THE ROLE OF INFLATION ON ECONOMIC GROWTH, WITH SPECIAL EMPHASIS ON THE REPUBLIC OF NORTH MACEDONIA

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DOI: http//doi.org/10.51331/EB08NT

INTRODUCTION

Inflation is a steady movement of increase in the general price level of goods and services in an economy. It corresponds to a loss of purchasing power for a currency that is used within the economy. As a result, more currency units are needed to buy the same amount of goods and services. A country's currency, for exapmle Denar, euro, dollar, etc., in relation to the value is not the same in the conditions of inflation and when the purchasing power of that currency can decrease. This means that the money you have earned will buy less of a given service or goods. The causes of inflation are debated by many economists but most of them agree that inflation can be good and bad. An advantage of inflation is a projected inflation which generally implies that an economy is healthy and growing. In situations where inflation is predicted, the demand for a product increases much faster than the supply, so the price of that product increases. If inflation is predicted by economists and as a result is expected, then the economy is likely to have negative effects. To keep the economy in balance, banks will lower interest rates and companies will raise wages.

Inflation occurs only when the overall prices of goods and services are rising. Two main forces are considered to be responsible for the increases: demand-pull inflation and cost-push inflation. Selective price increases are not an example of inflation. The prices of certain products may increase (such as oil, wheat, etc.) due to factors related to the supply constraints (war), but the general level may

not increase/change if the prices of other products decrease. As long as the quantity of money in circulation remains unchanged, there can be no change in the general price level. Nowadays, the euro is for the first time in 20 years at parity with the dollar, marking its lowest level since 1981 crisis, while Britain records the highest inflation in 40 years. The Republic of North Macedonia also recorded an almost-record inflation rate of 17.1 percent. Switzerland is among the rare countries that has not followed such a monetary policy (at least not to this extent) and therefore does not suffer from high inflation.

UNDERSTANDING AND DEFINING INFLATION

Understanding the inflation dynamics, first of all, requires an understanding of the fundamental concept of inflation and how to measure it. In this regard, relying on the theoretical definitions so far, we can define iInflation as a process of continuous price increase and decline in purchasing power. In other words, Inflation represents the general and broad-based increase in the price of goods and services over a continuous period of time.

So, inflation represents the percentage by which the prices of goods and services increase. Likewise, it also works as a percentage by which money loses its value. For example, in the 1970s, a cup of coffee cost 20 cents, today it is 1.50 Euros. For the same amount of money you can now buy fewer goods than you could have bought 50 years ago, because when prices rise and we all notice this change - the purchasing power of money declines. Inflation is measured by the consumer price index. This shows how much money someone would spend this year to buy the same products and services as last year.

Historically, inflation as a phenomenon is known very early. However, in its full sense, the word inflation was first used in the USA, to express the large increase in the level of prices and the circulation of money during the civil war 1861-1865, when the government was forced to issue paper money to finance the war. The word “inflation” comes from the Latin “inflare” which means to inflate, to enlarge, etc. From what was said above, it is not difficult to conclude what we mean by inflation.

It is necessary to emphasize that inflation is an economic phenomenon that expresses the rise of the general level of prices and not of particular prices. With the rise of the general level of prices we mean the rise of their average level. Of course, not all prices rise to the same extent during the period of inflation.

Specifically, inflation represents the long-term increase in the prices of services and goods due to the devaluation of the currency. Although inflation is a

negative thing, it can also be a positive thing for entrepreneurst (Zeqiri, S. 2023: 15). Usually, problems with high inflation rate arise when there is an unexpected spike. Accordingly, if incomes do not increase with inflation, everyone‘s purchasing power will effectively be reduced, which in turn leads to a stagnant or slow economy.

The main objective of central banks is to keep stable prices and preserve the integrity and purchasing power of people‘s money. The most common inflation indicator measures the average change in the price of a basket of consumer goods and services over time (European Parliament. (2022). *Inflation explained: What lies behind and what is ahead?*). The closest definition of what people intuitively understand by the term *inflation* is the change in their cost of living. In this context, the harmonized indicator for consumer prices (HCP), against which the European Central Bank (ECB) assesses the achievement of its objective of price stability, is based on this concept.

The inflation index is one of the most important economic indicators that also affects everyday life. Since everyone needs to buy and use a wide range of goods and services, they directly (implicitly) experience price changes on a daily basis. In a market economy, the prices of goods and services can always change, while some prices rise, others may fall or stay the same. However, when we talk about inflation, what we actually mean is an increase in the price levels of goods (eg food) and services (eg electricity or gas). In other words, inflation is defined as a general or broad-based increase in the price of goods and services over an extended period.

However, high inflation is generally concerning. In periods when prices rise significantly on a broad basis and purchasing power declines, wage-setting schemes can trigger the wage-price spiral. Such „second-round“ effects can occur if households and/or companies try to compensate for the loss of real incomes caused by high inflation when setting wages and/or prices (Koester, G., & Grapow, H. (2021). The prevalence of private sector wage indexation in the euro area. *Economic Bulletin, 7*, 12. European Central Bank). While falling prices may sound positive to a consumer, sustained and widespread falling prices throughout the economy can delay consumer and business spending and investment decisions, creating a vicious cycle for the economy where production and prices are reciprocally decreasing.

Overall, price stability is of vital importance to the country‘s economy. The consensus is that price stability contributes to smoothing the variability of production and employment in the short and medium term and contributes to the

growth and employment prospects of the economy in the long term. More specifically, price stability preserves the integrity and purchasing power of money.

At the individual level, in the stable price environment, people can hold money for transactions and other purposes without having to worry that a decline in purchasing power will reduce the real value of their funds. Stable prices are equally important, allowing people to make long-term decisions, enter into long-term contracts and engage in long-term planning, borrowing or lending for the future. Similarly, from a corporate perspective, price stability promotes efficiency and long-term growth by providing a monetary and financial environment in which sound economic decisions can be made and where concerns about unpredictable fluctuations in the purchasing power of money are limited. Therefore, the purpose of price stability is to keep the overall value of a basket of goods constant, rather than fixing each individual price for the many goods and services included in that basket.

In general, price stability reduces inflationary uncertainty and therefore helps prevent misinterpretation of changes in the general price level, thereby avoiding misallocation of resources. For creditors, stable inflation rates will reduce the demand for additional returns, or the „inflation risk premium", which would otherwise reduce the incentive to invest. Moreover, price stability reduces distortionary effects in tax and social systems, as fiscal systems normally do not allow for the indexation of tax rates and social security contributions to the rate of inflacionit (European Central Bank. *Price stability: Why is it important for you?*).

While it is clear that both very low and high inflation rates are undesirable, setting the optimum, the level of inflation to ensure price stability is not trivial. Central banks around the world have different objectives; those with a price stability objective target different levels of price growth. The European Central Bank (ECB) has recently revised its monetary policy strategy, which brought about a redefinition of the objective of price stability (the main objective).

Inflation can have a significant impact on a country's economy. On one hand, inflation can increase the revenues of producers and traders and can stimulate investment and economic growth. On the other hand, inflation can harm people with low incomes and investors who hold fixed value assets.

Inflation can also affect the exchange rate, the stock market and affect the stability of the financial system. To control inflation, central banks can intervene in the market by changing monetary policies, such as raising interest rates and reducing the quantity of money in circulation. Governments can undertake fiscal policies to improve business conditions and stop rising production costs. However,

controlling inflation can be a difficult challenge, and in some cases, it may be necessary to take drastic measures to curb rising inflation. In general, inflation is a process that affects many aspects of a country's economy and must be controlled to ensure the stability of the economy and the well-being of the people.

As long as the money supply remains unchanged, there can be no change in the overall price level (inflation). Here is an illustrative example: a citizen spends 100 euros on three different products, dividing the expenditure into 60, 30 and 10 euros. If he increases the spending on the first product, for example 70 instead of 50 euros, he must definitely reduce the spending on one or two other products. Any increase in the price of the first product is necessarily accompanied by a decrease in the prices of other products and vice versa. This is a simple example of selective price increases but not inflation.

Similarly, inflation should not be confused with the Consumer Price Index (CPI) or any other "basket of consumer" price index. These measures are narrower in definition and are typically used for products that consumers consider most essential, but are not general measures of inflation. Thus the definition stands: inflation is caused only by an increase in the amount of money in circulation beyond the demand for money.

The question arises as to why the central bank is doing this? Many economists think that the proper role of the Central Bank is to support economic activity by increasing or decreasing the money supply based on certain parameters. There are other economists, but I am also of the opinion that the markets do not need such a regulatory entity that plays the god-like role and that the historical track record of central banks (according to all relevant parameters) has been poor.

Inflation and Deflationi

Inflation is a steady upward movement in the overall price level of goods and services within an economy. It corresponds to a loss in the purchasing power of a currency used within that economy. As a result, more currency units are needed to buy the same amount of goods and services.

Inflation occurs only present when the overall prices of goods and services are rising. Two main forces are thought to be responsible for the increases: demand-pull inflation and cost-push inflation.With demand pull inflation, the demand for goods and services in the economy exceeds the economy's capacity to produce them. This supply puts upward pressure on prices, causing inflation.

Cost-push inflation occurs when the rising price of input goods and services increases the price of final goods and services and causes inflation. An oil crisis

often causes a decrease in the supply of oil and an increase in the price of oil, an important input product. The increase in the price of oil exerts upward pressure on the price of final goods and services, leading to inflation.

A country's central bank often adjusts short-term interest rates to maintain the desired inflation rate. Another monetary phenomenon in the economy is deflation. According to the economic literature, deflation is a decrease in the general level of prices of goods and services. Deflation occurs when the interest rate falls to 0% (a negative interest rate). Deflation as a concept should not be confused with disinflation, which is a slowdown in the rate of inflation (when inflation falls to lower levels). Inflation decreases the real time value of money, while deflation increases the value of money. In this sense, economists of different schools think that deflation is a problem in a modern economy as it increases the real value of debt and can lead to recession. Based on economic history, deflation does not always lead to the ruin of the economy. If we can refer to the deflation that occurred in the United States of America in the 19th century, the deflation was caused by technological progress, which created significant economic growth.

According to a study done by Akerlof et al (1996) deflation has high costs. In cases where inflation is below 2 percent, it produces inflation and leads to an increase in the natural level of unemployment. The authors argue that the downward rigidity of the nominal wage indicates that the reduction of the real wage can only occur in a period of inflation. The reasoning lies in the fact that a very low level of inflation can prevent real wages from adjusting to lower them, as a result of the decrease in the demand for work in some industries, which causes an increase in the level of unemployment.

Unexpected deflation can shift resources from lender to borrower in situations of long-term borrowing contracts with a fixed nominal interest rate. With a lower price level and fixed debt in nominal terms, the real weight of this debt increases. On the face of it, it seems as if the lender's losses could be offset by the borrower's gains at the macro level, given that unanticipated deflation is a wealth transfer, or a zero-sum outcome. But this is not true, as deflation can lead to financial instability which can create high costs in the economy. Such a situation is one more reason to worry about deflation. Irving Fisher (1933) called this phenomenon "debt deflation" and considered it an important factor that caused economic decline during the Great Depression. In conditions where the net worth falls, the value of the collateral that can be received by the lender falls when the value of the borrower's investments falls, and as a result this lost value of the collateral increases adverse selection, since the value of the loan has fallen . Subsequently, the decline in net worth encourages lenders to take on greater risk as

they now have less to lose if their investment is devalued. The increase in moral damage and adverse selection from deflation means that the markets of the financial system will no longer be able to allocate capital for productive purposes and as a result investment will fall and the economy will tighten. The transfer of wealth under these conditions is not insignificant as it affects the effective functioning of capital markets. The Great Depression is an example where deflation has very negative consequences on the rich economy from the example of Japan.

While inflation is associated with a general increase in the price of goods and services and a decrease in the value of money, deflation refers to a general decrease in the price and services and an increase in the value of money. You have deflation when the percentage change between the CPI (Consumer Price Index) from one period to another is negative. Inflation as mentioned is caused by an increase in demand or cost push, while deflation is caused by contractions in the economy or the supply of money or credit. Consumers may be able to buy more with a unit of currency as a result, while inflation generally does not allow people to buy as much unless their wages are kept high.

INFLATION RATE IN NORTH MACEDONIA: HIGH INFLATION AND SLOWED ECONOMIC GROWTH

The inflation rate is used to measure the rate of changes in the general level of prices of goods and services. By means of this rate we measure the price changes that occur for a number of different goods and services. There are many different measures of inflation, however, we will focus on the most commonly known index such as the consumer price index (CPI). There are several factors that need to be considered in calculating the current CPI, namely:

1. Measuring price changes for goods is complex, if not impossible. Instead, the market basket of goods and services that we often consume is used. Items such as shelter, food, transportation, communication, etc., are represented by certain goods, the changes in whose prices can be accurately recorded over time;
2. Individual items in the market basket are weighted according to their relative importance. The price of gasoline takes a more important weight than that of tomatoes, since we spend a larger percentage of our budget on fuel.
3. Prices of individual items and their respective weights used in the calculation of the CPI.

For example, the inflation rate for 2002 represents the rate of increase in the prices of a weighted basket of goods (CPI) compared to 2001. The calculation is:

$$\textbf{Inflation rate (2002)} = \frac{\text{CPI (2002) - CPI (2001)}}{\text{CPI (2001)}} \text{ x } 100 \qquad (1)$$

Although the CPI is the most commonly used index for measuring the rate of inflation, there are some limitations that can cause higher inflation rates to be reported than actually occur. The main disadvantages of using the CPI as a measure of consumer prices are:

- CPIs fail to adapt to improvements in quality;
- The weights used to combine the prices of the various goods and services that go into the index are often outdated.
- Consumers often substitute goods, which have an increase in price. CPI overestimates inflation by not allowing room for substitutes in consumption for goods whose prices change(Mehmeti, V. 2016).

Due to the above factors, the best assumption is that CPIs overstate inflation by 1-1.5% on an annual basis. This is an important issue, as economic policy often strives to achieve the lowest possible level of inflation. The implications are important for policymakers, who may mistakenly aim for zero inflation, which could cause economic growth to disappear.

According to the latest report of the World Bank on Global Economic Prospects, with the rate of inflation that North Macedonia is currently experiencing, the country ranks at the top of the countries in the region, a rate that is among the lowest in terms of forecasts for economic growth. Since the beginning of the economic and energy crisis, the country has consistently maintained the first position in terms of inflation rate. The statistics show a decrease in the month of May, but it still remains in double digits at 11.3%, which is the highest compared to other countries in the region that have published their data. Additionally, the report maintained its January forecast of 2.4% GDP growth in 2023. The report also predicts slight acceleration in economic growth to 2.7% in 2024 and 2.9% in 2025 (China-CEE Institute. (2023, July 3).

The World Bank's Global Economic Prospects report is a comprehensive assessment that measures and analyzes the economic trends and prospects of countries around the world. Published at regular intervals, it provides valuable insights into the global economic landscape, including growth forecasts, risks

and policy recommendations. It covers a wide range of indicators such as: GDP growth rates, inflation, investment trends, trade dynamics, poverty levels, etc.

The June 2023 report predicts that global growth will slow due to factors such as high inflation, tighter monetary policies and tighter credit conditions. He predicts that economic growth will slow down this year and reach 2.1% compared to 3.1% the previous year. Also, according to the report, the potential for increased banking disruptions and further tightening of monetary policies could worsen the situation, resulting in even weaker global growth and possible financial disruptions in vulnerable emerging markets and developing economies.

In addition to details on the state of the global economy, the report includes important indicators that shed light on the current and projected state of Macedonia's economy. These indicators are placed within a regional and global context, providing valuable insights into the country's economic landscape (World Bank).

According to the World Bank's June 2023 Global Economic Outlook report, Macedonia's economy is projected to grow steadily by 2.4% in 2023, in line with the unchanged January projection. The report also shows slight acceleration in economic growth, with a forecast of 2.7% in 2024 and 2.9% in 2025.

Regarding the regional perspective, the Western Balkans GDP growth is expected to reach 2.6% in 2023, influenced by various factors, such as the consequences of the war in Ukraine, the decrease in private consumption, tight global financial conditions and weaker demand from the euro area. Among the countries of the region, Kosovo is expected to have the highest economic growth this year with 3.7%, followed by Montenegro with 3.4%. Albania is predicted to have a growth rate of 2.8%, while Bosnia and Herzegovina will have a growth rate of 2.5%. Serbia is expected to grow by 2.3%, Croatia by 1.9%, and Bulgaria by 1.5%.

According to the IMF, the country is currently undergoing economic stabilization, with real GDP expected to grow by 2.1% this year and 3.4% in 2024. Likewise, inflation has begun to decline and is expected to reach 9.2%. during this year, 3.5% next year and return to the rate of 2% until 2026. Unlike the World Bank and the IMF, the EBRD expects the country's GDP to grow by no more than two percent this year, which is the lowest forecast among all institutions that measure the strength of the economy of Macedonia. If the slow pace of economic growth is a cause for concern, the situation worsens when inflation in the country is taken into account. The statistics show a decrease in the month of May; however, it remains in the double digits. Average consumer prices in Macedonia rose by 11.3% year-on-year in May, following an annual increase of 13% in April (China-CEE Institute. (2023, July 3).

On a monthly basis, consumer prices increased by 0.4% in May, after increasing by 0.7% in April. This makes it the highest among countries in the region that have published their data (China-CEE Institute. (2023, July 3). In its latest report, local inflation "Finance Think" calculated that, in the first quarter of 2023, inflation slowed to 16.1% on an annual basis, after its peak of 19.3% in the previous quarter. According to them, the slowdown, similar to previous growth, has been driven by the easing of global pressures on energy prices and various food groups. However, core inflation, which excludes these components, continues to show considerable persistence, necessitating further tightening of monetary policy and careful attention to fiscal policy. "Finance Think" also lowers its 2023 GDP growth projection to 2.0% from 2.4% previously, while the forecast inflation rate of 8.9% remains unchanged, both with significant uncertainty," as says the report of the Institute for Economic and Political Research Finance Think (Institute for Economic and Political Research Finance Think, 2023).

In terms of the business climate, expectations are that the economy will be overshadowed by political issues for a long time. The chamber of commerce has been determined in declaring that what has been prepared by the government and offered to businessmen in recent years is pure economic populism and not a real demonstration of interest in improving conditions.

Another cause of concern is the increase in the country's external debt. According to the statement of the Central Bank, Macedonia's gross foreign debt reached 11.1 billion euros (12 billion dollars) at the end of March, marking an increase of 11.1% compared to last year. This value accounted for 78.1% of the gross domestic product (GDP) forecast for 2023 (China-CEE Institute, 2023).

Moreover, the gross external debt experienced an increase of 2.1% compared to the previous quarter. As for the net external debt, the country's total at the end of March was 4.2 billion euros, reflecting an increase of 4.2% compared to the same period last year. A new financial instrument was introduced in June 2023 precisely in an effort to regulate the increase in external debt (China-CEE Institute, 2023).

From June 30, citizens can start the procedure for purchasing citizen bonds. The Ministry of Finance published the prospectus for the first bond auction in the amount of 600 million denars. The minimum value that can be invested is 10,000 denars, the coupon interest rate is five percent, and the bond has a maturity period of two years (China-CEE Institute, 2023).

In general, the latest reports from international and local financial institutions support the same opinion about the worrying state of the Macedonian economy.

High inflation remains a concern, calling for tighter monetary policy and prudent fiscal management. The business climate is hampered by political issues, where economic problems are not prioritized for solution, raising concerns about the effectiveness of economic policies (China-CEE Institute, 2023).

The increase in external debt is another area of concern, reaching 78.1% of the projected GDP for 2023. Addressing challenges such as inflation, political issues and debt levels is essential for sustainable and inclusive economic development. In this context, it is of utmost importance that policymakers prioritize prudent monetary and fiscal measures, business-friendly policies and sustainable debt management to foster a favorable investment and economic climate and support long-term growth.

Finally, we emphasize that the annual inflation rate in the Republic of North Macedonia has increased to 3.6% in December 2023, recovering from 3.1% in the previous month, after the increase in prices for food and non-alcoholic beverages (1.6% compared to 0.3% in November), clothing and shoes (4.6% compared to 4%), health equipment (5.3% compared to 5%) and beverages alcohol and smoking (11% versus 10.8%). Meanwhile, transport costs decreased at a slower pace (-0.4% versus -2.4%). On the contrary, prices have decreased for housing and communal services (4.5% vs. 5.1%), furniture and household appliances (7.4% vs. 9.3%), communication (2.2% vs. 2.4%), recreation and culture (7% vs. 7.3%), education. (2.8% to 2.9%), restaurants and hotels (6.3% to 6.8%). Meanwhile, in December, on a monthly basis, consumer prices increased by 0.2% (State Statistical Office).

In Macedonia, the most important category in the consumer price index is the category of food and non-alcoholic beverages (40 percent of the total weight). The housing and municipal services category accounts for 13 percent; of transport 8 percent; of clothing for 7 percent; furniture, household appliances and equipment for maintenance 6 percent; Restaurants and hotels 6 percent. Various goods and services; Alcoholic beverages, tobacco and narcotics; Communication; Recreation and Culture; and Education make up the remaining 21 percent of the total value (State Statistical Office).

Figure 1. Inflation Rate in North Macedonia

Source: (Trading Economics)

MAIN CAUSES OF INFLATION

Frequent increases in inflation are often the result of weak monetary policy. If the money supply increases too much relative to the size of the economy, the unit value of the currency decreases; in other words, its purchasing power falls and prices rise. This relationship between the money supply and the size of the economy is called the quantity theory of money and is one of the oldest hypotheses in economics.

Pressures on the supply or demand side of the economy can also be inflationary. Supply shocks that hamper production, such as natural disasters, or increase production costs, such as high oil prices, can reduce aggregate supply and lead to "cost-push" inflation, in which the impetus for increased price comes from a supply disruption.

The food and fuel inflation of 2008 was a case in point for the global economy – sharp increases in food and fuel prices were transmitted from one country to another through trade. Conversely, demand shocks, such as stock market surges, or expansionary policies, such as when the central bank lowers interest rates or the government increases spending, can temporarily boost aggregate demand and economic growth. However, if this increase in demand exceeds the productive capacity of an economy, the resulting strain on resources is reflected in „demand-pull" inflation. Policymakers must find the right balance between stimulating demand and growth when necessary, without overstimulating the economy and causing inflation (International Monetary Fund [IMF]).

Expectations also play a key role in determining inflation. If people or firms anticipate higher prices, they build these expectations into wage negotiations and contractual price adjustments (such as automatic rent increases). This behavior

partially determines the inflation of the next period; once contracts are exercised and wages or prices rise as agreed, expectations become self-fulfilling. And to the extent that people base their expectations on the recent past, inflation would follow similar patterns over time, resulting in inflationary inertia (International Monetary Fund [IMF]).

As mentioned above, inflation is a measure that shows how fast the prices of goods and services are increasing. If inflation increases, respectively, if the prices of basic products such as food products, housing products, medical care, utilities, etc. increase, inflation can have a negative impact on the entire economy of the country. Inflation can be troubling to businesses and economies because it makes money saved today less valuable in the future. There are various factors that can drive price rises or inflation in an economy. Typically, inflation results from rising production costs or from increased demand for products and services.

However, it is important to emphasize that inflation is not a random increase in the overall price. When considering the reasons behind the rise in prices over a period, economists identify three main causes: *cost-push inflation*, *demand-pull* inflation and *monetary inflation*. The consequences of inflation are affected not only by its cause, but also by its scale, the inflation rates of other countries and the government actions taken to mitigate its effects.

Cost-push inflation occurs when the price level rises as production costs increase. If firms face higher costs, they will usually raise their prices to maintain profit margins. There are a number of reasons for the increase in spending. One is increasing wages more than labor productivity. This will increase labor costs. Since labor costs constitute the highest percentage of total costs in many firms, such an increase can have a significant impact on the price level. Another important reason is the increase in the cost of raw materials. Some raw materials, especially oil, can change the price to a large extent Mehmeti, V. (2016: 8,9).

Demand-pull inflation occurs when the price level is pulled by excess demand. Aggregate demand for a country's products may increase because of higher consumption, greater investment, higher government spending, or higher net exports. Such an increase in aggregate demand will not necessarily cause inflation, if aggregate supply can increase accordingly.

When the economy has a lot of spare capacity, with idle workers and idle cars, higher aggregate demand will result in higher output, but no increase in the price level. If, however, the economy is short of some resources, or in case of full use of the resources it would not be possible to produce more. As a result, any increase in demand will be mere inflation.

When the economy has ample spare capacity, with unemployed workers and unused machinery, higher aggregate demand will lead to higher production, but will not increase the price level. If there is shortage of certain resources, or if resources are fully utilized, it would not be possible to produce more. As a result, any increase in demand would lead to inflation (Mehmeti, V. (2016: 9).

Monetary inflation is a form of demand pull inflation. In this case, excess demand is created by an excessive increase in the money supply. One group of economists, appropriately called monetarists, believe that the only cause of inflation is when the money supply grows faster than output. They argue that if the money supply increases, people will spend more and this will lead to an increase in prices. (Harvey, 2011) The well known monetary economist Milton Friedman (1992) stated, „Inflation is always and everywhere a monetary phenomenon, in the sense that it is, and can be, produced only by a more rapid increase in the quantity of money than in output".

MEASURING INFLATION

There are several ways of measuring inflation and millions of individual prices in an economy. These prices are subject to continuous movements which in essence reflect changes in the supply and demand for individual goods and services thus providing an indication of the „relative pay" of the respective goods and services. Clearly, it is neither feasible nor desirable to consider all of these prices, but neither is it appropriate to look at just some of them, as they may not be representative of the overall price level.

The most well-known indicator of inflation is the Consumer Price Index (CPI), which measures the percentage change in the price of a basket of goods and services consumed by households. Accordingly, inflation is usually measured using a price index to calculate how the price level has changed over a 12-month period. The most common and well-known price index is the consumer price index (CPI).

The Consumer Price Index (CPI) measures the change in the price level of goods and services used by households for personal consumption. The index is calculated using the structure of final consumption of household economic units.[1] The index is used as the official measure of inflation in RNM. In this context, the index also shows how much it costs to live in a certain place, eg in RNM, and

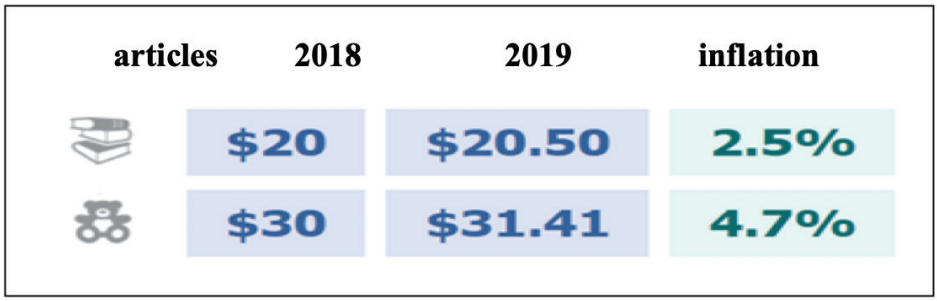
1 Indeksi i Çmimeve të Konsumit, gjetur në: https://www.instat.gov.al/al/temat/%C3%A7mimet/indeksi-i-%C3%A7mimeve-t%C3%AB-konsumit/, [Qasur: 21.01.2024].

how this cost develops over time. As we emphasized above, inflation represents an increase in the level of prices of goods and services that people buy. It is measured as the rate of change of these prices. Typically, prices rise over time, but prices can also fall (a situation called *deflation*).

Calculating Inflation-example

The price of a book was $20 in 2018, while the price has increased to $20.50 in 2019. The price of a toy for children was $30 in 2018, while in 2019 the price has increased to $31.41.

Figure 2. Inflation and its Measurement



Source: Inflation and its Measurement: Box: Calculating Inflation – An Example, gjetur në: https://www.rba.gov.au/education/resources/explainers/inflation-and-its-measurement.html

Using the relevant inflation measurement formula, inflation can be calculated for each of the items in particular. For books, annual inflation was 2.5 percent, while for children's toys, annual inflation was 4.7 percent. To calculate inflation for a basket that includes books and toys for children, CPI values based on how much households spend on these items should be used. Because families spend more on toys than on books, children's toys have more value in the basket. In this example, children's toys make up 73 percent of the basket and books make up the remaining 27 percent. Using these values and the change in item prices, annual inflation for this basket was 4.1 percent – calculated as (0.73 x 4.7) + (0.27 x 2.5).

The Consumer Price Index (CPI) measures inflation by tracking changes in the prices paid by consumers for a basket of goods and services over time. These goods and services include food and beverages, shelter, clothing, transportation, medical care, entertainment, education, and communication.

In this regard, it is of great importance to show how the consumer price index (CPI) is measured. Each month, Statistics of a given country must collect data on

the prices of a large number of goods and services consumed in that country. These goods and services are what the Statistics of the given country consider to be included in a representative consumption basket, that is, a sample that reflects what an average citizen consumes.

A product or service that is consumed on a large scale is given greater value than one that is consumed on a smaller scale. What consumers buy changes over time and once a year, Statistics of that country updates which goods and services will be included in the measurement.

What that country's Statistics try to measure is the price of the same goods and services sold over time. Therefore, those statistics also estimate how much of the price change is due to improved quality, such as when the performance of a computer is continuously improved, the price also increases as a result. After the prices have been compiled, an index is created for the price level that shows how much it costs to live in that country - this is the consumer price index (CPI). In this regard, inflation is usually calculated as the change in the CPI in a given month compared to the same month last year (Reserve Bank of Australia. *Inflation and its measurement: Box: Calculating inflation*).

The Consumer Price Index (CPI) measures the average change in prices for a basket of goods and services over time. Changes in the CPI reflect changes in the cost of living. *While the Personal Consumption Expenditure Price Index (CPI), the Producer Price Index (PII)* and *the Gross Domestic Product Deflator (GDP)* are alternative measures of inflation.

The Consumer Price Index is calculated by measuring the price within a period for a fixed basket of consumer goods and services compared to previous periods. Inflation is an increase in the general level of prices and is often expressed as a percentage. When inflation occurs in a particular country, the purchasing power of money decreases. Accordingly, when there is inflation in Macedonia, the purchasing power of the denar decreases.

Changes in the CPI reflect price changes in the economy. When there is an upward change in the CPI, there has been an increase in the average price change over time. This leads to adjustments in the cost of living and income, a process referred to as indexation. I.e. The CPI measures the change in price for retail goods and other items, but does not include savings and investment or spending by foreign visitors (Reserve Bank of Australia. *Inflation and its measurement: Box: Calculating inflation*)

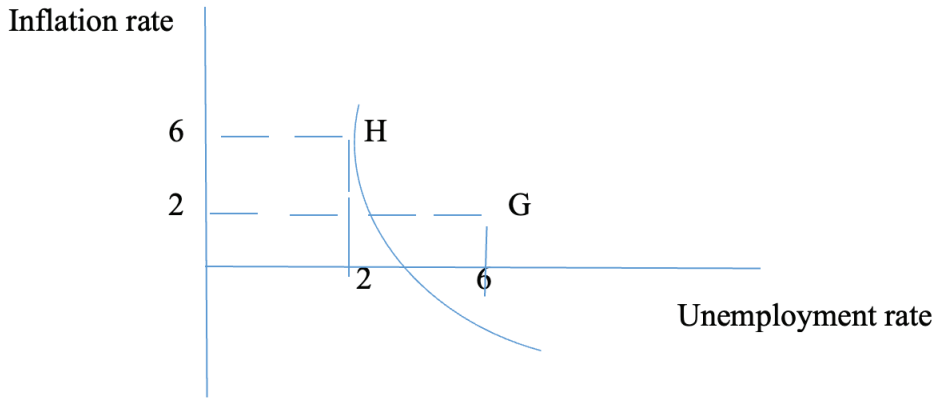
INFLATIONI AND UNEMPLOYMENT

A hypothesis named after A. W. Phillips states that there is a consistent negative relationship between the level of unemployment and the rate of change of wages - high levels of unemployment are associated with falling wages, low levels of unemployment with rising wages. Based on this connection, policy makers can choose a low inflation rate or even deflation as their objective. In this case they will have to accept higher unemployment (Mehmeti, V. 2016: 21).

The Phillips curve implies that wages and prices adjust slowly to changes in aggregate demand. We assume that the economy is in equilibrium with stable prices and unemployment at the natural rate. If the money stock increases by 4%, for the economy to return to equilibrium, both prices and wages must increase by an additional 4%. This will lead to an increase in the wage growth rate. Wages will begin to rise, prices will also rise, and finally, the economy will return to the level of output and full employment (Dornbusch, R., & Fischer, S. (1994:55).

Higher wages mean lower unemployment, so the graph below shows the unemployment rate going from 6% to 2%, caused by the 4% increase in the money stock. As a related indicator, this decline in unemployment is reflected in the increase in inflation from 2% to 6%.

Graph 1. Phillips curve



Empirical evaluations of the relationship expressed by the Phillips curve were unsatisfactory. The rate of inflation that appears to be consistent with a given level of unemployment did not remain fixed: in the post-World War II period, rates of inflation that had previously been associated with low levels of unemployment have been met with high unemployment. High unemployment actually means downward wage pressure, but real wages could be lower even if nominal

wages were higher, as long as prices offered were still higher. If everyone predicted that prices would rise by say 20% per year, then this prediction would be reflected in wages and contracts in the future, real wages would then behave as if there had been no rise in prices. prices, and there would be no reason for the 20% inflation rate. An unanticipated change is very different, especially in the presence of long-term commitments, partly as a result of incomplete information, the effect of which grows and dissipates over time.

Along these developments, E. S. Phelps and M. Friedman have developed an alternative hypothesis that distinguishes between short-term and long-term effects of unforeseen changes in nominal aggregate demand. Starting from a stable initial position, an unanticipated acceleration of nominal aggregate demand will come to each producer, as a sudden favorable demand for his product. He will be willing to pay higher nominal wages than before to attract additional workers. For employees, the situation is different: what matters for them is the purchasing power of wages not over the particular good they produce, but over all goods in general. Expressed in terms of the average of perceived future prices, real wages are lower; in terms of the perceived average future price, real wages are higher. But, this situation is temporary perception and perceptions will adapt to reality. When this happens, the initial effect will disappear, and then there will be a decline for a time when workers and employers find themselves locked into unsuitable contracts (Nobel Prize. (n.d.). *Economics sciences: Friedman lecture)*.

Key points: what matters is not inflation per se, but unexpected inflation; there is no stable relationship between inflation and unemployment; there is a "natural rate of unemployment" which is consistent with accurate forecasts; unemployment can be kept below this level only by rising inflation; or below, only accelerating deflation. Some economists still stand behind the original Phillips curve. There are many who accept the difference between the short-term and the long-term curve, but still consider the long-term curve to have a negative slope, although with a higher slope Mehmeti, V. (2016 :23)..

In recent years, high inflation has often been accompanied by a higher unemployment rate, rather than a lower one, especially for periods of several years. A simple Phillips curve based on such data should not have a vertical slope either, but positive. The apparent positive correlation between inflation and unemployment has been a source of great concern for government policy makers. "We thought we could only get out of a recession and increase employment by cutting taxes and increasing government spending. I am telling you, in all honesty, that this option no longer exists, and that for as long as it has, it has only worked by injecting large doses of inflation into an economy followed by high levels of

unemployment as a follow-up. . This is the story of the last 20 years." - says the Prime Minister of Great Britain, Callaghan. Just as the natural rate hypothesis explains the Phillips curve with a negative slope in short periods as a temporary phenomenon that will disappear as economic agents adjust their expectations to the real state, so too do the positive-sloping curves. in the longer term it may flow as a transitory phenomenon that will disappear when economic agents adjust not only their expectations, but their institutional and political arrangements in a new reality (Nobel Prize. (n.d.). Economics sciences: Friedman lecture).

HOW TO PROTECT YOUR MONEY FROM INFLATİON?

Even before the COVID-19 pandemic, rumors about the economic crisis, inflation and the general collapse of financial instruments were widely spread around the world. Although inflation in many European countries is not higher than usual, even catchable, but it is still happening and affecting different spheres of life. Therefore people are constantly looking for different ways to protect the value of their money in the long run.

Wealthy people and profitable companies often look for ways to protect their money from inflation. Many choose to invest in real estate or stocks hoping not only to protect their money, but also to make it work. Others are afraid of the risk of losing money and at least for a part of their money choose a safer and time-tested method of saving the value of money - gold. And although the price of gold is constantly fluctuating - in the long run it has an upward trend, just like inflation.

At the beginning of this scientific paper we mentioned that in the 1970s a cup of coffee was 20 cents, and today it is 1.50 EUR. Also an ounce of gold in the 1970s was 200 EUR, today it is more than 1600 EUR.

Based on the statistics it is quite clear because for short-term investment and quick return people choose real estate or securities, but in the long run (at least 10 years) when looking to shave the independent purchasing power of money - gold becomes a way great for diversifying your investment portfolio. And since gold prices are constantly fluctuating over the long term it has an upward trend, just like inflation. Therefore, as a conclusion, we can say that keeping savings in gold becomes more and more valuable for people.

However, we all feel it in different ways and are all affected differently, as we all use different goods and services to different extents. For example, if your rent makes up almost half of your monthly expenses and the price of rent increases slightly, you'll notice the share so compared to someone else - whose rent only makes up a small amount of their monthly expenses.

INFLATION AND PROPOSED TAX EXEMPTIONS FOR OIL AND ELECTRICITY PRODUCTS

In many countries, gas turns out to be the main source of heating. Also, in contrast to North Macedonia, where the excise rate of 22 denars per liter has an impact on the price almost similar to the VAT rate of 18%, in some European countries such as Germany, Luxembourg, Belgium, etc., the excise duty rate for gas used for heating (below 6 denars per liter) turns out to be much lower than the VAT rate. Therefore, the removal of VAT on gas in these countries, which is being encountered as a practice from year to year, is more influential.

In addition to the Ministry of Economy's decision (in 2022) to promote electricity savings in the public sector and to encourage households to conserve electricity, the government should also implement energy-saving measures in the private sector by following best practices from other countries. The government should continuously allocate funds for initiatives that support the increase in efficiency in energy consumption at home, where over 60% of the electricity billed during the year is consumed by households. The government should consider exemption from tax obligations for gas and pellets, the prices of which are expected to be controlled through the new law, which also makes the tax exemption more easily effective.

Table 1. Government Intervention Through Tax Rates to Alleviate the Rising Cost of Living For Citizens

Place	**Description**	**Old rate**	**Current rate**	**Validity**
Germany	Reduction of VAT on Gas	19%	7%	From 1 October 2022 until 31 March 2024
Luxemburg	Reduction of VAT on fuel used for agricultural and horticultural work, as well as for industrial fuel.	17%	14%	6 May 2022 – July 2022
Slovenia	Reduction of VAT on gas bills, electricity, and heating.	22%	5%	From 1 September 2022 until 31 May 2023

Cyprus	Zero VAT rate for gasoline, energy, and electricity.	21%	6%	14 July 2022 until the end of the year
Belgium	Reduction of VAT on gas bills, electricity, and heating.	21%	6%	Initially from 1 April to September 30, 2022, and then extended until December 31, 2022, by a new decision.
Estonia	Reduction of VAT on gas bills, electricity, and heating fuel.	20%	5%	From 30 April 2022 ...
Holland	Reduction of VAT on energy (natural gas, electricity, and central heating).	21%	9%	1 July 2022- 31 Decemberr 2022
Italy	Reduction of VAT on natural gas.	10%	5%	October 2021-December 2022
Poland	Reduction of VAT on coal, heating oil, diesel fuel, and LPG gas.	23%	8%	1 February 2022-31 July 2022
North Macedonia	Reduction of VAT on basic food items. Reduction of VAT on fuels.	5% 18%	0% 10%	From 17 March – 31 May 2022 From 12 March 31 May 2022
Rumania	Reduction of VAT on domestic heating energy.	19%	5%	November 2021 – March 2022
Turkiye	Reduction of VAT on domestically produced electricity.	18%	8%	28 February 2022 - xx

Source: VAT calc (https://bit.ly/3QP9HzF).

THE ROLE OF THE TAX SYSTEM IN THE REPUBLIC OF NORTH MACEDONIA

The Republic of North Macedonia has established a simplified tax system characterized by low tax rates, making it one of the most competitive in Europe (Ministry of Finance of the Republic of North Macedonia). The tax system consists of **direct taxes** (corporate income tax, personal income tax and property tax) and **indirect taxes** (value added tax and excise duties). The implementation of a proportional tax of 10% on corporate income tax and personal income tax has simplified tax administration and stimulated the operation of companies.

Structure of the Tax System in the Republic of North Macedonia

To better understand the structure of the tax system of the Republic of North Macedonia, the following table outlines, including all types of taxes, tax rates, and tax obligors/taxpayers.

Table 2. Tax Structure in RNM

Tax	Taxpayer	Tax rate
Corporate income tax	A legal entity resident in the Republic of North Macedonia and a permanent establishment of a foreign legal entity, for the income they generate from conducting activities within the territory of the Republic of North Macedonia.	10%
Personal Income Tax	A resident individual in the Republic of North Macedonia for their worldwide income, namely the income they generate both domestically and abroad, as well as a non-resident individual for the income they generate from sources within the Republic of North Macedonia.	10%

Value Added Tax	A legal or natural person conducting business activity in the territory of the Republic of Macedonia, as well as only those taxpayers who, in the previous calendar year, have achieved a total taxable turnover exceeding 2,000,000 denars, are required to register for VAT purposes.	18% - general rate 5% - preferential rate
Property Tax	Legal and natural person property owner.	0.10% until 0.20%
Inheritance and Gift Tax	Resident natural or legal persons of the Republic of Macedonia who inherit property or receive property as a gift within or outside the country, and foreign non-resident natural and legal persons for both movable and immovable property they inherit or receive as a gift within the territory of the Republic of Macedonia.	2% to 3% - for a second-degree inheritance obligation 4% until 5% for the other part
Real Estate Sales Tax	The legal person and the natural person – the seller of immovable property, and, as an exception, the legal person and the natural person – the buyer of immovable property may be responsible for the tax on the sale of real estate if it is agreed in the purchase and sale contract that the tax will be paid by the buyer.	2% up to 4%

Source: Ministry of Finance of RNM

The tax system of North Macedonia in the field of income tax is characterized by a flat tax both in Personal Income Tax and in Corporate Income Tax, at the rate of 10% at the moment (except for income for gaming luck that are taxed at 15% TAP tax rate).

The tax system of Macedonia from January 1, 2019 in the area of income taxes was characterized by a progressive tax in TAP (income from work is taxed at two rates, namely 10% for income up to 90,000 denars and a higher rate of 18% for amounts exceeding that threshold, while capital gains were taxed at a flat rate of 15%), and a flat rate of 10% applied to corporate income. This reform was introduced with the main goal of reducing inequality and improving income distribution. Moreover, in 2019, for the first time, TAP was divided into TAP on labor and TAP on capital.

The effects from the introduction of the progressive and higher tax rate have been analyzed based on preliminary data for the period January 1 - June 30 and compared to the same period in 2018. The findings from the analysis showed that although the effects of the reform were managed to increase income, the revenue generated could have been 51% higher if the behavior of taxpayers had not changed due to the introduction of progressive taxation.

The analysis showed that tax evasion is very likely to have occurred. Common ways to avoid taxes include opening accounts in neighboring countries and transferring earned income to other people (relatives and friends) who have not yet reached the progressive tax threshold. Therefore, such behavior of taxpayers artificially improved the distribution of income, significantly damaging the fiscal effect. The government's commitment to fight the informal economy, as one of the main obstacles to economic growth, led to the decision to suspend the reform.

Based on the assessment, from January 1, 2020, the government decided to suspend the TAP reform for 36 months, reintroducing the flat tax rate of 10% for all types of income, with the exception of gambling income (the tax rate remains 15%). Income taxes account for 17.1% of total budget revenue in 2018 (4.6% of GDP), of which TAP contributes 9.3% of total budget revenue (2.7% of GDP) while VAT gives 7.8 % of total budget revenues (2.2% of GDP). (Ministry of Finance, 2020).

Participation and effect of taxes on the budget of the Republic of North Macedonia

In order to accurately analyze the role and effect of taxes on public revenues, it is important to see their participation in the budget of North Macedonia, so through the budget reports, published in the Ministry of Finance, we have created a table that enables we see the first part of the budget, respectively the part of public revenues for five years in RNM.

Table 3. Budget of the RNM (2018-2022)

In million denars	2018	2019	2020	2021	2022
TOTAL INCOME	**188,505**	**203,822**	**189,554**	**218,021**	**243,085**
tax revenues and contributions	**170,994**	**178,895**	**173,464**	**196,317**	**220,186**
Tax Revenues (separate account)	1,682	1,615	1,187	1,404	2,049
Taxes	112,774	115,114	105,713	124,286	140,518
Personal Income Tax	17,559	18,706	18,625	20,552	23,852
Corporate Income Tax	14,745	11,555	10,497	10,871	15,776
VAT (net)	49,254	52,059	46,893	58,194	64,764
VAT (gross) *	73,871	78,021	72,444	89,466	109,492
Excise Tax	25,092	26,087	22,45	25,548	25,483
Import Duties	5,604	6,033	6,738	8,48	9,973
Other taxes	0,52	0,674	0,51	0,641	0,67
Contributions	56,538	62,166	66,564	70,627	77,619
Fund for Pension Insurance (SPIM)	37,981	41,922	45,044	47,819	52,509
Employment Agency	2,426	2,622	2,757	2,918	3,214
Health Insurance Fund	16,131	17,622	18,763	19,89	21,896
Non-tax Revenues	**12,26**	**18,687**	**11,173**	**13,882**	**17,189**
Non-tax Revenues (Separate Account)	**6,756**	**8,717**	**6,234**	**6,95**	**8,535**
Profits from Public Financial Institutions	169	36	47	45	83
Administrative Taxes and Fines	1,795	1,815	1,361	2,068	2,406
Contribution for Healthcare Services	442	442	436	438	447
Other Administrative Taxes	2,508	2,552	2,057	2,473	3,181
Other Non-tax Revenues	590	5,125	1,038	1,908	2,537
Compensation for the Road Agency	0	0	0	0	0
Capital Revenues	**2,197**	**2,369**	**1,846**	**1,928**	**2,273**
Foreign Donations	**2,978**	**3,871**	**3,071**	**5,894**	**3,437**
Revenue from Collected Loans	**76**	**0**	0	0	0

Source : Ministry of Financ of RNM.

As we can see, the total revenues in North Macedonia have gradually increased, except in 2020 where there was a decline in totalrevenues compared to the previous year. This decrease is mainly caused by the COVID 19 pandemic. From the table above we can observe that the largest share of total revenues consists of tax revenues. To simplify our analysis, we will present the same table with its main categories converted into percentages, in order to more clearly see the share of taxes in total revenues.

Table 4. Totasl revevnues RNM, 2018-2022

In million denars:	2018	2019	2020	2021	2022
TOTAL REVENUES	**100**	**100**	**100**	**100**	**100**
Tax Revenues and Contributions	**90,7**	**87,8**	**91,5**	**90,0**	90,6
Non-Tax Revenues	6,5	9,2	5,9	6,4	7,1
Capital Revenues	1,2	1,2	1,0	0,9	0,9
Foreign Donations	1,6	1,9	1,6	2,7	1,4
Revenues from Collected Loans	0,0	0,0	0,0	0,0	0,0

Source: Ministry of Finance RNM

Thus, as we can see from the table above, tax revenues play a key role in the total revenues of the RNM, specifically in the composition of the budget, where on average 90.12% of total revenues are from tax revenues and contributions, while the share other than non-tax revenues. We have the largest share of taxes in total income in 2020, while the smallest share during this analyzed period is in 2019. From Table 3, we can come to some other conclusions, analyzing what types of taxes we have and which are the most important in the composition of tax revenues in RNM during this analyzed period. Without delving into specific amounts, as in the example above, we have taken the share of tax revenues (excluding contributions).

Each type of tax has been converted into a percentage, using the total tax revenues (not total revenues) as the base. This provides an overview showing which tax contributes the largest share to overall tax revenues.It's worth emphasizing that, overall, there has been no significant change in the contribution of taxes to total revenues, nor in the share of any specific type of tax within total tax revenues.

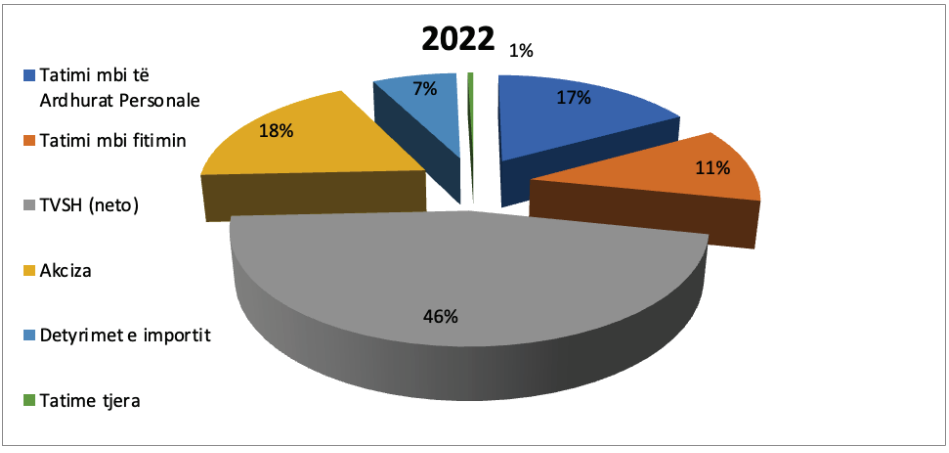
Table 5. Tax Participation in Tax Revenues in North Macedonia (2018-2022)

	2018	2019	2020	2021	2022
Taxes	**100%**	**100%**	**100%**	**100%**	**100%**
Personal Income Tax	15,6%	16,2%	17,6%	16,5%	17,0%
Corporate Income Tax	13,1%	10,0%	9,9%	8,7%	11,2%
VAT (Net)	43,7%	45,2%	44,4%	46,8%	46,1%
Excise Tax	22,2%	22,7%	21,2%	20,6%	18,1%
Import Duties	5,0%	5,2%	6,4%	6,8%	7,1%
Other taxes	0,5%	0,6%	0,5%	0,5%	0,5%

Source: Ministry of Finance of RNM

From this we can conclude that most of the tax revenues come from the Value Added Tax, where for example in 2022, about 46% of the tax revenues came from VAT, then comes the excise tax with about 18 % of total tax revenue, followed by personal income tax, which accounts for 17% of total tax revenue. Income tax also has a significant effect on total tax revenue, with a share of 11% in 2022.

Figure 3. Composition of Taxes in Tax Revenues in North Macedonia.



Source: Ministry of Finance of RNM

Meanwhile, below is presented a table which lets us understand the standard of the Republic of North Macedonia, in comparison with the countries of the region.

Table 6: Tax Rates in North Macedonia and the Region in 2018.

	RNM	Serbia	Albania	Kosovo	Bulgary	Croatia	Slovenia
Personal income tax	10% flat	10%-20%	13%-23% progressive	4%-20% progressive	10% flat	24%-36% progressive	16%-50% progressive
Corporate income tax	10% flat	15% flat	0-15% progressive	10% flat	10% flat	12%-18% progressive	19% flat
VAT	18% regular, 5% preferential	20% regular, 10% preferential	20% regular, 6% preferential	18% regular, 8% preferential	20% regular, 9% preferential	25% regular, 13% and 5% preferential	22% regular, 9.5% prefe-rential
Mandatory social contributions	27%	37.8%	27.9%	10%	23.7% to 24.4%	37.2%	38.2%
Periodic property tax	0.1%-0.2%	0.4%-2%	0.05-0.15%	0.05%-1%	0.15%	N/A	N/A
Property tax carried over	2%-4%	5%	1%	N/A	2%	5%	2%

Source: Ministry of Finance of RNM

As we can see from the table above, RNM is characterized by the lowest tax rates, where personal income and corporate income are taxed at a flat (proportional) rate of 10%, regular VAT at 18% and preferential at 5%, which remains the lowest in the region. Mandatory social contributions have a rate of 27%, which makes it second in the region after Kosovo, as well as property taxes of 2-4%.

Strategic Priorities for Tax Policy

The **Tax System Reform Strategy 2020-2023** of the Republic of North Macedonia outlines five priorities for tax policy and tax administration

- **Priority 1 – Increasing Tax Justice,** to ensure that everyone fulfills their social obligation and pays their fair share of tax. For the next three years, the main focus will be on establishing vertical equity, which can be considered more broadly than tax progressivity. The expected results are a redesigned model for progressive taxation, an implementation of minimum base erosion and profit shifting (BEPS) standards, a revision of national legislation to meet EU expectations.

- **Priority 2 – Improving revenue collection by increasing the efficiency and productivity of the tax system**, through the review of the tax base, the reduction of tax arrears, the implementation of the register of beneficial owners, a more efficient fight against illegal activities and evasion fiscal. and a strengthened institutional capacity. Anticipated measures to improve the efficiency and productivity of the tax collection system include the revision of existing tax regulations, the introduction of advanced technologies, the strengthening of institutions' capacities, the modernization and automation of work processes, an expanded institutional coordination as well. as well as better cooperation at the international level.
- **Priority 3 – Increasing tax transparency**, including improving the exchange of information between tax authorities and other entities, and based in particular on electronic services. This priority is expected to result in increased fiscal education and increased voluntary compliance.
- **Priority 4 – Improving the Quality of Services**, designed to simplify and speed up procedures and reduce the administrative burden. The intended results are more digitized services, a better management of the granting of import-export licenses, the elimination of unnecessary non-tariff barriers, as well as the improvement of internal control and tax control.
- **Priority 5 – Introducing the Green Tax**, in order to stimulate taxpayers to reduce their polluting behaviors and/or activities. The goal is to curb pollution and protect natural resources and increase government revenue.

It is worth emphasizing that all these tax reforms are essential for meeting the standards and requirements set by the European Commission for the Republic of North Macedonia's accession to the European Union

CONLUSION

Inflation targeting focuses on the management of expectations, which is seen as a very important element for the successful implementation of monetary policy. One consequence of adopting the inflation targeting regime is that it sets a nominal target which helps in determining inflation expectations. Modern monetary theories show that a strong nominal target that sets inflation expectations has many consequences for actual inflation and deflation is very unlikely to occur. These theoretical results have emerged from recent experience where monetary policy has worked to control inflation in many industrialized countries. This is not due to the fact that Central Banks are more in control of the monetary policy transmission mechanism, but due to the fact that currently Central Banks in

industrialized countries have set a clearer nominal target. The results have been very sensitive both in controlling the level of inflation and the level of production. This has been achieved through the adoption of inflation targeting in countries such as New Zealand, Canada, England, Sweden and Australia and to some extent in the European Monetary Union.

Monetary policy becomes more difficult during deflationary periods when the interest rate reaches zero as the general rules of monetary policy design are no longer applicable. In recent years, much research has been done on how central banks should design monetary policy according to the Taylor rule, where the central bank sets the short-term interest rate at the level that coincides with the optimal level of the output gap and inflation.

The consequences of inflation are not limited to the impoverishment of holders of depreciated currency. They also set in motion business cycles characterized by unprofitable long-term investments, misdirected by the inaccurate signals of artificially low interest rates. When the central bank raises interest rates to curb inflation, these unprofitable investments are exposed and wither in the absence of monetary oxygen. With them, businesses and jobs are extinguished, goods and services shrink, incomes and expenses decrease, and thus in a chain way it leads to economic recession.

The fundamental problem with inflation remains the monetary system that currently reigns in the world, a system of paper money not backed by physical goods such as gold, which is subject to numerous and frequent manipulations in the name of economic science. In this uncertain world, the individual is left to house wealth only by exchanging depreciating currency for real estate and other physical assets.

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