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ECONOMIC REFORM PROGRAMME

OF

NORTH MACEDONIA
(2025-2027)

COMMISSION ASSESSMENT

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1. EXECUTIVE SUMMARY

Following a slow post-pandemic recovery, the economic reform programme (ERP) optimistically projects real GDP growth to accelerate to 4% on average between 2025 and 2027, driven by domestic demand. Real output increased by 2.8% in 2024. Growth was driven by investment and by public consumption, with the latter partly reflecting a strong rise in public sector wages. Supported by increasing real incomes, household consumption growth picked up, too. The external balance made a negative contribution to growth as demand from key export markets was weak. The ERP expects annual growth of domestic demand to slow down somewhat in 2026 and to pick up again in 2027, while the negative contribution from the external sector would gradually diminish and turn marginally positive in 2027. The main growth driver is projected to be public and private investment, with the former based on implementation of a large road infrastructure project, and the latter benefiting from increased financial support to domestic companies. Well-calibrated monetary policy and abating foreign price pressures supported the further slowdown in headline inflation in 2024, to 3.5% on average. The ERP's growth scenario appears optimistic, partly as there are large deficiencies in public investment management and in the regulatory framework for attracting private co-financing. These add to downward risks surrounding external demand, stemming from uncertain growth prospects in key export markets and sectors, in particular Germany's car manufacturing industry, and potential volatility in commodity prices.

The programme's fiscal scenario projects a gradual reduction of the budget deficit in the medium term, with consolidation deriving entirely from the revenue side which however is not sufficiently underpinned by concrete measures. On the back of a large budget reallocation and a subsequent additional rebalancing which cut funds for capital expenditure, the 2024 fiscal deficit turned out lower than projected, at 4.4% of GDP. The government plans to lower the deficit gradually to 3% in 2027, postponing compliance with the fiscal rules as stipulated in the 2022 Organic Budget Law (OBL). The revenue ratio, low by regional comparison, is expected to rise strongly. This appears optimistic and is not underpinned by concrete tax policy measures. Rather, the government counts on increased tax revenue from measures to formalise the informal economy and to make tax collection more efficient. The general government expenditure ratio is also projected to rise, mainly due to higher capital spending and interest costs. Public debt remains at a relatively moderate level, yet posting a continuous climb over the past decade. It is projected to peak in 2025, at 62.8% of GDP, boosted by financing for road infrastructure projects that are carried out by public enterprises, before declining gradually to 61.6% in 2027.

The main challenges facing North Macedonia include the following:

- **Fiscal consolidation plans need to be underpinned by concrete revenue and expenditure measures.** The government's medium-term fiscal consolidation path is based entirely on a projected strong increase in revenue. However, a large rise in the revenue ratio is unlikely without concrete and credible measures aimed at broadening the tax base and reducing tax exemptions, which remain numerous. On the expenditure side, projected developments in the cost of public wages, pensions, and the health fund necessitate reforms to make these systems more sustainable. Strengthening the management of public investment remains key to improving the execution of the capital budget.
- **The government needs to restore fiscal space and accelerate compliance with the fiscal rules.** To this aim, any savings from underexecution of expenditure should be used to reduce the deficit and should not be reallocated to other spending items. In view of

stricter monitoring of fiscal risks and prevention of a build-up in arrears, the government needs to make swifter progress with the implementation of the OBL.

- **Key structural challenges arise from the large size of an informal economy; the skills mismatch in the labour market, and the low degree of digitalisation in the economy.** Distortions to competition from the informal economy, deficiencies in the education system, which does not adequately equip young people with the skills needed in the labour market, as well as muted innovation activity and a low level of digitalisation of the economy, including public administration services undermine the competitiveness of domestic companies. This impedes productivity gains amidst high wage growth. These challenges are expected to be addressed through key structural reforms identified in the country's reform agenda under the Growth Plan for the Western Balkans.

The implementation of the policy guidance set out in the conclusions of the Economic and Financial Dialogue of May 2024 has been limited. The government revised the 2024 budget and reallocated large sums from capital to current expenditure. However, it did not meet the original fiscal target. The adopted 2025 budget does not comply with the new deficit rule, which has been postponed. While energy subsidies were reduced, public sector wages were raised in the course of the year beyond the original budgeted funds, as were pensions. The government published a tax expenditure report, as required by the OBL, but it did not initiate any measures eliminating tax exemptions on this basis. It adopted a new law on the global minimum corporate profit tax, which will raise revenue from profit tax. A new IT platform, which is vital for the full implementation of the OBL, has not been installed yet. While the government adopted several by-laws, it postponed the full implementation of the OBL to 2026. The requirement for fiscal risk reporting has been fulfilled in the fiscal strategy, albeit in a general way only. The government has not yet adopted the decree on public investment management and the draft law on public-private partnerships.

2. ECONOMIC OUTLOOK AND RISKS

Following a slow post-pandemic recovery of the economy, the ERP projects a significant growth acceleration. Real output increased by 2.8% in 2024, which is above the ERP's full year projection of 2.1%.¹ Growth was driven by investment and by public consumption, with the latter partly reflecting a strong rise in public sector wages. Supported by a strong rise in real incomes, household consumption growth picked up. Gross capital formation increased by 8.9% in 2024, following onto a steep decline in 2023, and signalling the end of a prolonged drawdown of inventories. The contribution of net exports to growth turned negative due to slowing exports, largely reflecting the weakness in the German economy, the biggest trading partner.

The ERP projects the economy to grow by an average of 4% per year between 2025 and 2027, expanding by as much as 4.4% in 2027. The main growth driver would be gross investments, on the basis of a large rise in government capital spending, strong foreign direct investment, and large-scale financial support to domestic companies by the government. Investment is projected to increase by 7.6% y-o-y on average in 2025-2027. As a share of GDP it is projected to rise from 29.6% in 2024 to 33.9% in 2027. Private consumption growth is set to pick up gradually each year, to 2.9% in 2027, which is, however, still below the pre-COVID-19 five-year average. After contracting in 2023 and 2024, exports are projected to return to growth in 2025, which would accelerate each year to reach an average annual growth rate of 5.1% over the ERP's timeline. This is explained by the expected recovery in foreign demand, a favourable outlook for metal prices and for traditional export sectors, and expanding export capacities through increased FDI. This, together with strong investment growth is set to also spur imports (+4.6% y-o-y on average in 2025-2027). Overall, the ERP expects the negative contribution from the external balance to gradually diminish and turn into a marginally positive contribution in 2027. Compared to last year's ERP, growth projections for 2024-2026 have been revised downwards significantly, by 1.3 pps annually on average, stemming from both a more pessimistic outlook for domestic demand, in particular for household spending as well as for the external balance. The programme would have benefited from an explanation of the deviations between the two programmes. The output gap is projected to narrow gradually, albeit at a slower pace than projected in last year's programme, but to remain negative throughout the programme's timeframe.

The baseline scenario is usefully complemented by two alternative scenarios. Assuming that annual export growth turns out to be lower by 1.4 pps per year in 2025-2029, compared to the baseline scenario and implying a negative impact on the growth of domestic demand, average annual output growth would be 3.3%, which is 1.2 pps lower compared to the baseline scenario over this period. The second, domestic risks scenario assumes weaker growth of investment, by an average of 1.9 pps per year, mainly in response to a lower rate of implementation of public infrastructure projects. This would lead to average annual output growth that is 0.6 pps lower than in the baseline scenario.

The ERP baseline scenario seems optimistic given the downside risks weighing on both domestic and external demand. The expectation of a large surge in private and public investment is subject to a number of risks. Deficiencies in public investment management and fiscal risk monitoring may impact negatively on the strength and the efficiency of public

¹ Macroeconomic and fiscal estimates and forecasts covering the period 2024-2027 have been taken from the ERPs themselves; if available, preliminary macroeconomic and fiscal out-turn data for 2024 have been taken from the relevant national sources (Statistical Office, Ministry of Finance, Central Bank).

capital spending. While domestic demand is plausibly expected to benefit from works on Road Corridors 8 and 10d, as these have a large domestic component, there is ample uncertainty surrounding the execution and the financing of this project. Moreover, competitiveness of domestic companies suffers from a number of growth-restraining factors in the economy such as low productivity growth against a background of strong nominal wage increases; the mismatch between educational outcomes and labour market needs; and the low digitalisation and innovation, which may also dampen expectations about a substantial increase in household consumption and private investment. Lastly, the external environment might turn out less favourable than expected in the ERP, dampening export growth. In particular, the automotive component manufacturers, largely integrated into European supply chains and playing an important role in North Macedonia's exports, could face headwinds.

Table 1:

North Macedonia - comparison of macroeconomic developments and forecasts

	2023		2024		2025		2026		2027	
	COM	ERP	COM	ERP	COM	ERP	COM	ERP	COM	ERP
Real GDP (% change)	2.1	2.1	2.0	2.1	2.6	3.7	2.9	4.0	n.a.	4.4
<i>Contributions:</i>										
- final domestic demand	1.9	-2.9	3.1	4.5	4.0	4.5	4.1	4.2	n.a.	4.4
- change in inventories	-4.8	n.a.	0.0	n.a.	0.0	n.a.	0.0	n.a.	n.a.	n.a.
- external balance of goods and services	5.0	5.0	-1.1	-2.5	-1.4	-0.8	-1.2	-0.2	n.a.	0.1
Employment (% change)	8.1	-0.5	1.0	0.9	1.1	1.6	0.3	1.6	n.a.	1.8
Unemployment rate (%)	13.2	13.1	13.0	12.5	12.1	11.2	11.8	10.1	n.a.	9.0
GDP deflator (% change)	7.8	7.8	3.1	4.5	4.2	3.0	4.5	2.6	n.a.	2.3
CPI inflation (%)	9.4	9.4	3.4	3.5	2.2	2.5	2.1	2.0	n.a.	2.0
Current account balance (% of GDP)	0.4	0.4	-2.5	-2.1	-2.3	-2.3	-2.3	-2.2	n.a.	-2.3
General government balance (% of GDP)	-4.6	-4.3	-4.8	-4.7	-4.1	-4.0	-3.4	-3.5	n.a.	-3.0
Government gross debt (% of GDP)	49.7	49.7	57.5	53.5	56.4	53.4	55.8	53.6	n.a.	53.5

Sources: Economic Reform Programme (ERP) 2025, Commission Autumn 2024 forecast.

Inflationary pressures are expected to decrease further in 2025-2027, but upside risks are related to higher wages and pensions. As North Macedonia is a small and open economy with a de facto currency peg, its price level is largely determined by international price developments. After rising to 14.1% in 2022, inflation slowed down to 9.4% in 2023, and further to 3.5% in 2024. This reflected mainly the drop in global commodities prices, and a gradual, albeit slow, abatement in second-round effects of high energy and food prices on other domestic sectors. Inflation has been rising again since September 2024, while core inflation remained sticky at above 5%.² Temporary price controls by the government, which put limits on retailers' margins of basic food products, have enhanced inflation volatility in the last quarter of 2024 and beyond.³ The central bank loosened its monetary stance by lowering the key policy rate in several steps as of September 2024, from 6.30% to 5.35% in February 2025. While uncertainties in global commodity price developments remain high,

² Food and energy together account for almost 60% of the domestic CPI structure and price increases for these two categories explain about 75% of headline inflation, which is much higher than in the euro area.

³ Following onto a temporary limit in the autumn, and a one-month cap from mid-December to mid-January, the government, on 17 February, introduced graduated caps of 5%, 10% and 15% margin limits in both retail and wholesale trade for basic food products until 30 April.

monetary policy increasingly faces challenges from domestic inflation risks arising in particular from high wage and credit growth, including the disbursement of government-subsidised corporate loans. The programme projects that annual average consumer price inflation will drop further, to 2.5% in 2025, before reaching its long-term average of 2% in 2026 and 2027.⁴ This is mainly based on a projected slowdown in second-round effects of recent rises in commodity prices on domestic sectors. While the programme's assumptions about global price developments seem plausible in the medium term, domestic inflationary pressures stem from recent and planned increases in wages⁵ and pensions⁶. An amendment to the central bank law was adopted in a shortened parliamentary procedure in January 2025. The amendment concerns the mechanism established in March 2024 in line with IMF recommendations, which aimed at building general reserves and strengthening the financial independence of the central bank by retaining the majority of its profits. Following the legislative change, most of the profits will be distributed to the government budget.

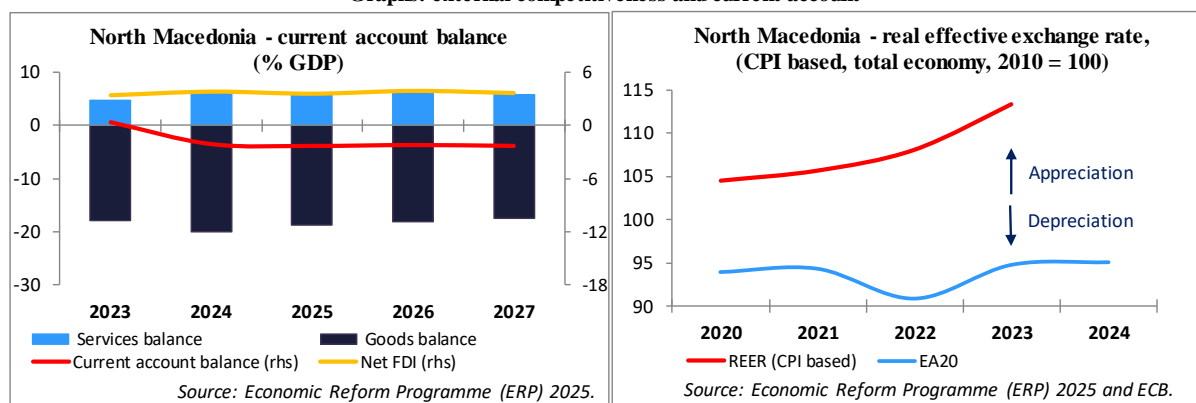
The current account deficit is projected to remain moderate. While the decline in energy prices took the current account balance into a small surplus at the end of 2023, it slipped back into deficit in 2024, on the back of a deterioration in the merchandise trade deficit and a lower secondary income surplus. The primary income deficit also widened. This more than offset the increase in the services trade surplus. Foreign direct investment rose by 3.3 pps y-o-y to 7% of GDP in 2024, hence exceeding the current account deficit by a large margin. The ERP projects the current account deficit to remain broadly stable until 2027, at around 2.2% of GDP. While the merchandise trade deficit would drop from 20.9% of GDP in 2024 to 17.9% in 2027, on account of a recovery in external demand as well as strong GDP growth, the secondary income surplus is projected to decline somewhat further over the programme's horizon, from 16.1% of GDP in 2024 to 14.3% in 2027, due to an expected further normalisation of remittances inflows, after a record high in 2022 and 2023. However, the projection for the goods trade balance might be over-optimistic, as the economy imports a large share of inputs for export production (not only energy), and the import elasticity of domestic demand is also relatively high, which may dampen the positive impact on the trade balance. Yet, some relief may come on the import side after 2025 as imports related to the highway Corridor 8 and 10d project are expected to drop somewhat. The surplus in the services trade balance, at about 1% of GDP, and the primary income deficit, at about 5.2% of GDP, are both forecast to remain stable over the programme's horizon. Foreign direct investment is also expected to remain broadly stable at an average of 3.8% of projected GDP between 2024 and 2027, fully financing the current account deficit during this period. This assumption is plausible, underpinned by ongoing 'nearshoring' (foreign companies relocating production facilities closer to their main markets in the EU) and by the positive prospect of EU accession, as well as by the continued large government subsidy programmes for FDI.

⁴ In last year's programme, the 2% inflation target was projected to be reached by 2025.

⁵ Average monthly gross wages rose by 13.6% in the first 10 months of 2024, which is slightly less than in the same period one year earlier (15%). Reflecting the slowdown in inflation, the annual increase in real wages amounted to 10% in the first 10 months of the year, compared to 3.9% in the same period one year earlier.

⁶ The minimum wage was raised by 12% starting from April 2023, and again in March 2024 and in March 2025, to reflect the previous year's increase in gross nominal wages and in the cost of living. In September 2024 and again in March 2025, the government raised pensions in a linear way (by 2 500 MKD, or 40 euro per month and per pensioner) rather than by indexation.

Graphs: external competitiveness and current account



The banking sector remains well-capitalised and liquid. Banks' capital adequacy ratio, already at comfortable levels, increased further to 18.9% in the fourth quarter of 2024. This was supported by the gradual rise in the central bank's countercyclical capital buffer throughout 2024, amidst solid bank profitability. The central bank had gradually raised the capital buffer since its implementation in August 2023 at a rate of 0.5% of exposures by banks, based on cyclical systemic risk assessments and credit growth⁷. Banks also continued to retain a high share of profits to strengthen their capitalisation. Bank lending to the private sector, in particular to companies, picked up gradually throughout 2024. The share of foreign-currency-denominated loans in total loans is declining, though mainly in the corporate sector. Liquidity in the banking sector, which is already high, rose further, and the central bank increased reserve requirements to absorb excess liquidity. The annual growth of deposits accelerated in 2024, driven by deposits in domestic currency and by longer-term deposits. Pressures in the housing market through fast mortgage growth and high real estate prices abated in 2024, aided by the introduction of borrower-based instruments by the central bank in 2023. Implementation of the 2023 Bank Resolution Law which sets up a bank resolution fund and guidelines for the process of bank resolution, with the central bank as the responsible body, is slow as half of the by-laws still need to be adopted. North Macedonia's application to join the Single Euro Payments Area (SEPA) was accepted by the European Payments Council on 5 March 2025. Once operational, SEPA will reduce settlement time and cost for euro payments, and facilitate trade, remittances, and other cross-border activity.

⁷ In the first quarter of 2025, the central bank kept the countercyclical capital buffer unchanged at 1.75%.

Table 2:

North Macedonia - financial sector indicators

	2020	2021	2022	2023	2024
Total assets of the banking system (EUR million)	9 490	10 363	11 103	12 131	13 405
Foreign ownership of banking system (%)	75.0	76.3	77.7	78.8	79.7
Credit growth (% , average)	6.4	5.8	9.6	6.2	7.6
Deposit growth (% , average)	7.8	8.3	4.2	9.1	9.8
Loan-to-deposit ratio (end of period)	82.0	81.8	85.5	81.6	81.5
Financial soundness indicators (% , end of period)					
- non-performing loans to total loans	3.4	3.2	2.9	2.8	2.7
- regulatory capital to risk-weighted assets	15.3	15.8	16.5	17.1	18.1
- liquid assets to total assets	32.5	32.4	30.0	31.8	32.6
- return on equity	11.3	12.9	12.2	16.1	17.6
- foreign exchange loans to total loans	42.3	41.2	43.2	42.2	38.6

Sources: National Bank of North Macedonia, IMF.

3. PUBLIC FINANCE

The new government significantly increased the 2024 fiscal deficit target to accommodate existing and new spending commitments. In a mid-year budget revision, the projected fiscal deficit was increased by over 33% compared to the original plan, from 3.4% of GDP to 4.9%. Notably, current expenditure was raised by 9% in the revision, while capital expenditure was cut by 17.3%⁸. According to the government, the adjustments were justified by the need to repay payment arrears; the implementation of the 2023 General Collective Agreement for wages in the public sector; higher than anticipated transfers to the health fund and to local government units; as well as new spending priorities by the new government, in particular a linear pension increase. Hence, the wage bill rose by 0.5pps y-o-y to 4.6% of GDP, while transfers to the pension fund increased by 1pp to 11% of GDP. On the basis of an upward adjustment of projected GDP later in the year, the deficit target was lowered to 4.7%. Ultimately, arrears, protracted VAT refunds and under-implementation of capital expenditure helped the government to reach a lower fiscal deficit of 4.4% of GDP. Capital expenditure implementation remained significantly even below the revised target (77%), amounting to 3% of GDP. This is considerably lower than anticipated for 2024 in both the ERP (5.3%) and the October Fiscal Strategy (4.7%) and can at least partly be linked to the protracted implementation of infrastructure works on Road Corridor 8 and 10d. Total revenue amounted to 31.9% of projected GDP (+1 pp y-o-y), and thus remained much below the 35% of GDP as projected by this year's ERP. Revenues remained below the revised target (96% implementation), in particular due to shortfalls in direct tax revenue, while VAT income overperformed (104%). The expenditure ratio was at 36.3%, also much lower than projected in the ERP (39.7%).

The programme's mid-term fiscal scenario projects a gradual reduction of the budget deficit in 2025-2027, based on higher revenue. The general government revenue ratio, low by regional comparison, is expected to rise gradually, to 37.4% in 2027. This contrasts with the projection of the previous year's ERP, whereby revenue would remain at just below 34% of GDP in 2024 and drop gradually to 33.1% of GDP in 2026. The programme refers to only

⁸ In addition to the budget revision, which was enacted by the Parliament in August 2024, the government undertook a budget reallocation in December 2024, in which it implemented most of the changes in the funding for current and capital expenditure.

one revenue-enhancing tax measure that would have a fiscal impact as of 2026, adopted by the Parliament in December 2024 and providing for an increase in the profit tax⁹. The general government expenditure ratio is projected to first rise from an expected 39.7% of GDP in 2024 (outcome: 36.3%) to 41.1% in 2025, and then to decline gradually to 40.4% in 2027. This would be driven by fluctuations in current spending, in particular an initial rise in the share of social transfers in GDP in 2025, which would be partly reversed in the following two years. The programme does, however, not indicate specific measures underpinning this decrease in social spending. Capital spending is set to rise gradually from 5.3% of GDP in 2024 (outcome: 3%) to 5.7% in 2026, and to remain at that level in 2027 (which for each year is much higher than projected in the October 2024 Fiscal Strategy). Overall, the budget deficit is projected to drop by 1.4 pps to 3% of GDP between 2024 and 2027 (in line with the revised date of implementing the new fiscal rules). The deficit targets for 2025 and 2026 are significantly above the previous year's projections. The ERP expects the primary deficit to decline gradually to its pre-pandemic level of 0.9% of GDP in 2027¹⁰. The projected evolution of the cyclically-adjusted primary balance between 2024 and 2027 points to fiscal tightening in 2025 (0.8pps), and a broadly neutral stance thereafter, while the output gap is expected to remain negative.¹¹

⁹ The Parliament adopted the new *Law on the global minimum corporate profit tax*, which introduces a tax rate of an additional 5 percentage points for domestic companies which are subsidiaries of multinational companies, with an annual turnover of 750 million EUR. For these companies, the corporate profit tax rate will be 15% instead of 10%, and will be applicable as of 2026, based on the companies' performance in 2025. This change will affect only a few companies operating in the country, mainly in the sectors of telecommunications, cement production, and energy distribution. The government estimates that the annual fiscal impact will amount to EUR 30 million.

¹⁰ The previous ERP projected the primary deficit to drop to 0.9% already in 2026, while the 2023 programme had also projected that the deficit would reach its pre-COVID-19 level only in 2027.

¹¹ The figures on cyclical developments in Table 4.12 in the programme are not consistent with Table 5 in Annex 1.

Table 3:

North Macedonia - composition of the budgetary adjustment (% of GDP)

	2023	2024	2025	2026	2027	Change: 2024-27
Revenues	32.7	35.0	37.0	37.3	37.4	2.4
- Taxes and social security contributions	29.6	31.8	33.0	33.6	33.8	2.1
- Other (residual)	3.0	3.3	4.0	3.7	3.6	0.3
Expenditure	37.0	39.7	41.1	40.9	40.4	0.7
- Primary expenditure	35.6	37.9	39.0	38.9	38.4	0.5
<i>of which:</i>						
Gross fixed capital formation	5.3	5.3	5.4	5.7	5.7	0.4
Consumption	10.2	11.3	11.3	11.4	11.3	0.0
Transfers & subsidies	20.0	21.3	22.3	21.8	21.4	0.1
Other (residual)	0.0	0.0	0.0	0.0	0.0	0.0
- Interest payments	1.4	1.9	2.0	2.0	2.0	0.2
Budget balance	-4.3	-4.7	-4.0	-3.5	-3.0	1.7
- Cyclically adjusted	-3.7	-3.7	-3.3	-3.1	-3.0	0.7
Primary balance	-2.9	-2.8	-2.0	-1.6	-0.9	1.9
- Cyclically adjusted	-2.2	-1.8	-1.2	-1.1	-0.9	0.9
Gross debt level	49.7	53.5	53.4	53.6	53.5	0.0

Sources: Economic Reform Programme (ERP) 2025, Commission calculations.

The programme projects the fiscal deficit to fall in 2025 based on a large revenue increase, which is not supported by policy measures. The ERP expects the general government revenue ratio to rise to 37% of GDP in 2025, up by 2 pps compared to the projected 2024 value and as much as 5.1 pps compared to the actual outcome.¹² The expenditure ratio is also set to rise, from 39.7% of GDP (expected, outcome: 36.3%) in 2024 to 41.1% in 2025. As a result, the fiscal deficit is projected at 4.1% of GDP (-0.3pps compared to the 2024 outcome). The government expects revenue to rise by 17.4% y-o-y in 2025, compared to the 2024 outcome, but it does not specify concrete revenue-raising measures. Rather, it points to ongoing efforts to formalise the informal economy and to improve tax collection as guarantors of increased public revenue. Social transfers would rise by 1 pp, to 18.7% of GDP, including the planned increase in pensions in March (estimated by the government at a total cost of some 0.7% of GDP), while wages and interest payments would increase by 0.1 pps each. Overall, current expenditure is projected to rise by 1.2 pps y-o-y. Capital expenditure would increase from 3% of GDP in 2024 (outcome) to 5.4% in 2025. As the main reasons for the increase in total expenditure the programme cites the implementation of the 2023 collective agreement for public sector wages, as well as the next linear rise in pensions (implemented in March 2025); clearing arrears; and higher costs than previously anticipated for highway projects on Corridor 8 and 10d.

Public debt has been rising at an accelerated pace since the pandemic. At the end of 2024, general government debt amounted to 53.8% of GDP (+4 pps y-o-y). Public debt, which includes the guaranteed and non-guaranteed debt of public enterprises, amounted to 62.4% of GDP (+4.3 pps y-o-y). The programme expects public debt to peak in 2025, at 62.8%, mainly

¹² Figures in the ERP and in the Fiscal Strategy are not consistent. Both the revenue ratio and the expenditure ratio for each year 2025-2027 are lower in the Fiscal Strategy projections than in the ERP.

as the government envisages rising costs for road infrastructure projects that are carried out by public enterprises, before declining gradually to 61.6% in 2027¹³. Financing needs would rise from 8.7% of GDP in 2024 to 12% in 2025, and decline gradually thereafter, to reach 8.7% again in 2027. They are driven by large repayments of Eurobonds that are due during the programme's horizon, notably a EUR 700 million Eurobond to be repaid in June 2026, and a EUR 500 million Eurobond due in March 2027. In January 2025, the government repaid a EUR 700 million Eurobond from 2018. Partly for refinancing this loan, the government contracted two loans from the Hungarian state-owned Eximbank of EUR 500 million each. The actual use of the remainder of these funds is not very transparent, partly involving the payment of outstanding arrears by government bodies, partly financing local government activities, and a large share to be disbursed as investment support to domestic companies. The structure of government debt points to moderate, yet increasing risk. External debt accounted for some 56% of total general government debt at the end of 2024, down from 57.5% at end-2023. Overall, foreign currency debt made up some 66% of total debt. Some 91% of the foreign currency debt is in euro, which is significantly above the threshold set in the public debt strategy (80%). Hence, risks stemming from exchange rate depreciation are mitigated by the 'de facto' currency peg to the euro. Regarding interest rate risk, the share of fixed interest rate debt in total debt increased from 73.9% at end-2023, to 75.4% in 2024.¹⁴ North Macedonia's public debt strategy stipulates that at least 60% of total debt must pay a fixed interest. However, there has been a sizeable rise in the cost of sovereign borrowing in recent years, as well as in interest expenditure by the government, which puts increasing pressure on the budget¹⁵ and limits fiscal space for productive expenditure and for emergency support in case of a sudden economic shock.

¹³ The previous programme had expected public debt to decline to below 60% by 2025, and to continue falling in 2026. This was partly based on assumptions that the financing of road infrastructure works would go ahead in 2023-2024, but this was de facto delayed.

¹⁴ Yet, the share of fixed interest debt in total government debt was still lower in 2024 than in 2021 (79%), as the government, faced by rising borrowing cost, sought to finance an increasing share at (a lower) variable rate.

¹⁵ Interest expenditure rose from 3.9% of total expenditure in 2023 to 5.1% in 2024 and is set to remain at about this level until 2027.

North Macedonia						<i>Debt dynamics</i>	
Composition of changes in the debt ratio (% of GDP)							
	2023	2024	2025	2026	2027		
Gross debt ratio [1]	49.7	53.5	53.4	53.6	53.5		
Change in the ratio	0.1	3.8	0.0	0.1	-0.1		
Contributions [2]:							
1. Primary balance	2.9	2.8	2.0	1.6	0.9		
2. 'Snowball effect'	-3.0	-1.2	-1.3	-1.3	-1.4		
Of which:							
Interest expenditure	1.4	1.9	2.0	2.0	2.0		
Growth effect	-0.9	-1.0	-1.9	-2.0	-2.2		
Inflation effect	-3.5	-2.1	-1.5	-1.3	-1.2		
3. Stock-flow adjustment	0.2	2.2	-0.7	-0.1	0.4		
[1] End of period.							
[2] The 'snowball effect' captures the impact of interest expenditure on accumulated debt, as well as the impact of real GDP growth and inflation on the debt ratio (through the denominator).							
The stock-flow adjustment includes differences in cash and accrual accounting, accumulation of financial assets, and valuation and other effects.							
Source: Economic Reform Programme (ERP) 2025, Commission calculations.							

The ERP projects that general government debt will remain above 50% of GDP during the programme's lifespan. Following a sizeable annual rise (+3.8pps) in 2024, the debt ratio is forecast to stabilise. The primary deficit is set to decline by 2 pps between 2024 and 2027 and therefore diminish gradually as a debt-increasing factor. The improvement in the primary balance is slower than projected in last year's programme which projected a primary deficit of 1% of GDP in 2026, compared to 1.6% in this year's programme. Reflecting expectations of moderating price pressures, the debt-decreasing impact of inflation is projected to diminish after 2025, while the effect from real growth is forecast to increase and to become the main debt-reducing factor. Interest payments are expected to have a stronger debt-driving impact (with interest expenditure expected to increase to 2% of GDP as of 2025, compared to 1.4% in 2023), assuming rising refinancing costs. The contribution from stock-flow adjustments is projected to turn negative in 2025 and 2026, hence reducing the debt burden, possibly in response to a drawdown of government deposits at the central bank to partially meet large upcoming financing needs, and to turn positive again (hence contributing to the debt increase) in 2027. Projections for 2024-2026 are above those in last year's programme, which, contrary to the current programme, also projected an annual decline in the debt-to-GDP ratio in 2025.

The fiscal consolidation plans, based entirely on increased revenue, are subject to substantial risks. There are no concrete policy measures underpinning the projected large increase in tax revenue and social contributions,¹⁶ which therefore seem very optimistic. Rather, the government projects revenue to increase on account of measures to reduce the informal economy and make tax collection and procedures more efficient. The planned measures remain vague, however, and leave doubt as to the magnitude of their fiscal impact. The ERP includes an estimate of tax expenditures for the biggest tax categories, in line with the respective legal requirement.¹⁷ However, it does not present any policy follow-up that would reduce tax exemptions. On the expenditure side, there are substantial risks of both under- and overspending. First, given the little progress on improving the management of public infrastructure, the implementation of the ambitious capital expenditure agenda may

¹⁶ The remainder of the revenue increase would come from not further specified "other" income.

¹⁷ The Organic Budget Law requires the government to present a report to the Parliament every year, as of 2025, on foregone revenue from tax expenditure, to accompany the Final Account of the State Budget for the previous year.

again remain behind the target, or capital expenditure might be cut in a budget reallocation in favour of current expenditure increases. This is particularly likely in the run-up to the local elections in autumn 2025. Second, considerable uncertainty remains about the total costs of the large Corridor 8/10d project. Third, the mandatory indexation of minimum wages, which is raising average wages (and therefore also public sector wages) and the indexation of pensions create uncertainty as to their size, given dependence on both price and nominal wage developments in the economy. Furthermore, risks to public expenditure arise from government guarantees, as well as from a lack of clarity on, and still insufficient, control mechanisms regarding the build-up of unpaid obligations/arrears.

Sensitivity analysis

The programme includes a sensitivity analysis of the fiscal deficit, based on three parameters, in line with the alternative macroeconomic scenarios. The first parameter is GDP growth. If average annual real GDP growth is lower than projected, by 1.2pps on average in 2025-2029, the budget deficit would increase by an average of 0.5pps per year, compared with the baseline projections. The second parameter is capital expenditure. Lower capital expenditure (about 75% realisation compared with the baseline) would imply an annual reduction in GDP growth of 0.6pps and an average annual increase in the deficit of 0.2 pps, mainly on account of the negative impact on tax revenue. The third parameter is tax collection. If tax collection falls by 5% per year, this would increase the budget deficit to 4.3% on average in 2025-2029 (compared with 3.8% in the same risk scenario set out in last year's programme for the period 2024-2028).

The programme also assesses the exposure of the debt portfolio to interest and exchange rate risk. If interest rates were to rise in 2025 by 1 pp more than assumed in the baseline scenario, the debt-servicing cost would surge by 7.6% in 2025, compared to the baseline scenario, with the impact gradually diminishing until 2029. For comparison, the ERP 2024 projected a rise of 6.1% in 2025 in debt-servicing cost in response to the same rise in interest rates. The impact of a 10% depreciation of the euro with respect to other currencies in the portfolio would lead to an increase in debt-servicing cost of 1.9% in 2025 (ERP 2024: 0.3% in 2025). The impact on debt developments in 2025 stemming from a deterioration in these two parameters is hence projected to be considerably more pronounced than projected in last year's programme for this year.

The quality of public finances can be improved by measures on the revenue and the expenditure side. Public revenue relies heavily on income from indirect taxes – about 40% of total revenue is derived from VAT and excise collection. The share of personal and corporate income tax revenue increased only marginally in recent years, mainly in response to the 2023 tax policy reforms, which broadened the tax base for direct taxation (and also for VAT). The share of current expenditure in total, has been rising gradually in recent years. Social transfers, including pension payments (taking into account the new pension indexation formula and the ad hoc pension increase in 2024) amounted to some 49% of total expenditure in 2024, with pensions accounting for 30.2% of total spending (11% of GDP, up from 4.5% in 2012). A large share of current spending is of a rigid nature, mainly regarding social insurance and public wages. These statutory payments restrict fiscal space for more productive expenditure and for crisis buffers. The share of rigid expenditure has increased in recent years, mainly due to the collective wage agreement in the public sector, and to rising interest expenditure. The ERP projects a gradual shift from current to capital spending until 2027. The share of social transfers in total expenditure would decline to 44.5% in 2027. The programme does not include projections for pension transfers in 2025-2027. Capital expenditure would

make up some 14% of total expenditure on average, up from 8.3% in 2024, between 2025 and 2027, which is above the long-term average of 10.4% in the period 2014-2024.

The fiscal framework has been improved, but compliance is lacking. The 2022 OBL introduces fiscal rules for the general government deficit and for public debt. While the government benefited from a crisis-related escape clause for the deficit rule in 2023, it did not comply with the 3% deficit target in 2024 either. In December 2024, the government postponed compliance with the rule to 2027, citing the need to reduce previously unbudgeted spending items, such as payment of arrears, over a longer time period than anticipated. It also postponed the full entry into force of the OBL by one year to 2026. The OBL provisions are focused on strengthening the medium-term budget framework. However, a number of key provisions depend on the operationalisation of an Integrated Information System for Financial Management (IFMIS), which is heavily delayed as its procurement process ran into legal obstacles. Moreover, while 17 by-laws to the OBL have been adopted in December 2024, the adoption of the 15 remaining by-laws is progressing slowly. The OBL also provides for the establishment of a Fiscal Council, which was set up in 2024. Importantly, while the new Fiscal Council is fulfilling its tasks as required by the new OBL, it lacks staff and financial resources. The OBL also calls for better monitoring and presentation of fiscal risks in the public sector, by attributing a key role in this to the new Fiscal Council, and by mandating a description of fiscal risks as part of the mid-term fiscal strategy. Public investment management capacities have been strengthened further in 2024, as staffing in the new dedicated government unit progressed, but the government adoption of a new decree, which would operationalise the department's activities, is delayed. Lastly, the government has still not adopted the new legal framework for public-private partnerships.¹⁸ This would extend the government's choices of funding and thus contribute to modernising the ageing public infrastructure, while providing a better management of fiscal risks.

4. MAIN MACRO-RELEVANT STRUCTURAL CHALLENGES

The Commission approved the Reform Agenda of North Macedonia in October 2024. In November 2023, the Commission proposed a New Growth Plan for the Western Balkans with the aim of supporting the region's economic convergence and accelerating the accession process. The plan involves a Reform and Growth Facility¹⁹ (EUR 2 billion in grants, EUR 4 billion in loans) that is to be disbursed in 2024-2027 as investment²⁰ and budget support in exchange for implementing reforms that are set out in reform agendas prepared by the Western Balkan partners. Under the Reform and Growth Facility, the allocation for North Macedonia amounts to EUR 750.4 million, with EUR 215.3 million planned in grants and EUR 535 million in concessional loans. Of the total amount of support, EUR 349.1 million is to be allocated in the form of budget support, with the remaining EUR 401.3 million allocated for the financing of infrastructure projects and implemented through the Western Balkan Investment Framework. The New Growth Plan is an important tool to increase reform incentives to boost growth and convergence. In this context, with a view to ensuring an

¹⁸ According to the government, the reason is the multitude of public institutions which need to give their consent, rather than substantial issues.

¹⁹ <https://eur-lex.europa.eu/eli/reg/2024/1449/oj/eng>

²⁰ Infrastructure investments need to comply with the EU environmental *acquis*, national and international nature protection and water management obligations, ensure public participation and consultation, and guarantee high quality environmental impact assessment reports that include cumulative impacts on nature and biodiversity.

integrated surveillance of the economy of North Macedonia, this chapter briefly outlines the main structural challenges facing the country.

Convergence with EU income levels has stalled, battered by low productivity growth.

After a steady, though gradual catching up with EU living standards prior to the financial crisis, the pace of convergence has slowed down considerably in the past decade, with real GDP per capita increasing from 37% of the EU-27 average in 2017 to 43% in 2021, and then dropping gradually to 41% in 2023. Structural problems of the labour market, the skills mismatch between labour market requirements and graduate qualifications, a large informal economy, low innovation activity, as well as substantial infrastructure investment needs to boost the competitiveness of the domestic economy are among the factors restraining productivity growth. The industry structure is characterised by a sizeable share of low value-added sectors and a large number of state-owned enterprises exhibit further productivity-restraining deficiencies in their operations and in their investment planning and implementation.

The high level of informality in the economy causes competitive distortions for domestic companies.

According to IMF estimates, the informal economy in North Macedonia could account for as much as 38% of GDP,²¹ while the number of informal employees as a proportion of total employees is estimated to have decreased in recent years. The main forms of informality are unregistered labour and partially undeclared wages. The implementation of the government's 2018 strategy and action plan to combat the informal economy remained incomplete, and in September 2023 the government adopted a new (2023-2027) strategy for formalisation of the informal economy. The strategy aims at reducing the size of the informal economy from an estimated 28.9% of GDP in 2019 down to 26% by end-2027. Another major competition-distorting factor in the economy are deficiencies in the country's State aid system. The provision of State aid continues to suffer from a multitude of providers and a lack of transparency, which not only distorts the level playing field for companies, but also necessitates streamlining in order to achieve some fiscal savings. In this regard, the reform agenda provides for a number of measures intended to make the State aid regime more transparent and efficient, including a reassessment of State aid schemes against the EU *acquis*.

The labour market is marked by persisting structural challenges which hold back economic growth and fuel wage growth.

Supported by a multitude of government measures, the labour market proved resilient throughout the recent crises. However, long-term features, such as: (i) low participation rates (around 53%), in particular for women (around 42%); (ii) high outflows from the labour force due to emigration; (iii) high youth unemployment; and (iv) the skills mismatch, are increasingly impacting on macroeconomic and wage developments as well as heightening fiscal risks through the trends in public sector wages and pensions.

While the number of higher education graduates is rising, the skills they obtain often do not meet labour market requirements.

While the proportion of people with higher education has been rising in North Macedonia in the past decade, education curricula are not well suited to equipping graduates with skills to match labour demand. The government addressed this issue in the 2018-2025 education strategy, which, however, has not been fully implemented due to insufficient funds. Public spending on education, at just over 4% of GDP

²¹ Kelmanson, Kirabaeva, Medina, Mircheva, and Weiss (2019) "Explaining the shadow economy in Europe: size, causes and policy options," Working Paper No. 19/278, International Monetary Fund. The IMF figure is at the upper range of estimates.

in 2023, remains below the EU average, and is focused on wages and goods and services, rather than maintenance of and investment in infrastructure. Furthermore, spending is inefficient due to outdated formulas for the redistribution of public education funds by the municipalities. While a new funding formula for secondary education has not been adopted yet, this is included in the Reform Agenda, as a measure to be implemented by December 2026. The percentage of adults participating in learning remains low, compared to the EU-27 average, at 2.8% in 2023. The Reform Agenda provides for a number of measures that aim at raising the share of adults in continuing education. The further development of qualifications is key to bringing medium-skilled and low-skilled people into the labour market.

Low digitalisation and muted innovation activity restrain the competitiveness of business. The economy would benefit from increased access to broadband, the digitalisation of public services to facilitate administrative procedures, and the development of digital skills. The percentage of households with internet access at home increased by 10.1pps. between 2017 and 2021 (no data for 2022 and 2023) to 83.6%. A fixed broadband connection to the internet is used by 88% of households, and by 92% of businesses with 10 or more employees, but smaller companies still face obstacles. More effort needs to be undertaken to improve digital skills, including by: (i) setting up a national framework for digital skills for students and teachers; (ii) increasing IT tools in primary and secondary schools; and (iii) expanding access to fast-speed internet to small business and to non-urban areas. There are also large deficiencies in the security of digital infrastructures and of government services, which need to be addressed. R&D activity in the economy remains muted, partly as R&D funding, at 0.4% of GDP, remains low and significantly below the EU average (about 2.3% of GDP), with the government providing almost half of the funding, and the business sector adding another 25% (the rest is funded by higher education and foreign sources). Links between businesses and others involved in innovation are weak.

The transition to renewable energy sources and improvements in energy efficiency require large investments. North Macedonia's economy relies heavily on coal-fired electricity production. Renewable energy accounted for only 19.9% of energy consumption in 2023. In the transport sector, the share of renewables is, however, negligible, and a new Law on biofuels, intended to increase the use of renewable energy in transport, has still not been adopted. In the post-pandemic period, North Macedonia has managed to increase domestic electricity production, thus reducing its dependence on energy imports. North Macedonia adopted its National Energy and Climate Plan in 2022. It aims to increase the share of renewable energy sources in gross domestic energy consumption to 38% by 2030. The shift towards renewable energy sources, as well as improvements in energy efficiency, to meet targets for greenhouse gas reductions set under the European Green Deal will require significant investments. Timely introduction of a carbon tax can contribute to meeting the emissions targets and to preparing for the full implementation of the carbon border adjustment mechanism. Well-managed public investment and improved access to private investments, such as through a risk-mitigating framework for public-private partnerships would also facilitate the green transition.

5. CONSISTENCY OF THE REFORM AGENDA WITH THE ERP'S MACRO-FISCAL FRAMEWORK

The ERP contains a first attempt to estimate the economic impact of selected reform measures under the Reform Agenda. The chosen areas concern energy/digital transition; human capital; and private sector and business environment. The analysis contains estimates on the growth impact of reforms, while fiscal impacts are not yet included.

- Align electricity sector regulation with the electricity integration package to enable electricity market coupling of the EU and North Macedonia. Planned investment in renewable energy, in line with the targets set in the country's 2022 National Energy and Climate Plan, is projected to add 2% of GDP annually and to create some 6 000 jobs in the medium term.
- Invest in renewable energy and implementation of the Renewable Energy Directive.
- Enhance public e-services offered through the governmental e-platform and simplify administrative and electronic procedures. The reform aims to increase the availability of government e-services by 50% by 2027. This reform will save over 10.2 million kW hours per year, equivalent to around EUR 58 million per year. The time saving is projected to increase Gross Value Added by 0.46% and GDP by 0.40%.
- Reinforce the education system to address the skills mismatch, increase access to and quality of VET, and improve access to work-based learning and dual education.
- Increase participation in adult education and improve recognition of non-formal and informal learning. The measure would improve productivity by 0.55pp, leading to a similar increase in GDP.
- Expand the use of e-customs services for economic operators. The programme explains that a positive impact on productivity can be expected from the reduction in customs clearing times, the reduction of administrative and compliance burdens, and improved revenue collection. The presentation in the programme could have been supported by the assessment of the revenues generated by customs and the status of the application of customs law.

The scoring and selection of reforms for the impact assessment was carried out based on three pre-selected criteria. First, the measure should provide an opportunity to assess the direct economic impact. Second, it should have a strong positive impact on the economy. Third, the measure must be based on a clear plan with activities that will begin immediately after the adoption of the Reform Agenda. Additionally, the measure must take account of its impact on the business environment.

Overall, the reforms presented in the programme are appropriate to be assessed on their economic (and in most cases also their fiscal) impact. The measures are well explained in their goals and in their concrete steps, which are in many cases based on quantitative targets. In some cases, the government explains the analytical approach chosen for calculating the measure's impact on productivity and GDP growth, as in the case of the planned increase in public e-services and the measures to mitigate the skills mismatch. For other measures, notably the planned increase of renewable energy capacity by 0.8 GW until 2027, the programme would have benefited from more detail on how it calculated the economic benefit.

An assessment of the fiscal impact of implementing the Reform Agenda would likely also have added clarity to the government's mid-term fiscal plans. The revenue forecast of the 2025 budget contains only the pre-financing amount (about EUR 24.5 million paid directly to the Treasury), not the payments linked to individual reforms. The programme could have detailed the projected expenditure linked to the implementation of the measures, including information on whether respective projects are included in the capital spending projected for 2025. These calculations are likely to be available at least for those measures that have been in the pipeline for quite some time, such as the ones on electricity integration and renewables. Moreover, the reform agenda contains several measures from the area of public financial management that would have been suited to be assessed with a view to their fiscal impact and hence their contribution to the government's fiscal consolidation plans, notably regarding the implementation of the OBL including measures to improve public investment management, or the introduction of a new public sector salary system.

ANNEX 1: OVERVIEW OF THE IMPLEMENTATION OF THE POLICY GUIDANCE ADOPTED AT THE ECONOMIC AND FINANCIAL DIALOGUE IN 2024

Every year since 2015, the Economic and Financial Dialogue between the EU and enlargement partners has adopted targeted policy guidance for all partners. The guidance represents the participants' shared view on the policy measures that should be implemented to address macro-fiscal vulnerabilities and structural obstacles to growth. The underlying rationale of the guidance is similar to that of the country-specific recommendations usually adopted under the European Semester for EU Member States. Implementation of the guidance is evaluated by the Commission in the following year's ERP assessments.

The following table presents the Commission's assessment of the implementation of the 2024 policy guidance jointly adopted at the Economic and Financial Dialogue on 14 May 2024.

Overall: Limited implementation (36.1%) ²²	
2024 policy guidance (PG)	Summary assessment
<p>PG 1:</p> <p>Implement the 2024 budget as adopted and ensure the fiscal target is met, in particular by controlling wage spending and reducing energy subsidies (as foreseen under the current IMF programme); adopt the budget for 2025 in a timely manner and in line with the fiscal rules.</p>	<p>There was limited implementation of PG 1:</p> <p>1) No implementation: The original deficit target of 2024 (3.4% of GDP) was not met. In a budget revision adopted in the summer of 2024, the new government increased the deficit target to 4.7%, with the actual outcome coming in somewhat lower at 4.4% of GDP.</p> <p>Wage spending was not controlled, with a further increase in some public sector wages, introduced in the budget rebalancing in summer. There was an additional revision in December 2024, increasing the overall public sector wage bill by 8.3% compared to the original budget. The wage bill increased by 19% y-o-y (+0.2pps of GDP) in 2024 and the 2025 budget increases it further by 9.7%.</p> <p>There were no further energy subsidies in 2024, but the government heavily supported the domestic electricity company, ESM, via loans and grants, mainly for investment purposes.</p> <p>The 2025 budget was adopted in December 2024, projecting a fiscal deficit of 4% of GDP. At the same time, the government amended the Organic Budget Law to postpone its implementation to 2026. The application of the new fiscal rules has also been postponed, to 2027, when the deficit is expected to comply with the 3% of GDP ceiling.</p>
<p>Strengthen the administrative capacity for the regular</p>	<p>2) Limited implementation: As the only</p>

²² For a detailed description of the methodology used to assess policy guidance implementation, see Section 1.3 of the Commission's Overview and Country Assessments of the 2017 Economic Reform Programmes. This is available at https://ec.europa.eu/info/publications/economy-finance/2017-economic-reform-programmes-commissions-overview-and-country-assessments_en.

<p>preparation and publication of the tax expenditure report and explore all options to further broaden the tax base.</p> <p>Introduce an integrated approach for reducing the build-up of arrears of public sector entities, through putting in place an Integrated Financial Management Information System and by setting up an effective system for monitoring of fiscal risks in the Ministry of Finance, including the fiscal risks stemming from SOEs and arrears.</p>	<p>measure raising tax revenue in 2025, the Parliament adopted the new Law on the global minimum corporate profit tax, which raises the tax rate for domestic companies which are subsidiaries of multinational companies, with an annual turnover of EUR 750 million from 10% to 15%, applicable as of 2026. This change will affect only a few companies operating in the country, mainly in the sectors of telecommunications, cement production, and energy distribution. Estimates are that an additional EUR 30 million annually will be paid to the treasury. The new tax is in line with the OECD global minimum tax agreement which North Macedonia has committed to implement. The government reported in the Fiscal Strategy on the amount of tax expenditure by tax category, as required by the OBL. The same table is taken up in the ERP. There were no new measures aiming at the reduction of tax exemptions. The government benefits from technical assistance to build capacities in this area.</p> <p>3) Limited implementation: An integrated approach for reducing the build-up of arrears has not yet been introduced, due to legal problems with the procurement process, which likely needs to be relaunched. Some fiscal risks are being reported in the Fiscal Strategy, as required by the OBL, but the reporting remains rather general.</p>
<p>PG 2:</p> <p>Ensure timely implementation of the new Organic Budget Law (OBL) in its entirety by 2025, by adopting the necessary by-laws, in particular on budget classification and on the statement on fiscal policy; and by updating the manual on macro-fiscal projections.</p> <p>To improve public investment management, adopt a methodology/guidelines for appraisal of projects, in line with the recommendations of the IMF and the World Bank, and ensure sufficient training of staff in the new PIM department of the Ministry of Finance.</p>	<p>There was limited implementation of PG 2:</p> <p>1) Partial implementation: In December 2024, the government adopted an amendment to the OBL postponing its implementation by one year, to 2026. The government adopted 17 out of 32 by-laws, in December 2024. These by-laws include the one on budget classification. The Fiscal Statement was published by the government in early October 2024.</p> <p>The manual on macro-fiscal projections has been updated.</p> <p>2) Limited implementation: The adoption of the PIM Decree has been postponed due to the need for additional inter-governmental consultations following the request of relevant national institutions for additional time to better prepare for the reform. This consultation process is finalised, and the draft decree is in the final stage of adoption by the Government. The PIM Department currently consists of 6 employees, out of 14 planned. In 2025, two new recruitments are planned. Training for the PIM Department staff is due to take place in spring with World Bank help. Trainings will also be organised for the ministries, SOEs and municipalities after the</p>

<p>To enhance private sector financing of public infrastructure projects based on a suitable regulatory framework, adopt the Law on public-private partnership.</p>	<p>PIM Decree is adopted.</p> <p>3) No implementation The Law on public-private partnership (PPP) has not been adopted.</p>
<p>PG 3:</p> <p>Ensure a sufficiently tight monetary policy stance as long as necessary to anchor inflation expectations at levels consistent with price stability and support the peg, underpinned by a thorough assessment of potential second-round effects.</p> <p>Safeguard the independence of the central bank in its key statutory tasks, including in staffing and wage issues, by excluding the national bank from the scope of all related laws on administrative servants and public sector employees.</p> <p>Further enhance risk-based supervision in line with best international and European practices, including by operationalising the Bank Resolution Law by amending by-laws and building capacity ahead of implementation, upgrading the deposit insurance law, further implementing measures to promote the role of the domestic currency and improving data collection, notably on real estate, to enable a comprehensive assessment of financial sector risks.</p>	<p>There was substantial implementation of PG3:</p> <p>1) Full implementation: The central bank has carefully monitored the evolution of price dynamics, and inflation expectations remained well anchored. It kept a sufficiently tight monetary policy stance by maintaining a substantive interest rate differential to the euro area in support of the peg, while gradually increasing the Countercyclical Capital Buffer.</p> <p>2) Limited implementation: The parliament adopted the amendments to exclude the central bank staff from the administrative servants' law, but similar changes to the public sector employees' law are still pending. The January 2025 revision to the central bank law, made without consulting the central bank, severely restricts its profit retention rate. This sets an unwelcome precedent and may endanger the central bank's financial independence.</p> <p>3) Substantial implementation: In January 2024, application of the new credit risk management methodology started and in January 2025, a regulation enhancing banks' data reporting was implemented. However, improvements in data availability as regards in particular the real estate sector have been limited. The counter-cyclical capital buffer has been further increased to curb potential risks. Final by-laws on bank resolution are set for completion in April 2025. However, the bank resolution framework can only be operationalised once the revised framework on deposit insurance is established, creating the institution managing both the deposit insurance and resolution funds. Despite overall progress in denarisation, efforts should continue to improve the use of the local currency.</p>

ANNEX 2: COMPLIANCE WITH PROGRAMME REQUIREMENTS

The government of North Macedonia submitted the 2025-2027 ERP on 16 January 2025. None of its components are missing.

Inter-ministerial coordination

The Ministry of Finance of North Macedonia coordinated the preparation of the ERP and an inter-ministerial working group comprised of several ministries, agencies and other offices were involved in this work. The ERP includes an annex listing the institutions and individuals involved in its preparation. The government formally endorsed the ERP on 16 January 2025. The coordination process worked well and the attendance to technical meetings was high.

Stakeholder consultation

The ERP's 2025-2027 draft structural reforms were posted on the Ministry of Finance's website on 15-29 December 2024, and interested parties were invited to send written contributions. The written comments and suggestions are set out in an annex to the ERP.

Macroeconomic framework

The macroeconomic framework is coherent and consistent, while somewhat optimistic. The ERP presents two alternative scenarios compared to the baseline: (i) assuming lower export growth; and (ii) assuming weaker investment. It does not include a low-growth scenario combining both domestic and external risks. The ERP's sensitivity analysis would have benefited from a more comprehensive impact assessment, including on employment, deficit and debt. The external sector outlook is described in detail and an analysis of external debt sustainability is provided in the annex. Overall, the quality of national accounts data has gradually deteriorated in recent years, with the number and size of revisions having become more frequent. This points to deficiencies in GDP data collection.

Fiscal framework

The ERP is based on the latest budget projections following the latest budget reallocation and on the fiscal data available at the end of Q3. It includes: (i) information on the expected budgetary impact of new policy measures; (ii) an analysis of the budget balance's sensitivity to lower GDP, lower execution of capital expenditure, and lower collection of revenue; (iii) an analysis of public debt's sensitivity to changes in interest rates and exchange rates; and (iv) a short assessment of the long-term sustainability of public finances based on a number of assumptions, including population ageing.

Structural reforms

The chapter on structural reforms has been prepared in line with the ERP guidance note.