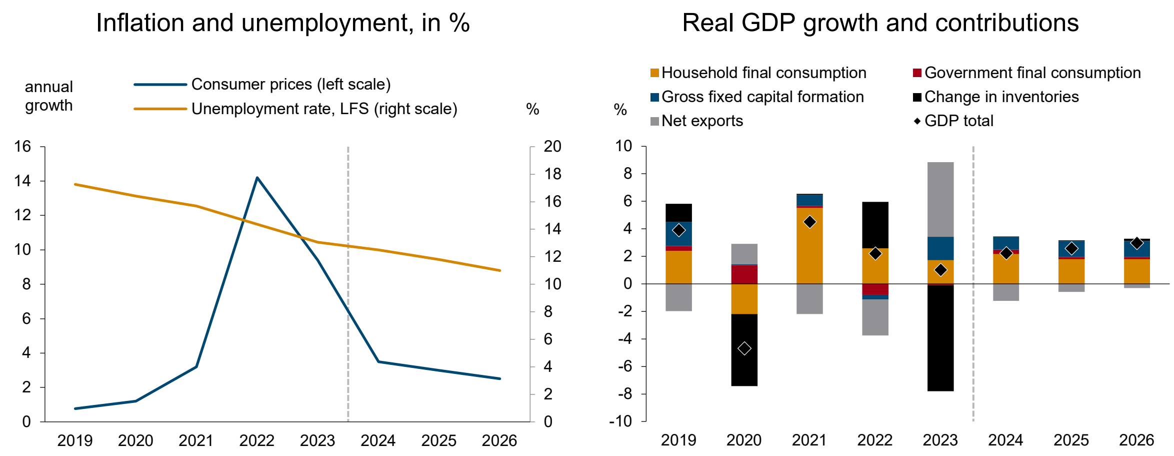
NORTH MACEDONIA: Pre-election calm, post-election storm

BRANIMIR JOVANOVIĆ

The measures adopted by the government ahead of the elections in April and May are breathing life into the economy, with all the indicators now pointing in a positive direction. There is some doubt, though, about the extent to which this can sway the election outcome, and a transfer of power seems likely. If that happens, the biggest question will be how the new government positions itself on the constitutional changes required for EU accession talks to commence. In terms of economic policy, one should expect no great change, as both the main parties support neoliberal agendas. The second half of the year will continue to be exciting, as the current stimulus measures are due to expire, and the new government (whoever leads it) will have to tighten the country's belt.

Figure 6.15 / North Macedonia: Main macroeconomic indicators



Source: wiiw Annual Database incorporating national and Eurostat statistics, own calculation. Forecasts by wiiw.

After a gloomy 2023, economic activity seems to be coming back to life at the start of 2024. The growth in GDP of just 1% in 2023 was the lowest in the Western Balkans. Although household consumption increased by 2.5%, all other GDP components saw a decline. The most significant of these was in gross investment, which plummeted by a whopping 17%, due primarily to the depletion of inventories (likely a result of the stockpiling of gas and oil in 2022 amid the energy crisis). The start of 2024 appears slightly rosier. Industrial production in January and February increased by 1.5%, and retail trade (excluding fuels) saw a 3.3% improvement, both measured in real terms on a year-on-year basis.

One of the reasons for the improvement is the generous fiscal support provided by the government ahead of the presidential and parliamentary elections scheduled for April and May. The package, which was adopted in November, envisages higher public-sector wages, bigger pensions, increased social assistance transfers, cash transfers to pupils and students, direct financial subsidies to firms that undertake to raise wages, and favourable loans for small and medium-sized enterprises. Most of the measures are designed as short-term stimuli, though, and are set to expire by May.

After spending most of 2022 and 2023 in decline, real wages have returned to positive growth. This may be attributed to a combination of factors: the government's fiscal stimulus, the increase in the minimum wage and, most significantly, the fact that inflation has slowed sooner than anticipated. As a result, real wages ended 2023 some 5% up on the previous year, which more than made up for the 3% drop experienced in 2022. In January 2024, real wages were 13% above their level the year before, signalling robust consumer spending in the coming months.

After several months of slowing down, inflation again rose in March to 4%. This increase is attributable to the government's decision that from March onwards, the price controls that were introduced in October 2023 will no longer be in place. That pushed the average inflation rate for the first three months to 3.4%. The uptick could be further exacerbated by the double-digit growth in real wages, which may prompt firms to raise their prices in order to maintain profit margins. Therefore, we are maintaining our initial forecast of a 3.5% inflation rate for the entire year.

Despite the slowdown in inflation, the central bank has yet to adjust its policy interest rate. It has kept this at 6.3% since September, and we forecast that it will maintain that rate until the European Central Bank cuts its own rate. Following this, we anticipate four cuts in the latter half of the year, which we expect will bring the base interest rate down to around 5.5%.

The rosy start to the year comes at a price, though – the elevated budget deficit. This reached 6% of GDP in Q4 2023 and averaged close to 5% for the whole year. The first two months of 2024 saw it range between 8% and 9% of GDP. Public debt will certainly exceed 60% of GDP in 2024, though fiscal stability will not be undermined. The government's fiscal package, which is due to expire after the elections, suggests that the deficit will shrink in the second half of the year. However, this also implies that the economic momentum supplied by the fiscal policies will wane as the year progresses. This slowdown will be further compounded by an anticipated moderation in real wages. Consequently, the economic outlook for the second half of the year would appear to be significantly less optimistic. Hence, we maintain our previous forecast for GDP growth in 2024 at 2.2%.

The upcoming elections in April and May are set to be the most significant since Gruevski's fall in 2017. The parliamentary and the presidential elections are to be held together, with 8 May as the decisive day when both results become known. The polls consistently show the ruling social democratic SDSM party heading for defeat, as it pays the price of unfulfilled domestic promises and lack of progress in its EU accession efforts. The conservative VMRO party is poised for a comeback, though there are questions about the potential coalition partners in the upcoming government. As is customary in the country, the new government will need to include some ethnic Albanian party – something that has traditionally been challenging for the VMRO, due to its nationalistic tendencies. This does not seem to be a problem at the moment, as the VMRO is indeed cooperating with some Albanian parties at the local level. However, the formation of a new government may necessitate an alliance with smaller ethnic-

Macedonian parties, which could have agendas and demands that conflict with those of the Albanian party. Thus, even if the VMRO succeeds in winning the election and forming a government, the new coalition could be unstable.

Whoever wins the elections, there will be hardly any change in terms of economic policies. The two main parties have historically embraced neoliberal principles, a stance that is clearly mirrored in their current electoral platforms. The only difference in this respect is that the VMRO is not so keen on wages rising, which may put a spoke in one of the engines of growth over the past few years. On the other hand, it is again promising tax cuts for businesses (although how that could be achieved is none too clear, as taxes are already very low).

However, the two parties do diverge significantly on cultural and social issues. A government led by the VMRO is likely to adopt a more conservative and authoritarian stance, and past experience raises concerns regarding respect for democratic standards and civil liberties.

The biggest uncertainty revolves around the constitutional amendments needed to initiate EU accession negotiations. The VMRO, while in opposition, has stoutly resisted the inclusion of Bulgarians in the constitution’s preamble. However, that stance would prove quite challenging to maintain if the party did gain power. It would come under considerable international pressure (with responsibility for the stalemate in the accession talks falling squarely on its shoulders), and would also be under pressure from whatever Albanian party became its coalition partner. But on the other hand, if it accepted an amendment to the constitution, it would alienate its nationalist supporters, who may then feel bound to gravitate towards smaller parties. Consequently, the VMRO finds itself on the horns of a dilemma, whereby any decision could have an unfavourable outcome. This suggests that a win in the elections could ultimately be something of a pyrrhic victory for the party.

The presidential race, on the other hand, offers a less predictable scenario. It is likely to culminate in a second-round showdown between the incumbent, Stevo Pendarovski, backed by the ruling SDSM, and the VMRO candidate, Gordana Siljanovska-Davkova. The final outcome will depend on the support of voters from other parties; and while Siljanovska-Davkova is marginally the favourite, Pendarovski may well cling on. This raises the possibility of a divided government after the elections, with the president and the prime minister coming from opposing parties. While not unprecedented in the country’s political history, such an outcome would undoubtedly introduce a fresh dynamics into the political landscape of the country.

Table 6.15 / North Macedonia: Selected economic indicators

	2020	2021	2022	2023 1)	2024	2025 Forecast	2026
Population, th pers., average 2)	2,073	1,837	1,832	1,822	1,812	1,802	1,792
Gross domestic product, MKD bn, nom.	669.3	729.4	803.1	840.6	890	940	992
annual change in % (real)	-4.7	4.5	2.2	1.0	2.2	2.6	3.0
GDP/capita (EUR at PPP)	11,420	14,110	15,010	15,510	.	.	.
Consumption of households, MKD bn, nom.	436.4	487.4	550.2	603.7	.	.	.
annual change in % (real)	-3.4	8.5	3.9	2.5	3.0	2.5	2.5
Gross fixed capital form., MKD bn, nom.	144.5	171.1	189.0	194.5	.	.	.
annual change in % (real)	0.4	3.8	-1.5	7.2	4.0	5.0	5.0
Gross industrial production 3)							
annual change in % (real)	-9.5	1.4	-0.2	0.6	2.0	3.0	3.5
Gross agricultural production 4)							
annual change in % (real)	1.7	-7.6	2.0	-4.0	.	.	.
Construction industry							
annual change in % (real)	1.3	-11.4	-11.9	-2.2	.	.	.
Employed persons, LFS, th, average 5)	794.9	795.1	692.0	688.3	700	710	720
annual change in %	-0.3	0.0	-0.2	0.0	1.0	1.0	1.0
Unemployed persons, LFS, th, average 5)	155.9	147.9	116.0	103.4	100	90	90
Unemployment rate, LFS, in %, average 5)	16.4	15.7	14.4	13.1	12.5	11.8	11.0
Reg. unemployment rate, in %, eop 5)6)	25.8	19.7	19.8	19.3	.	.	.
Average monthly gross wages, MKD	40,566	42,887	47,637	54,916	58,500	61,500	63,700
annual change in % (real, gross)	7.0	2.4	-2.7	5.4	3.0	2.0	1.0
Average monthly net wages, MKD	27,182	28,718	31,859	36,614	39,000	41,000	42,400
annual change in % (real, net)	6.5	2.3	-2.9	5.1	3.0	2.0	1.0
Consumer prices, % p.a.	1.2	3.2	14.2	9.4	3.5	3.0	2.5
Producer prices in industry, % p.a.	0.6	11.1	17.3	1.2	1.0	2.0	2.0
General governm. budget, nat. def., % of GDP							
Revenues	29.9	32.0	32.1	33.0	32.5	32.0	32.0
Expenditures	38.1	37.4	36.5	37.9	36.5	35.0	34.5
Deficit (-) / surplus (+)	-8.2	-5.4	-4.4	-4.9	-4.0	-3.0	-2.5
General gov.gross debt, nat. def., % of GDP	50.8	51.4	50.4	53.1	55.0	56.0	57.0
Stock of loans of non-fin. private sector, % p.a.	4.6	8.2	9.4	5.0	.	.	.
Non-performing loans (NPL), in %, eop	3.3	3.2	2.8	2.7	.	.	.
Central bank policy rate, %, p.a., eop 7)	1.50	1.25	4.75	6.30	5.50	5.00	4.50
Current account, EUR m	-318	-329	-797	95	-110	-290	-380
Current account, % of GDP	-2.9	-2.8	-6.1	0.7	-0.8	-1.9	-2.4
Exports of goods, BOP, EUR m	4,820	6,041	7,320	7,292	7,660	8,080	8,560
annual change in %	-9.9	25.3	21.2	-0.4	5.0	5.5	6.0
Imports of goods, BOP, EUR m	6,623	8,378	10,801	9,868	10,460	11,140	11,860
annual change in %	-9.2	26.5	28.9	-8.6	6.0	6.5	6.5
Exports of services, BOP, EUR m	1,445	1,746	2,320	2,648	2,890	3,180	3,530
annual change in %	-11.1	20.8	32.9	14.2	9.0	10.0	11.0
Imports of services, BOP, EUR m	1,021	1,248	1,568	1,915	2,200	2,460	2,710
annual change in %	-20.8	22.2	25.6	22.1	15.0	12.0	10.0
FDI liabilities, EUR m	28	575	788	650	.	.	.
FDI assets, EUR m	-127	187	134	127	.	.	.
Gross reserves of CB excl. gold, EUR m	3,019	3,288	3,486	4,125	.	.	.
Gross external debt, EUR m	8,536	9,577	10,790	11,463	12,400	13,400	14,500
Gross external debt, % of GDP	78.7	80.9	82.8	83.9	86.0	88.0	90.0
Average exchange rate MKD/EUR	61.67	61.63	61.62	61.56	61.6	61.6	61.6

Note: Introduction of new index 2021=100 (new weights) for gross industrial production.

1) Preliminary and wiiw estimates. - 2) From 2021 according to census September 2021. - 3) Enterprises with 10 and more employees. - 4) wiiw estimate from 2022. - 5) From 2023 new LFS methodology in line with the Integrated European Social Statistics Regulation (IESS). From 2022 according to census September 2021. - 6) In % of labour force (LFS). - 7) Central Bank bills (28 days).

Source: wiiw Databases incorporating national statistics. Forecasts by wiiw.