

NORTH MACEDONIA

Table 1 **2022**

Population, million ^a	2.1
GDP, current US\$ billion	13.6
GDP per capita, current US\$ ^a	6597.7
Upper middle-income poverty rate (\$6.85) ^b	19.1
Gini index ^b	33.6
School enrollment, primary (% gross) ^c	95.5
Life expectancy at birth, years ^c	74.5
Total GHG emissions (mtCO2e)	10.2

Source: WDI, Macro Poverty Outlook, and official data.
a/ Most recent WDI value (2020) for population.
b/ Most recent value (2019), 2017 PPPs.
c/ WDI for School enrollment (2020); Life expectancy (2021).

The economic growth is decelerating as inflationary pressures remain persistent, and public finances are stretched amidst monetary tightening and rising borrowing costs. Poverty reduction resumed slowly. Fiscal consolidation needs to be prioritized given new spending commitments for highways and public sector wages. Boosting growth calls for structural reforms that have been delayed amidst a parliamentary impasse. The outlook over the forecast horizon is positive, but downside risks prevail.

Key conditions and challenges

Despite setbacks stemming from the energy crisis and Russia's invasion of Ukraine, growth in early 2023 proved to be more resilient than expected. After surpassing a two-decade peak in 2022, inflation dropped to single digits in June 2023, but core inflation remained elevated. Poverty reduction has resumed in 2023 albeit at a slower pace, with the poverty rate projected to fall by less than 1 percentage point given the disproportionate erosion of real incomes of the relatively less well-off and an anemic labor market. Namely, the employment rate (15+) remained at just over 47 percent during 2021-22, and the reduction in the unemployment rate from 15.4 percent in 2021 to 14.4 in 2022 came on the back of the increase in inactivity of the older age cohort, rather than transitions into employment.

Fiscal policy continues to be challenging. The additional fiscal cost of the public sector wage increase negotiated in July 2023 is estimated at around 0.7-0.8 percent of GDP a year. Furthermore, the construction costs for a highway to Albania worth 10 percent of GDP will need to be absorbed in the budget, adding to the need for fiscal consolidation. While public debt slightly declined, it is projected to rise over the medium term, while expenditure arrears remain consistently above 3 percent of GDP. Monetary tightening continued to confront rising inflationary expectations, with the

main policy rate in August 2023 reached 6.15 percent. Credit growth slowed largely due to reduced borrowing by firms as financial conditions tightened.

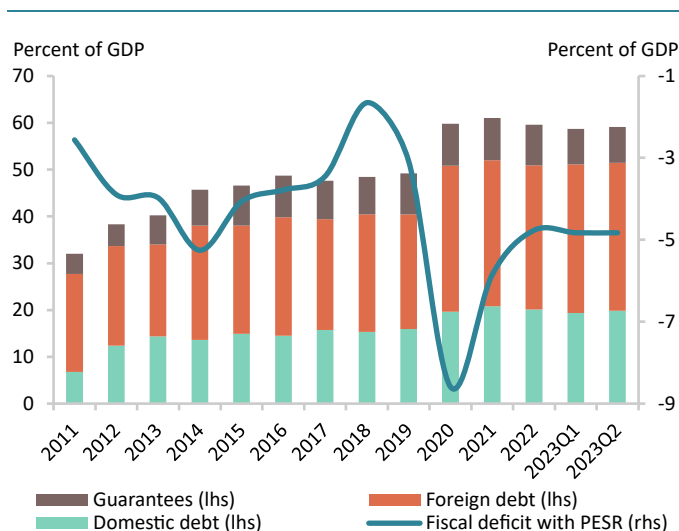
Overlapping crises have scarred the growth potential and further slowed convergence with the EU. Boosting productivity, advancing on inclusion, and enhancing fiscal and environmental sustainability are critical for long-term steady growth in the context of pronounced and widespread uncertainty. Rebuilding resilience to climate change shocks and decarbonizing to maintain international competitiveness given the EU CBAM implementation.

Recent developments

Output increased by 1.6 percent in H2 2023, led by decelerating consumption and exports, as imports and stockpiling pressures subsided. Growth was driven by services and industry which is slowing due to lower external demand, while agriculture and construction remained negative.

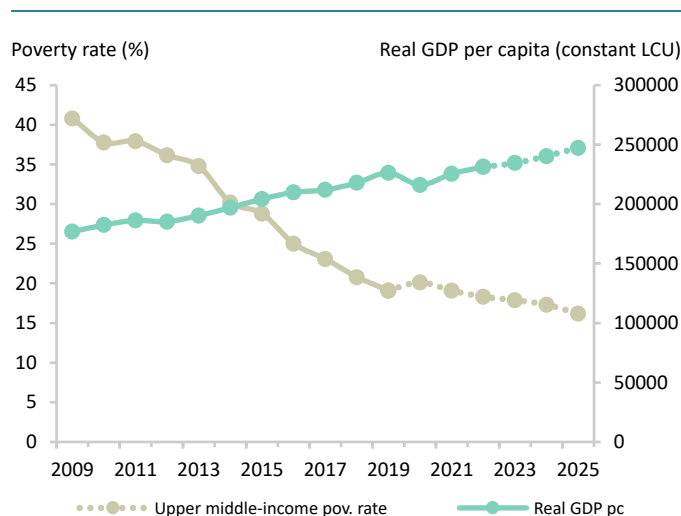
The Q2 2023 labor market data, lacking comparability due to census and methodological changes with previous years, reveal an unemployment rate of 13.1 percent, with the youth unemployment rate declining to 25.6 percent. The labor force participation rate (ages 15+) stood at a low of 52.4 percent (for women at 42.5 percent), while the employment rate remained stagnant at 45.5 percent. Wage growth surpassed inflation as of April 2023 after the minimum wage correction. Wages will increase

FIGURE 1 North Macedonia / Fiscal performance



Sources: North Macedonia State Statistics Office, Ministry of Finance, and World Bank staff calculations. Note: Fiscal deficit with PESR included.

FIGURE 2 North Macedonia / Actual and projected poverty rate and real GDP per capita



Source: World Bank. Notes: see Table 2.

further as the Government signed a new collective agreement for the public sector that includes a 10-percent wage rise from September 2023 and a revision to the wage-setting methodology from 2024 linking the public sector wage to the national gross wage; an annual leave bonus at 30 percent of the average net wage; as well as loyalty bonuses. The fiscal deficit (with the State Roads) will likely remain at 4.8 percent of GDP for 2023 after the technical budget reallocation to accommodate new spending commitments. The central government deficit reached 2.7 percent of GDP by June as revenue growth decelerated and spending increased led by investments and social spending. Public debt to GDP stood at 59.1 percent of GDP in June 2023 and is expected to rise by 2025. Banking sector stability was preserved with an increase in the capital adequacy ratio to 18 percent in Q1 2023 despite a drop in the liquidity rate to 19.1 percent.

At the same time, the NPL ratio declined to 2.8 percent. Headline inflation fell to 8.4 percent in July 2023, but core inflation remains sticky at above 8 percent. The pegged exchange rate has remained stable and FX reserves have recovered from losses incurred largely at the start of the war in Ukraine, standing at more than 4 months of imports in June 2023.

Outlook

The medium-term outlook is positive, but risks are tilted to the downside. Growth in 2023 is expected to increase modestly by 1.8 percent, reflecting a slowdown in external demand, and a persistent cost-of-living crisis, offset in part by the impact of the highway construction. Growth is expected to moderately accelerate in the medium term led by the rise in public investments,

recovered consumption and exports, before slowing towards the potential growth trend thereafter. Annual inflation is projected to remain elevated at 9.1 percent in 2023 and fall to the long-term average of 2 percent in 2025. The baseline scenario is built on the assumption that the impact of crises subsides over the forecast horizon. While underlying risks remain largely skewed to the downside and reflect the outlook for the country's main trading partners, moving ahead with EU accession negotiations may accelerate critical reforms and unlock growth. However, heightened political uncertainty and a prolonged parliamentary impasse due to lack of consensus for constitutional changes and upcoming elections may delay reform implementation. Finally, policy slippages may risk fiscal sustainability and inflation persistence in turn requiring further monetary tightening that can further restrict financing options and decelerate economic activity going forward.

TABLE 2 North Macedonia / Macro poverty outlook indicators

(annual percent change unless indicated otherwise)

	2020	2021	2022	2023e	2024f	2025f
Real GDP growth, at constant market prices	-4.7	3.9	2.1	1.8	2.5	2.9
Private consumption	-3.4	7.8	3.1	4.2	1.5	2.4
Government consumption	9.7	-0.4	-2.6	0.3	0.2	0.2
Gross fixed capital investment	-15.7	0.9	15.9	8.0	6.5	6.5
Exports, goods and services	-10.9	11.7	13.4	6.0	5.5	5.0
Imports, goods and services	-10.9	11.9	16.1	5.8	4.5	4.5
Real GDP growth, at constant factor prices	-4.3	4.1	2.5	1.8	2.5	2.9
Agriculture	2.5	-5.2	2.0	2.0	2.5	1.8
Industry	-6.9	-1.8	-4.3	2.1	3.4	3.0
Services	-4.1	7.5	4.9	1.7	2.2	3.0
Inflation (consumer price index)	1.2	3.2	14.2	9.1	3.0	2.0
Current account balance (% of GDP)	-2.9	-3.1	-6.0	-3.7	-3.2	-2.8
Net foreign direct investment inflow (% of GDP)	1.4	3.3	5.2	5.2	4.7	4.2
Fiscal balance (% of GDP)	-8.2	-5.4	-4.6	-4.7	-4.1	-3.5
Fiscal balance incl. public enterprise for state roads (% of GDP)	-8.6	-5.8	-4.8	-4.8	-4.5	-3.8
Revenues (% of GDP)	29.9	32.5	32.4	34.9	35.0	35.7
Debt (% of GDP)	59.8	61.0	59.6	60.2	61.5	62.2
Primary balance (% of GDP)	-7.0	-4.1	-3.4	-3.2	-2.4	-1.5
Upper middle-income poverty rate (\$6.85 in 2017 PPP)^{a,b}	20.1	19.1	18.3	17.9	17.3	16.2
GHG emissions growth (mtCO₂e)	-5.5	-1.1	-3.0	-2.9	-3.0	-3.1
Energy related GHG emissions (% of total)	70.6	70.7	70.0	69.0	68.0	66.8

Source: World Bank, Poverty & Equity and Macroeconomics, Trade & Investment Global Practices. Emissions data sourced from CAIT and OECD. Notes: e = estimate, f = forecast.

a/ Calculations based on ECAPOV harmonization, using 2020-SILC-C. Actual data: 2019. Nowcast: 2020-2022. Forecasts are from 2023 to 2025.

b/ Projection using neutral distribution (2019) with pass-through = 0.87 (Med (0.87)) based on GDP per capita in constant LCU.