation and reduced oil prices. These factors will contribute to growth strengthening, whereby, in line with European Commission projections, growth in the EU is expected to surge to 1.8% in 2015 and 2.1% in 2016. GDP growth in the Eurozone is expected to increase to 1.5% in 2015 and 1.9% in 2016. Inflation in the EU and the Eurozone is expected to remain low in the coming period, reaching 0.1% in 2015 and 1.5% in 2016. Positive economic trends are expected to contribute to further improvement on the labour market, while low inflation rate is expected to provide for increased real income which, together with the improved financing conditions, will have positive effects on both the consumption and the investments.

Positive trends in the global economy, especially the expectations for growth in the EU in the coming period, provide for a favourable external surrounding for growth strengthening of the Macedonian economy and using the export potential.

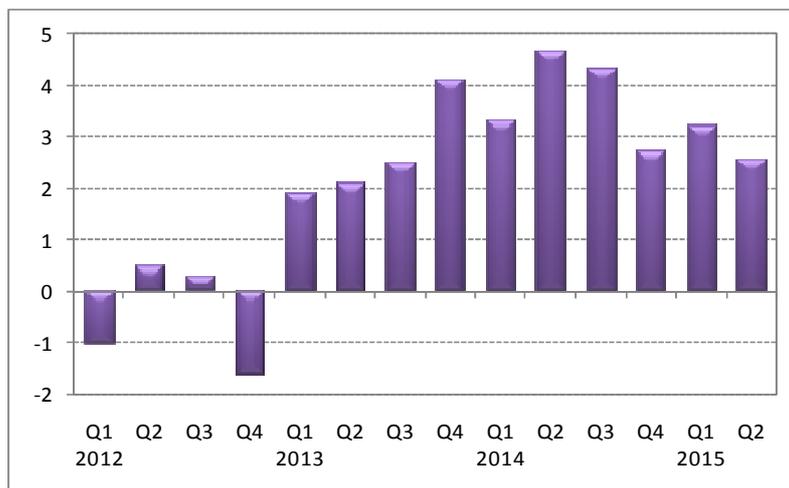
Economic Trends in the Republic of Macedonia

Gross Domestic Product. Upward trend of economic activity continued in 2015, reaching 2.9% in the first half of the year.

Analyzed according to GDP by production method, positive performance was observed in many sectors. Favourable trends in the construction sector continued in 2015, reaching 4.5% growth in the first half of the year. Growth in the services sector amounted to 3.2%, whereby trade, transport and catering sector, experiencing 5.9% growth, contributed the most to the increased economic

activity. Industry sector experienced 1.1% growth in the first half in 2015 in conditions of favourable trends in the manufacturing industry. In the course of August and September, industrial production grew by 12.7% and 8.6% on annual basis respectively, pointing out that industry returns on the solid growth path. Agricultural production experienced 1.4% decline due to the unfavourable weather conditions.

Chart 1. Real GDP growth (%)



Source: State Statistical Office

Analyzed according to the expenditure side, growth in the first half in 2015 was driven by the export of goods and services, experiencing real growth of 8.3%. Increase in export was result of the increased export potential of the country, in conditions of gradual recovery of the external demand. Export growth was also accompanied by the change in the structure of the higher value-added products, as a result of the activity of capacities in the free economic zones. In fact, according to monthly data on export of goods, export of machines and transport device in this period surged by 28.4% and export of chemical products increased by around 20%. Import of goods and services experienced lower growth compared to export, accounting for 3% in real terms, hence net export significantly contributed to the economic growth.

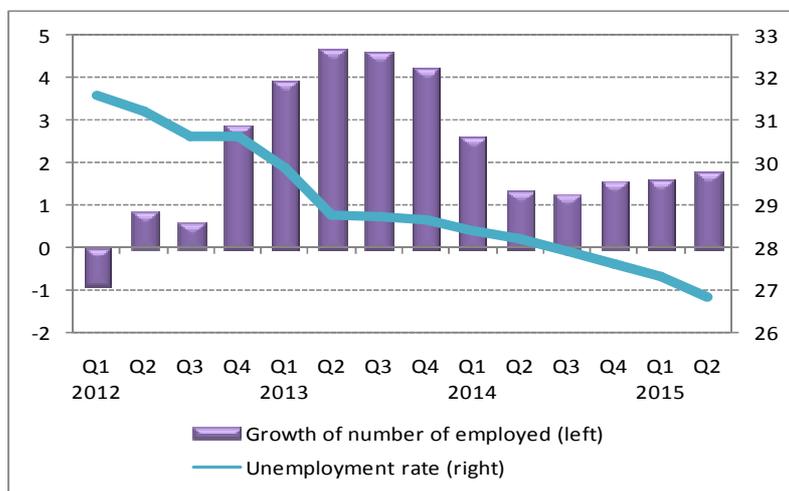
Final consumption in the first half in 2015 grew by 2.3%, being a result of the increase of both private and public consumption. Private consumption experienced 2.1% real growth as a result of employment increase, increase of salaries, as well as increase of household credits, while public consumption surged by 3.3%. Gross investments in this period declined by 3.3% in real terms.

Labour Market. Positive trends on the labour market continued in 2015. According to the Labour Force Survey, unemployment rate continuously declines, dropping to 26.8% in the second quarter, i.e. dropping by 1.4 percentage point compared to the same quarter last year.

Number of employees in the first half in 2015 increased by 1.7% in relation to the same period in 2014. Increase of the employment rate was mainly due to the operations the companies in the free economic zones and realization of the active measures and the unemployment reduction policies, including the new measure

“Macedonia Employs”. Employment rate in the second quarter in 2015 picked up to 41.7%, increasing by 0.6 percentage points in relation to the same period last year. Average net salary in the period January – June 2015 was higher by 2.4% in nominal terms and by 2.7% in real terms.

Chart 2. Growth of number of employed and unemployment rate (%)



Source: State Statistical Office

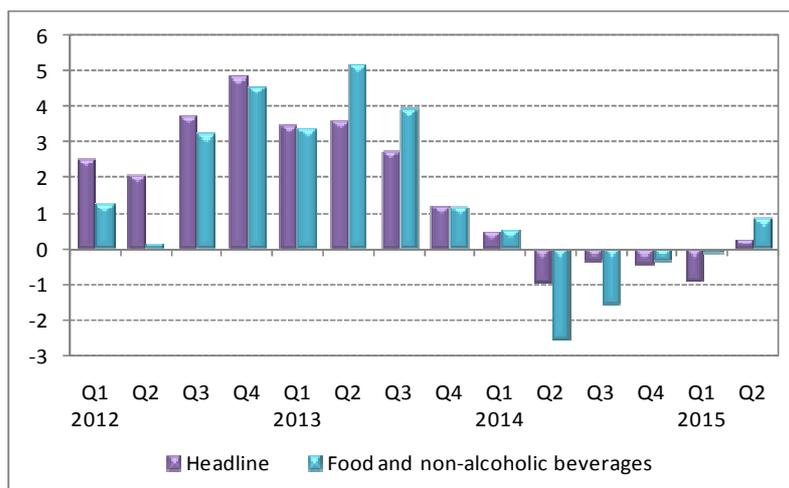
External Sector. Current account deficit in the first half in 2015 amounted to EUR 121 million, i.e. 1.3% of GDP, dropping by EUR 102.9 million compared to the same period last year. Current account deficit narrowed as a result of the decreased deficit in trading of goods and improved positive balance of the services account.

Foreign direct investments in the first eight months in 2015 amounted to EUR 153.4 million, being higher by 6% compared to the same period in 2014. Gross foreign currency reserves amounted to EUR 2,188 million at the end of October 2015, providing for 4.6-month coverage of import of goods and services in the 12-month period starting from November 2014 to October 2015, being at a satisfactory level to conduct the monetary policy.

Inflation and Monetary Trends. Average inflation rate in the first half in 2015 amounted to -0.3%. Negative inflation was a result of the price decline in the categories Transport, Communications and Recreation and Culture. Decline of prices in the Transport category of 9.2% contributed the most thereto, mainly as a result of the declined domestic prices of liquid fuels and lubricants.

As a result of negative inflation and favourable trends in the external sector, National Bank of the Republic of Macedonia kept the low interest rate on central bank bills (3.25%). Support to private sector by the banks continued with a solid pace, hence total credits of banks in June 2015 grew by 9% on annual basis, mostly as a result of increased household credits, as well as increased credits to enterprises.

Chart 3. Inflation rate (%)



Source: State Statistical Office

Total deposits of the banking system in June 2015 surged by 8.9% on annual basis, mostly as a result of domestic currency deposits, increasing by 11.7% annually. Such trends caused for the share of domestic currency deposits to increase to 59%, showing increased confidence of the economic entities in the domestic currency.

2015 FISCAL FRAMEWORK

Budget of the Republic of Macedonia

Budget revenue and inflow performance exceed the expectations for this period of the year, while expenditures are executed on regular and timely basis. In the period January - September 2015, total revenues were collected in the amount of Denar 117,445 million, i.e. collection was higher by 12.3% in relation to the revenue collection in the analyzed period last year. Denar 68,584 million out of this amount are tax revenues, being higher by Denar 7,807 million or by 12.8% more compared to last year. Thereby, divergent trends were observed in the tax revenue structure. Collection of VAT revenues was lower by 2.5% compared to the analyzed period in 2014, i.e. VAT revenues were collected in the amount of Denar 30,623 million, accounting for the most in the tax revenues – 44.6%. On the other hand, profit tax revenues were collected in the amount of Denar 9,592 million, being higher by Denar 6,002 million or by 167% in relation to the same period in 2014. Collection of excise revenues was also higher than the projections. These revenues were collected in the amount of Denar 14,521 million, being by Denar 2,136 million more or by 17.2% higher compared to last year.

Revenues collected on the basis of social contributions amounted to Denar 34,957 million. This amount is by Denar 2,803 million or by 8.7% more in relation to the respective period in 2014. Denar 23,493 million was collected on the basis of pension insurance, while revenues collected on the basis of health insurance contributions amounted to Denar 9,975 million. Revenues performance corresponded to the positive trends in the real sector and the growth of economic activity respectively.

In the first nine months in 2015, non-tax revenues were collected in the amount of Denar 9,351 million, being higher by Denar 1,672 million, i.e. by 21.8%, in relation to the same period in 2014. Non-tax revenues of budget users on their special revenue accounts, being collected in the amount of Denar 4,985 million, and revenues on the basis of administrative fees, being collected in the amount of Denar 1,407 million, accounted for the most. Capital revenues, generated from sale of construction land and social flats, were collected in the amount of Denar 1,968 million, being by 25.9% higher compared to the analyzed period last year. Budget users generated Denar 2,585 million from donations on the basis of international multilateral and bilateral cooperation.

In the period January - September 2015, expenditures were executed in the amount of Denar 131,319 million, i.e. execution was higher by Denar 9,301 million or by 7.6% in relation to the same period last year. All liabilities of the budget users, legal rights of the citizens and the due liabilities towards domestic and foreign creditors were settled on time and on regular basis during this period.

Within this framework, current expenditures were executed in the amount of Denar 119,961 million. During this period, Denar 18,376 million was paid for salaries and allowances to the employees with the budget users, while expenditures related to goods and services were executed in the amount of Denar 12,950 million.

Transfers-related expenditures accounted for the most in the current expenditures, amounting to Denar 83,656 million in this period. Government liabilities on the basis of payments related to exercising the rights to guaranteed social protection of the citizens (pecuniary allowances to vulnerable categories of citizens, as well as child allowance and parenting payments) were settled on regular basis, accounting for Denar 5,333 million. Increase of social rights by 10% was realized within these expenditures with the payments made in July. As regards regular payment of pensions, Denar 33,667 million was allocated therefore, whereby around 300,000 pensioners were increased their pensions by Denar 621 or by 5% in average. With respect to financing health services and benefits, Denar 17,544 million was paid, while Denar 859 million was allocated for payment of unemployment benefits through the Employment Agency. Denar 10,852 million was transferred from the Budget of the Republic of Macedonia to the municipalities, as block grants for financing the transferred competences, as well as earmarked grants for financing the operating costs in local public institutions. In addition, Denar 1,300 million was transferred on the basis of VAT revenues. During this period, agricultural subsidies were paid on continuous and regular basis, aimed at improving the quality and the competitiveness of the sector.

Denar 4,979 million was allocated for regular servicing of liabilities on the basis of interest, according to the repayment schedules on domestic and foreign borrowing. Denar 2,925 million out of this amount was allocated for payment of interest on foreign borrowing.

In the period January - September 2015, capital expenditures were executed in the amount of Denar 11,358 million. In this period of the year, activities for realization of major infrastructure projects were intensified, such as the construction of Corridor X highway and investments in reconstruction and construction of the railway infrastructure. At the same time, many projects were realized, aimed at improving the infrastructure in education sector, health sector and utilities infrastructure, by constructing schools, sports facilities, playgrounds, water supply and sewerage network, as well as reconstruction of health facilities.

During this period, budget deficit amounted to Denar 13,874 million, being by Denar 3,580 million or by 20.5% less compared to the respective budget in 2014. Inflows to the Budget provided for regular and early repayment of principal, amounting to Denar 17,277 million, on the basis of liabilities upon credits.

To the end of further managing both the government and the public debt, Republic of Macedonia made early repayment, in full, of the debt towards the International Monetary Fund (IMF). Both public and government debt were reduced by 1.7 percentage points by the early buyback. IMF credit line in the amount of SDR 197 million was borrowed in March 2011 and it started to be repaid in mid-2014, while the remaining debt, fully repaid, amounted to SDR 123.1 million (US\$ 174 million).

Table 1

(Denar million)

	2015 Budget	January - September 2015 execution
Budget of the Republic of Macedonia		
1. Total revenues	166,842	117,445
1.1. Tax revenues and contributions	142,527	103,541
1.1.1 Tax revenues	95,338	68,584
1.1.2 Contributions	47,189	34,957
1.2. Non-tax revenues	16,433	9,351
1.3. Capital revenues	2,880	1,968
1.4. Donations	5,002	2,585
2. Total expenditures	186,981	131,319
2.1. Current expenditures	164,747	119,961
2.1.1 Salaries and allowances	25,082	18,376
2.1.2 Operating expenditures	19,766	12,950
2.1.3 Transfers	113,447	83,656
2.1.4 Interest	6,452	4,979
2.2. Capital expenditures	22,234	11,358
3. Deficit	-20,139	-13,874
4. Deficit financing	20,139	13,874
4.1 Inflows	48,958	31,151
4.2 Outflows	28,819	17,277

Local Government Budget

Local government development is one of the priorities stemming from the Accession Partnership of the Republic of Macedonia with the EU, the realization of which opts for careful and phased approach, which is successfully implemented by the Government. Phased approach for transferring and managing the operating and the financial resources for the transferred competences in the field of education, culture, child care and social protection, is completed, i.e. all municipalities (except Plasnica) are financed with block grants. On the basis of the carried out evaluation, it has been concluded that Plasnica Municipality has acquired sufficient number of points so as to move to the second fiscal decentralization stage, however, the requirement as regards the number of employees in the municipal administration has not been met¹.

Process of administering and collecting special revenues, performing the transferred competences and managing the financial resources and other resources necessary for their performance, has been successfully continued by strengthening the special revenues of the municipalities and the capacity to manage the funds. Municipalities successfully perform the administrative competences in the field of taxes and fees, they manage more funds in a more flexible manner as a result of the increased volume of transfers (grants) in the field of education, culture, social protection (mainly kindergartens) and fire fighting.

Financial capacity of the municipalities has been strengthened by many legal amendments, increasing the existing and prescribing new revenues for the municipalities as regards the transferred competences. At the same time, access to the capital market has been easier, under more liberal and transparent requirements for borrowing. Hence, interest of the municipalities for financing larger investment projects on the basis of borrowing increased. To that end, the Government has provided credit lines from international financial institutions (World Bank, EIB, KfW and EBRD), which have provided for substantial investments, especially in: reconstruction and rehabilitation of local streets and bridges, construction and reconstruction of water supply and atmospheric water networks, improvement of public hygiene and increasing energy efficiency in municipal public facilities and local spatial landscaping.

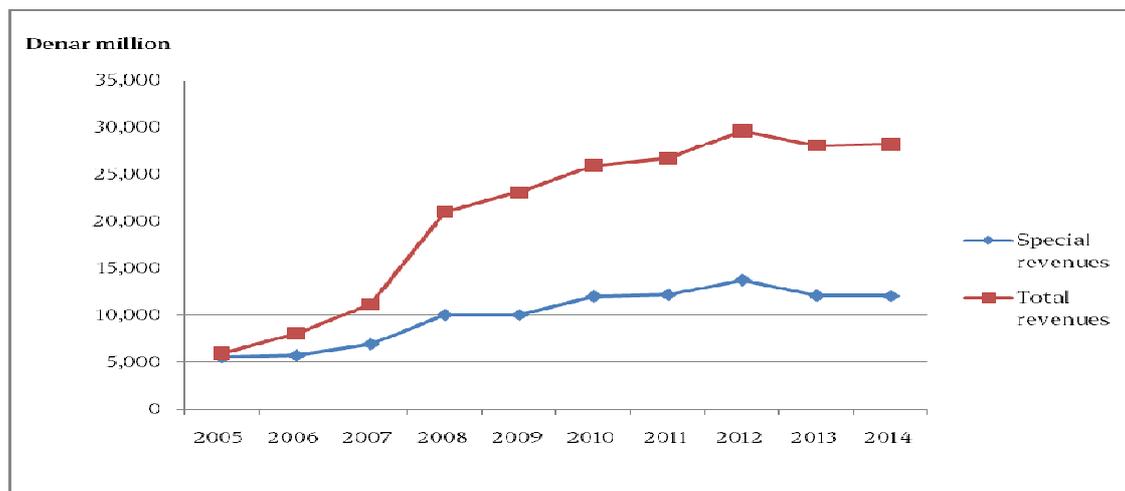
As regards the level of decentralization, Republic of Macedonia, according to the data on 2014 expenditure execution (more than 5% of GDP), has joined the group of decentralized countries.

Today, compared to 2005, when the process of transferring competences and fiscal decentralization commenced, municipal revenues have increased by five times (Denar 5.9 billion in 2005, Denar 28 billion in 2014). Tax revenues, which the

¹ Pursuant to the Law on Local Government Financing, the municipal administration, in order to meet the requirements to move to the second stage, is to have at least 2 employees, qualified to work in the area of financial management, and at least 3 employees, qualified to work in the area of calculating and collecting taxes.

municipalities are authorized to collect, have increased by more than twice during the same period.

Chart 4 - Special and total revenues in the period 2005-2014



III. ECONOMIC TRENDS IN THE COMING MEDIUM-TERM PERIOD

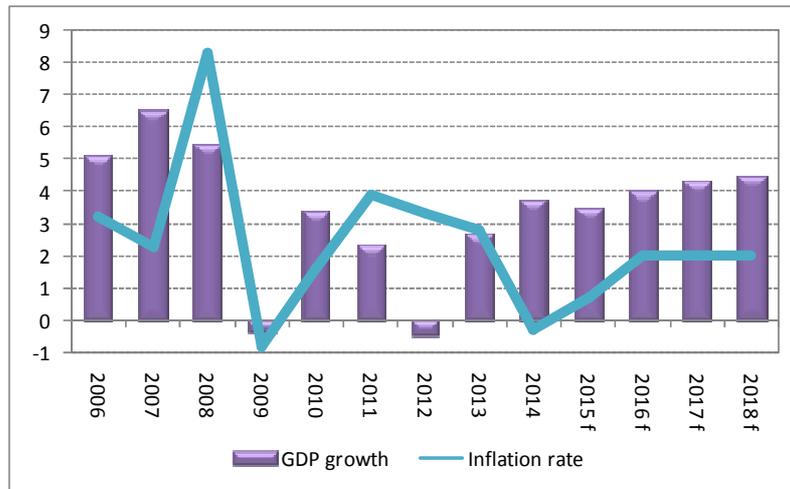
MEDIUM-TERM MACROECONOMIC SCENARIO

Macroeconomic policy of the Republic of Macedonia in the coming period is aimed at fulfilling the strategic commitments of the Republic of Macedonia to long-term and sustainable economic growth, boosting competitiveness of the economy and job creation, as well as better living standard of the population.

2016-2018 Macroeconomic Policy provides conditions for increased economic activity through sustainable fiscal policy, which, in coordination with the monetary policy, will contribute to achieving sustainability of the external position of the country and low and stable inflation.

Taking into account the expectations for the external surrounding, the sound macroeconomic policies, i.e. the structural reforms aimed at boosting country's competitiveness, as well as the active fiscal policy, favourable economic trends are expected to continue in the period 2016 – 2018. Real GDP growth is expected to be 4% in 2016, 4.3% in 2017 and 4.5% in 2018.

Chart 5. Real GDP growth and inflation rate (%)



Source: SSO and Ministry of Finance projections

Positive growth of industrial production is envisaged to continue in the period 2016 – 2018, with projected growth rate of 4.3% in average, in line with the expectations for increase of foreign demand and the increased production potential of the country as a result of the investments in the free economic zones. Construction sector is expected to achieve average growth rate of around 6% in this period, as a result of realization of the planned infrastructure projects and investments in the TIDZ and the industrial zones. Services sector, accounting for the most in GDP, is expected to register average growth rate of 3.8% in real terms, while agriculture sector is expected to achieve 2.2% growth in this period.

In the period 2016 – 2018, export of goods and services is envisaged to achieve average real growth of around 9%, mainly as a result of the expectations as regards the operating of the export capacities of the companies in the free economic zones, in conditions of gradual growth of the foreign demand. Increase of the export is expected to be accompanied by further improvement of the export structure, to the end of increased share of higher value-added products. Projected growth of domestic demand and export activity also provides for growth of import which, in this period, is expected to be 7.7% in average.

Growth of gross investments in the period 2016 - 2018 is projected at 7.8% in average. Projected growth of gross investments is based upon the planned investments in the public sector, as main driving force of investments in infrastructure, as well as the expectations for gradual growth of private investments, mainly driven by FDIs. As for the public investments, investments aimed at improvement of transportation network in the country (highways, railroad tracks, regional and local roads) are envisaged, as well as investments in energy and utilities infrastructure, and education, social and health system. These investments, in addition to the current positive effect on the economic activity, will also contribute to boosting the competitiveness of the country in the long run, being of key importance for increasing productivity and production.

In the period 2016 - 2018, personal consumption is expected to experience real

growth of 3.2% in average, as a result of the expected increase in the number of employees and the projected salary increase. Growth of personal consumption is projected at 1.1% in this period.

Envisaged economic growth in the period 2016 - 2018 is expected to have positive effects on the labour market trends. According to the projections, average increase of the number of employees of around 3% is expected on annual basis in this period, as a result of the job creation in the free economic zones, the active employment measures and programs, as well as the realization of infrastructure projects. This will, on other hand, result in decline in the number of unemployed persons by 4.3% in average in this period. Increase of demand in this period is expected to also reflect on the labour supply, projected to increase by 1.2% in average. Such trends on the labour market will provide for the unemployment rate to drop to around 22% by the end of 2018.

In the period 2016-2018, inflation rate is expected to be both low and stable, at around 2%. Inflation pace will be influenced by the trends of global prices of primary commodities, and partially by the trends of the economic activity in the national economy.

Inflow of foreign direct investments and projections for moderate BOP current account deficit are factors that are to result in stable external position and keeping foreign currency reserves at an adequate level of more than 4-month import coverage. Stable Denar exchange rate in relation to the euro will be retained in the coming period as well, aimed at maintaining price stability, as ultimate goal of macroeconomic policy.

Risks as regards projected economic growth rates are generally related to the global economic trends, i.e. the growth pace of the EU economy, as the main trading partner of the country, as well as the geopolitical developments and the situation on the oil and natural gas markets. The Government will continue to carefully monitor the risks on daily basis, to the end of reacting promptly.

MEDIUM-TERM FISCAL FRAMEWORK

Fiscal policy in the coming medium-term period will be aimed at maintaining macroeconomic stability and encouraging economic activity through capital expenditures and investments in infrastructure and improving the doing business conditions to stimulate the potential of the private sector for growth and job creation.

Projections for public finances in the next medium-term period are based on the commitment to their gradual consolidation, by reducing the budget deficit to below 3% starting 2017.

Projected revenues of the consolidated government budget in the next three-year period decline, as a share of GDP, from 32.2% of GDP in 2015 to 31.2% in 2018. As a result of continuity in implementing disciplined budget policy and strengthened consolidation of public spending, in the period 2015 - 2018, total expenditures will also decline from 35.8% in 2015 to 33.8% in 2018.

Set basic postulates of the fiscal policy in the coming period provide for gradual reduction of the deficit level and its positioning at around 2.6% of the projected GDP in 2018.

Table 2

(Denar million)

Consolidated general government budget	2015	2016	2017	2018
Consolidated general government budget - revenues	177,764	188,884	198,366	205,607
% of GDP	32.2	32.3	32.0	31.2
Consolidated general government budget - expenditures	197,903	207,868	216,194	222,600
% of GDP	35.8	35.6	34.9	33.8
Consolidated general government budget - deficit	-20,139	-18,984	-17,828	-16,993
% of GDP	-3.6	-3.2	-2.9	-2.6
Central Budget - revenues	101,748	109,671	115,753	119,950
% of GDP	18.4	18.8	18.7	18.2
Central Budget - expenditures	121,837	128,621	133,590	136,945
% of GDP	22.1	22.0	21.6	20.8
Central Budget - deficit	-20,089	-18,950	-17,837	-16,995
% of GDP	-3.6	-3.2	-2.9	-2.6
Budget Funds - revenues	47,551	49,645	52,119	54,601
% of GDP	8.6	8.5	8.4	8.3
Budget Funds - expenditures	47,601	49,679	52,110	54,599
% of GDP	8.6	8.5	8.4	8.3
Budget Funds - deficit	-50	-34	9	2
% of GDP	0.0	0.0	0.0	0.0
Local government budget - revenues	28,465	29,568	30,494	31,056
% of GDP	5.2	5.1	4.9	4.7
Local government budget - expenditures	28,465	29,568	30,494	31,056
% of GDP	5.2	5.1	4.9	4.7
Local government budget - deficit	0	0	0	0
% of GDP	0.0	0.0	0.0	0.0

Budget of the Republic of Macedonia

Budget of the Republic of Macedonia, as the most important instrument of the economic policy, will, in the coming medium term as well, reflect the expected fiscal trends, public expenditures for financing priority policies and goals to the end of maintaining social protection and economic growth,

Total genuine revenues of the Budget of the Republic of Macedonia (central government) for the period 2015-2018 are projected to around 30% of GDP, whereby their share in GDP by years is reduced in conditions of keeping low tax rates and low the tax burden on the business sector. Thereby, tax revenues account for around 57.5% of the projected revenues, followed by revenues on the basis of social contributions accounting for around 27.9%, non-tax revenues and

capital revenues accounting for around 11.9%, while the rest of the revenues are expected to be generated from IPA Funds and other donations. With respect to tax revenues, most revenues will be generated on the basis of VAT, personal income tax and excises.

In the next medium-term period, projections for social contributions, which are genuine revenues of the Pension and Disability Insurance Fund, Health Insurance Fund and the Employment Agency, are based on the expected positive economic trends, which will appropriately reflect on the growth rates of both employment and salaries. Non-tax revenues in the next medium-term period account for around 10.4% of the total revenues, wherein revenues on the basis of administrative fees and other non-tax revenues the budget users generate on their own accounts account for the most.

In the coming period, budget revenue projections with regard to foreign donations include the donations the budget users will realize for specific projects, as well as disbursements from the EU pre-accession funds.

Table 3

(Denar million)

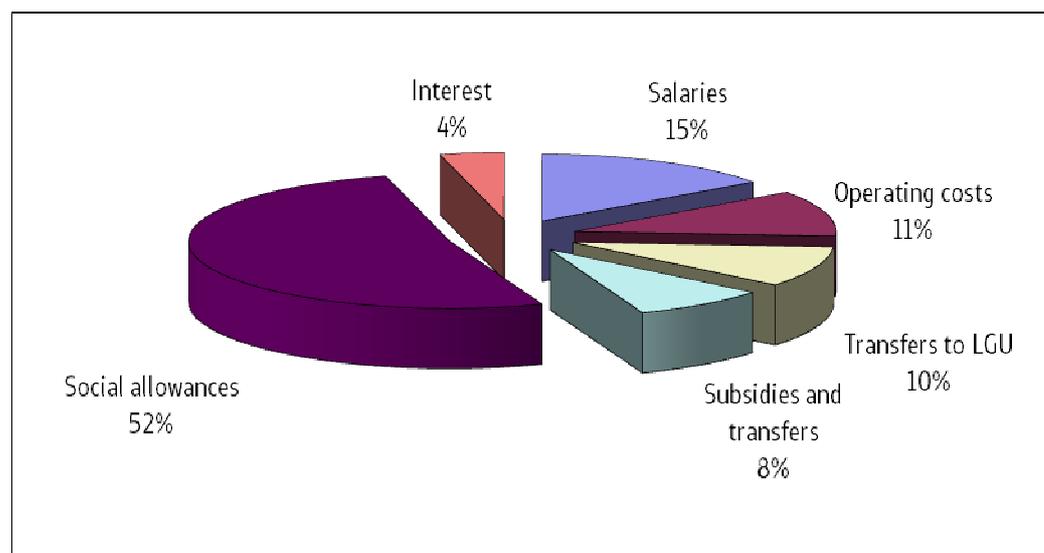
Budget of the Republic of Macedonia	2015 Budget	2016 Budget	2017 Budget	2018 Budget
1.Total revenues	166,842	177,292	186,724	193,855
1.1. Tax revenues and contributions	142,527	150,718	158,614	166,816
1.1. 1 Tax revenues	95,338	101,531	107,001	112,772
1.1. 2 Contributions	47,189	49,187	51,613	54,044
1.2. Non-tax revenues	16,433	18,387	20,687	19,616
1.3. Capital revenues	2,880	3,155	2,391	2,391
1.4. Donations	5,002	5,032	5,032	5,032
2. Total expenditures	186,981	196,276	204,551	210,848
2.1. Current expenditures	164,747	170,698	178,586	184,579
2.2. Capital expenditures	22,234	25,578	25,965	26,269
3. Deficit	-20,139	-18,984	-17,827	-16,993
4. Deficit financing	20,139	18,984	17,827	16,993
4.1 Inflows	48,958	40,546	39,557	43,675
4.2 Outflows	28,819	21,562	21,730	26,682

In the coming medium-term period, expenditure side of the Budget will be aimed at realization of two components: development component aimed at supporting the growth of the Macedonian economy by investing in major infrastructure projects, and social component aimed at maintaining social stability and

improving the living standard of the citizens, above all the vulnerable categories of citizens (pensioners beneficiaries of social welfare social welfare and farmers).

Thereby, disciplined budget spending will continue to be implemented, with an emphasis to restrictiveness and rigorous control over less productive costs, on one hand, and increase of investments in capital projects on the other. Average share of expenditures in the Budget of the Republic of Macedonia in the period 2015-2018 is around 33.1% of GDP.

Chart 6 - Current expenditure structure



When projecting the **current expenditures** for the next period, the following assumptions were taken into account:

- as regards expenditures related to wages and salaries and allowances, continuation of strict control over new employments. Further increase of salaries will be a result of detailed calculations for each fiscal year, in order to determine the specific volume and dynamics in line with the Budget possibilities, and depending on the fiscal condition and the effects from the external economic trends;
- increase and timely payment of pensions and social benefits, for the purpose of ensuring the well being of the beneficiaries of these rights. In the course of 2016, pension-related expenditures are projected with the respective increase, hence around 307,000 pensioners will have their pensions increased by 5% in average, i.e. Denar 650 each, starting with the September pension to be paid in October 2016. Subsequently, 5% pension increase in average is also planned in 2017, starting with the September pension to be paid in October 2017. Policy for planned increase of pensions is depends on the fiscal condition and it will be implemented if no serious external crisis occurs that would adversely affect the economic and the financial situation in the Republic of Macedonia. Medium-term projections also include increase of social benefits for socially most vulnerable families as social welfare (increased by 5% starting June, to be paid in July 2016) and regular servicing of liabilities on the basis of child allowance, allowances on the basis of rights of disabled persons, war invalids and civilian invalids and asylum seekers. Planned reforms in the social sphere, by simplifying the procedures for exercising

these rights, as well as the effects from the integration of social centers in unique information system, will provide certain savings, at the same time extending the scope and proper targeting of these allowances towards the most vulnerable categories.

Government activities and measures as regards social policy are supported under the Conditional Cash Transfers Project, financed with World Bank loan, aimed at supporting the Government of the Republic of Macedonia in its efforts to reduce poverty of vulnerable groups by conditioning the existing pecuniary allowances.

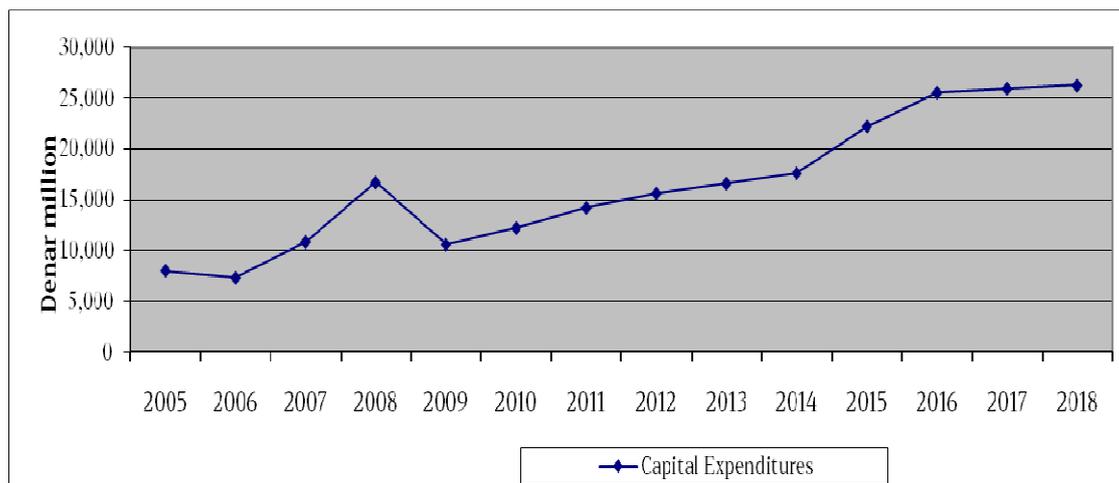
- further provision of substantial amounts for payment of agricultural subsidies, to the end of strengthening and supporting this sector. Planned reforms in the agricultural sector, as well as the substantial amount of subsidies and funds under the IPARD Program will provide for its further enhancement and support, to the end of boosting the export of Macedonian agricultural products and conquering new markets.

- improvement of the quality of university education and vocational education, as well as public financial support for stimulating the innovations in Macedonian companies. To that end, implementation of the Skills Development and Innovation Support Project, funded with World Bank loan, will continue in 2016. At the same time, quality of vocational education will be strengthened, to the end of adjusting to labour market needs. In addition, innovation capacity of companies will be improved through the Fund for Innovation and Technological Development.

In the coming medium-term period, fiscal policy will focus on ensuring substantial public investments, being a precondition for improvement of economic perspectives, as well as better and more quality life of the citizens. To the end of realizing and maintaining positive economic growth rates, significant amount from the Budget is expected to be intended for public investments in the coming three-year period. **Public investments** presenting the development component of the fiscal policy will continue to be of priority and dominant importance. In the past several years, capital projects financed from the Budget of the Republic of Macedonia fully affirmed their justification, having strong influence when tackling the effects from the economic crisis. Denar 25,578 million is envisaged for capital investments in 2016 Budget.

Within budget funds allocated for capital expenditures, substantial investments are envisaged in completion of the construction of the remaining part of Corridor X highway and the railway infrastructure, energy and utilities infrastructure, as well as capital investments in improving the conditions in the educational, social and health system, agriculture, environmental protection and judiciary.

Chart 7 - Capital expenditures in the Budget of the Republic of Macedonia



Efficient usage of budget funds and funds provided with loans from international financial institutions and bilateral creditors will be basis for series of investment activities and reforms, which will provide for job creation and favourable business surrounding.

Road infrastructure is planned to be improved through construction of motorway section Demir Kapija – Smokvica along Corridor X, being 28.18 km long, thus completing the main axis of Corridor X passing through the Republic of Macedonia. Construction of this section is financed with loans from EBRD and EIB, grants under the IPA and Budget funds.

At the same time, substantial investments in road infrastructure, financed with World Bank loans, are ongoing through the Public Enterprise for State Roads, such as the “National and Regional Roads Rehabilitation Project”, including the following road sections: Bitola – Resen – Bukovo, junction with A4 (Novo Selo) – Mavrovo – Zirovnica – Debar, Tetovo – Brvenica – Cegrane – Gostivar, Delcevo – Golak, Mokrino – Smolari, Melnicki Most – Centar Zupa, Lazani – Ropotovo – Crniliste, Krivogastani – Obsrani – Vogani, Kocani – Delcevo, Nov Dojran – Nikolik; Road Upgrading and Development Project (Kriva Palanka – Rankovce), as well as Miladinovci – Stip Motorway Project and Kicevo – Ohrid Motorway Project, funded by Export – Import Bank of China. Activities envisaged under the National Roads Program, funded with EBRD loan, will be intensified in the coming period, envisaging construction of new road sections: Stip – Kocani, Ohrid – Pestani, Gradsko – Prilep and Trebeniste – Struga, and “National and Regional Roads Construction and Rehabilitation Project” will commence in 2016 as well, including: Probistip – Ponikva Ski Center, Toranica – Sasa (Kriva Palanka – Kemanica), Staro Konjarevo – Novo Konjarevo, Garski Most – Izvor, to be financed with World Bank loan, as well as Stip – Radovis Road Section and Kriva Palanka – border with Republic of Bulgaria, to be financed with EBRD loan.

Regarding the railway infrastructure, implementation of the Rail Corridor X Project, financed with EBRD loan, will continue, encompassing overhaul of several sections along Corridor X, the total length of which is around 53 km. Main objective of the Project is improvement of the railway line, reduction of its maintenance costs and ensuring safe, stable and faster traffic on the above-

mentioned sections. Focus will be also placed on implementation of the Project for Completion of Rail Corridor VIII, being aimed at connecting the Black Sea with the Ionian Sea, this speaking in favour of the huge strategic and economic significance of this Project. Construction of the eastern part of Rail Corridor VIII, i.e. the part towards Bulgaria, will be carried out in 3 phases and it will be financed with loans from EBRD and EIB, as well as IPA funds. Reconstruction of the first section Kumanov-Beljakovce, 30.8km long, financed with EBRD loan, commenced in March 2014. Loan Agreement with EBRD was concluded in December 2014, aimed at financing the construction of the second section Beljakovce – Kriva Palanka, 34 km long. In parallel to the investments in railway infrastructure, implementation of the “Macedonian Railways Fleet Renewal Project”, financed with EBRD loan in the amount of EUR 50 million, will continue.

By implementing the “Project for Construction of Gas Pipeline System in the Republic of Macedonia”, business sector, public sector and households will be provided supply with cheap and environmentally friendly energy, at the same time reducing the emission of harmful gases in the atmosphere. Construction of the section of the national gas pipeline system Klecovce - Stip, which is to be financed with funds provided from the clearing debt with Russia, as well as Government contribution, commenced in 2015. Construction of the other sections of the national gasification system Stip – Negotino – Bitola and Skopje – Tetovo – Gostivar is expected to commence at the beginning of 2016.

Strengthening the management at local level is supported under the Municipal Services Improvement Project, financed by the World Bank. Project enables the municipalities and the public utility enterprises, which can borrow funds, in line with the legislation, to finance investment operations in line with their priorities. Implementation of the second phase of the “Municipal Services Improvement Project” will continue in 2016 as well. Loan proceeds are intended for financing infrastructure investment projects in the field of water supply and wastewater drainage, management of solid waste and other investments in municipal services, having potential for generating revenues, i.e. making savings or being of high priority for the municipalities. As a result of the increased interest by the municipalities for such favourable loans, third phase of the Project is expected to commence in 2016. IPA funds are additionally provided for this Project, which the municipalities can use, as grants, by 2019 so as to finance their priority projects.

To the end of improving both the conditions and the quality of life, above all in the rural areas in the Republic of Macedonia, by supplying clean drinking water, “Water Supply and Waste Water Collection Project”, financed with EIB loan, will continue to be implemented in the coming period. This Project is part of the priorities of the Government of the Republic of Macedonia for equal regional development and is expected to boost development in rural areas through investments in utility infrastructure.

Implementation of the first phase of the “Project for Rehabilitation of Health Provider Institutions in the Republic of Macedonia – Phase I”, funded by Council of Europe Development Bank (CEB), will continue in 2016. Main objective

of the Project is to improve health infrastructure, operational services for delivery of respective health services, as well as to introduce new and modern equipment and technology to replace most of the existing obsolete equipment. This phase includes reconstruction or rehabilitation of the most urgent 24 health provider institutions. Implementation of the “Project for Consolidation and Modernization of the Clinical Centre “Mother Teresa“ in Skopje and the Regional Clinical Hospital in Stip will commence in 2016, Loan Agreement for which was signed with CEB in 2015.

Project for Building Physical Education Facilities in Secondary Schools, financed with CEB loan and contribution of the Republic of Macedonia, will continue to be implemented in the coming period. This Project covers construction or reconstruction of 30 physical education facilities aimed at improving the pupils' performance in relation to the subjects they learn, long-term improvement of their health and encouragement of social interaction among pupils with different nationality and abilities.

In addition, realization of the Project for Building Physical Education Facilities in Primary Schools and Rehabilitation of Primary and Secondary Schools in the Republic of Macedonia, financed with CEB loan and contribution of the Republic of Macedonia, will continue, aimed at improving the physical education, as well as the overall learning conditions in the primary and the secondary schools.

Second and third phases of the “Zletovica Water Basin Utilisation Improvement Project” will be implemented with a support by EIB. Main objective of the second phase is provision of irrigation for 4,570 ha net area in the region of Probistip and Kratovo municipalities. Implementation of the third phase, which includes construction of small hydro power plants along the flow of Zletovica River, will provide for reducing electricity shortage in the region, safe, secure and quality supply of energy for the consumers and increased energy efficiency.

Second phase of the “Irrigation Program Southern Vardar Valley”, to continue in 2016 as well, will be financed with KfW loan. This phase, covering rehabilitation and modernization of the irrigation systems in the Southeastern region of the Republic of Macedonia, will contribute to achieving both increased productivity and sustainable development of the agricultural production in this region.

Implementation of the Lake Ohrid Sewage Improvement Project will commence with the support by the Japanese International Cooperation Agency - JICA in 2017. This Project will cover the most urgent measures to be implemented for the purpose of improving the sewerage collector of the Ohrid Lake, by rehabilitating and upgrading the wastewater treatment plant in the region.

To the end of ensuring, exercising and promoting human rights as regards conditions for accommodation, hygiene, health protection and leisure time activities of the convicted and detained persons, the Project for Reconstruction of Houses of Correction, financed with the Council of Europe Development Bank loan, continues to be implemented in 2016. Realization of this Project will

contribute to reconstruction of several houses of correction, thus implementing the standards set in the European Prison Rules.

One of the important elements in the social development policy is to increase the quality of life of low-income persons and the vulnerable groups by providing for their appropriate housing. Government activities and measures as regards social policy are also supported under the Project for Housing of Vulnerable Groups, by investing in construction of flats for low-income persons, the funds being provided under a loan from the Council of Europe Development Bank (CEB). Part of the CEB loan was on-lent to the Joint Stock Company for Construction and Management of Business and Housing Premises of relevance to the Republic of Macedonia – Skopje in 2014 in order to realise the Project more quickly.

Projected Deficit and Its Financing

As for the period 2016-2018, budget deficit is envisaged to gradually reduce, as follows: 3.2% of GDP in 2016, 2.9 of GDP in 2017 and 2.6% of GDP in 2018.

Funding of the projected deficit will be provided from foreign sources (favourable loans from international financial institutions, credit lines intended for financing certain projects, Eurobonds and other type of foreign borrowing) and domestic sources (issues of government securities).

Foreign borrowing as source of financing will be used by budget users for realization of specific projects.

As for the borrowing on the domestic market, Ministry of Finance will continue to issue government securities in the next period as well. The purpose is, by regular issuance of government securities, to provide for more efficient financing of budget needs in the short and long run, reduction of financing costs, as well as encouragement of the further development of the financial markets in the Republic of Macedonia.

In the coming period, Ministry of Finance will continue extending the maturity structure of government securities portfolio by issuing long-term securities, i.e. by issuing 2-, 3-, 5-, 10- and 15-year government bonds. Pension funds, as well as commercial banks and insurance companies, are expected to, in particular, show interest in investing in long-term securities issued by the Republic of Macedonia.

Table 4 (Denar million)

Deficit and financing sources	2016	2017	2018
Budget balance	-18,984	-17,827	-16,993
Deficit financing	18,984	17,827	16,993
Inflows	40,546	39,557	43,675
Foreign sources	22,861	18,100	17,578
Domestic sources	18,894	21,422	25,249
Deposits	-1,209	35	848

Outflows	21,562	21,730	26,682
Repayment upon foreign borrowing	12,381	9,155	10,340
Repayment upon domestic borrowing	9,181	12,575	16,342

Local Government Budget

In the course of 2015, as well as in the medium run, it is expected for the municipalities to continue the trend of strengthened collection of special revenues, strengthening the capacities for development of policies for financing the municipalities and enhancing the capacities for financial management.

For the purpose of realizing the strategic commitments, the strong commitment to encouraging the sustainable local development, good local governance and creating conditions for more active, more effective and more innovative role of the local authorities in implementing the national objectives for growth and development will continue in the next period as well.

Increased revenues from VAT grant (general grant), in the amount of 4.5% of VAT collected in 2013 from the Budget of the Republic of Macedonia, provided for additional stable revenues for municipalities.

New revenues will be provided by allocating funds from lease of state-owned agricultural land to the municipalities the proportion of which is 50% for the Republic of Macedonia and 50% for the municipalities and the municipalities in the City of Skopje depending on the location of the agricultural land being under lease if the revenue performance on the basis of tax on real estate exceeds 80% in relation to the projected ones. During the interim period, the distribution will be carried out in the following proportion: 90%:10% in 2015, 80%:20% in 2016, and 70%:30% in 2017. Additional increase of special revenues of the municipalities is expected to be realized from the fee collected by issuing concession for usage of water resources for electricity generation the proportion of which is 50% for the central budget and 50% for the local authorities, depending on which area the concession activity is performed as of 2016, and, in the meantime, revenues will be distributed in the following proportion: 75%:25%.

Increase of the special revenues of municipalities, in particular revenues on the basis of taxes on real estate, fully including the tax base of natural persons and legal entities and re-assessment of the value of real estate are expected to continue in the next medium-term period. Increase is also expected by applying the improved elements of calculation in the Methodology for Determining the Market Value of the Real Estate. Commencing the application of the legal provisions as regards professional training in determining the value of the real estate for the needs of taxation on the basis of property taxes by evaluators is expected to provide for better quality and more objective assessment of the value of real estate, thus providing the municipalities the possibility to employ an expert – an evaluator or to use the services of licensed evaluators.

In the coming medium-term period, the municipalities will continue to execute the transferred competences for management of construction land and treatment

of facilities illegally built on the construction and agricultural land, for which respective sources of revenues in the municipal budget are determined.

Government of the Republic of Macedonia will continue to carry out the activities aimed at equal regional development and enhancement of all regions in the country in the next period as well. Implementation of the 2009-2019 Strategy for Equal Regional Development of the Republic of Macedonia in the eight planning regions (Vardar, Eastern, Southwestern, Southeastern, Pelagonija, Polog, Northeastern and Skopje regions), by better vertical and horizontal coordination of the national and local policies and the integrated development projects adjusted to the local needs and conditions, will provide for more balanced and local development. Council for Equal Regional Development will continue to play significant role as promoter of partnership between the regions/the municipalities and the Government, within which the usage of funds will be coordinated from all sectoral programs intended for the planning regions and the municipalities. Special efforts will be put for supporting the municipalities, by encouraging the local development via supporting the local projects and harmonizing them with the national ones.

Realization of a series of infrastructure projects related to improvement of the quality of life will appropriately improve the regional development and the active integration in the economy. To that end, a series of projects will be implemented, which will be aimed at improving the overall road infrastructure, bridges, local streets and roads, followed by projects in the field of utility infrastructure (water supply, sewage systems, wastewater treatment station collectors, pedestrian crossings, horticultural arrangement, public hygiene), as well as improving of the infrastructure of villages through urbanization, connection of inhabited areas and construction of local roads, pedestrian crossings and lighting, development and support of rural tourism and recreational centers.

More dynamic local development and quality services of citizens in the next period will be provided by implementing the projects selected as priority projects of the municipalities, which will be financed with long-term subloans within the first and second phase of the World Bank's Municipal Services Improvement Project, by which favourable loans are provided for all municipalities in Macedonia intended for financing infrastructure investments in line with the municipal priorities. Therefore, the municipalities have at their disposal funds they may provide under very favourable conditions, intended for construction and reconstruction of utility infrastructure and water supply systems, energy efficiency of public municipal facilities, procurement of specialized vehicles for utility hygiene, street lighting, local road infrastructure, arrangement of urban areas and similar, as well as performance grants provided within the same project for municipalities, which successfully realize the projects financed with the respective subloan. To the end of improving the services and the quality of life in the rural areas, reducing the social and economic differences, as well as boosting the competitiveness of these areas, funds have been provided through the EU IPA grant funds for rural infrastructure.

At the same time, pursuant to the legal regulations, the municipalities fulfilling the legal criteria to borrow, will be able, in the coming period, to finance their projects by borrowing on the basis of concluding loan agreements at domestic or foreign creditors or on the basis of issuing municipal bonds. Municipalities will be helped to issue first municipal bonds as additional instrument for improving liquidity and providing financial resources for capital and municipal projects.

Government will continue to successfully implement this process within the fully established legal and institutional framework of local government, with developed, responsible and functional local government units and level of local democracy that will bring the citizens closer, as much as possible, to the local government institutions.

Improvement of Public Finance Management

Public finance management is a serious obligation and challenge requiring continuous adjustments, reforms and improvement, particularly in conditions of unpredictable and turbulent economic surrounding. Efficient public finance management and establishing stable fiscal position in the long run provide for solvency as regards the assumed liabilities and the payment of expenditures.

Improvement of public finance management system, by improving the both medium-term budget framework and the transparency, will remain to be the key priority in the next medium-term period.

Thus, during 2015, within the Public Administration Reform Project, in cooperation with the European Commission, SIGMA conducted a mission so as to provide relevant information in the field of public administration and public finances on the basis of collecting data from the relevant institutions. SIGMA will publish the Report on Public Finance Management after the EC's Republic of Macedonia Progress Report is published.

In the course of 2015, public expenditures and financial accountability were assessed in line with the PEFA (Public Expenditure Financial Accountability) Methodology. PEFA assessment is aimed at determining the state of play of the Public Finance Management (PFM) system in the Republic of Macedonia. Report (draft version at the moment) should serve as a common base of information on the dialogue between the Government of the Republic of Macedonia and its partners to the end of improving the public finance management.

Within IPA TAIB 2011, as of November 2015, the Twinning Project "Strengthening the Medium-Term Budgeting for Effective Public Financial Management" is planned to be realized.

Main activities of the Project for Strengthening the Medium-Term Budgeting for Effective Public Financial Management will be focused on determining a program expenditure classification, enhancing the capacities for medium-term planning and reporting in line with ESA Methodology, all to the end of improving the quality of public expenditures.

Main Project objective is improving the public finance management, the central focus being placed on medium-term budget planning as a main precondition for sound public finances and maintenance of stable fiscal position.

Expected results from the Project, apart from the program classification, are also preparation of medium-term fiscal framework, whereby the concept for implementation of MTEF and MTBF will be appropriately defined, and respective legal amendments, manuals and bylaws will be prepared accordingly.

Funds have been provided under IPA 2011 Technical Assistance Facility Envelope for realizing the Project “Development of Proposals for Implementation of Modern Integrated Financial Management Information System”. Under the Project, Ministry of Finance plans to engage experts who are to prepare a study, together with an analysis and assessment of the state of play of the financial management information systems of the Ministry of Finance, and solutions will be proposed for establishing a modern integrated financial management information system.

Use of EU Pre-Accession Assistance

Republic of Macedonia, as a candidate country for EU membership, has the possibility to use financial support from the European Union through the five components under the IPA instrument.

According to the Multi-Annual Indicative Financial Framework, under which EU assistance is allocated to countries and continents, Republic of Macedonia can use funds in the amount of EUR 619.290 million or around Denar 38.1 billion in Denar equivalent through the five IPA Components in the period 2007- 2013.

Out of five IPA Components in total, the assistance for four of them is decentralised starting 2009 (except for IPA Cross-Border Cooperation Component, which is still centralised).

Funds for national co-financed intended from the projects, being decentralized, are planned under the budget of the Ministry of Finance, organizational code 09002 - Functions of the State, as well as under the budget of the Agency for Financial Support in Agriculture and Rural Development, organizational code 14004.

IPA Component 1

Under IPA Component 1, in conditions of decentralised implementation of IPA assistance, four annual National Programs (NP) were prepared and adopted, such as 2009 NP, 2010 NP, 2011 NP, 2012 NP and 2013 NP, and the respective financial agreements were signed. These Programs generally provide support to the state administration in order to enhance its capacities at central and local level, undertake reforms, as well as to fulfill the obligation of the membership more quickly and more efficiently.

National Program TAIB 2009 – Available funds within the National Program for 2009 amounted to EUR 33.1 million. Up to the deadline for concluding contracts (21st December 2013), 75 projects were concluded in the amount of EUR 29.7 million, thus the contracting rate accounted for 89.9%. Out of the total amount of

concluded contracts, 44.2% comprise projects for enhancing the capacities of government institutions, accompanied by projects for procurement of equipment (18.9%) and projects related to approximation of the legislation (17.4%). Implementation of National TAIB Program 2009 is expected to be completed in November 2016.

National Program TAIB 2010 – Available funds within the National Program TAIB 2010 amounted to EUR 30.1 million. As of 1st December 2014, the deadline for concluding contracts, total of 22 projects were concluded, amounting to EUR 18.8 million, i.e. the contracting rate accounted for 62.4%. Under this Program, around 30% of the projects being implemented refer to the sector justice, 43% are intended for building capacities of institutions such as the Ministry of Information Society and Administration, the Public Revenue Office, etc., while the assistance intended for supporting the sectors agriculture and food protection and environmental protection accounts for 13% for each of them. There is ongoing implementation of the projects financed through the National Program TAIB 2010.

Programs of the Union and the Agencies

Starting with the National Program TAIB 2011 of the first IPA Component, the payment of entry tickets for participation in the respective programs for the financial perspective under the period 2014-2020 will be executed under the decentralized implementation system through the National Fund within the Ministry of Finance, whereby, IPA participation is planned within the budget of the Ministry of Finance, while the planning of the national participation is an obligation of the competent institutions within their budget.

Union Programs cover almost every area of social and economic life of European citizens: education, culture, youth, media, social affairs, development of small- and medium-sized enterprises, environment, transport, public health, legal cooperation, fight against violence, crime, terrorism, information society, customs duties and taxes. All legal entities may participate in the Programs, and, in some cases, natural persons from the participating countries may also participate therein.

To the end of participating in the Union Programs, Republic of Macedonia signs a Memorandum of Understanding/Accession Agreement, by which the participation in the Program is legally regulated. As regards paying the entry ticket for participation in the Union Programs, an opportunity is open for using the EU Pre-Accession Funds therefor.

National Program TAIB 2011 – for which around EUR 33 million has been allocated, for which, by the end of 2015, around 32 projects are planned to be concluded aimed at activities related to public administration reforms, support to the reforms as regards the freedom of expression, further support in the field of agriculture and rural policy (with special emphasis on the enhancement of the capacities of IPARD Agency) and approximation towards the Acquis Communautaire in the field of environment (NATURA 2000). So far, agreements in the amount of EUR 3.7 million have been concluded. With respect to the Programs of the Union and the Agencies, all 4 planned agreements have been

concluded and payments there under have been executed, amounting to total of EUR 5.1 million.

At the same time, the **National Program TAIB 2012** (in the total amount of EUR 30.85 million) and the **National Program TAIB 2013** (in the total amount of around EUR 30.6 million) are being implemented. What was introduced for the first time under these two national Programs, was integrated sectoral access when defining the priorities and projects to be financed through IPA TAIB Component, focusing the EU assistance on several priority areas and designing projects, which will enhance the mutual cooperation among institutions from the same or similar area.

Financial assistance within the Program TAIB 2013 is focused on the following six sectors: public administration reform, justice and internal affairs, private sector development, environmental protection and climate changes, agriculture and rural development and participation in the Commission Programs.

As for the Programs of the Union and the Agencies, 8 agreements have been concluded and payments there under have been executed, amounting to EUR 7.2 million, while, in 2016, payments for another 4 agreements are expected to be executed in the total amount of EUR 0.1 million.

IPA Component 3

IPA Regional Development Component is aimed at preparing the country for using the funds from the EU Structural and Cohesion Funds.

As for the period 2007-2013, EUR 199.9 million is available to Macedonia under the IPA Regional Development Component intended for infrastructure projects in the sectors transport and environment.

-There is ongoing implementation of three so-called “large infrastructure projects” as follows: The Project for Construction of New Motorway Section Demir Kapija-Smokvica as Part of Pan-European Corridor X signed in August 2012, being EUR 210,148,177.23 million worth. Construction works have been commenced and according to the agreement, they should be completed by the end of 2016;

- Project for Upgrading and Extension of Sewerage Network in Prilep in the total amount of EUR 16,930,597.52 million, under which, two construction agreements have been planned - Agreement for Construction of Waste Water Treatment Plant in Prilep (signed in 2014) and Agreement for Upgrading and Extension of Sewerage Network in Prilep (signed in July 2013) and

- Project for Renewal with Reconstruction of the Railway Section Bitola-Kremenica, as part of Xd, the implementation of which started in February 2015 and which should be completed by the end of 2016.

At present, 30 projects financed through this Operating Program, are being implemented, most of which in the transport sector, such as the road and railway transport in the Republic of Macedonia. In addition to the three mentioned large projects, other projects are also financed under this Program, related to the following:

- Preparation of project studies and main projects for the railway sections Corridor 8 and Corridor 10
- Construction works for rehabilitation and upgrading of the Railway Station Skopje and its equipping in line with the EU Standards, which should be completed by the end of 2015.
- In April 2015, construction activities aimed at rehabilitating ten (10) railway stations along Corridor 10, commenced;
- Preparation of project documentation for construction of railway line from Kicevo to Lin, to the end of railway connection with the Republic of Albania;
- Preparation of project documentation and implementation of infrastructure activities for construction of wastewater treatment stations in the Municipalities Radovis, Kicevo and Strumica, which are expected to start at the beginning of 2016;
- Preparation of project documentation and implementation of infrastructure activities for rehabilitation of the sewage network in the Municipalities Kumanovo and Berovo, which are expected to start at the beginning of 2016;
- Preparation of project documentation for improving the infrastructure for wastewater treatment in the City of Skopje;
- Preparation of the documentation necessary for upgrading the wastewater treatment plant in Vranista, extension of the collector system for Ohrid Lake and separation of the foul and storm priority water network in the Cities of Ohrid and Struga;
- Rehabilitation of Veles-Katlanovo section, Smokvica-Gevgelia section and Kumanovo-Miladinovci sections (in both directions), as part of the road Corridor X.

These projects will contribute to modernizing the road and railway infrastructure in the Republic of Macedonia. Other significant aspect of most of the financed activities, in both sectors transport and environment, is the fact that they are operations contributing to preparation of the future infrastructure activities in these two areas. This contributes to further building of the portfolio of priority projects to be financed by the Republic of Macedonia in the pre-accession period through IPA, and in future, through the structural instruments following the accession to the EU.

IPA Component 4

IPA Human Resources Development Component supports projects in the field of employment, education and social inclusion. As regards the period 2007-2013, IPA funds in the amount of EUR 56.89 million is available to the Republic of Macedonia under the IPA Human Resources Development Component.

The ongoing activities which are to be financed in the next several years under this Program, are mainly focused on the labour market and the main institutions acting in this sector (for instance Employment Agency, Ministry of Labour and Social Policy, State Labour Inspectorate, etc.) aimed at restructuring and

reforming their operations, all to the end of creating a possibility for more efficient coping with the unemployment. These measures for institutional restructuring are combined with financing of activities directly oriented towards the unemployed people.

On the other hand, IPA funds are also focused on the sector education and training, and among other, on two very significant sub-sectors-vocational education and training, as well as education of adults, which in light of lifelong learning have specific influence on the labour market and the creation of competitive labour force.

At present, there is ongoing realization of 24 projects, while 20 projects have been already completed. Under the projects, a number of activities have been undertaken, among which:

- Modernization of the operations of the Employment Agency of the Republic of Macedonia by establishing methodology and procedures for introducing standard services for unemployed persons and employers in all employment centers, preparation of proposals for both simplifying some of the processes in EARM and improving the manner of planning, monitoring and reporting of Agency's activities;
- Organization of trainings for more than 300 persons from the civil society, the local government, the social partners for preparation and implementation of projects in the field of social inclusion;
- Building capacities of the State Labour Inspectorate by providing technical assistance and equipment in the total amount of EUR 1.3 million;
- Provision of second direct grant for the Employment Agency of the Republic of Macedonia in the amount of around EUR 2 million for co-financing the active employment measures of the Government of the Republic of Macedonia (internship, trainings for general skills and trainings for specialized skills for the unemployed persons);
- Construction activities for rehabilitation and modernization by procuring equipment for the local employment centers and the centers for social work on the territory of the Republic of Macedonia;
- In September 2014, direct grant in the total amount of EUR 1.2 million was allocated to the International Labour Organization (ILO) as support to the social dialogue.

IPA Component 5

IPA Rural Development Component supports projects that will provide for attaining EU standards introduced in the field of agricultural production, food processing and rural development. In the period 2007-2013, total of EUR 67.65 million was available to the Republic of Macedonia under this Program, which amount was reduced to EUR 32.55 million since it was decommitted in 2012, 2013 and 2013.

In addition, for the purpose of preventing decommitment of 2013 allocations, funds in the amount of EUR 18 million were transferred from this Component into

Component 1. These funds will be allocated as a direct World Bank's grant intended for supporting the rural infrastructure.

In the period 2009-2015, eleven public calls were realised and agreements were signed between the Agency for Financial Support in Agriculture and Rural Development and the final beneficiaries, in the amount of EUR 11.45 million.

Assistance through this Component is aimed at supporting projects related to investments in agriculture and processing capacities and marketing of agricultural products and fish. These investments will contribute to improvement of the quality and safety of food and cattle, increased competitiveness of farmers by using modern production technologies and reduced production costs, promotion of ecological methods of production, improvement of the performance of farms in primary production and marketing so as to attain EU standards in the field of environmental protection, public health status (food quality and safety), safety at work, opening new markets, improvement of management of animal waste and waste waters, as well as job creation.

Measures for diversification and rural development will be realised through support to rural tourism, support to small- and medium-sized enterprises for modernization of farm production, modernization/adaptation of the infrastructure, encouraging traditional craftsmanship, support to rural and agricultural services (organizing workshops for maintenance and repair of agricultural machines and tools, construction of youth centers, children playgrounds, procurement of office supplies).

IPA 2

In future, Republic of Macedonia will continue to use financial assistance from the European Commission through the Instrument for Pre-Accession Assistance - IPA 2 within the new financial perspective under the period 2014-2020. Preparatory activities for accreditation of the 2014 Programs are ongoing. Accreditation of IPA 2 is expected to be granted by the end of 2015, when its implementation is to start.

IPA 2 Regulation introduces certain changes that influence the programming of the assistance for the period 2014-2020 for more coherent and strategic access to pre-accession assistance. In fact, so-called sectoral access in programming is introduced, where the components are replaced with "areas of acting" so as to increase continuity in the actions and encourage closer cooperation among the European Commission's services in determining one and common strategy for each separate country.

IPA 2 Regulation indicates that the financial assistance will mainly refer to five areas:

- reforms in the preparation for EU membership and building capacities of the related institutions,
- social and economic and regional development,
- employment, social policies, education, promotion of gender equality and development of human resources,

- agriculture and rural development and
- regional and territorial cooperation.

2014 IPA Program was approved by IPA Management Committee in EC on 28th November 2014.

- Action Document - Support to the Justice Sector;
- Action Document - Implementation of Business Continuity and Disaster Recovery System- phase 2;
- Action Document - Further Development of the Capacities for Crime Scene Investigation;
- Multi-Annual Sectoral Operational Program for Transport 2014 -2020;
- Multi-Annual Sectoral Operational Program for Environment and Climate Action 2014-2020;- Action Document – Support to Participation in Union Programs; - Action Document - Local and Regional Competitiveness and
- Action Document – EU Integration Facility

In addition, the new 2014-2020 IPARD Program was finalized. It is proposed for the Program implementation to start with 3 already accredited measures (1.1 Investments in fixed assets of agricultural enterprises, 1.3 Investments in fixed assets for processing and marketing of agricultural and fish products and 3.2. Diversification of agricultural enterprises and development of businesses) and two additional measures for which preparatory activities for accreditation were commenced (3.1 Improvement and development of rural infrastructure and 4.2. Technical assistance for implementation of the Program).

IV. TRENDS OF PUBLIC DEBT OF THE REPUBLIC OF MACEDONIA

Public debt management policy sets the framework for the Government of the Republic of Macedonia to act towards prudent public debt management in the medium run. Public debt management policy, in the medium run, gives instructions, i.e. sets goals and measures necessary to be realised for the purpose of providing the necessary financial resources. Main measures and activities the Ministry of Finance undertakes for achieving the already defined goals are the following:

- financing the needs of the state with the lowest cost possible, in the medium and long run and sustainable level of risk;
- identifying, monitoring and managing the risks which public debt portfolio is susceptible to; and
- developing and maintaining efficient domestic financial market.

Pursuant to the Public Debt Law (Official Gazette no. 145/2014), the public debt is broader definition about the debt, including the government debt and the guaranteed debt of public enterprises and companies fully or dominantly owned by the state or the debt of municipalities.

Government debt comprises financial liabilities incurred on the basis of borrowing by the Republic of Macedonia, public institutions established by the

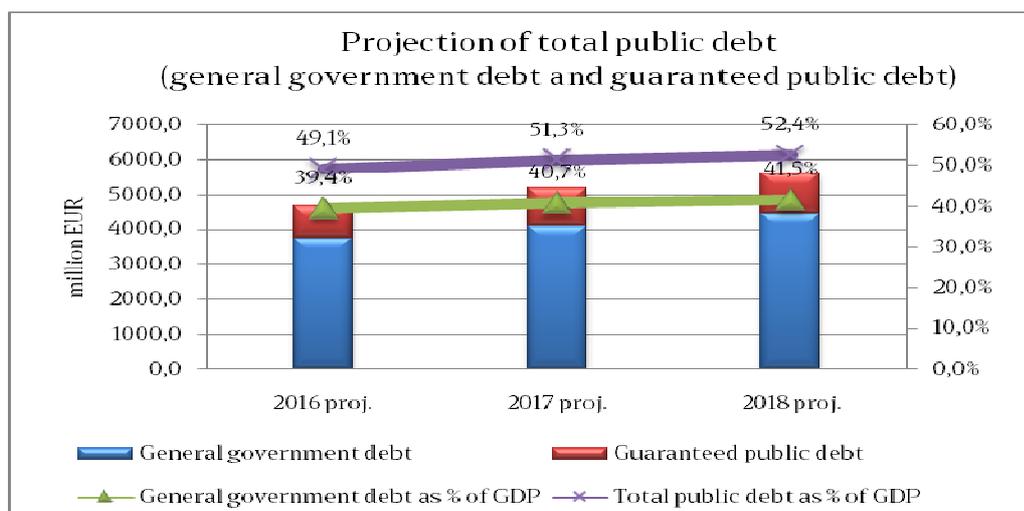
Republic of Macedonia and the municipalities, the municipalities within the City of Skopje and the City of Skopje.

As a result of the prudent fiscal policy in the past years, public debt at the end of the first half of 2015 accounted for 43.7%, while government debt accounted for 36.1% of GDP. Thereby, Republic of Macedonia remains to be moderately indebted country, the government debt being significantly lower than the average debt level of the EU countries.

Investments launched in the past period in the field of road and rail infrastructure, water supply and sewerage, sports facilities, education, health, energy, construction of the National Gasification System, as well as other projects that are in line with the Programme of the Government of the Republic of Macedonia, are expected to continue realizing in the period 2016 - 2018. The projects, co-financed with foreign loans, will be implemented by the state administration bodies, strongly committed not to jeopardize the long-term sustainability of the debt level of the country.

On the basis of such commitment, trends of public debt, including the government debt and the guaranteed debt, will be retained within the projections, i.e. there will be moderate growth that will not jeopardize the sustainability of public finances.

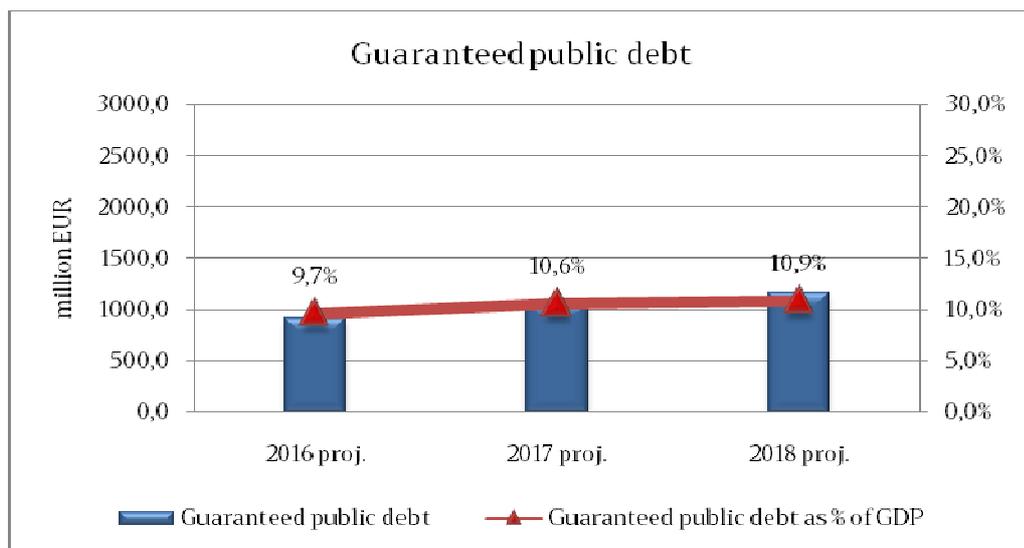
Chart 8 - Projection of total public debt



Source: Ministry of Finance

Sustainable level of guarantees issued over the next three years is of great importance for the Ministry of Finance and therefore when selecting projects to be issued with sovereign guarantee, special emphasis will be placed on those projects that are in line with the strategic priorities of the Government of the Republic of Macedonia, being self-sustaining, generating income, supporting the economic growth, and, in the medium run, providing for boosted competitiveness of the domestic economy and having justification for the purpose for which the funds are used.

Chart 9 - Guaranteed public debt



Source: Ministry of Finance

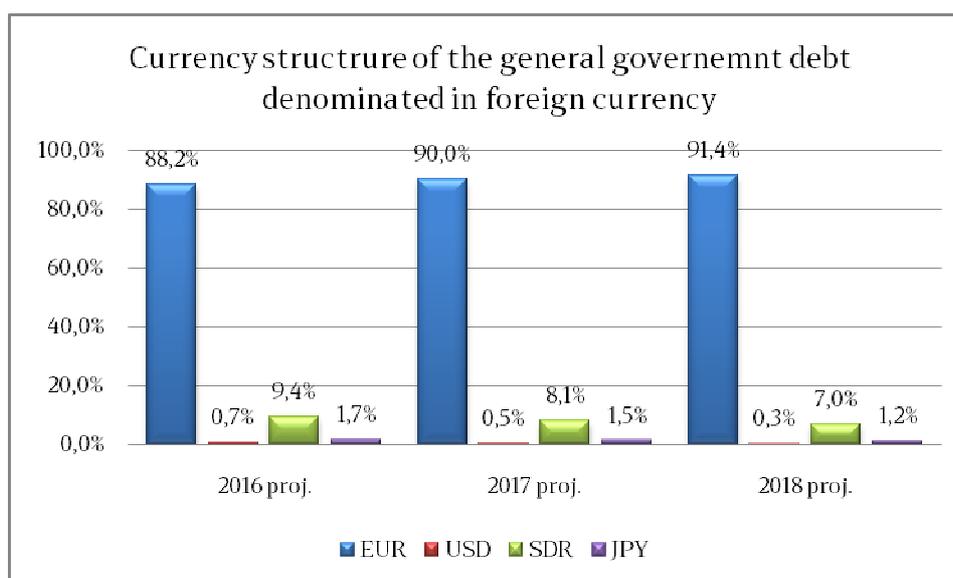
Currency Structure of Government Debt Denominated in Foreign Currency

Changes in the exchange rate risk could largely affect, i.e. increase the envisaged costs for repayment of the debt denominated in foreign currency. However, taking into account the fact that since 1995, the Republic of Macedonia applies de facto fixed exchange rate of the denar in relation to the Deutsch Mark, and since 2002 onwards, in relation to the euro, the exposure to such risk would be measured also as a share of the euro in the total debt portfolio.

Ceiling for the currency structure of the government debt:

In the period 2016-2018, the share of euro-denominated debt to be at least 80% of the foreign currency debt portfolio.

Chart 10 - Currency structure of government debt



Source: Ministry of Finance

Interest Structure of Government Debt

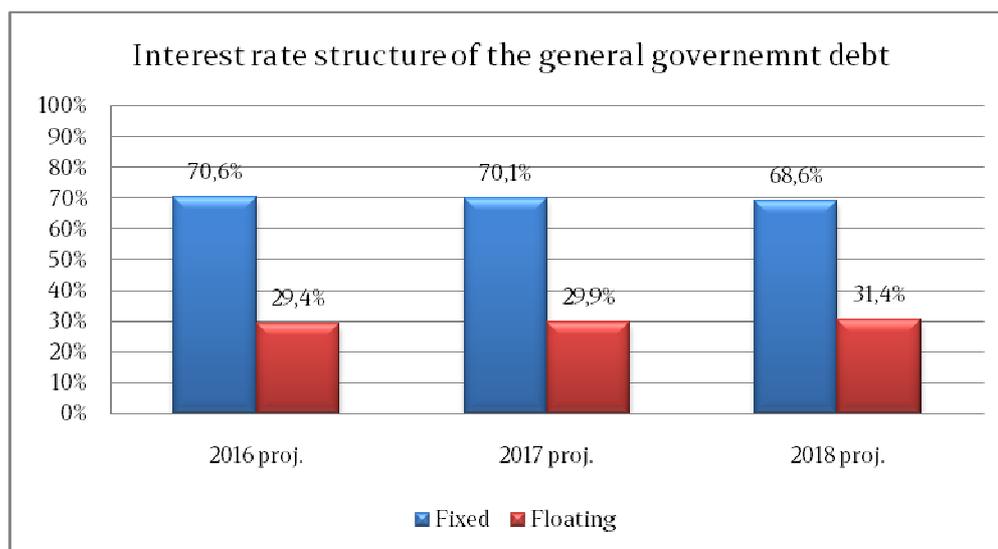
In order to protect the government debt portfolio against possible future market shocks from adverse changes of interest rates that directly lead to increase of the costs to the Budget of the Republic of Macedonia, maintaining optimal interest structure of the government debt portfolio is one of the objectives at which debt managers should aim.

Ceiling for the interest structure of the government debt

In the period 2016-2018, the share of debt with fixed interest rate should be at least 50% of the total debt portfolio.

Taking into account the current structure of the government debt portfolio, as well as the medium-term projections, the fixed interest rate debt exceeds the set ceiling as a result of the commitment of the Ministry of Finance to issue long-term securities with fixed interest rate on the domestic market. In addition, repayment of the debt towards IMF contributed to reducing the variable interest rate debt in the interest structure of the debt portfolio.

Chart 11 - Currency structure of government debt



Source: Ministry of Finance

Risk Management Indicators

Uncertainty arising from the future trends of macroeconomic variables on the international and domestic capital market significantly affects the reaching of decisions for efficient management of the debt portfolio of the country. Accordingly, within this Strategy, limits for the debt refinancing indicator (showing the average time for refinancing the debt), as well as for the indicator of measuring the interest rate risk (showing the average time for changing the interest rates of the debt portfolio) are calculated.

Limit for refinancing risk In order to protect the central government debt portfolio against the refinancing risk, the minimum level of the "average time to maturity" indicator in 2016 should be 3 years.

Limit for interest rate risk:

In order to protect the central government debt portfolio against the interest rate risk, the minimum level of the "average time to refixing" indicator in 2016 should be 2 years.

MEASURES TO IMPLEMENT PUBLIC DEBT MANAGEMENT STRATEGY

Development of Government Securities Market

Ministry of Finance will continue to regularly issue government securities (GS) on the domestic market in the coming period as well. The purpose is, by regular issuance of government securities, to provide for more efficient financing of budget needs in the short and long run, reduction of financing costs, as well as encouragement of the further development of the financial markets in the Republic of Macedonia.

In the upcoming period, Ministry of Finance will intend to both retain regular issuance of treasury bills and stay focused on expanding the maturity structure of the portfolio of government securities with longer maturities. Thus, special emphasis will be put on extending the maturity of the existing government securities portfolio.

This measure will be realized through the following activities:

- issuance of government bonds with 10-year maturity period at least 4 times per year;
- issuance of government bonds with 15-year maturity period at least 4 times per year;
- Issuance of government bonds with maturity period of 2, 3 or 5 years on regular basis;
- reduction of the share of government securities with foreign exchange clause in the total issued government securities;

Special interest in investing in long-term securities issued by the Republic of Macedonia is expected from the pension companies, as well as from commercial banks and insurance companies.

To the end of improving and further developing the government securities market, activities aimed at expanding the investor base will be continued, by considering the possibility to introduce new financial instruments, adequate to the needs of the market participants, carrying out marketing campaign before different target groups of investors and maintaining regular dialogue with all participants on the government securities market.

So-far experience in issuing GS pointed out to the conclusion that frequency of issuing securities corresponds to the market needs and accordingly, the dynamics will continue to be carried out in line with the market conditions.

RISKS IN PUBLIC DEBT MANAGEMENT

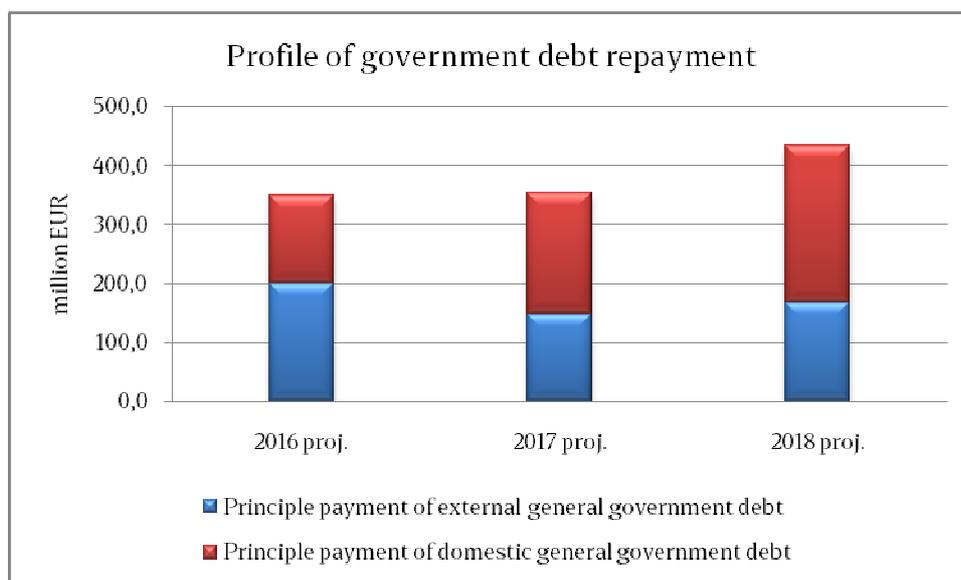
In conditions of large oscillations of economic variables, a need arises to actively manage the risks which the debt portfolio in the Republic of Macedonia is exposed to.

Following appear as main risks identified at managing the debt portfolio of the Republic of Macedonia:

1. Refinancing risk:
2. Market risk, including the following risks:
 - Interest rate risk
 - Exchange rate risk
3. Risk associated with the contingent liabilities and
4. Operational risk

Refinancing risk is managed by preventing major part of the liabilities to fall due at once at any time and providing evenly distributed maturity of debt-related liabilities. Exposure of public debt portfolio to refinancing risk is measured by the debt repayment profile and the indicator showing the average time to maturity.

Chart 12 –Profile of government debt repayment



Source: Ministry of Finance

Table 5 - Average Time to Maturity- ATM (years)

	2016	2017	2018
Domestic debt	2.3	2.5	2.6
External debt	5.7	5.2	4.8
Central government debt	4.3	4.1	3.8

Source: Ministry of Finance

Market risk is determined by the exposure of the debt portfolio to economic variables, especially the variation of interest rates on the domestic and the international capital markets and the trends in foreign exchange rates. Market risk may be divided into two components, i.e. the interest rate risk and the exchange rate risk. Identifying and managing market risks in the Republic of Macedonia is crucial for the debt portfolio since this risk is determined mainly by external factors, i.e. variations in interest rates on the international financial markets, where, due to their constant turbulences, the medium- and long-term trend is very difficult to project.

Measuring and managing interest rate risk is especially important in the countries where domestic financial markets are underdeveloped and the need to borrow is covered from external sources under non-concessional terms, where exposure to interest rate risk is greater. The variation of interest rates on the domestic and international markets affects the debt-related costs, especially when the fixed interest rate debt should be refinanced or on the day when the interest is re-set for variable interest rate debt. Hence, close connection between the interest rate risk and the debt re-financing risk is evident.

ATR indicator measures the average time to refixing. Higher value of this indicator shows that larger portion of the debt portfolio will not be subject to significant interest rate refixing and such portfolio is a lower risk one.

Table.6 Average time to refixing (years)

	2016	2017	2018
Domestic debt	2.3	2.5	2.6
External debt	4.4	3.9	3.3
Central government debt	3.5	3.3	3.0

Source: Ministry of Finance

Exchange rate risk refers to debt indexed or denominated in foreign currency. Major portion of the debt denominated in foreign currency in relation to the total debt points out to higher exchange rate risk. This risk is crucial for the developing countries where external debt is fully indexed, and major portion of the domestic debt is denominated in foreign currency.

As a result of the projected investments being exceptionally important for the further development of the energy sector, the infrastructure, as well as the support of small- and medium-sized enterprises, moderate but controlled increase of the level of guaranteed public debt is projected in the coming period. In order to obtain better conditions for financing by the creditors, the state issues sovereign guarantee, after carried out comprehensive analyses of the borrower and its ability to independently service any future debt. Taking into account the risk the state may face in future in case the issued guarantees are called-up, analysis was made as regards the possible increase of the costs related to servicing the matured debt.

Guaranteed debt in relation to GDP maturing in the period 2016-2018 register moderate upward trend, however it will be independently serviced by borrowers. In order for the Budget of the Republic of Macedonia not to be exposed to risk of calling-up guarantees, the process of issuance of new guarantees is strictly regulated and it is subject to certain criteria the claimants of guarantees should fulfill, as well as to assessment of risks to which they are subject.

Operational risk includes the settlement risk and the error risk. Settlement risk appears if a number of non-automated activities are used during data processing, while error risk often refers to the manner of division in executing the transactions and functions related to settlement across the units within the institution in charge of the public debt management. Public debt management is carried out by an information system and adequate software platform, thus significantly reducing the risk from human resources. In addition, the use of this information system provides for reducing the intensity of manual daily tasks, i.e. more time is spent in performing more productive activities. In addition, measures for applying the "four eyes" principle are being undertaken on time, so as to avoid the risk from untimely performance of the tasks in case the responsible person is prevented from fulfilling the working tasks due to whatever reason.

Sensitivity of Servicing-Related Costs

In order to examine the exposure of the debt portfolio of the Republic of Macedonia to market risk, i.e. interest rate risk and exchange rate risk, influence of variations of interest rates and exchange rate over the costs for servicing the external government debt was analyzed.

Table 7:

Sensitivity analysis of servicing-related costs of the external government debt when changes occur in both the interest rates and the foreign exchange rates

<i>index numbers</i>	2016	2017	2018
Baseline scenario	100.0	100.0	100.0
Scenario I - increase of corresponding interest rates by 1 percentage point	107.7	107.2	107.3
Scenario II - increase of corresponding interest rates by 2 percentage points	115.4	114.4	114.6
Scenario III - appreciation of other currencies in the portfolio in relation to the euro by 10%	101.1	101.4	101.2
Scenario IV - appreciation of other currencies in the portfolio in relation to the euro by 10%	98.9	98.6	98.8

Such sensitivity analysis of the trends at the servicing-related costs in the Budget of the Republic of Macedonia on the basis of external debt is based on the following assumptions:

- by changing one variable, all other variables remain unchanged, i.e. ceteris paribus.
- in conditions of possible currency movements in relation to the euro, Denar exchange rate in relation to the euro retains the stable value,
- non-correlation between interest rate movements and exchange rate movements.

Main conclusions that may arise from this analysis are some of the following:

1. servicing-related costs on the basis of interest on external government debt are sensitive to the interest rate movements. Should interest rates in 2016 surge by 1 percentage point, it would cause for interest-related costs to increase 7.7%. Such sensitivity could be explained as a result of exposure of debt portfolio to interest rate risk, being a result of the relatively high share of the variable interest rate debt portfolio.
2. future euro appreciation/depreciation, in relation to the other currencies in the portfolio (US dollar, Japanese yen and special drawing rights) by 10% will cause an increase/decrease of servicing-related costs by 1.1% in 2016. Given the obtained results, it may be concluded that possible unfavourable trends at exchange rates of other currencies in relation to the euro will not cause any significant increase of the servicing-related costs, as a result of the fact that most of the external government debt is euro-denominated.