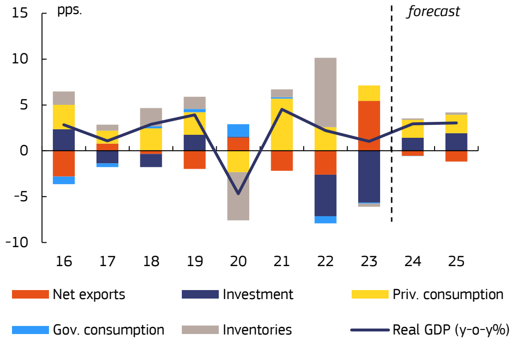
33. NORTH MACEDONIA

Annual GDP growth dropped to 1% in 2023, reflecting a sharp decline in domestic investment and weak external demand. Headline inflation declined substantially on the back of lower global energy prices. Growth is projected to accelerate mainly on account of strengthening domestic demand, in particular by a significant increase in public investment. The fiscal deficit widened in 2023. However, it is projected to decline gradually thanks to the impact of recently adopted tax base broadening measures and a cut in energy subsidies, and in spite of new spending commitments related to public sector wages.

Domestic demand to take over as growth driver

Economic growth slowed to 1% in 2023, from 2.2% in 2022. This slowdown was driven by net exports. Nonetheless, private consumption benefited from a steep rebound in real wages from July 2023 and strong inflows of remittances. Investment dropped sharply, in annual terms, mainly due to companies continuing to draw down their inventories. The current account balance posted a surplus in 2023 as the goods trade balance improved on account of decreasing energy prices.

Graph II.33.1: **North Macedonia - Real GDP growth and contributions**



Looking ahead, public investment is set to become an increasingly important driver of growth in 2024. The implementation of the government's major public roads project, covering parts of the so-called Corridor 8 and 10d, is expected to start in early summer and have a high domestic input share. Both, import and export growth are expected to pick up gradually. The recent improvement in the current account is projected to turn around, as the goods trade deficit is likely to widen again with strengthening domestic demand. Rising interest expenditure outflows are likely to contribute to a higher primary income deficit, which is expected to be offset by a rise in the services surplus thanks to the positive outlook for tourism and IT. Private consumption is projected to remain the key driver of the expected pick-up in GDP growth over the forecast horizon

Inflation projected to ease further

Supported by tighter monetary policy, annual consumer price inflation gradually declined from its peak of 19.8% in October 2022 to 3% in February 2024. Core inflation also eased substantially, with the spillover effects from high energy and food prices on other sectors petering out. Inflation is projected to ease further, and to return to around 2% on average in 2025. The central bank has kept its key policy rate unchanged at 6.3% since September 2023.

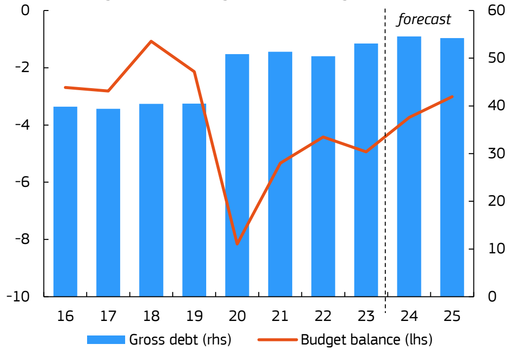
Structural problems burden the labour market

The labour market lost momentum towards the end of 2023, with employment stagnating in the fourth quarter. Labour market participation, already low, dropped further in 2023. The labour force continued to shrink, in particular concerning young workers. The outlook for the forecast period is more muted than in recent years, as employers will have to accommodate higher wages while already faced with a shortage of qualified labour supply.

Budget balance to improve, while risks are mounting

The 2023 budget deficit, at 4.9% of GDP, was above the government's target and higher than in 2022. This was mainly a result of weaker-than-projected GDP growth and in spite of revenue-enhancing tax policy changes and the reduction in electricity subsidies. Capital expenditure increased by some 52% compared to 2022 thanks to a high implementation of budget allocations (97%). In 2024, revenues are expected to be boosted by the full-year effect of tax policy measures adopted in 2023. Reforms to lower electricity and agricultural subsidies are projected to reign in current expenditure, while capital expenditure is budgeted to rise by 3.8% over the 2023 outcome. The fiscal deficit is projected to decline gradually to 3% of GDP in 2025, in line with the new fiscal rules. However, a collective agreement for the public sector entered into force in September 2023, providing for a 10% wage increase, and linking public sector wages to the domestic average wage. This adds to fiscal risks from the indexation of pensions, given dependence on both price and nominal wage developments. Further risks to the budget stem from a potential rebound in energy prices, which would again drive up mandatory spending on electricity subsidies. The government debt-to-GDP ratio is projected to hover above 50%, with higher borrowing costs acting as a debt-increasing factor. The public debt-to-GDP ratio, which includes the debt of state-owned enterprises, is expected to rise above 60% in 2024, mainly as a result of financing requirements for public energy and road investments carried out by these enterprises.

Graph II.33.2: **North Macedonia - General government budget balance and gross debt**



Risks are mainly on the downside

The growth outlook could be challenged if the major public investment project, Road Corridor 8 and 10d, continues to face significant implementation delays. The fiscal outlook might deteriorate if this project suffers from serious cost overruns; or, given the public sector's large borrowing needs in view of infrastructure financing and the 2025 Eurobond repayment, if the cost of financing rises faster than projected.

Table II.33.1:

Main features of country forecast - NORTH MACEDONIA

		2023		Annual percentage change						
	bn MKD	Curr. prices	% GDP	04-19	2020	2021	2022	2023	2024	2025
GDP		840.6	100.0	3.3	-4.7	4.5	2.2	**1.0**	**2.9**	**3.0**
Private Consumption		612.6	72.9	3.0	-3.6	8.6	3.8	**2.4**	**2.7**	**2.9**
Public Consumption		141.1	16.8	1.4	9.8	0.9	-5.0	**-0.6**	**-0.2**	**0.0**
Gross fixed capital formation		146.1	17.4	4.8	0.4	0.1	-19.2	**-27.0**	**8.2**	**9.6**
Exports (goods and services)		611.9	72.8	9.3	-10.9	14.3	11.4	**-0.1**	**5.9**	**8.6**
Imports (goods and services)		725.6	86.3	8.4	-10.9	14.8	12.4	**-5.8**	**5.6**	**8.6**
GNI (GDP deflator)		794.5	94.5	3.0	-3.2	3.7	1.9	**-0.1**	**2.6**	**2.3**
Contribution to GDP growth:	Domestic demand			3.7	-0.9	5.8	-2.7	**-4.0**	**3.3**	**4.0**
	Inventories			0.7	-5.3	0.8	7.6	**-0.4**	**0.1**	**0.2**
	Net exports			-1.1	1.5	-2.2	-2.6	**5.4**	**-0.5**	**-1.2**
Employment				2.4	-0.4	-12.8	-0.2	**-0.5**	**0.8**	**0.8**
Unemployment rate (a)				29.7	16.9	15.4	14.4	**13.1**	**12.9**	**12.8**
Compensation of employees / head				:	2.5	27.0	17.5	**10.4**	**6.2**	**4.1**
Unit labour costs whole economy				:	7.2	6.1	14.7	**8.7**	**3.9**	**1.8**
Saving rate of households (b)				:	:	:	:	**:**	**:**	**:**
GDP deflator				2.7	1.4	4.3	7.7	**3.6**	**5.6**	**5.5**
Consumer price index				1.7	1.2	3.2	14.2	**9.4**	**3.0**	**1.9**
Terms of trade goods				1.0	0.1	-0.9	:	**:**	**:**	**:**
Trade balance (goods) (c)				-21.8	-16.6	-20.0	-27.4	**-18.9**	**-19.7**	**-20.6**
Current-account balance (c)				-2.8	-2.9	-2.8	-6.1	**0.7**	**-1.0**	**-1.1**
General government balance (c)				-1.7	-8.2	-5.3	-4.4	**-4.9**	**-3.7**	**-3.0**
Structural budget balance (d)				:	:	:	:	**:**	**:**	**:**
General government gross debt (c)				32.3	50.8	51.4	50.4	**53.1**	**54.6**	**54.2**

(a) as % of total labour force. (b) gross saving divided by adjusted gross disposable income. (c) as a % of GDP. (d) as a % of potential GDP.