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ANALYSIS OF THE DEGREE OF LEGAL INDEPENDENCE OF THE CROATIAN NATIONAL BANK AND THE NATIONAL BANK OF THE REPUBLIC OF NORTH MACEDONIA[**]

ABSTRACT: The stability of each country's monetary system depends on the quality of operations of its central bank, as one of the most important institutions. Due to their great importance, central banks hold a special place in scientific analysis. For a central bank to successfully achieve its objectives, it has to operate independently of the executive and legislative powers. Through content analysis and the comparative method, this paper analyzes and compares different parameters and indices measuring the independence of the central banks of the Republic of Croatia and the Republic of North Macedonia. Considering that the independence of a central bank is inextricably linked with its credibility, this paper conducts research that answers the question – what is the level of legal independence of the Croatian National Bank and the National Bank of the Republic of North Macedonia? It can be said that, in the last

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decade, both the legal and actual independence of these central banks has reached its peak, but a certain degree of political dependence is still noticeable. There are certain differences in terms of political influence from country to country, but in any case, the syndrome of political dependence in former Yugoslav countries when compared to developed countries is extremely recognizable. The Republic of Croatia, as a member of the European Union, had to harmonize its laws on this issue, so it can be said that there are certain differences compared to other countries in this region. Central banks in countries that once belonged to the same communist bloc, and which today have different statuses in relation to the European Union, are excellent examples for analyzing the degree of operational independence in relation to state power. The status of the central bank in a certain national and economic system depends on the legislation of that country, i.e., the constitutional norms and laws governing the central bank.

Keywords: Croatian National Bank, National Bank of the Republic of North Macedonia, independence of central banks, legislative power, executive power, Cukierman Index

INTRODUCTION

The contemporary world of banking, money flow, and financial institutions and their administrative regulations would be almost unimaginable without central banking. Money has existed for millennia and banks for centuries, but pinpointing the emergence of the first central banks in today's sense is no easy task.[1]

Contemporary central banks are organized in various ways from country to country and perform different functions. They can also have different names, such as central bank, national bank, reserve bank, state bank, and the name of the country can be used with the noun "bank" as well. Central banks have never been more powerful than they are today. Monetary policy has become a central instrument of macroeconomic stabilization and monetary policy is in the hands of independent central banks in an increasing number of countries.[2]

The greater the degree of independence of a central bank, the easier it is for it to identify signs of financial problems and warn financial markets about

[1] Rapajić, M., Dimitrijević, P. (2018). Pravna priroda Narodne banke Srbije u svojstvu vršioca uprave (centralno bankarstvo, položaj i pravni karakter Narodne banke), *Collcetion of Papers of the Faculty of Law in Niš*, no. 81, LVII, 188.

[2] Fabris, N. (2006). *Central banking in theory and practice*. Podgorica: Central Bank of Montenegro, 41.

them. This is precisely why independence is seen as a way of bringing the economy to a higher level. The fact is that an independent central bank is less likely to be exposed to the inflationary bias inherent to monetary policy.[3]

The independence of a central bank implies the existence of a high degree of decision-making freedom in conducting monetary policy. Increasing the independence of a central bank is primarily aimed at its protection from short-term and often myopic political pressures, which are linked to the electoral cycle. The main objective of a central bank is price stability. Numerous empirical studies have proven that this objective is best achieved by an independent central bank.[4]

Central banks in every country are considered institutions of immense importance for the functioning of a country. The purpose of this paper is to analyze the operations and the degree of independence of the Croatian National Bank and the National Bank of the Republic of North Macedonia, focusing primarily on legal provisions related to key aspects for achieving and maintaining price stability. Emphasis is placed on explaining the main objectives of the aforementioned central banks, as well as their authority to determine and implement monetary and foreign exchange policies and to appoint and dismiss bank staff. Mutual relations with the executive and legislative powers are highlighted, and the restrictions on state funding and other legal aspects determining the strength of the mandate and independence of a central bank are explained. This analysis provides a historical perspective of the evolution of independence of the aforementioned central banks from the first year of transition to the present. This research aims to show why and how important it is for a central bank to operate as an independent institute. To achieve this, it is necessary for it to have leadership that is entirely independent of political influence. This implies a transparent selection of the central bank governor, as well as the main decision-making bodies.

The analysis of this topic leads to the conclusion that there is rich theoretical and empirical literature on the independence of central banks. Unlike fiscal policy, monetary policy should be independent, and the highest officials must have a term longer than the political cycle. The Great Depression and the collapse of the gold standard resulted in a widespread practice of governments

[3] Ćorić, T., Cvrlje, D. (2009). *Central Bank Independence: The Case of Croatia*. EFZG working paper series (09), 4.

[4] Gozev, R. (2006). Strengthening the Guarantees for Independence of a Central Bank in Compliance with EU Requirements: The Case of Bulgaria. *The European Integration Process: A Changing Environment for National Central Banks*, 112.

taking over monetary policy where setting the official interest rate was a governmental exercise.[5]

By the mid-1980s, most central banks were subordinate to governments and functioned almost like a department of the Ministry of Finance responsible for various functions, including financing the national deficit. This was a period marked by continuous periods of high inflation. The trend of delegating monetary policy to an independent institution began in the 1980s and was particularly pronounced during the 1990s based on three foundations: the success of the Bundesbank in controlling inflation and the success of the German economic model, theoretical literature on inflationary bias - discretionary monetary policy – and empirical literature on the relationship between an independent central bank and macroeconomic aggregates.[6] The essence is understanding that monetary authority can successfully implement and maintain a socially desirable target path for price stability if it has a clear mandate and is independent in deciding how to implement monetary policy.[7]

Regardless of the significant differences between central banks, their position in a particular country and its economic system depends on: 1) the law on the central bank, which determines the institutional construction, functions, and authority of the central bank 2) laws that normatively regulate the issuance of national currency 3) other legislation, such as laws on banks, insurance organizations, and other financial institutions. The rules of the International Monetary Fund, World Bank, and financial and banking institutions of supranational organizations (for example, the European Union) also influence the activity and organizational structure of central banks. Differences in the way of forming, administrative authority, the election of the highest officials, and control over central banks exist, but two models of central banking can still be singled out –European and American.[8]

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[5] Goodhart, C.A.E. (2010). *The changing role of central banks*. BIS Working Paper, 326.

[6] Debelle, G., & Fisher, S. (1994). How independent should a central bank be? In: Fuhrer, J. C (Eds.), *Goals, Guidelines and Constraints Facing Monetary Policymakers*. Federal Reserve Bank of Boston, 26

[7] Niemann & von Hagen. (2008). Coordination of Monetary and Fiscal Policies: A Fresh Look at the Issue. *Swedish Economic Policy Review*, vol. 15 (1), 89–124.

[8] Rapajić, M., Dimitrijević, P. (2018). Pravna priroda Narodne banke Srbije u svojstvu vršioca uprave (centralno bankarstvo, položaj i pravni karakter Narodne banke), *Collcetion of Papers of the Faculty of Law in Niš*, no. 81, LVII, 189.

HISTORICAL REVIEW OF THE BANKING SECTOR IN THE REPUBLIC OF CROATIA

Taking into account the economic and social aspects (regardless of the differences between central banking institutions both in comparative and historical terms), the most significant objective for which central banks were created is the maintenance of monetary stability, and consequently the increase in employment and income levels, and economic development and prosperity of the country. Therefore, objectives set by the constitution, but more so by laws (given that the legislative process is simpler than the process of creating a constitution), are characteristic of central banking after the end of World War II.[9]

The dependence of the central bank on state powers, or on an extremely authoritarian executive, continued in the Yugoslav socialist federation, even though all authorities were subordinate to and under the control of the Federal Assembly in the parliamentary system, at least formally.

> "In Yugoslavia, throughout the period after World War II until the breakup of the SFRY, the central bank never had full independence, which is understandable given that in every country, the socio-political order, or the nature of the economic system, is the basic determinant of the domestic monetary and financial system. Therefore, the role of the National Bank in Yugoslavia in the period 1944–1991 cannot be evaluated outside the framework of the institutional structure of Yugoslav society and the political and economic system. In certain historical periods, the existing institutional solutions directly predetermined the position, role, and scope of operations of the National Bank and other financial institutions in Yugoslavia".[10]

After gaining independence in 1991, political turbulence and war paralyzed a more serious transition and redesign of the banking sector in Croatia. Only the branch of the National Bank of Yugoslavia (hereinafter NBY) in Zagreb was promoted to the central bank of Croatia, in accordance with the examples of the dissolution of other federations. At the time of gaining independence, there were 26 banks operating in Croatia, of which 20 were "old" credit institutions. The two largest banks – Privredna banka and Zagrebačka

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[9] Rapajić, M., Dimitrijević, P. (2018). Pravna priroda Narodne banke Srbije u svojstvu vršioca uprave (centralno bankarstvo, položaj i pravni karakter Narodne banke), *Collcetion of Papers of the Faculty of Law in Niš*, no. 81, LVII, 189.

[10] Hoffman, G. (2004). *Narodna banka 1944–1991.* Belgrade, 19, in: Rapajić, M. (2021). Kraći pogled na odnose Narodne banke Srbije sa zakonodavnom i izvršnom vlašću. *Zbornik radova „Usklađivanje pravnog sistema Srbije sa standardima EU",* Kragujevac, 161.

banka, operated throughout the Republic of Croatia. Also, 18 financial institutions were medium-sized, regional banks, and 6 new – private banks operated only in Zagreb.[11]

Due to the freezing of deposits in Belgrade, 197 banks in Croatia were technically illiquid, and many were insolvent. In the second half of 1991, the NBY suspended the transfer of deposits to banks in Croatia. These deposits were deposited in the central bank because they had a foreign denomination. At the moment of suspension of deposit transfers, about 5.8 billion German marks were blocked in the NBY. A program of decentralized linear rehabilitation was launched to rehabilitate the banking sector, with two important lines of action. The first one meant that government bonds were transferred to banks to consolidate balance sheets, while the other meant that large-denomination state bonds were transferred to state-owned enterprises in order to repay bank loans. This had only a cosmetic significance, as this mechanism "decontaminated" bank balance sheets, while operational efficiency reform was omitted.[12]

The crisis in the banking sector provoked selective measures of traditional rehabilitation, while in some banks, measured (selective and calculated) liquidity support was applied. In December 1998, a new Banking Law was adopted that radically changed the "balance of power" of certain banks, prudential standards, and the "terrain" of the Croatian banking sector. The capital adequacy standard was increased from 8 to 10%, with the strengthening of the regulatory infrastructure. Also, parameters for assessing risk exposure, bank licensing procedures, internal and external audit, and supervision standards were tightened. Based on the new regulations, a procedure for the liquidation of 11 small and medium-sized banks was initiated, and 5 banks were placed under administrative control. The 1999 budget rebalancing approved additional funds for the Bank Rehabilitation and Deposit Insurance Agency to refinance the deposits of failed banks. The objective of all these measures was harmonization with generally accepted international standards for bank operations, as well as the introduction of financial discipline in the disorganized and inefficient banking sector. In doing so, the implementation of new regulatory mechanisms had "an ear" for inherited and emerging problems in the banking sector of Croatia in order to preserve financial stability in the transitional phase of development. The new measures were implemented at the micro and

[11] Barisitz, S. (2008). *Banking in Central and Eastern Europe 1980–2006.* London, UK: Routledge (Taylor & Francis Group), 48.

[12] Jovančević, R. (2002). Reforming the Banking System in Croatia and its Broader Macroeconomic Environment. Chapter in: *Banking Reforms in South–East Europe*, Editor: Šević, Ž.; Edward Elgar Publishing Limited, Cheltenham, UK, 245.

macro levels in order to restore confidence in the banking system and increase the efficiency and competitiveness of banks and savings institutions.[13]

Very soon there were serious changes in the market structure and competition. A number of banks were shut down, new banks were established, and the market was opened for the entry of foreign banks (by establishing branches or buying smaller banks). These processes improved the competitive environment and reduced concentration in the Croatian banking market. The structure of the banking industry was transformed from an oligopoly with clear monopolistic elements, to an oligopoly with visible elements of competition.[14] Considering the volume of financial resources involved, Croatia incurred significant fiscal costs for bank rehabilitation. The cumulative public debt for bank rehabilitation in Croatia in the period 1991-1999 was estimated at 32% of the GDP.[15]

The marketization of the banking sector enabled a strong "credit boom" that threatened to jeopardize monetary stability. In order to limit the bilateral borrowing enthusiasm in the bank (motivated by profit) - non-bank transactors (motivated by economic prosperity) relationship, the CNB established an administrative mechanism for directing placements. In January 2003, the CNB made a Decision on the mandatory purchase of CNB notes, obligating banks with annual credit growth of more than 16% to invest double the amount of excess in low-yield CNB notes.[16]

Later, this administrative standard was suspended, but a stricter regulatory mechanism for calculating capital adequacy was established. Also, a special (penalty) system of mandatory reserve allocation on foreign cross-border loans was established. Stringent regulation and market circumstances forced banking groups to channel credit potential through substitutes for banking services, primarily through leasing and asset management. This formed a non-banking segment of the financial system, creating conditions for cross-competition. However, regardless of these tendencies, the financial system of Croatia at the end of the transition episode was extremely bank-centric, as banks owned 82% of total financial assets.[17]

[13] Jovančević, R. (2002). Reforming the Banking System in Croatia and its Broader Macroeconomic Environment. Chapter in: *Banking Reforms in South–East Europe*, Editor: Šević, Ž.; Edward Elgar Publishing Limited, Cheltenham, UK, 245.

[14] *Ibid.*

[15] Jankov, L. (2000). *Banking Sector Problems: Causes, Solutions and Consequences*. Zagreb: Croatian National Bank, Survey 1, 8.

[16] Croatian National Bank. (2004). *Annual Report*. Zagreb: CNB, 56.

[17] EBRD, (2005). *Transition Report 2001 (Business in transition)*. London, UK: European Bank for Reconstruction and Development, 118.

CROATIAN NATIONAL BANK

The Croatian National Bank (hereinafter CNB) is the central bank of the Republic of Croatia. In achieving its objectives and performing its tasks, the CNB is independent and autonomous. The CNB has the status of a legal entity but is not registered in the court register. The headquarters of the CNB is in Zagreb. The seal of the HNB contains the image of the coat of arms of the Republic of Croatia and the name CNB. It is represented by the governor and is exclusively owned by the Republic of Croatia. The CNB is an integral part of the European System of Central Banks (ESCB). The CNB is obligated, in accordance with the provisions of the Treaty on the Functioning of the European Union, the Statute of the ESCB and the European Central Bank, and fully applicable European Union legislation and the CNB Act, to work towards achieving the objectives and carrying out the tasks of the ESCB.[18]

In accordance with Article 130 of the Treaty on the Functioning of the European Union and Article 7 of the Statute of the ESCB and ECB, the CNB and members of its bodies are independent in achieving their objective and in performing their tasks based on the CNB Act, the Treaty on European Union, the Treaty on the Functioning of the European Union, and the Statute of the ESCB and ECB. The CNB and members of its bodies do not seek nor are bound by instructions from the institutions and bodies of the European Union, governments of the Member States of the European Union, and other bodies. The institutions and bodies of the European Union, governments, agencies, offices, and other bodies of the Member States of the European Union are obligated to respect the independence of the CNB as stipulated in Article 130 of the Treaty on the Functioning of the European Union and Article 7 of the Statute of the ESCB and ECB, and cannot influence the independence of the CNB, the making and implementation of its decisions, and its organs, and cannot approve, annul, delay, repeal, or otherwise influence any decision of the CNB within its authority. These provisions do not call into question the powers of the ECB according to the Statute of the ESCB and ECB in relation to the Croatian National Bank.[19]

[18] Croatian National Bank. (2004). *Annual Report*. Zagreb: CNB, 57.

[19] Croatian National Bank. (2004). *Annual Report*. Zagreb: CNB, 57.

THE DEGREE OF INDEPENDENCE OF THE CROATIAN NATIONAL BANK

In most modern economies, the role of central bank independence has become more important. Central Bank Independence (CBI) is seen as a way of bringing the economy to a higher level. It is argued that an independent central bank is more credible and that a higher degree of central bank independence allows the central bank to identify signs of financial problems and warn financial markets. Furthermore, an independent central bank is less likely to be exposed to the inflationary bias inherent in monetary policy and is more aware of the inflationary costs of expansionary monetary policy. This is consistent with Friedman's theoretical concept that the phenomenon of inflation should be regulated by controlling the amount of money that the central bank injects into the national economy. To achieve the main objective – price stability, it is necessary for the central bank to be as little associated with the government as possible. However, governments generally have some influence on central banks, even in the case of banks claiming to be independent.[20]

In this part of the text, we examine the level of independence of the CNB. The Act on the Croatian National Bank (Art. 2, para. 2) states that the CNB is independent in achieving its objectives and tasks. It is also stated that all its members are independent in making and implementing their decisions and do not depend on or seek any instructions from the country or its institutions. When it comes to functional independence, we must examine the degree of freedom in choosing the objectives of monetary policy. The main objective of the CNB is to achieve and maintain price stability. According to Art. 3.2., the CNB will support the economic policy and operate on the principles of open market economy and free competition, as long as this does not jeopardize its main objective. As for its main objective, the CNB has adapted its legislation to the requirements of the Maastricht agreement.[21]

In examining the institutional freedom of the CNB, emphasis should be placed on the freedom to choose the instruments of monetary policy, their definition, and implementation. The CNB claims to be independent while implementing its decisions. It is also stated that this does not depend on the instructions of the Croatian government, bodies representing the EU, or a third party. In achieving its objectives, but not endangering its main objectives and tasks, the CNB is allowed to cooperate with the government and state bodies.

[20] Eijffinger S.C.W. et al. (1997). Central Bank Independence: A Panel Data Approach. *Public Choice*, vol. 89, 163–182.

[21] Croatian National bank, The act on the Croatian National bank, Publication: June 2008, http://www.hnb.hr/propisi/zakoni-htm-pdf/e-zakon-hnb-2008.pdf?tsfsg=df72c24360efa155d626a7396bdeb798, accessed on October 15, 2022.

The government provides the CNB with all proposals and reports related to the objectives, operations, and tasks of the CNB. In addition, the Government also submits decision proposals, directives, and acts before they are forwarded. The CNB Council gives its opinions. The Ministry of Finance consults with the CNB at least once every six months on semi-annual plans for domestic and foreign borrowing (Art. 38). Furthermore, the Ministry of Finance is obligated to inform the CNB about all transactions concerning domestic and external debt. The CNB can propose the adoption of a law; related to its objectives, tasks, or generally related to its operations, which the government is expected to then propose to the Parliament (Art. 39.1). In the case of the CNB, the law emphasizes the independence of functions and their implementation.[22]

Personal independence refers to the role and status of the central bank. It also refers to the appointment and election process, dismissal from office, term of office, and the possibility of re-election.

The CNB Council consists of the governor, four vicegovernors at the most, the deputy governor, and up to 8 independent members. The governor of the CNB is appointed by the Croatian Parliament on the proposal of the Elections, Appointments, and Administration Committee, taking into account the opinion of the Finance and Central Budget Committee. In Croatia, the governor's term lasts 6 years. The deputy governor and vicegovernors are appointed by the Croatian Parliament on the proposal of the CNB governor. Independent members of the CNB Council are appointed by the Croatian Parliament on the proposal of the Elections, Appointments, and Administration Committee, taking into account the opinion of the Finance and Central Budget Committee. Members of the CNB Council must be citizens of the Republic of Croatia and should have professional experience in the monetary, financial, banking, or legal sector. Members of the CNB Council are appointed for a period of six years. The law usually sets certain restrictions for members of the Council to avoid possible conflicts of interest, so there are also restrictions in Croatia that members should comply with, which is that they cannot be representatives in the Parliament or perform duties to which they had been appointed by the Parliament or the Government. Furthermore, a CNB member cannot be a member of the Government. Also, they cannot perform duties in the local and regional self-government bodies, political parties, and trade unions. Members are not allowed to work as associates in banks, audit firms, and other legal institutions related to banks or controlled by the CNB. Also, they cannot own shares or holdings in legal entities that are authorized or under the supervision of the CNB, nor may they own shares or holdings in other legal entities

[22] Croatian National bank, The act on the Croatian National bank, Publication: June 2008, http://www.hnb.hr/propisi/zakoni-htm-pdf/e-zakon-hnb-2008.pdf?tsfsg=df72c24360efa155d626a7396bdeb798, accessed on October 15, 2022.

connected with said entities by ownership, management, or function. In addition, the spouse and children of a member may not own shares or holdings in institutions that are authorized or under the supervision of the CNB (Art. 45.). In terms of removal from office, it will occur in the case of a criminal offense, serious misconduct, and if they are permanently unable to perform their duties owing to illness. Moreover, this will happen if a member himself requests to be removed from office or if he fails to submit or submits false statements regarding restrictions.[23]

Financial independence refers to budgetary independence and the prohibition of monetary financing. Central banks should not allow themselves to fall into a position of insufficient financial resources necessary for fulfilling their duties. There are certain issues that central banks must address to be financially independent; managing the budget, how to offset a net loss, whether government funding is allowed and if so, when it is permissible, etc. It is important to note that the CNB is independent of the Ministry of Finance. However, certain contact exists. The CNB performs the function of a fiscal agency, a depositary, a participant in the legislative process, and a consultant to the Ministry of Finance. Nevertheless, the CNB asserts that the bank manages the budget independently of any government institution. The CNB Council adopts the financial plan, while capital remains in the hands of the state. As for the net loss, if it occurs, it is usually covered by CNB reserves. In case of insufficient reserves, the loss can also be covered by the state budget or by issuing shares. In Croatia, direct government funding is strictly prohibited, but the CNB is allowed to buy government securities on the secondary market, indirectly financing the government.[24]

The increasing importance of CBI[25] is present in most developed economies. CBI is perceived as a conventional trend that almost all central banks follow. It seems to be a requirement for directing credible monetary policy.

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[23] Croatian National Bank, The act on the Croatian National Bank, Publication: June 2008, http://www.hnb.hr/propisi/zakoni-htm-pdf/e-zakon-hnb-2008.pdf?tsfsg=df72c24360efa155d626a7396bdeb798, accessed on October 15, 2022.

[24] *Ibid*.

[25] *Central bank independence* – the earliest definition offered is David Ricardo in to his "Plan for the Establishment of a National Bank" in 1824, where he said, "It is said that Government could not be safely entrusted with the power of issuing paper money; that it would most certainly abuse it… There would, I confess, be great danger of this, if Government — that is to say, the ministers — were themselves to be entrusted with the power of issuing paper money. But I propose to place this trust in the hands of Commissioners, not removable from their official situation but by a vote of one or both Houses of Parliament. I propose also to prevent all intercourse bettween these Commissioners and ministers, by forbidding every species of money transaction between them. The Commissioners should never, on any pretence, lend money to Government, nor be in the slightest degree under its controul or influence... If Government wanted money, it should be obliged to raise it in the

Delegating monetary policy to an independent central bank should encourage greater price stability and a better overall economic situation, as an independent central bank is less likely to be exposed to the inflationary bias inherent in monetary policy and is more aware of the inflationary costs of expansionary monetary policy.

EVALUATION OF THE INDEPENDENCE OF THE NATIONAL BANK OF THE REPUBLIC OF NORTH MACEDONIA

The interconnection between the central banking institution, as the highest monetary institution, on one hand, and the executive branch on the other, is crucial for the institutionalization of central bank independence. If we analyze the laws of different legal systems in which different models of executive power organization are also present, it is not difficult to notice that the central bank in some of them is subject to detailed legal regulation. Such a normative approach is less characteristic of some other economic and financial institutions. The realization of the objectives and execution of the functions of the central bank is of utmost importance in the economic life of any country, given the far-reaching consequences, not only on the economy and finance but indirectly on all direct and indirect budget beneficiaries. As the executive branch creates the political course of the country and is responsible for the state of the nation not only when it comes to the economy, finance, education, culture, and foreign policy but also partially to the monetary sphere, it is particularly interested in the legitimate functioning of the central bank. Different views of the main directions of macroeconomic policy, and central bank leadership in relation to the main executive representatives, can have far-reaching and usually very negative consequences for the entire economy. To prevent this to a greater or lesser extent, based on the constitution and laws in many legal systems, it is stipulated that government influence on the central bank can be dual: 1) staffing and 2) political (control-supervisory). There are fewer countries in the world where the government, the prime minister, or the president of the state do not have a certain influence on the selection of the highest officials in the central bank. The level of this influence can range from consultations,

legitimate way; by taxing the people; by the issue and sale of exchequer bills, by funded loans, or by borrowing from any of the numerous banks which might exist in the country; but in no case should it be allowed to borrow from those, who have the power of creating money."

to proposals, to appointments. When it comes to the parliamentary system of governance, competent administrative sectors can also play a significant role.[26]

The independence of a central bank is considered a key prerequisite for achieving the primary objective of a central bank, which is price stability. Adequate institutional mechanisms protect a central bank from short-term political events and are key in preserving its control over monetary aggregates, maintaining the credibility of the central bank and, consequently, price stability. Current trends regarding institutional arrangements point to an institutional separation of responsibility for monetary and fiscal policy, accompanied by a high degree of independence for central banks, which can be seen as protection from rash fiscal policy. The first Law on the NBRNM was enacted in 1992, establishing the NBRNM as the central bank of the newly independent state. In order to strengthen the independence of the central bank, the legal framework has been changed several times, including the adoption of a new central bank law in 2002 and 2010.[27]

The assessment of the NBRNM's independence is based on the Cukierman et al. (1992) index (hereinafter: Cukierman's index), as one of the most frequently used indices, and the modified Cukierman index of Jacome and Vazquez (2005) (hereinafter: MCI). The index evaluates the legal aspect of independence as one of the main components of real independence, although the latter depends on many other additional factors. The measurement is based on the statutory provisions of the central bank that regulate its mandate, authority, tasks, and operations and do not reflect the aspect of the practical application of legal provisions. Unlike other research papers that evaluate the NBRNM's independence over a certain period of a year, this paper provides a historical perspective by measuring the level of independence provided by the laws on the NBRNM adopted from 1992 to the present day.

CUKIERMAN INDEX

The Cukierman Index uses 16 legal variables in the following 4 clusters: the main executive director (appointment, dismissal, mandate, government duties), defining the formulation of monetary policy (authority to make decisions on monetary policy, resolving conflicts related to monetary policy, and

[26] Purić, S., Rapajić, M. (2018). Odnos Centralne banke i grana državne vlasti. *Glasnik prava*, br. 1, vol. IX. Kragujevac, 54.

[27] Jankoski, B. (2010). *Trends and challenges of the contemporary central banking - a case study for the National Bank of the Republic of Macedonia*. Saarbrucken: VDM Verlag Dr. Muller Gmbh & Co.KG.

the inclusion of the central bank in the budget process), central bank objectives and restrictions on the central bank's lending to the government (safe and unsafe lending, potential borrowers, terms and conditions of lending). The coding scale ranges from 0 (the lowest level of independence) to 1 (the highest level of independence). A higher number indicates a stronger mandate and independence of the central bank from the executive branch in the pursuit of price stability. The coding for the first group of variables depends on the government's involvement in the appointment and dismissal process of the governor and his mandate. Less government involvement and a longer term imply greater insulation of monetary policy from short-term political considerations that can threaten price stability. Similarly, less government involvement in the formulation of monetary policy (second group) indicates greater independence of the central bank. The assessment of objectives (third group) depends on the importance given to price stability compared to other objectives that could conflict with price stability. A higher score for lending restrictions (last group) is assigned when lending to the government is not allowed or is allowed under strict conditions. Also, the stricter the lending conditions (interest rate, maturity, collateral), the higher the value of this variable. The legal restrictions on the central bank's financing of the government is considered instrumental in preserving the central bank's control over monetary aggregates and inflation. Its importance is even more pronounced for transition economies with undeveloped financial markets where there is a greater need for central bank financing. The composite Cukierman index of independence is calculated as a weighted average of the values assigned to individual variables. The largest weight is assigned to the group of variables related to lending restrictions to the government (50%), the executive director's official group of criteria carries a weight of 20%, and the policy formulation and objectives groups each carry 15%. For the main executive director, coding at the group level is performed as a simple average of the coding of the four variables in the group. Coding for the policy formulation group is performed as a weighted average of the codes of each individual variable in the group. Each of the 8 variables in the group regarding lending to the government is assigned an individual weight. Generally speaking, the Cukierman Index indicates that the legal independence of the NBRNM has increased over the years. The first law on the NBRNM, adopted in 1992, provides only a moderate level of independence with a composite index value of 0.60. The law adopted in 2002 strengthened its mandate and independence as seen through the increased index value (0.70), and the law adopted at the end of 2010, subsequently amended several times, provides a high degree of independence with an index value reaching 0.92[28].

[28] Rating independence given by the Law on NBRM adopted in 2010 takes into account the amendements and supplements of the Law adopted in 2012, 2014, and 2015.

The index indicates room for further strengthening in the areas of appointment, dismissal, governor's mandate, and the central bank's participation in the budget process.[29]

Table 1. Measurement of the independence of the NBRNM - Cukierman Index

No. of Variable	Description of variable	Weight	Numerical value	2011–2017	2002–2010	1992–2001
1.	**Director General**	0.20		0.77	0.77	0.44
	a. Mandate			0.75	0.75	0.75
	• Over 8 years • 6 to 8 years • 5 years • 4 years • Less than 4 years		1.00 0.75 0.50 0.25 0.00			
	b. Who Appoints the Director			0.50	0.50	0.50
	• Central Bank Committee • Central Bank Committee Council, Executive Power, Legislative Power • Legislative Power • Executive Committee • One of the Two Members of the Executive Power		1.00 0.75 0.50 0.25 0.00	0.50	0.50	0.50
	c. Dismissal			0.83	0.83	0.50
	• No Provisions for Dismissal • Only for Reasons Unrelated to Politics • By Order of the Central Bank's Main Board • For Legal Reasons • Unconditional Dismissal by Legislative Power • By Order of Executive Power • Unconditional Dismissal by Executive Power		1.00 0.83 0.67 0.50 0.33 0.17 0.00	0.83	0.83	0.50
	d. The Possibility for the General Director to Have Another Role in the Government			1.00	1.00	0.00

[29] Cukierman, A., Kalaitzidakis, P., Summers, L., Webb, S. (1993). Central bank independence, growth, investment, and real rates. *Carnegie-Rochester Conference Series on Public Policy*, 39 (1), 95–140.

No. of Variable	Description of variable	Weight	Numerical value	2011–2017	2002–2010	1992–2001
	• No • Only With the Approval of the Executive Power • No Prohibition for the General Director to be in the Executive Branch		1.00 0.50 0.00	1.00	1.00	0.00
2.	**Policy Formulation**	0.15		0.75	0.45	0.37
	a. Who Formulates the Monetary Policy	0.25		1.00	1.00	0.67
	• The Bank is Entirely Independent • The Bank Participates but Has Little Influence • The Bank Makes Decisions on the Advice of the Government • The Bank Has No Voting Rights		1.00 0.67 0.33 0.00	1.00	1.00	0.67
	b. Who Has the Final Say in Conflict Resolution	0.50		1.00	0.40	0.40
	• The Bank According to Rules that Are Clearly Defined by the Law on Objectives • The Government on Issues that Are Not Clearly Defined as the Bank's Objectives or in Case of Conflict within the Bank • The Central Bank's Board, Executive Power, and Legislative Power • Legislative Power According to Political Mandate • Executive Power According to Political Mandate • Executive Power Has Unconditional Priority		1.00 0.80 0.60 0.40 0.20 0.00	1.00	0.40	0.40
	c. Role in Budget Decision-Making	0.25		0.00	0.00	0.00
	• Active Role of the Central Bank • Central Bank Has No Influence		1.00 0.00	0.00	0.00	0.00

No. of Variable	Description of variable	Weight	Numerical value	2011–2017	2002–2010	1992–2001
3.	**Objectives**	0.15		1.00	1.00	0.60
	• Price Stability Is the Main Objective and the Central Bank Has the Final Say in Case of Conflicts With Other Government Objectives • Price Stability Is One of the Objectives Compatible With Other Government Objectives That Maintain a Stable Banking System • Price Stability Is One of the Objectives That Is Potentially Conflicting With Objectives Such As Full Employment • No Objective Condition in the Bank Charter • Stated Objectives Do Not Include Price Stability		1.00 0.80 0.60 0.20 0.00	1.00	1.00	0.60
4.	**Restrictions on Loans to the State**	0.50		0.50	0.33	0.37
	a. Restrictions on Unsafe Lending	0.15		1.00	0.67	0.67
	• No Advance Lending • Advance Lending but With Strict Restrictions • Advance Lending but Without Strict Restrictions • No Legal Restrictions on Lending		1.00 0.67 0.33 0.00	1.00	0.67	0.67
	b. Secured Lending	0.10		1.00	0.67	0.67
	• Not Allowed • Allowed With a Limit of up to 15% of Government Revenue • Allowed Above the Limit of 15% of Government Revenue • No Legal Restrictions on Lending		1.00 0.67 0.33 0.00	1.00	0.67	0.67
	c. Credit Terms	0.10		1.00	0.33	1.00

No. of Variable	Description of variable	Weight	Numerical value	2011–2017	2002–2010	1992–2001
	• Controlled by the Bank • Determined by the Bank's Statute • In Agreement Between the Central Bank and the Executive Power • Determined Exclusively by the Executive Power		1.00 0.67 0.33 0.00		1.00 0.33	1.00
	d. Potential Borrowers from the Bank	0.05		1.00	1.00	1.00
	• Government Only • All Levels of Government • All of the Above and Public Enterprises • Public and Private Sector		1.00 0.67 0.33 0.00	1.00	1.00	1.00
	e. Central Bank Lending Limits Defined in	0.025		1.00	1.00	1.00
	• Currency • Shares, Bonds, or Capital • Government Revenue • Government Expenditures		1.00 0.67 0.33 0.00	1.00	1.00	
	f. Maturity of Loans	0.025		1.00	0.25	0.25
	• Up to 6 Months • Up to One Year • More Than One Year • No Legal Restrictions on Loan Maturity		1.00 0.67 0.33 0.00	1.00	1.00	0.67
	g. Interest Rates on Loans Must Be	0.025		1.00	0.25	0.25
	• Above Minimum Rates • At Market Rates • Below Maximum Rates • Interest Rates Are Not Considered • No Interest on Government Debt at the Central Bank		1.00 0.75 0.50 0.25 0.00	1.00	0.25	0.25
	h. The Central Bank Can Prohibit the Purchase or Sale of Securities on the Market	0.025		1.00	1.00	1.00
	• Yes • No		1.00 0.00	1.00	1.00	1.00
	Total Index Value			**0.92**	**0.70**	**0.60**

Source: National Bank of the Republic of Macedonia, Journal of Central Banking Theory and Practice, vol. 6, No. 3, 2017.

The Law on the NBRNM was first adopted in 1992 as part of a legislative package, providing the basis for a new monetary system independent of the monetary system of former Yugoslavia. The NBRNM was established as the central bank responsible for the stability of the Macedonian currency, monetary policy, and the stability of internal and external payments. These three objectives of the central bank are also included in the Constitution. As a result, price stability is not explicitly stated as an objective of the central bank either in the law or in the Constitution. However, the Parliament adopted an annual Decision on the objective and objectives of monetary policy, which defines price stability as the central bank's objective. This shows some ambiguities and inconsistencies in the bank's objectives. Given that the Parliament's decision identified price stability as the main objective, the value of the variable assigned to it is not 0 but 0.60.

The formulation of monetary policy was not solely the responsibility of the central bank. The NBRNM was required to prepare an annual projection on monetary and credit aggregates, based on which the Parliament passed the Decision on the objectives and objectives of the monetary and credit policy for the following year. The decision defined numerical inflation targets and monetary aggregates in accordance with the inflation target. The foreign exchange regime and policy were also adopted by the Parliament annually by the Decision on foreign exchange policy and projection from the balance of payments. The law defines the instruments available to the NBRNM, including reserve requirements, loans to banks and other financial institutions, issuance of central bank bills, transactions with domestic and foreign securities, and interventions in the foreign exchange market. Decisions on the implementation of monetary and foreign exchange policy were adopted by two-thirds of the members of the bank's council. In case of disputes over monetary and foreign exchange policy, the Parliament had the final word. The central bank had no legal requirement to participate in any phase of the budget cycle. The preparation, adoption, execution, and supervision of the national budget were the responsibility of the executive and legislative powers. The inability of the central bank to participate in the budget process, along with the absence of full authority in formulating monetary policy and resolving conflicts, resulted in a low score for the bank policy formulation group (0.37).

The value of the executive director group is also quite low (0.44). The Governor was appointed by the Parliament, on the proposal of the President, for a term of 7 years, with the possibility of being re-elected only once. Re-election of the same council members was not allowed. Similar to the appointment process, the dismissal process was initiated by the president and decided by the Parliament. There were no provisions on the criteria for dismissal that would suggest that the Parliament had wide discretion when dismissing the Governor. Also, the law did not contain provisions prohibiting the governor from holding other positions in the government.

The law passed in 2002 granted somewhat greater independence to the NBRNM, as seen through the increased value of the composite index (from 0.60 to 0.70), which reflects improvements in all 4 clusters. The law established price stability as the central bank's primary objective. In addition, the NBRNM supported economic policy and financial stability without compromising its primary objective. This meant that the law was not fully in accordance with the Constitution, which defined currency stability, monetary policy, and stability of internal and external payments as the objectives of the NBRNM. However, this criterion was assigned a maximum value of 1.

The latest Law brought improvements in other segments that are not directly covered by the index. Independence in conducting monetary policy is reinforced by stipulating that council members and bank employees should not seek or receive any instructions from the government or other natural or legal persons. The previous provision allowing the Minister of Finance to participate in council meetings was replaced by a new provision stating that the presence of other members is allowed only at the invitation of the bank. However, the Minister of Finance and the Governor are required to meet regularly in order to coordinate monetary and fiscal policy. In doing so, the government is obligated to consult with the NBRNM when drafting laws and regulations that may have implications for the bank's objectives and functions, and the bank is allowed to express its opinion on these draft laws when they are debated in Parliament.

CONCLUSION

Through this paper, it is evident that the independence of a central bank is a key precondition for achieving the primary objective of the central bank, which is price stability. Adequate institutional mechanisms that protect the central bank from short-term political considerations are crucial in preserving the central bank's control over monetary aggregates, and the credibility of the central bank, and as a result, they are key to price stability. Whether discussing the Croatian National Bank or the National Bank of the Republic of North Macedonia, this research shows that a high degree of independence of central banks from political turbulence is of utmost importance for the stability of monetary systems and national economies as a whole.

For the Croatian National Bank, the most suitable indicator of independence is the governor's average mandate. Cukierman defined the upper limit for this rate as 0.2 – 0.24 when the governor is elected every 4 to 5 years. A lower rate indicates that the central bank is more isolated from government pressures and simultaneously indicates greater independence of the central bank in defining monetary policy objectives.

Based on Cukierman's index, it is evident that, in the case of the NBRNM, significant progress has been made in the degree of independence from political influence from the time the Republic of Macedonia became an independent country to the present day. As the independence of the NBRNM is based on legal regulations, the index alone cannot serve as an indicator of the actual independence of the central bank. Therefore, the results of measuring independence should be interpreted with caution. Actual and real independence seems like a challenging task and is usually measured through the rate of change of governors and questionnaires filled out by central banks. Based on the criteria for the governor's fluctuation rate, actual independence at the NBRNM seems high. The fluctuation rate is 0.16, which means approximately one governor every 6 years.

One thing that certainly needs to be taken into account when dealing with countries of former Yugoslavia is that the rates of fluctuation of governors, as well as the analyzed indices for measurement, are just one of the angles from which actual independence can be viewed and therefore cannot be used as strong evidence of *de facto* independence. By taking into account all indicators and looking at central banks within the broader picture of the entire country, it becomes evident that political influence on central banks in these regions is still very present. Although there have been certain shifts compared to a few decades ago, it cannot be said that the real interest of any of these countries is the permanent independence of central banks.

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