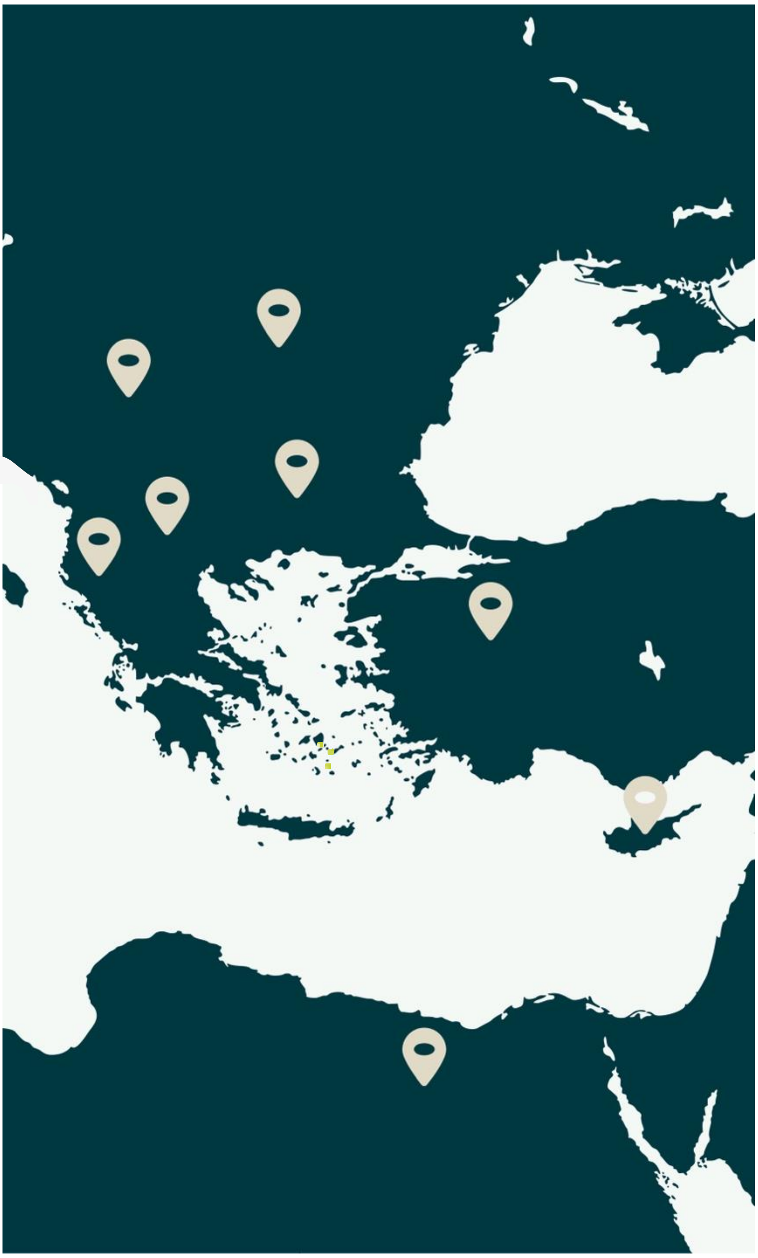
Bi-WEEKLY REPORT

Emerging Markets Analysis

2 – 15 April 2024



COUNTRIES IN FOCUS:

North Macedonia & Serbia

Economic activity should firm gradually through the course of 2024, underpinned by wage-driven private consumption, lower inflation and accelerating public investment, with full-year GDP growth projected at a modest 2.1%

The opposition VMRO-DPMNE stands ready to return to power

Further delays in the EU accession process are on the cards

Banks' profitability skyrocketed in FY:23, on the back of higher interest rates

Banking sector's profitability is set to remain at high levels in FY:24

APPENDIX:

NATIONAL BANK OF GREECE

NBG – Economic Analysis Division

https://www.nbg.gr/en/group/studies-and-economic-analysis

Emerging Markets Analysis

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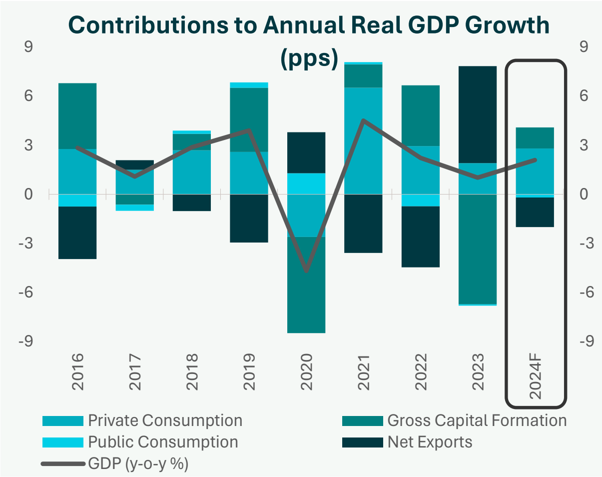
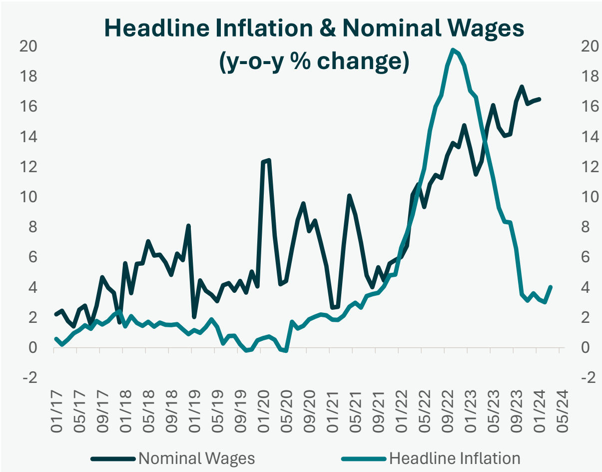
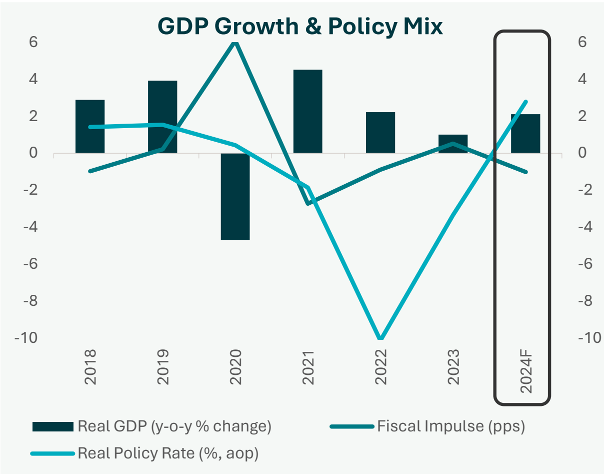
North Macedonia

BB- / NR / BB+ (S&P / Moody's / Fitch)







	15 Apr.	3-M F	6-M F	12-M F
1-m SKIBOR (%)	4.4	4.3	3.9	3.5
MKD/EUR	61.6	61.6	61.6	61.6
Sov. Spread (2028, bps)	296	290	285	270

	15 Apr.	1-W %	YTD %	2-Y %
MBI 100	7,061	-0.9	15.4	16.4

	2021	2022	2023	2024F	2025F
Real GDP Growth (%)	4.5	2.2	1.0	2.1	3.3
Inflation (eop, %)	4.9	18.7	3.6	3.4	2.4
Cur. Acct. Bal. (% GDP)	-2.8	-6.1	0.7	-0.8	-1.5
Fiscal Bal. (% GDP)	-5.3	-4.4	-4.9	-3.9	-3.3

Sources: Reuters, NBRNM, MAKSTAT, Ministry of Finance & NBG

Economic activity should firm gradually through the course of 2024, underpinned by wage-driven private consumption, lower inflation and accelerating public investment, with full-year GDP growth projected at a modest 2.1%. With inflation consolidating at lower levels (3.3% in FY:24, down from 9.5% in FY:23, but still above the past decade's average of c. 1.0%), growth in private consumption is set to rebound, sustained by strong real wage growth. The latter has climbed into double-digit rates since Q4:23, mainly thanks to a loose incomes policy and its spillover to the private sector. Note that labour market conditions have been tightening, as suggested by the declining unemployment rate, but mostly due to falling participation and shrinking labour force (with the latter largely associated with immigration).

At the same time, fixed investment is set to gain momentum, with public sector holding the lead role, following the construction of the Corridor 8/10d (road and rail) highway. Private investment (including from FDI, which has proven resilient so far, thanks, *inter alia*, to the growing nearshoring trend) is also set to add to overall growth, albeit modestly.

Worryingly, amid sluggish growth in the EU (especially Germany, which absorbs 45% of the country's exports) and firming domestic demand, especially gross capital formation (due, *inter alia*, to the need to replenish inventories, which have been depleted, amid disruptions in global supply chains), net exports should turn into a drag on overall growth.

Aside from the positive contribution of increasing public investment, policies are not expected to sustain economic growth this year. On the one hand, after stalling in FY:23. fiscal consolidation is set to resume in FY:24, following the phasing-out of energy subsidies. On the other hand, given strong upside risks to inflation and the need to avoid maintaining significant price differentials with euro area, the country's main trade partner, the NBRNM cannot but maintain a cautious stance, with the first cuts in the policy rate expected in H2:24.

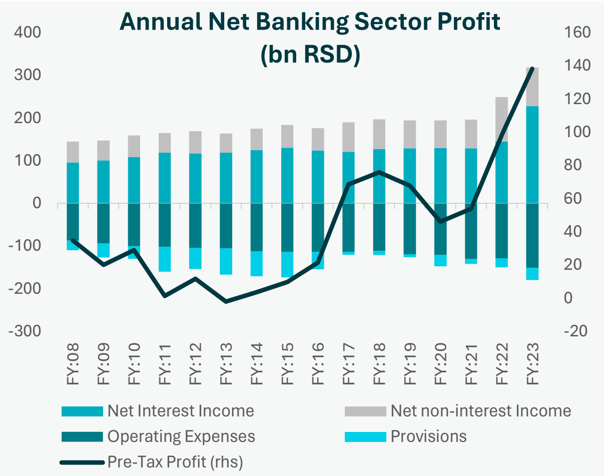
All said, GDP growth is set to pick up to 2.1% in FY:24 from 1.0% in FY:23, slightly below the regional average, with the output gap remaining negative, largely due to the significant output losses recorded during the pandemic and the subsequent energy crisis. Should delays in the execution of the ambitious public investment programme arise or price pressures re-emerge (reflecting repercussions from geopolitical tensions and/or a price-wage spiral), GDP growth could come in lower than projected.

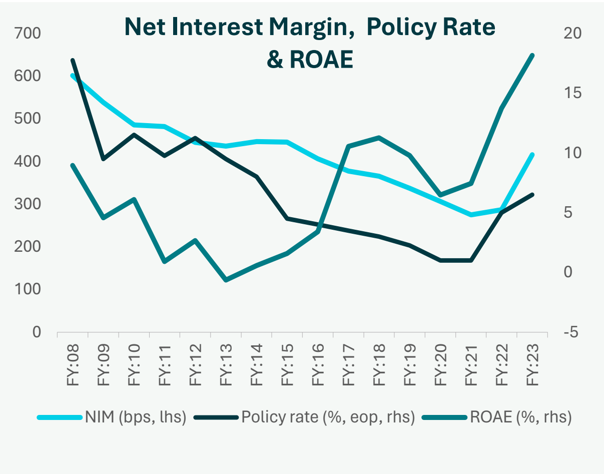
The opposition VMRO-DPMNE stands ready to return to power. Parliamentary election is scheduled for May 8, along with the 2nd (if needed) round of Presidential election. After 6½ years in opposition, the right-wing nationalist VMRO-DPMNE is poised to return to power, currently leading the polls over the outgoing centre-left SDSM by a wide margin (of more than 15 pps). However, it appears that the VMRO-DPMNE would not be able to secure an absolute majority of seats in Parliament, meaning that it would need to team up with one or more allies to form a Government. In this context, the ethnic Albanian "European Alliance for Change" could emerge as the kingmaker, replacing in this role the largest ethnic Albanian party, DUI, junior partner in the outgoing ruling coalition.

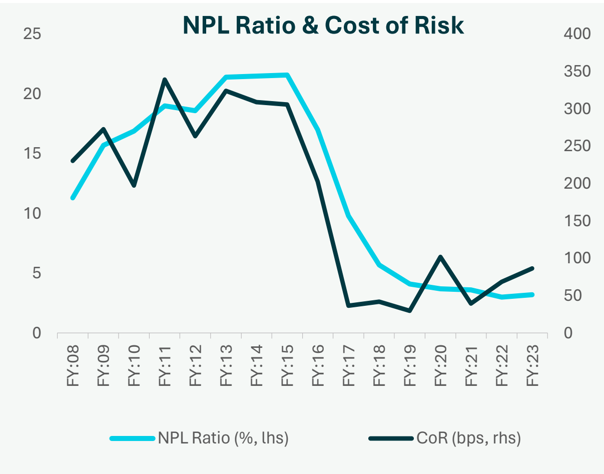
Further delays in the EU accession process are on the cards. Recall that, in a bid to unlock EU membership talks, the Government of North Macedonia reached a compromise deal with that of Bulgaria in mid-2022, settling the two countries' long-standing dispute. According to the deal, North Macedonia's Parliament should endorse constitutional changes, providing, among others, for the recognition of a Bulgarian minority in the country. The outgoing Government did not manage to pass them, due to lack of appropriate ($^2/_3$^{rds}) majority in Parliament. Worryingly, given the VMRO-DPMNE's firm opposition to the amendment of the constitution, and considering its projected representation in the next Parliament, the formation of such a supermajority appears a distant prospect.

Serbia

BB+ / Ba2 / BB+ (S&P / Moody's / Fitch)







	15 Apr.	3-M F	6-M F	12-M F
1-m BELIBOR (%)	5.6	5.4	5.0	4.6
RSD/EUR	117.0	117.5	117.5	117.5
Sov. Spread (2029, bps)	262	255	248	230

	15 Apr.	1-W %	YTD %	2-Y %
BELEX-15	1,000	0.8	14.3	16.9

	2021	2022	2023	2024F	2025F
Real GDP Growth (%)	7.7	2.5	2.5	3.7	3.5
Inflation (eop, %)	7.9	15.1	7.6	2.8	3.4
Cur. Acct. Bal. (% GDP)	-4.2	-6.9	-2.6	-4.2	-5.4
Fiscal Bal. (% GDP)	-4.1	-3.2	-2.2	-2.0	-1.5

Sources: Reuters, NBS, OPBC & NBG estimates

Banks' profitability skyrocketed in FY:23, on the back of higher interest rates. Banking sector's pre-tax profits surged by 40.6% to RSD 138.2bn (1.7% of GDP) in FY:23, leading the ROAE and ROAA to historic highs of 18.0% and 2.4%, respectively, from 13.8% and 1.9% in FY:22.

Stronger net interest income (NII, up 57.5%), on the back of higher interest margins, was the main driver behind the jump in profitability. Indeed, fast repricing of loans, in an environment of rising interest rates (with the NBS's key policy rate having increased by 550 bps since April '22), lifted the net interest margin (NIM) to 416 bps in FY:23 -- more than double that of EU banks -- from 287 bps in FY:22. NII would have been even higher without the NBS's measure capping lending rates on housing loans during FY:22-23. At the same time, growth in banks' loan portfolio slowed down markedly to 1.1% y-o-y at end-2023 from 6.9% a year ago, reflecting not only the impact of the NBS's (and ECB's) measures to curb lending growth (including a hike in banks' required reserves on both RSD and FX-denominated liabilities in September '23) and banks' tightened credit standards, but also a negative base effect from the maturing of the state guarantee scheme for loans to businesses hit by the pandemic.

Increased top line revenue was only partly offset by a broad-based rise in operating expenses (up 17.5% in FY:23), in line with higher inflation. That said, the cost-to-income ratio improved sharply to c. 48.0% in FY:23 from c. 52.0% in FY:22, below that of EU banks (c. 56%).

Unsurprisingly, given challenges stemming from high inflation and interest rates, provisioning charges were raised in FY:23, (with the cost of risk increasing modestly by 18 bps to 86 bps, higher than that of EU banks), putting a lid on profits. Note that the NPL ratio inched up only slightly, from 3.0% at end-2022 to 3.2% at end-2023 yet remaining among the lowest in the region.

Banking sector's profitability is set to remain at high levels in FY:24. Moderating inflation (projected at 4.0% on average in in FY:24 against 12.5% in FY:23) should prompt the NBS to start easing its stance in mid-year (with a total cut of 125 bps predicted by year-end). Against this backdrop, we are inclined to believe that NIM has exhausted its upside potential. Still, banks' abundant liquidity (with a loan-to-deposit ratio of less than 70%) advocates for a slow adjustment in interest margins. At the same time, credit growth is expected to pick up, but at a very slow pace, following, *inter alia*, easing in banks' lending standards. As a result, following an outstanding performance in FY:23, net interest income growth is set to cool down significantly in FY:24.

At the same time, despite the envisaged acceleration in GDP growth (to 3.7% in FY:24 from 2.5% in FY:23), elevated interest rates should prompt banks to take significant loan loss provisions this year as well. On the other hand, operating expenses are due to continue rising, albeit at a slower pace, in line with easing inflation.

All said, banks should see profitability in terms of ROAE/ROAA hovering around record-high levels in FY:24 as well, before moderating to high double-digit figures from FY:25 onwards.

Importantly, solid profitability has been translated into stronger capital buffers, with the capital adequacy ratio firming to 21.4% at end-2023 (more than 90% of which constitutes CET1) from 20.2% at end-2023, well above the minimum regulatory threshold of 8.0%, suggesting significant headroom to absorb any potential stress. Note that banks' capitalization has been supported by the NBS's temporary measure to exclude unrealized losses from government bond valuation in CET1 calculations in FY:22-23. The measure is expected to lapse at end-2024.

Consolidation in the banking sector continued in FY:23, with AIK Bank acquiring Eurobank Direktna and Raiffeisen Bank officially merging with RBA Bank, to form the 3rd and 4th largest banks in terms of assets, respectively.

DETAILED MACROECONOMIC DATA

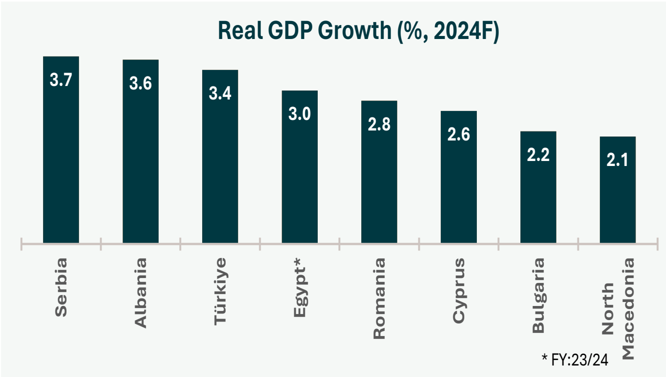
NORTH MACEDONIA	2021	2022	2023	2024f	2025f
Real Sector					
Nominal GDP (EUR million)	11,855	13,053	13,667	14,404	15,281
GDP per capita (EUR)	6,454	7,135	7,501	7,937	8,454
GDP growth (real, %)	4.5	2.2	1.0	2.1	3.3
Unemployment rate (%, aop)	15.4	14.4	13.1	12.9	12.6
Prices and Banking					
Inflation (%, eop)	4.9	18.7	3.6	3.4	2.4
Inflation (%, aop)	3.2	14.0	9.5	3.3	2.7
Loans to the Private Sector (% change, eop)	8.0	8.8	5.2		
Customer Deposits (% change, eop)	8.5	5.1	9.5		
Loans to the Private Sector (% of GDP)	52.5	51.9	52.1		
Retail Loans (% of GDP)	27.5	26.4	26.9		
Corporate Loans (% of GDP)	25.0	25.3	25.1		
Customer Deposits (% of GDP)	60.7	58.0	60.7		
Loans to Private Sector (% of Deposits)	86.5	89.5	85.9		
Foreign Currency Loans (% of Total Loans)	40.7	42.6	42.0		
External Accounts					
Merchandise exports (EUR million)	6,041	7,320	7,292	7,640	7,952
Merchandise imports (EUR million)	8,378	10,801	9,868	10,534	11,118
Trade balance (EUR million)	-2,337	-3,481	-2,576	-2,894	-3,166
Trade balance (% of GDP)	-19.7	-26.7	-18.9	-20.1	-20.7
Current account balance (EUR million)	-0,329	-0,797	-0,095	-0,114	-0,233
Current account balance (% of GDP)	-2.8	-6.1	0.7	-0.8	-1.5
Net FDI (EUR million)	0,388	0,654	0,523	0,471	0.499
Net FDI (% of GDP)	3.3	5.0	3.8	3.3	3.3
International reserves (EUR million)	3,643	3,863	4,538	4,838	5.038
International reserves (Months[a])	4.5	3.7	4.6	4.6	4.5
Public Finance					
Primary balance (% of GDP)	-4.1	-3.3	-3.4	-2.5	-2.0
Fiscal balance (% of GDP)	-5.3	-4.4	-4.9	-3.9	-3.3
Gross public debt [b] (% of GDP)	59.8	58.5	61.5	62.8	62.7
External Debt					
Gross external debt (EUR million)	9,577	10,856	11,453	12,028	12,531
Gross external debt (% of GDP)	80.8	83.2	83.8	83.5	82.0
External debt service (EUR million)	2,689	2,558	4,043	3,761	4,342
External debt service (% of reserves)	73.8	66.2	89.1	77.7	86.2
External debt service (% of exports)	34.5	26.5	40.7	35.9	39.5
Financial Markets					
28-d CB bill rate (%, eop)	1.3	4.8	6.3	5.3	4.5
28-d CB bill rate (%, aop)	1.3	2.5	5.8	6.0	4.7
1-Y T-bill rate [c] (%, eop)	0.7	3.5	4.3	3.5	3.0
Exchange rate: EUR (eop)	61.6	61.6	61.6	61.6	61.6
Exchange rate: EUR (aop)	61.5	61.5	61.5	61.6	61.6

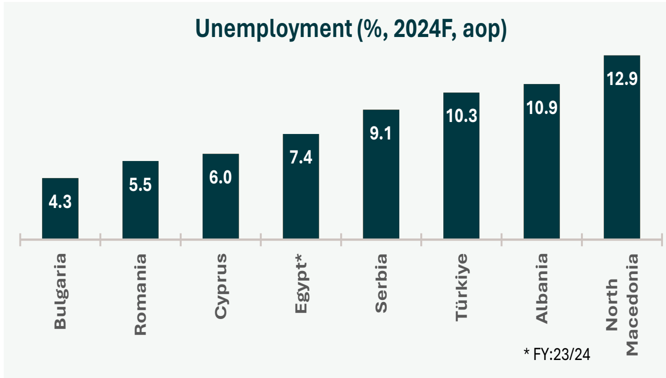
f: NBG forecasts; a: months of imports of GNFS; b: incl. guaranteed debt; c: primary market

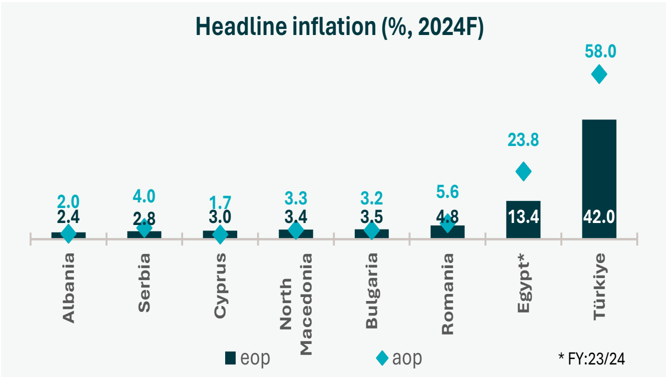
SERBIA	2021	2022	2023	2024f	2025f
Real Sector					
Nominal GDP (EUR million)	53,379	60,463	69,858	75,283	80,589
GDP per capita (EUR)	7,810	8,909	10,356	11,205	12,043
GDP growth (real, %)	7.7	2.5	2.5	3.7	3.5
Unemployment rate (%, aop)	11.2	9.6	9.5	9.1	8.8
Prices and Banking					
Inflation (%, eop)	7.9	15.1	7.6	2.8	3.4
Inflation (%, aop)	4.1	11.9	12.5	4.0	3.6
Loans to the Private Sector (% change, eop)	10.1	6.9	1.1		
Customer Deposits (% change, eop)	13.3	6.9	11.7		
Loans to the Private Sector (% of GDP)	47.3	44.7	39.2		
Retail Loans (% of GDP)	21.9	20.5	18.0		
Corporate Loans (% of GDP)	25.4	24.2	21.2		
Customer Deposits (% of GDP)	52.1	49.2	46.4		
Loans to Private Sector (% of Deposits)	90.9	90.8	84.5		
Foreign Currency Loans (% of Total Loans)	61.1	64.1	64.7		
External Accounts					
Merchandise exports (EUR million)	21,018	26,928	27,930	29,239	30,527
Merchandise imports (EUR million)	27,038	36,292	34,534	37,510	40,410
Trade balance (EUR million)	-6,020	-9,364	-6,604	-8,271	-9,884
Trade balance (% of GDP)	-11.3	-15.5	-9.5	-11.0	-12.3
Current account balance (EUR million)	-2,266	-4,162	-1,810	-3,135	-4,370
Current account balance (% of GDP)	-4.2	-6.9	-2.6	-4.2	-5.4
Net FDI (EUR million)	3,657	4,328	4,220	4,431	4.652
Net FDI (% of GDP)	6.9	7.2	6.0	5.9	5.8
International reserves (EUR million)	16,455	19,416	24,909	25,955	25,986
International reserves (Months[a])	5.9	5.2	6.7	6.4	5.9
Public Finance					
Primary balance (% of GDP)	-2.4	-1.7	-0.4	-0.3	0.2
Fiscal balance (% of GDP)	-4.1	-3.2	-2.2	-2.0	-1.5
Central Government debt (% of GDP)	56.5	55.1	52.0	50.0	48.0
External Debt					
Gross external debt (EUR million)	36,488	41,885	45,128	47,127	50,449
Gross external debt (% of GDP)	68.4	69.3	64.6	62.6	62.6
External debt service (EUR million)	6,000	5,300	5,500	6,300	4,800
External debt service (% of reserves)	36.5	27.3	22.1	24.3	18.5
External debt service (% of exports)	20.8	13.9	13.4	14.5	10.4
Financial Markets					
Policy rate (2-w repo rate, %, eop)	1.0	5.0	6.5	5.0	4.0
Policy rate (2-w repo rate, %, aop)	1.0	2.6	6.1	6.0	4.2
10-Y T-bill rate (%, eop)	4.1	7.3	6.2	5.8	5.4
Exchange rate: EUR (eop)	117.5	117.2	117.2	117.2	117.5
Exchange rate: EUR (aop)	117.5	117.4	117.2	117.2	117.4

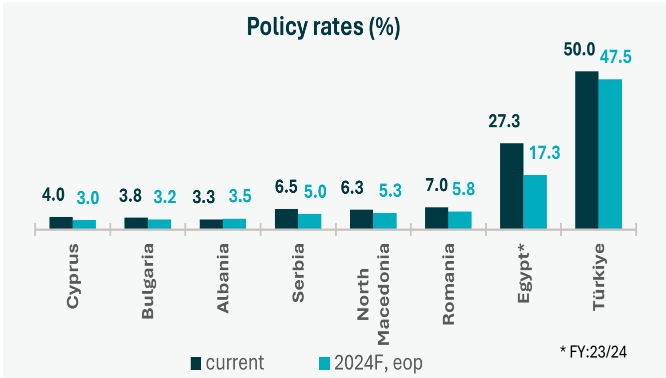
f: NBG forecasts; a: months of imports of GNFS

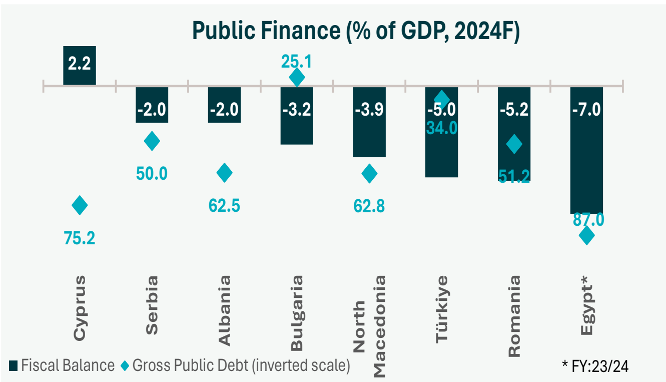
REGIONAL SNAPSHOT: MACROECONOMIC INDICATORS

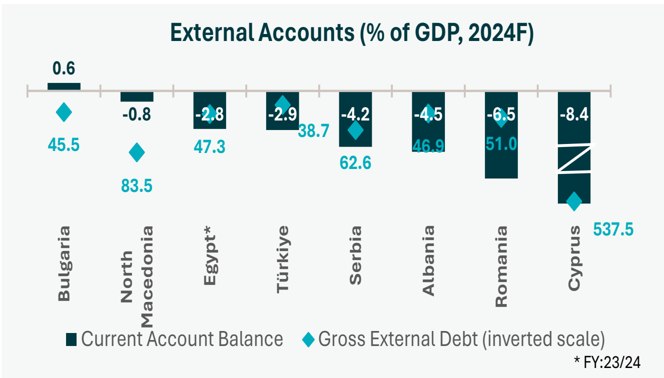


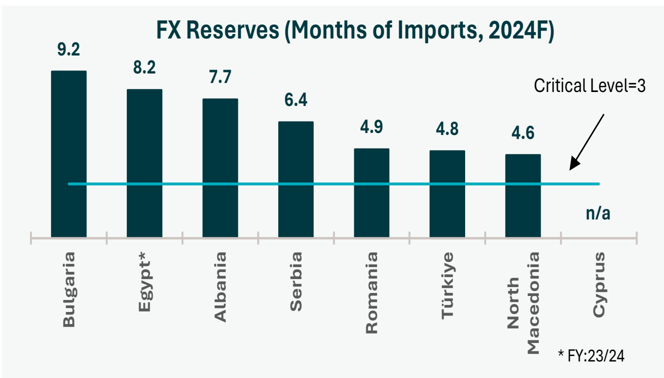






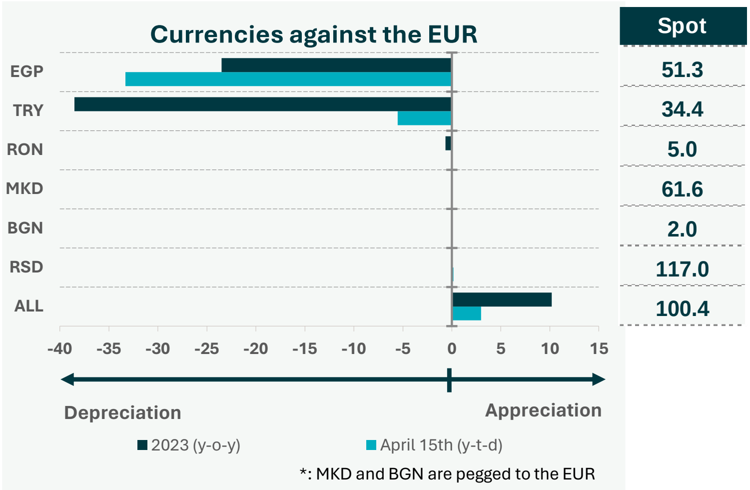


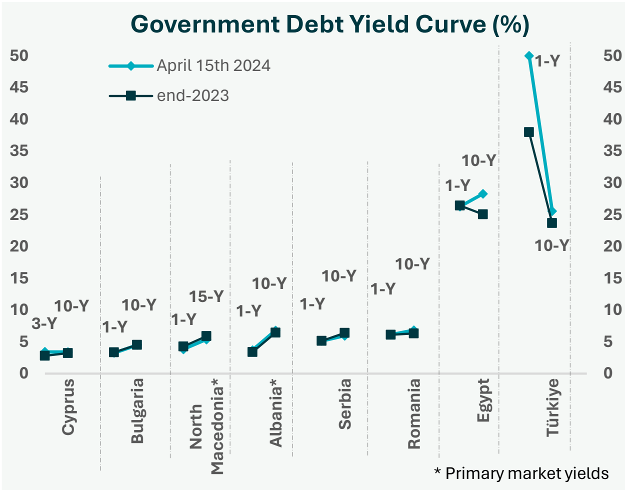


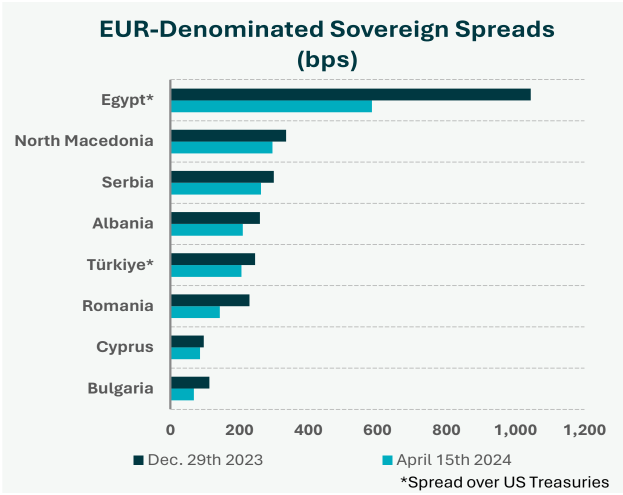


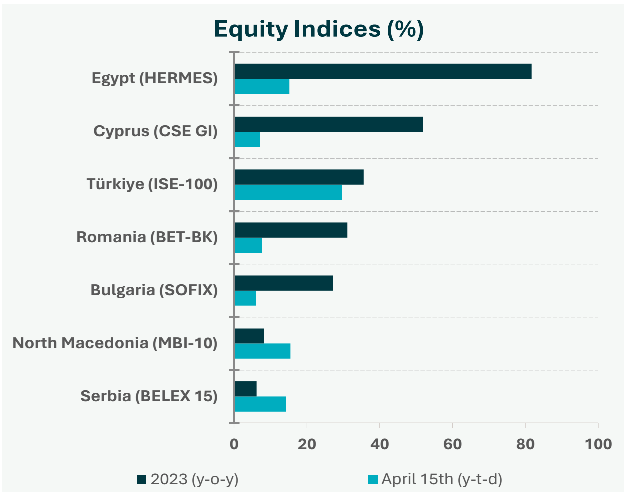
Sources: National Sources & NBG estimates

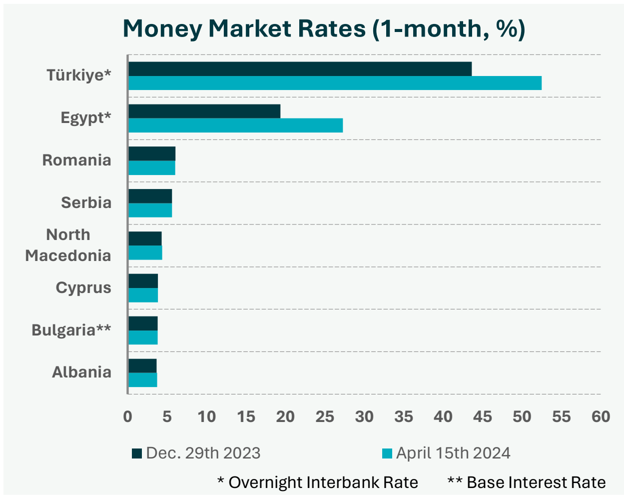
REGIONAL SNAPSHOT: FINANCIAL MARKETS











Sources: Reuters & NBG estimates


FOCUS
ECONOMICS
Analyst Forecast Awards
2023
NATIONAL BANK
OF GREECE
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