



REPUBLIC OF NORTH MACEDONIA  
GOVERNMENT OF THE REPUBLIC OF NORTH MACEDONIA

# **2022-2024 FISCAL STRATEGY OF THE REPUBLIC OF NORTH MACEDONIA (with prospects until 2026)**

Skopje, May 2021

## Summary of the 2022-2024 Fiscal Strategy of the Republic of North Macedonia (with prospects until 2026)

Fiscal Strategy comprises medium-term guidelines and goals of the fiscal policy, main macroeconomic projections, amounts of the main categories of projected revenues and expenditures, as well as budget deficit and debt projections. Fiscal Strategy reflects the medium-term fiscal goals and strategic priorities of the Government of North Macedonia.

Upon the severe collapse in 2020, economy is expected to recover in 2020, after which economic growth intensification is projected in the upcoming years. Government support has continued in 2021 through various economic measures, by extending the measures undertaken last year, the realisation of which continued in the course of this year, being also coupled by new measures, all to the end of faster recovery of domestic economy and creating basis for accelerated economic growth in the longer term. With respect to the external environment, gradual stabilisation of the global supply chains is expected, as well as increase of the foreign demand, which, coupled with the decreased pressures from the pandemic globally, are expected to have positive effect on the domestic economic developments in the coming period, both the foreign trade and the investments and consumption. Favourable international environment and mass immunisation process in the country are expected to have beneficial effect on the expectations and the confidence of the domestic economic entities and the propensity for investments and consumption. Fiscal policy and redesigned public expenditures, with an emphasis on the public investment cycles, as well as the measures geared towards accelerated, inclusive and sustainable economic growth, will have significant impact on both investment demand and potential growth. According to the baseline medium-term scenario, economic growth in 2021 is projected at 4.1%, with average annual growth of 5.4% projected for the period 2022-2026, boosted by domestic demand, while net export is expected to have negative contribution, amid projected growth of both export and import.

Key elements of the medium-term fiscal policy are redesigned and improved public finance structure, through increased share of capital expenditures, as well as the gradual fiscal consolidation, by reducing the budget deficit as percentage share of GDP, as follows: 4.3% in 2022, 3.5% in 2023, 2.9% in 2024, 2.5% in 2025 and 2.2% in 2026. Primary budget deficit will also accordingly decline gradually from 3.0% of GDP in 2022 to 1.2% in 2026. In order to strengthen the fiscal discipline, the Medium-Term Fiscal Strategy introduces budget expenditure ceilings and ceilings by budget users.

Main priorities as regards the tax system are increased fairness in taxation, increased efficiency and effectiveness of revenue collection, enhanced tax transparency, improved quality of services rendered by tax system institutions, by simplifying and speeding up procedures and reducing the administrative burden through many digital services, as well by introducing environmental (green) taxation, in order to stimulate taxpayers to contribute, through duties and fees, to pollution reduction. Main objective of the tax policy is to ensure sustainable economic growth and development, thereby providing for legal safety of taxpayers and collection of tax revenues on regular basis.

Expenditures side of the Budget of the Republic of North Macedonia, in the next period, is fully created in terms of achieving the strategic priorities, accelerating the economic growth, and the EU integration process and the obligations deriving from the NATO membership and similar.

For the purpose of strengthening the fiscal decentralisation, in the 2021-2024 period, many activities and measures have been envisaged, grouped in three pillars, as follows: I. Improved fiscal capacity and increased municipal revenues, II. Strengthened fiscal discipline and III. Increased transparency and accountability as regards municipalities' operations. Ultimate goal of this process is achieving better quality of public services, higher economic growth and better living standard.

Public debt management policy is aimed at ensuring the funds necessary to finance the budget deficit and repay the due debt liabilities from the previous years, as well as funds for project financing, thereby not increasing the debt to a level that can jeopardise the stability of the economy and the economic growth of the country.

Ministry of Finance is in the final stage of preparing the Growth Acceleration Financing Plan. The essence of the Plan is to produce a multiplying effect by creating and using new mechanisms, instruments, funds and sources of financing, i.e. in addition to the planned public investments amounting to more than EUR 4 billion for the period 2021-2026 financed from the Budget, IPA funds and by international financial institutions, much more funds and investments from the private sector to be mobilised.

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Pursuant to paragraph 2, Article 16 of the Budget Law („Official Gazette of the Republic of North Macedonia“, nos. 64/2005, 04/2008, 103/2008, 156/2009, 95/2010, 180/2011, 171/2012, 192/2015 and 167/2016), Government of the Republic of North Macedonia, at its session held on \_ May 2021, adopted the 2022 - 2024 Fiscal Strategy of the Republic of North Macedonia (with prospects until 2026).

## Introduction

Fiscal Strategy sets the medium-term projections and, in line with the Budget Law, it is adopted for a three-year period, proposing guidelines and goals of the fiscal policy, the key macroeconomic projections and indicators, determining the amounts of the main categories of projected revenues and allocations for the respective period, as well as projections on the budget deficit and the debt. In the interest of improved fiscal predictability, medium-term planning under this Fiscal Strategy covers the next five-year period.

Fiscal Strategy remains to be a crucial instrument as regards the medium-term budget planning, whereby reliable medium-term budget planning is of great significance when creating the medium-term fiscal framework.

Improving public finance management, thus improving the Fiscal Strategy as one of the most important strategic documents of a government, is set among the key priorities of the Government, also being a priority on the road to EU accession.

Medium-term Fiscal Strategy is in line with the medium-term fiscal goals and strategic priorities of the Government of the Republic of North Macedonia and it provides for monitoring the dynamics of revenues and expenditures in relation to the fiscal goals.

In line with the 2022 Decision on Determining Strategic Priorities, Government of the Republic of North Macedonia remains to be further committed to achieving the most important strategic priorities, as follows:

- ensuring accelerated and sustainable economic growth, higher living standard and better quality of life of the citizens;
- coping with the consequences of COVID-19 induced global pandemic;
- successful accession negotiations with the European Union;
- developing defensive policy in support of development, independence, territorial integrity, safety of citizens, as well as collective safety;
- rule of law, independence of the judiciary, consistent and non-selective fight against crime and corruption with broad and binding transparency;
- high-quality education available to all according to the demand on the labor market, development and promotion of culture and sport;
- modern and efficient public administration based on digitalisation that provides for high-quality and fast services to citizens and businesses;
- full implementation of Ohrid Framework Agreement, building a civil state with ethnic cohesion and social cohesion based on the principles of mutual tolerance and respect and
- environmental protection, green development, reduction of air pollution and the impact of climate change.

Key elements of the medium-term fiscal policy are redesigning of the budget policy and the fiscal consolidation, aimed at supporting the macroeconomic stability, accelerating the economic growth, thus strengthening the growth potential of the national economy.

Redesigning the budget policy is closely related to the Strategy for Economic Recovery and Intensified Growth, comprising four pillars: (i) economic recovery from COVID-19, (ii) intensified, inclusive and sustainable economic growth, (iii) boosted competitiveness of the private sector and (iv) development of human resources and equal opportunities.

First pillar, Economic Recovery from COVID-19 covers the following two priorities: 1/ protection of the citizens' health and social protection of the most vulnerable categories in the society, and 2/ support to the economy and the private sector, as well as job protection.

Second pillar, Accelerated, Inclusive and Sustainable Economic Growth, is focused on the following priority areas: 1/ good governance (rule of law, combatting corruption and capacity building of institutions), 2/fiscal sustainability, macroeconomic and financial stability, 3/local and balanced regional development 4/sustainable and healthy environment and 5/digitalisation of the economy and public services, under which various measures and activities have been envisaged.

As regards the third pillar, Strengthening the Competitiveness of the Private Sector, the focus is placed on the following: 1/ strengthening trade links and integration into global value creation chains, 2/Improving the business environment and combating the informal economy, 3/improving the access to finance and technology adaptation, and 4/modernisation of agriculture.

The fourth pillar, Human Resources Development and Equal Opportunities, covers the following three priority areas: 1/ human resources development (education, science and health), 2/greater activity of the working age population, and 3/social protection and social insurance, under which various measures and activities have been envisaged.

Planned fiscal consolidation covers three main aspects:

- improving budget revenue collection, via measures aimed at reducing informal economy and measures aimed at preventing and combatting corruption;
- reduction and restructuring of budget expenditures, by cutting non-priority and non-essential costs, greater support to the private sector and innovations aimed at strengthening competitiveness, high allocations for social protection and revision of the methodologies for transfers and subsidies, etc.;
- changes in the sources of financing the budget deficit, greater diversification of sources of financing the deficit, financing and realising certain projects through public-private partnerships and establishing Development Fund for Strategic Investments.

To the end of the commitments to fiscal decentralisation, as well as the commitments to double the economic growth and achieve around 5% GDP annual growth rates, Ministry of Finance is in the final stage of preparing the Growth Acceleration Financing Plan. This Plan presents the existing and the new mechanisms for access to capital to finance the recovery and the acceleration of the economic growth, through investment projects in both the public and the private sector, also quantifying the effects on gross investments and the economic growth. The purpose of the Plan is to scale up total investments in the economy, thereby staying on the set path of fiscal consolidation, thus maintaining the stable public debt level.

The essence of the Plan is to produce a multiplying effect by creating and using new mechanisms, instruments, funds and sources of financing, i.e. in addition to the planned public investments amounting to more than EUR 4 billion for the period 2021-2026 financed from the Budget, IPA funds and by international financial institutions, much more funds and investments from the private sector to be mobilised.

The Plan involves establishment of development funds, innovation support funds, guarantee funds, equity funds, venture capital funds and similar instruments for support of export-oriented companies, small- and medium-sized enterprises, as well as social enterprises. Public-private partnerships, concessions and other instruments for financing public capital projects are also planned to be put into place, to be coupled with financing private sector projects. Some of the projects have been already considered within the National Investment Committee, while the remaining ones will result as initiatives of the public or the private sector. Priority funding areas are: environment, digitisation, innovations, human capital and social inclusion.

It has been envisaged to establish various development funds, which will target projects in both the public and the private sector, applying different mechanisms for capital mobilising. One of them is the Fund for Export Companies Support, which will, via favourable credits, support their promotion on foreign markets. Another possibility is establishment of Investment Fund, which will support capital projects such as construction of kindergartens, schools, sports halls, etc., whereby when selecting the companies that would participate in the overall process, priority would be given to small- and medium-sized enterprises. Thus, in addition to investments in capital goods, small- and medium-sized enterprises would be also supported. Micro, small- and medium-sized enterprises will also be supported by the Hybrid Investment Fund for "green" and digital economy.

Strategic Investment Fund is also envisaged to be established, intended for financing infrastructure and green investments. This Fund will provide the necessary financial support to cover the robust infrastructure and investment agenda in the free economic and industrial zones in the Republic of North Macedonia. Following the trial period, the model can be expanded so as to include all such activities in the country, without any limitations, however, with the support from international private and institutional investors.

Law on Alternative Investment Funds, being in preparatory stage, will regulate the establishment and the operations of the venture capital funds, geared towards mobilising resources from institutional investors and private entrepreneurs, which will invest larger amounts.

As regards establishment of some of these Funds, it is possible to use the already established institutional capacities, such as the Innovation and Technological Development Fund, the Development Bank and the Directorate for Technological Industrial Development Zones.

Apart from the Funds, crowdfunding is planned as additional financing instrument. Timeframe for its introduction is by second half of 2022.

Technical assistance for preliminary design, concepts, institutional and legal framework will be provided in cooperation with the international financial institutions, such as the World Bank Group, the European Bank for Reconstruction and Development (EBRD) and the European Investment Bank (EIB). In addition, in the period to come, it is expected for the World Bank to deliver a Pre-Feasibility Study, which will give full picture and complete the specific steps in creating and implementing these activities.

## **1. Macroeconomic Trends and Projections**

### **1.1 International Economic Trends and Forecasts<sup>1</sup>**

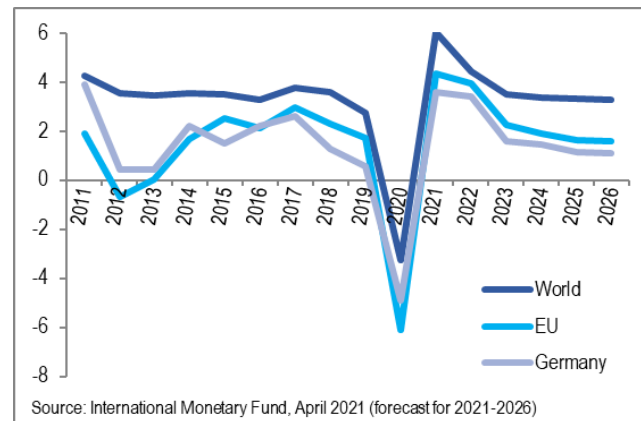
Global economy in 2021 is expected to be under the influence of the effects of the Coronavirus-induced pandemic. However, upon the economic activity contraction in 2020, which has never been seen in history before, due to its nature and

<sup>1</sup>Analysis in this section is based on the "World Economic Outlook" of the International Monetary Fund, published in April 2021.

speed of spread, global economy is expected to recover in 2021, which will greatly depend on the additional fiscal support in the advanced economies, as well as the speed of vaccination throughout the year. As a result of timely policies to cope with the pandemic impact, the resulting economic effects therefrom are expected to leave smaller scars than the 2008 global financial crisis.

Global economic activity is projected to grow by 6% in 2021, surging by 4.4% in 2022. In the medium term, global economic growth is projected to additionally slow down, reaching 3.4% average annual growth in the period 2023-2026. EU economy in 2021 is projected to grow at 4.4%, following its 6.1% decline the previous year. Growth rate in 2022 is projected at 3.9%, while average economic growth in the EU is projected at 1.8% annually in the period 2023-2026. As regards Germany, as the largest economy in the EU and our major trading partner, economic activity is projected to grow by 3.6% in 2021, 3.4% in 2022, while in the medium term, i.e. in the period 2023-2026, average annual growth of 1.3% is projected (Figure 1). Slowdown of economic growth, in the medium term, is expected to reflect the expected adverse effects of the crisis on the side of supply and the slowed down increase of labour force in the developed and some of the emerging market economic as a result of the population aging.

Figure 1. Global economic growth (%)



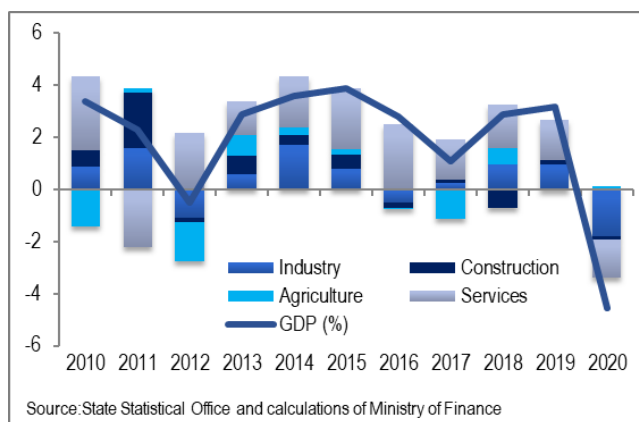
Uncertainty over the global growth projections is also accompanied by numerous downside and upside risks. Many things are still under great influence of the race between the virus and the vaccines. Advancement in vaccine take-up may improve the projections, while the new virus variants which vaccines might not be effective against may deteriorate them. Moreover, health crisis may additionally exacerbate the potential of aggregate supply, which may result from the reduced labour force activity rate, the numerous bankruptcies, as well as the disruptions in production networks. Geopolitical, trade and technological risks, above all the possibility for introducing trade barriers to protect the labour force, should not be overlooked.

## 1.2 Economic Trends in the Republic of North Macedonia

In 2020, GDP decreased by 4.5% in real terms on annual basis. Reduced economic activity is mostly a result of the unfavourable trends in the second quarter, when real GDP decreased by 14.9% on annual basis, being a result of the containment measures aimed at preventing the COVID-19 spread in the country, as well as the deteriorated international environment, thus affecting the activity of the majority of service activities, construction and industry. During the third and the fourth quarter, contraction of economic activity significantly slowed down, i.e. it decreased by 3.3% and 0.7%, respectively, amid slowed down dynamics of the activity in the industrial and services sectors, i.e. more favourable trends of export and investment activity, and continuous increase of public consumption to the end of coping with the pandemic.

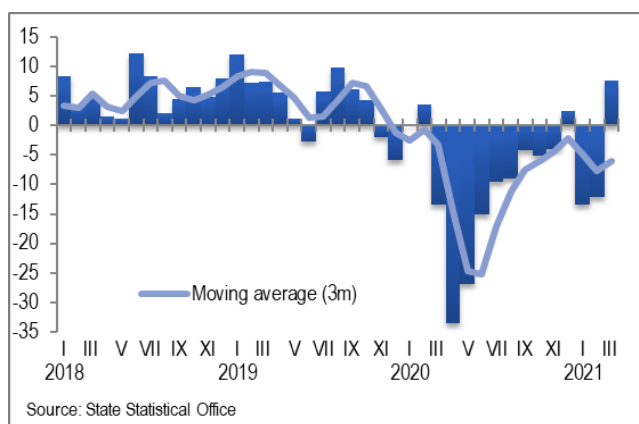
According to the estimates, the drop of economic activity could have been deeper by almost twice, if it had not been for the government support via the four sets of economic measures, aimed at supporting companies and employees in the activities hit the most by the pandemic, as well as the vulnerable categories. Such responsiveness of the fiscal policy resulted, above all, in mitigating the drop of income, private consumption and employment caused by the pandemic, as well as substantial growth of public consumption.

Figure 2. Economic growth structure according to production method (contribution to growth, percentage points)



Activity in the services sector dropped by 2.6% in 2020, being a result of the unfavourable trends in the Trade, transportation and food and accommodation services, experiencing 7.9% drop, being partially neutralised by the favourable trends in the ICT sector. High-frequency data on internal trade in the first three months of 2021 show increased turnover by 2.9% in nominal terms, arising from the increased trade in non-food products. In 2020, construction sector registered 2.1% decline in real terms which, in line with the monthly data, is due to the unfavorable trends in the construction activities as regards buildings, while construction activities as for civil engineering structures, experienced growth. Construction works in the first quarter of 2021 grew by 4.6% in nominal terms, being a result of the increased construction works in the segment of buildings. Agriculture sector in 2020 grew by 1.7% in real terms.

Figure 3. Year-on-year growth of industrial production (%)

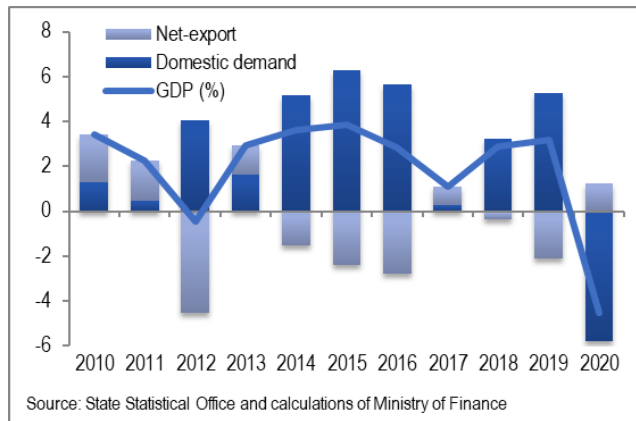


In 2020, activity in industrial sector declined by 10%, being mostly due to the decreased manufacture of machinery, equipment, electrical equipment and motor vehicles, i.e. activities, being, to a great extent, integrated in the global value chains, as well as the reduced manufacture of wearing apparel, textile and food products. In the course of first three months in 2021, industrial production dropped by 6.1%, thus interrupting, in March, the drop of production recorded in the previous two months, i.e. registering annual 7.6% growth (Figure 3), whereby in addition to the accelerated growth of production of machinery, equipment and electrical equipment compared to the first two months, Manufacture of textile, food products, motor vehicles, etc. shifted to the positive zone. Utilisation of the capacities in Manufacturing continued to grow in the first quarter of 2021, reaching 71.1% in March, thus reaching the approximate level before the health and the economic crisis.

Decomposition of GDP, according to the expenditure side, shows that private consumption and investments had negative contribution to the economic activity, while public consumption and net export had a positive contribution (Figure 4). Private consumption decreased by 5.6% in real terms, amid consumption restraint and significant decline of foreign remittances, which adversely affected the household income and subsequently the consumption. Thereby, the anti-crisis economic measures and the credit support of banks have, to a great extent, mitigated the significant decline of consumption.

In addition, declined total consumption is mitigated by the high increase of public consumption by 10.1%, due to the expenditures related to managing the pandemic and its consequences on the citizens. Gross investments decreased by 10.2% in real terms, corresponding to the drop of investments in construction works.

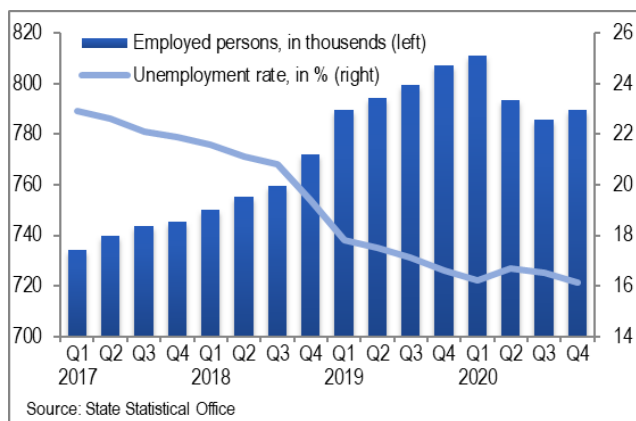
Figure 4. Economic growth expenditure structure (contribution to growth, percentage points)



Export of goods and services dropped by 10.9% in real terms, being mostly a result of the deteriorated international economic environment, resulting primarily in drop of the export of machinery, transport equipment and chemical products. Import of goods and services decreased by 10.5%, conditioned mostly from the reduced import of intermediary goods. In the last several months of 2020, foreign trade showed signs of recovery, followed by its intensification in the first three months of 2021, i.e. export of goods increased by 18%, while import of goods picked up by 14.1% in nominal terms.

As regards the labour market, employment continued to increase in the first quarter of 2020, followed by somewhat deterioration of the developments in the next quarters, as a result of the effects of the pandemic, being cushioned as a result of the government support for companies, aimed at keeping the jobs. Thus, according to the Labour Force Survey, average number of employees in 2020 recorded slight drop of 0.3% compared to 2019. Employment mainly dropped in the agriculture sector and electricity and water supply, while construction sector, transportation and food and accommodation services and experienced slighter decline. On other hand, employment was mostly increased at information and communication activity, health sector, social protection and trade. Average employment rate in 2020 accounted for 47.2%, being almost unchanged in relation to 2019, while average unemployment rate was reduced, accounting for 16.4%. Figure 5 shows the trends of employment and unemployment rate, by quarters.

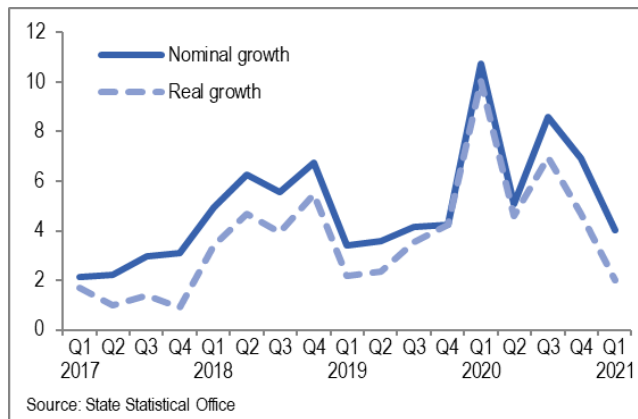
Figure 5. Number of employed persons and unemployment rate





Average monthly net wage in 2020 picked up by 7.8% in nominal terms and 6.5% in real terms, arising from the measures undertaken before the pandemic outbreak, such as: increased level of minimum wage, government measure for financial support of employers, who will increase wages up to a certain amount, increased wages for public sector employees in September 2019, as well as additional increase in wages in education and health sectors in 2020, while the wage financial support measure for employers affected by the health crisis mitigated the downward trend of wage growth throughout the pandemic. Wages were mostly increased in the following activities: information and communications, education, health and social protection, trade, manufacturing and construction. On the other hand, wages in food and accommodation services dropped due to the reduced scope of operations in this activity. Figure 6 shows the growth wage dynamics by quarters. In the course of the first quarter of 2021, average net wage increased by 4% in nominal terms, mostly as a result of the increased wages in information and communication activity, health sector, arts and some of the activities in the industrial sector.

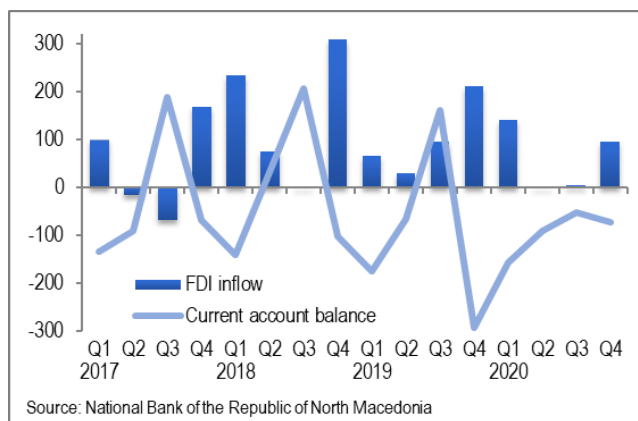
Figure 6. Annual increase of average net wage (%)



BOP current account in 2020 recorded a deficit of EUR 373 million, accounting for 3.5% of GDP. Compared to the previous year, current account registered insignificant deterioration as a percentage of GDP, due to private transfers from abroad, which decreased by around 24%, primarily in the second and third quarters, as a result of the global economic crisis caused by the pandemic. Such trends were neutralised by narrowing the trade deficit and the primary income deficit, as well as the improved balance in the services account.

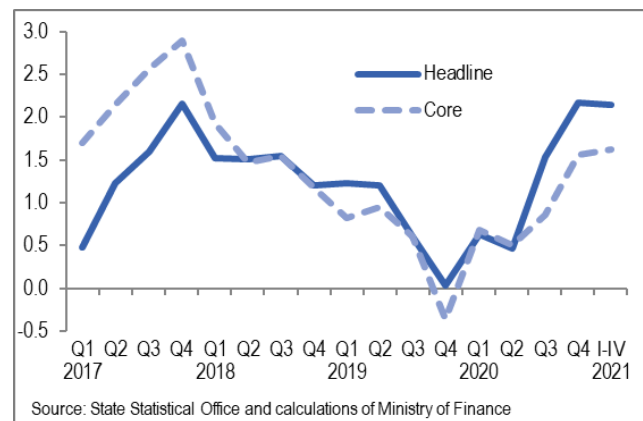
Inflow of foreign direct investments (FDIs) amounted to EUR 240 million (2.2% of GDP), financing the majority of the current account deficit, reflecting a solid inflow in the first and fourth quarter, while in the course of the second and third quarter, amid increased pandemic-induced uncertainty, inflow of FDIs stalled (Figure 7). FDIs are mostly in the form of debt instruments, on the basis of which inflow amounting to EUR 128 million was generated. Inflow, in the form of equity, was generated in the amount of EUR 97 million, while the remaining inflow is on the basis of reinvested earnings of companies with foreign capital. At the end of 2020, reserve assets provided for 5.3-month coverage of import of goods and services in the previous 12-month period, amounting to EUR 3.4 billion.

Figure 7. Current account balance and inflow of FDIs (EUR million)



Inflation rate in 2020 accounted for 1.2%. Increase of consumer prices was a result of the increase in price of food products by 2.6%, as well as the core inflation accounting for 0.9%, boosted by the increased price of tobacco, while price of oil derivatives recorded double-digit drop, in line with the reduced oil price on the global stock markets. In the period January-April 2021, inflation rate accounted for 2.2%, boosted by the increase of prices of food, electricity and tobacco, while the change of prices of oil derivative shifted to the positive zone in April. Core inflation accounted for 1.6% in this period (Figure 8).

Figure 8. Headline and core inflation (%)



During the first half of 2020, amid high level of foreign exchange reserves and low inflationary pressures, the National Bank continued to pursue its accommodative monetary policy by reducing the policy rate at three occasions, in January, March and May, respectively, by a total of 0.75 percentage points, i.e. to 1.5%, as well as via other additional measures, for the purpose of mitigating the effects of the pandemic on the domestic economy. Credit activity in December 2020 picked up by 4.7% on annual basis, boosted by the increased credits to households by 8%, while credits to enterprises experienced 1.1% growth. Total deposits in the banking system in December were higher by 5.9% on annual basis, whereby denar deposits surged by 3.6%, while foreign currency deposit registered 9.5% growth.

In March 2021, by additionally reducing the policy rate by 0.25 percentage points, the National Bank continued to further loosen the monetary policy. Thus, its policy rate accounts for 1.25%, being at the lowest level so far. On annual basis, total credits grew by 5.7% in April 2021, amid growth of both credits to households of 8.9% and credits to enterprises of 2.3%. Total deposit potential in April 2021 grew by 6.9% on annual basis, whereby such acceleration of the deposit growth arises from the more dynamic increase of denar deposits.

### 1.3 Medium-Term Macroeconomic Projections

Upon the severe collapse in 2020, economy is expected to recover in 2020, after which economic growth intensification is projected in the upcoming years, i.e. getting back to the pre-crisis growth trajectory throughout 2022 and its further acceleration.

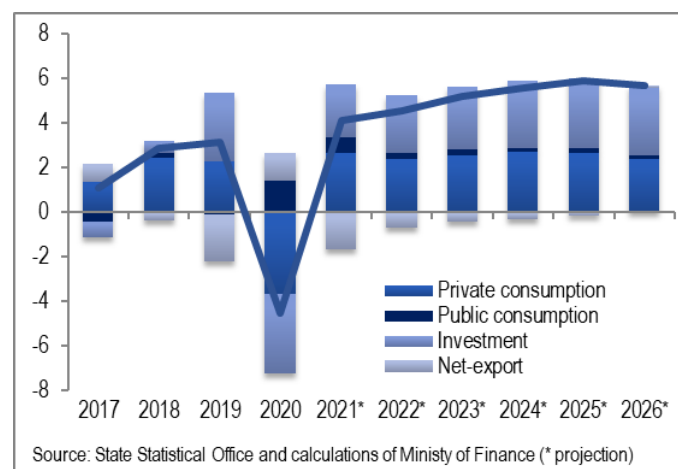
Government support has continued in 2021 through various economic measures, by extending the measures undertaken last year, the realisation of which continued in the course of this year, being also coupled by new measures, aimed at mitigating the effects of the pandemic on the vulnerable categories and supporting the domestic economy, all to the end of its faster recovery and creating basis for accelerated economic growth in the longer term. With respect to the external environment, gradual stabilisation of the global supply chains is expected, as well as increase of the foreign demand, which, coupled with the decreased pressures from the pandemic globally, are expected to have positive effect on the domestic economic developments in the coming period, both the foreign trade and the investments and consumption.

Favourable international environment and mass immunisation process in the country are expected to have beneficial effect on the expectations and the confidence of the domestic economic entities and the propensity for investments and consumption. Fiscal policy and redesigned public expenditures, with an emphasis on the public investment cycle, as well as the measures geared towards accelerated, inclusive and sustainable economic growth, will have significant impact on both investment demand and potential growth.

For the purpose of supporting investment activity, intensifying economic growth and increasing employment, in the longer term, as well as boosting the competitiveness of the economy, thereby remaining on the path of fiscal consolidation, Growth Acceleration Financing Plan is under preparation, providing for new manners of access to capital, via projects in both the public and the private sector, applying new mechanisms, instruments, Funds and sources of financing, which will generate multiplier effects on the economic activity.

According to the baseline medium-term scenario, economic growth in 2021 is projected at 4.1%, with average annual growth of 5.4% projected for the period 2022-2026, boosted by domestic demand, while net export is expected to have negative contribution, amid growth of both export and import.

Figure 9. GDP growth expenditure structure (contribution to growth, percentage points)



Economic growth decomposition shows that investments will play crucial role in the recovery of the economy and its gradual intensification (Figure 9). Real growth of gross investments is projected at 8% in 2021, whereby investments are expected to record 8.8% average annual growth in the 2022-2026 period. Growth of investments is based on the expected growth of private investments, in conditions of gradual restoring of business entities' confidence, more intensive inflows of FDIs, expected fiscal stimulus, to be channeled through increased capital expenditures, as well as increased support for private sector development and boosting the competitiveness, support to innovations and technological development of enterprises.

Consumption is also expected to underpin the growth of domestic demand. Upon the collapse in 2020, being significantly mitigated via the economic measures providing support to those most severely hit by the pandemic, private consumption is expected to increase by 4% in real terms in 2021, amid gradual restoring of the confidence and the optimism by starting the intensive vaccination, through increased remittances, being also supported by the undertaken fiscal measures aimed at coping with the pandemic. Favourable trends at private consumption are expected to continue in 2022-2026 period, when average annual growth of 3.9% is projected, underpinned by the expectations for further improvement of the trends on the labour market, the strengthened social protection system, as well as the growth of household disposable income. Positive effects on private consumption are also expected by the credit support of banks, supported by the measures undertaken by the monetary authorities.

Growth of public consumption is projected at 4.3% in real terms in 2021, being partially a result of the expenditures for coping with the health crisis. In the coming years, public consumption is expected to grow with a slower pace, i.e. 1.4% average annual growth is projected in the period 2022-2026, as a result of the efforts to reduce the non-essential expenditures and their rationalisation, as well as implementation of the fiscal consolidation process.

Export of goods and services is expected to grow by 10.6% in real terms in 2021 as a result of exhausting the adverse economic effects of the pandemic, recovery of the global value chains and external demand, and hence improved utilisation of the production capacities in the country. In the medium term, in conditions of expected stabilisation of the growth of external demand and increased export potential in the country via inflow of FDIs, export is expected to have a solid contribution to the economic growth, i.e. it is projected to experience average annual growth of 8.8% in real terms in the period 2022-2026.

Growth of the export activity and recovery of the domestic demand in 2021 provide for increased import of intermediary, investment and consumer goods, the real growth of import of goods and services being projected at 11%, which implies a negative contribution of the net export to the economic growth. Certain stabilisation of the import demand is envisaged in the period to come, i.e. average annual growth of import of goods and services is projected at 7.7% in real terms in the period 2022-2026, with a gradual narrowing of the negative contribution of the net export to the economic growth (Figure 9).

Table 1. Main macroeconomic indicators for North Macedonia

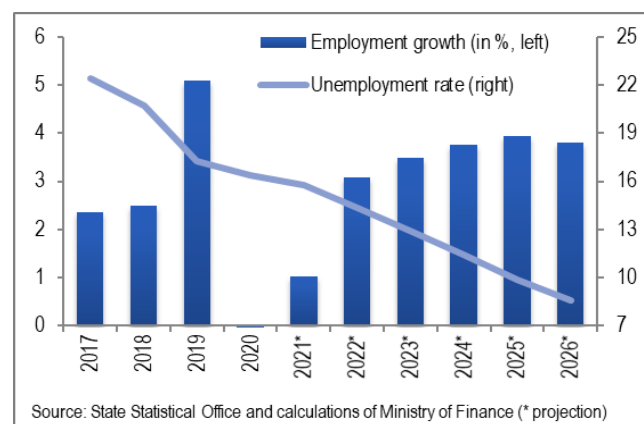
	2020	2021*	2022*	2023*	2024*	2025*	2026*
GDP, real growth rate (%)	-4.5	4.1	4.6	5.2	5.6	5.9	5.7
Inflation rate (average)	1.2	2.1	1.8	2.0	2.0	2.0	2.0
Gross capital formation (% of GDP)	29.6	30.8	31.8	32.9	34.0	35.1	36.2
Trade balance (% of GDP)	-16.9	-17.9	-17.7	-17.3	-16.8	-16.2	-15.6
Current account balance (% of GDP)	-3.5	-3.0	-2.4	-2.0	-1.6	-1.2	-0.7
Net wage - nominal growth (%)	7.8	3.0	3.5	3.8	4.1	4.2	4.2
Unemployment rate (average)	16.4	15.8	14.4	12.9	11.4	9.9	8.6
Employment rate (average)	47.2	47.5	48.6	49.8	51.3	52.8	54.3

Source: State Statistical Office, NBRNM and projections of Ministry of Finance (\*)

By reducing the pressures from the health crisis, the gradual restoring of investors' confidence and improvement of the expectations of business entities, labour demand is projected to grow in the upcoming period, being also boosted by the active employment measures and programs and the support for domestic and foreign enterprises geared towards job creation.

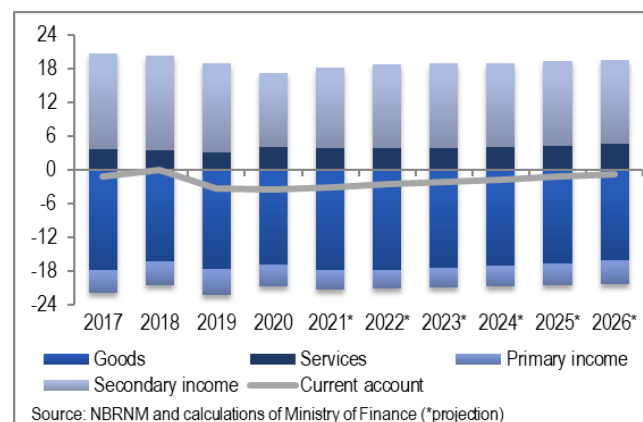
According to the baseline macroeconomic scenario, number of employees is expected to increase by 1% in 2021, while in the period 2022-2026, employment growth is expected to speed up, i.e. average annual increase of 3.6% is projected (Figure 10). Employment growth in this period is expected to also reflect on the labour supply, projected to increase by 1.7% in average on annual basis. Such trends on the labour market will contribute for the average unemployment rate in 2026 to drop to 8.6% and the average employment rate to surge to 54.3%. Increase of the average net wage in this period is expected to be 3.8% annually in nominal terms, with prospects for moderate intensification of the increase during the forecasting period.

Figure 10. Increase in the number of employees and unemployment rate



Inflation rate is projected at 2.1% in 2021, being somewhat intensification of the inflation compared to 2020, amid projected upward movement of foreign effective inflation and the prices of primary commodities on global stock markets. In the 2022-2026 period, inflation is expected to remain low and stable, projected at 1.8% in 2022 and 2% annually in the period to come, amid expected moderate increase of foreign effective inflation and partially under the influence of domestic demand.

Figure 11. Current account by components (balance, % of GDP)



In the period to come, BOP current account deficit is projected to gradually narrow. In 2021, deficit is expected to reduce to 3% of GDP, being mostly due to the projected increase of private transfers from abroad, amid gradual reduction of the adverse effects of the pandemic. Improvement of the deficit is expected to continue in the next years and to reduce below 1% of GDP in 2026, i.e. projected current account deficit accounts for 1.6% of GDP in average on annual basis in the forecasting period (Figure 11). Such improvement arises from the projected gradual narrowing of the trade deficit and the increased surplus on the services account, amid expected stabilisation of the level of current transfers from abroad in the medium term. Inflow of FDis is expected to exceed the current account deficit in the 2022-2026 period, thus having positive effects on retaining the foreign exchange reserves at adequate level.

Baseline macroeconomic scenario is accompanied by risks, being assessed as downside risks mostly related to the protraction and the consequences of the health crisis. Thus, potential slowed down implementation of the vaccination process, both in the country and globally, or in case of a new wave of infections due to the new variants of the Coronavirus and their greater resistance to the existing vaccines, may result in introducing and/or tightening the containment measures, repercussions on the global supply chains and the external demand, deteriorated expectations of business entities and households, reduced inflow of investments and foreign pecuniary remittances, and hence adverse consequences on the overall domestic economic activity. On the other hand, commencement of the EU accession negotiations could have a significant impact on both the investment activity and the implementation of the structural reforms in the country, the pace of which, if intensified, will boost long-term economic growth, while delays in resolving structural deficiencies could hinder the country's rapid and convergent economic growth. Thereby, maintenance of the political stability in the country is a key precondition for achieving the projected economic growth. Risks as regards the projected inflation dynamics are mainly related to the high uncertainty regarding the price trends of the primary products on the global stock markets.

## 2. Fiscal Projections

### 2.1. 2021 Budget of the Republic of North Macedonia

2021 Budget of the Republic of North Macedonia was prepared in the second half of 2020, amid significant impact of the health and the economic crisis caused by the Coronavirus. As a response to coping with the consequences of the economic crisis, the Government undertook all necessary comprehensive measures aimed at protecting the jobs, servicing the highest-priority liabilities, as well as reducing all less productive budget expenditures to the minimum.

What was taken into account in the assumptions concerning the 2021 fiscal projections, was the still present unpredictability related to the duration and the intensity of the health pandemic, its implications on the budget and the economy as a whole, and its impact on the economic recovery, as well as ensuring accelerated growth thereafter.

Total revenues of the 2021 Budget of the Republic of North Macedonia are projected at Denar 212.6 billion, being higher by 8.3% in relation to the second 2020 Supplementary Budget, while expenditures are projected at Denar 247.5 billion, being lower by 2.1% in relation to the second 2020 Supplementary Budget.

Such projected revenues and expenditures result in budget deficit of 4.9% of the projected GDP or Denar 34.9 million in absolute terms, thus providing for regular and undisrupted settlement of the liabilities of budget users.

### 2.1.1 Revenue Performance and Expenditure Execution in the period January – April 2021

In the period January-April 2021, total revenues of the Budget of the Republic of North Macedonia<sup>2</sup> (Table 2) were collected in the amount of Denar 67,840 or by around 31.9% of the 2021 Budget, i.e. they were higher by 11.7% compared to the collected ones in the same period last year. Denar 39,743 million out of this amount was tax revenues, being higher by 17.7% compared to last year. VAT revenues were collected in the amount of Denar 18,510 million, accounting for the most in the tax revenues – 46.6%. PIT revenues were collected in the amount of Denar 6,156 million, profit tax revenues were collected in the amount of Denar 4,756 million, while collection of excise revenues amounted to Denar 7,190 million. All types of tax revenues experienced growth compared to the analyzed period last year. Revenues on the basis of social contributions were collected in the amount of Denar 22,527 million, being by Denar 1,222 million or 5.7% higher than the respective period in 2020. Denar 15,226 million was collected on the basis of pension insurance, while revenues collected on the basis of health insurance contributions amounted to Denar 6,373 million.

Non-tax revenues were collected in the amount of Denar 4,364 million in the period January - April 2021. The largest share reflects non-tax revenues of budget users on their own accounts, collected in the amount of Denar 2,437 million. Capital revenues were collected in the amount of Denar 287 million, while budget users generated Denar 919 million on the basis of donations from international multilateral and bilateral cooperation.

In the period January - April 2021, total expenditures of the Budget of Republic of North Macedonia were executed in the amount of Denar 74,701 million, or around 30.2% of the 2021 Budget, i.e. execution was higher by 2.5% in relation to the same period last year. All liabilities of the budget users, legal rights of the citizens and the due liabilities towards domestic and foreign creditors were settled on time and on regular basis during this period.

Within this framework, current expenditures were executed in the amount of Denar 70,007 million. During this period, Denar 10,105 million was paid for wages and allowances to the employees with the budget users, while expenditures related to goods and services were executed in the amount of 5,157 million.

Transfers-related expenditures accounted for the most in the current expenditures, amounting to Denar 52,730 million in this period. Government liabilities on the basis of payments related to exercising the rights to guaranteed social protection of the citizens (pecuniary allowances to vulnerable categories of citizens, as well as child allowance and parenting payments) were settled on regular basis, accounting for Denar 3,938 million. As regards regular payment of pensions, Denar 20,622 million was allocated therefore. With respect to financing health services and benefits, Denar 10,662 million was paid, while Denar 558 million was allocated for payment of unemployment benefits through the Employment Agency. Denar 6,364 million was transferred from the central government budget (Budget of the Republic of North Macedonia) to the municipalities as block grants for financing the transferred competences, as well as earmarked grants for financing the operating costs in local public institutions. In addition, Denar 746 million was transferred on the basis of VAT revenues.

Denar 2,015 million was allocated for regular servicing of liabilities on the basis of interest, according to the repayment schedules on domestic and foreign borrowing. Denar 1,090 million out of this amount was allocated for payment of interest on foreign borrowing. For the purpose of regular servicing of the liabilities on the basis of repayment of principal, funds in the amount of Denar 7,019 million has been spent.

In the period January - April 2021, capital expenditures were executed in the amount of Denar 4,694 million, i.e. execution was higher by Denar 1,596 million or by 51.5% in relation to the same period last year.

During this period, state budget deficit amounted to Denar 6,861 million or 1% compared to the GDP projected in 2021.

During 2021, Ministry of Finance, to the end of increasing the fiscal transparency, created new transparency tool "Fiscal Counter", presenting the collected revenues and executed expenditures, as well as the execution of capital expenditures on a daily basis, with the general government debt presented on monthly basis.

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<sup>2</sup> In line with the 2021 Budget of RNM (Official Gazette number 307/20)

Table 2. 2021 Budget of the Republic of North Macedonia and its Execution in the period January - April 2021

	Budget 2021	Realization January- April 2021	Realization January- April 2020	Realization January- April 2021/Budget 2021 (%)	Realization January-April 2021/Realization January-April 2020 (%)
	in %				
<b>TOTAL REVENUES</b>	<b>212.630</b>	<b>67.840</b>	<b>60.725</b>	<b>31,9%</b>	<b>11,7%</b>
<b>Taxes and Contributions</b>	<b>186.282</b>	<b>62.270</b>	<b>55.061</b>	<b>33,4%</b>	<b>13,1%</b>
Taxes	117.982	39.743	33.756	33,7%	17,7%
Personal Income Tax	20.290	6.156	5.793	30,3%	6,3%
Profit Tax	11.501	4.756	4.383	41,4%	8,5%
VAT (net)	52.280	18.510	14.495	35,4%	27,7%
Excises	25.285	7.190	6.448	28,4%	11,5%
Import Duties	5.968	2.605	2.102	43,6%	23,9%
Other Taxes	2.658	526	535	19,8%	-1,7%
Contributions	68.300	22.527	21.305	33,0%	5,7%
<b>Non Tax Revenues</b>	<b>16.954</b>	<b>4.364</b>	<b>4.290</b>	<b>25,7%</b>	<b>1,7%</b>
<b>Capital Revenues</b>	<b>3.187</b>	<b>287</b>	<b>453</b>	<b>9,0%</b>	<b>-36,6%</b>
<b>Foreign Donations</b>	<b>6.207</b>	<b>919</b>	<b>921</b>	<b>14,8%</b>	<b>-0,2%</b>
<b>TOTAL EXPENDITURES</b>	<b>247.568</b>	<b>74.701</b>	<b>72.863</b>	<b>30,2%</b>	<b>2,5%</b>
<b>Current Expenditures</b>	<b>223.513</b>	<b>70.007</b>	<b>69.765</b>	<b>31,3%</b>	<b>0,3%</b>
Wages and Allowances	31.394	10.105	9.829	32,2%	2,8%
Goods and Services	21.322	5.157	4.558	24,2%	13,1%
Transfers to LGUs	21.315	7.110	7.075	33,4%	0,5%
Subsidies and transfers	17.138	5.835	8.056	34,0%	-27,6%
Social Transfers	122.866	39.785	38.090	32,4%	4,4%
Interest	9.478	2.015	2.157	21,3%	-6,6%
<b>Capital Expenditures</b>	<b>24.055</b>	<b>4.694</b>	<b>3.098</b>	<b>19,5%</b>	<b>51,5%</b>
<b>BUDGET BALANCE</b>	<b>-34.938</b>	<b>-6.861</b>	<b>-12.138</b>	<b>19,6%</b>	<b>-43,5%</b>
<b>BUDGET BALANCE (% of CDP)</b>	<b>-4,9%</b>	<b>-1,0%</b>	<b>-1,8%</b>		
<b>Primary budget balance (% of GDP)</b>	<b>-3,6</b>	<b>-0,7</b>	<b>-1,5</b>		
<b>FINANCING</b>	<b>34.938</b>	<b>6.861</b>	<b>12.138</b>		
<b>Inflow</b>	<b>78.291</b>	<b>13.880</b>	<b>24.427</b>		
Domestic	23.137	8.731	17.850		
Foreign	48.770	45.353	12.139		
Deposits	6.384	-40.204	-5.562		
<b>Outflow</b>	<b>43.353</b>	<b>7.019</b>	<b>12.289</b>		
Domestic	6.119	3.388	1.100		
Foreign	37.234	1.782	11.189		
Other outflows		1.849			

source: Ministry of Finance



### 2.1.2 2022-2026 Medium-Term Framework of the Budget of the Republic of North Macedonia

2022-2026 Fiscal Policy reflects the commitment to further strengthening of public finance management and fiscal sustainability, which is to contribute to maintaining macroeconomic stability and gradual fiscal consolidation (Table 3).

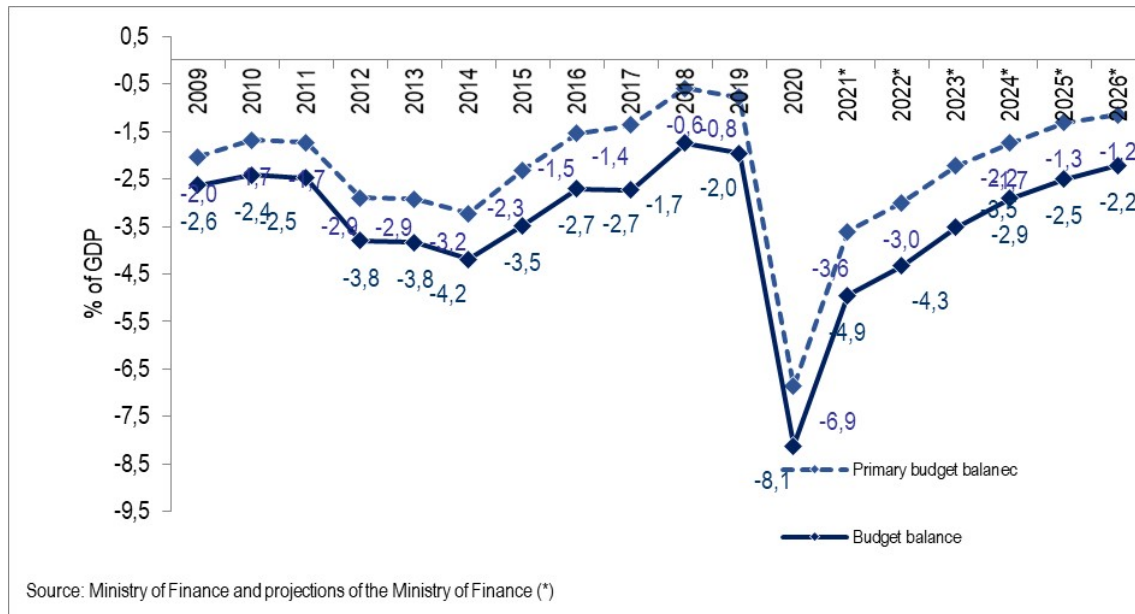
In the coming medium-term period, private consumption of citizens and additional support for the business sector related to innovative and export activities, will be continued, to be also accompanied by boosted both competitiveness and productivity, as well as modernisation and digitalisation of the processes.

Medium-term priorities will be geared towards coping with the consequences from the COVID-19 pandemic, by scaling up investments through direct support of investment activities of companies, promotion and facilitation of the investment climate, job creation through active employment measures, as well as support and development of micro, small- and medium-sized enterprises. This means that such support will be realised by establishing development funds, innovation support funds, guarantee funds, equity funds, venture capital funds and similar instruments for support of export-oriented companies, small- and medium-sized enterprises, as well as social enterprises. Thereby, public-private partnerships, concessions and other instruments for financing public capital projects are also planned to be put into places, to be coupled by financing private sector projects.

Government will remain committed to fiscal sustainability, supporting the economy with investments in infrastructure projects, redesigning the public finance structure by increased share of capital expenditures, as well as strengthening the process of planning, executing and reporting as regards the public finance.

Medium-term Fiscal Strategy sets the total budget expenditure ceilings, as well as the total ceilings by budget users (Attachment 1). Expected revenue collection will provide for gradual narrowing of total budget deficit from 4.9% of GDP in 2021 to 2.2% in 2026. Primary budget deficit will accordingly decline gradually from 3.6% of GDP in 2021 to 1.2% in 2026. (Figure 12).

Figure 12. Overall and Primary Budget Deficit (% of GDP)



Total revenues of the Budget of the Republic of North Macedonia (central government and Funds) for the period 2022-2026 are projected to around 31.3% of GDP. Revenue projections in the coming medium-term period are based on revenues generated in the previous years and the effects from the planned tax reforms.

In fact, upon two public debates held with all stakeholders, the Government adopted the 2021-2025 Tax System Reform Strategy, being harmonised with all remaining strategic documents of the Government and the Ministry of Finance. In line therewith, the working group in charge of the Strategy implementation also adopted the 2021 Action Plan, comprising the main goals, priorities and activities related to tax policy for the next period. Main objective of the tax policy is to ensure sustainable economic growth and development, thereby providing for legal safety of taxpayers and collection of tax revenues on regular basis. Main priorities of the Strategy are the following:

- greater fairness of taxation, in order to ensure that everyone meets its social obligation and pays its fair share of tax,
- increased efficiency and productivity of the tax system for the purpose of improved revenue collection, via more efficient fight against illicit activities and tax evasion, and a strengthened institutional capacity, as well as reduction of the tax arrears,



- increased tax transparency, including an improvement of the exchange of information between tax authorities and other entities, to be, in particular, based on e-services, which will result in enhanced fiscal literacy and increased voluntary compliance,
- improved quality of services rendered by tax system institutions, designed to simplify and speed up the procedures and reduce the administrative burden, by increasing digitalised services, better management of the import-export licenses' issuance, elimination of unnecessary non-tariff barriers and improved internal and tax controls.
- introducing environmental (green) taxation, in order to stimulate taxpayers to contribute, through duties and fees, to pollution reduction, i.e. discourage them to pollute the environment. Effects of this priority are also expected to reflect on the budget revenues, as well as the environment.

Slight easing of tax policy, at the same adjusting certain tax rates, which is expected to cause multiple effect, i.e. - it is envisaged to provide greater tax coverage, fair and streamlined administrative procedures, as well as support to the private sector, which would result in reducing the tax evasion, as well as increasing the tax base.

As regards tax reforms, it is worth mentioning the reform for VAT refund for individuals, which started to apply as of July 2019, expecting to cover increasing number of individuals in future. In fact, individuals, by collecting the fiscal receipts and reporting them to the tax authority, will be entitled to refund of part of the VAT, i.e. 15% of the tax shown on the receipts, i.e. in the course of 2020, change was made at "MyVAT", i.e. 20% instead of 15% refund on Macedonian products and services. This measure ensures additional income to each household, strengthens the purchasing power and has positive effects on increased consumption and VAT collection, as well as reduction of tax evasion and grey economy. This measure is planned to be extended in 2021, whereby the possibility for increasing the highest amount as regards the individuals' right to VAT refund, is being analysed.

In the course of 2021, Ministry of Finance staff has worked on preparing draft legal amendments to the Law on Value Added Tax from the aspect of its harmonisation with the EU VAT Directive, which amendments would pertain to introducing the term tax representative, regulation of the place of the rendered supply of services, analysis for increasing the mandatory VAT registration threshold from Denar 2 million to Denar 3 million, precise regulation of the e-invoice concept, regulation of the self-billing treatment, as well as other modifications and amendments.

At the same time, as regards the Value Added Tax, and for the purpose of reducing the informal economy in the hospitality industry, as well as reducing the prices of restaurant services, new 10% preferential VAT rate was introduced as of 1<sup>st</sup> January 2021.

Excise Law simplifies and improves the manner of reporting excise duty for small producers of alcohol, and strengthens the capacity to administer excise duties on excise goods by introducing the excise movement and control system.

Taxation of motor vehicles will be carried out on the basis of the new Motor Vehicles Tax Law which, in addition to the basic tax parameter, also envisages introduction of an environment pollution indicator, which contributes to improvement of environment quality, which is to increase by 25% in average annually in the next 4 years.

Modifications and amendments to the Personal Income Tax Law, being applied as of 1<sup>st</sup> January 2020, stipulate freezing of the progressive personal income tax rates, as well as refund of the 10% flat tax rate for all types of income, except for the income generated from games of chance, whereby in the meantime, optimal income taxation model will be created through a number of analyses.

Certain analyses for many types of tax base, arising from the different types of income described in the law, are planned to be made in the course of 2021.

As for the tax procedures in 2021, it is planned to adopt new Law on Tax Procedure, as well as modifications and amendments to the Law on PRO, for the purpose of streamlining the tax processes and their digitalisation.

As regards direct taxes, certain changes have been made, aimed at equitable calculation of the tax base at profit tax, thus complying with the international tax practice. In fact, in 2021, amendments to the Profit Tax Law are planned, from the aspect of granting certain tax exemptions to affected workers and simplifying the manner of loss coverage for tax purposes.

In 2021, tariff rates have been, for the first time, to such extent, harmonised with the EU ones - by more than 300 tariff numbers (goods) being generally used as intermediate goods in manufacturing, which would, to a great extent, boost the increase of production, export and employment. Analyses have shown that companies using the mentioned products in their production process would increase export and employment by more than 36%.

Additionally, as of the middle of 2021, the application of the new automated VAT refund system should start with respect to taxpayers registered therefor, thus significantly reducing the average deadline for tax refund and automating the overall process, all to the end of increasing liquidity in the economy.

In line with the strategic goals of the Ministry of Finance, analysis and assessment of all tax expenditures has commenced, arising from the existing tax laws, as well as related laws, granting certain tax exemptions, all to the end of timely recording and assessment of the potential tax revenues. Obligation for assessing the tax expenditures on annual basis would, at the same time, arise from the new Budget Law, pending parliamentary procedure, thus complying with the Directive on Requirements for Budgetary Frameworks of the Member States, being obliged to prepare reports on the tax expenditures and their impact on the revenues.

The process of strengthening the capacities of the Public Revenue Office and the Customs Administration to implement the aforementioned legal provisions is carried out in parallel with the process of the respective legal amendments.

Tax revenues account for 59.9% of the projected revenues, followed by revenues on the basis of social contributions accounting for 30.1%, non-tax revenues and capital revenues accounting for 7.7%, while the rest of the revenues are expected to be generated from IPA Funds and other donations. With respect to tax revenues, most revenues will be generated on the basis of VAT, personal income tax and excises.

Projections for social contributions, which are genuine revenues of the Pension and Disability Insurance Fund, Health Insurance Fund and the Employment Agency, in the next medium-term period, are based on the existing legal regulations on determining the amount of pension and health insurance rates, as well as the expected economic trends, which will appropriately reflect on the growth rates of employment and wages.

Non-tax revenues in the next medium-term period account for around 6.3% of the total revenues, wherein revenues on the basis of administrative fees and other non-tax revenues, which the budget users generate on their own accounts, account for the highest share. With respect to capital expenditures, activities related to sale of agricultural land are planned to be intensified.

In the coming period, budget revenue projections with respect to foreign donations include the donations the budget users will realise for specific projects, as well as disbursements from the EU pre-accession funds.

Table 3. 2022-2026 Budget of the Republic of North Macedonia (Denar million)

	Final account 2020	2021*	2022*	2023*	2024*	2025*	2026*
<b>Total revenues</b>	<b>189.554</b>	<b>212.630</b>	<b>233.217</b>	<b>251.273</b>	<b>273.525</b>	<b>296.815</b>	<b>321.844</b>
<b>Tax revenues and contributions</b>	<b>173.464</b>	<b>186.282</b>	<b>207.047</b>	<b>224.467</b>	<b>246.319</b>	<b>268.909</b>	<b>293.738</b>
Tax revenues	106.900	117.982	133.719	146.748	163.946	181.603	201.202
Contributions	66.564	68.300	73.328	77.719	82.373	87.306	92.536
<b>Non-tax revenues</b>	<b>11.173</b>	<b>16.954</b>	<b>16.516</b>	<b>17.152</b>	<b>17.352</b>	<b>17.552</b>	<b>17.752</b>
<b>Capital revenues</b>	<b>1.846</b>	<b>3.187</b>	<b>3.334</b>	<b>3.334</b>	<b>3.534</b>	<b>4.034</b>	<b>4.034</b>
<b>Donations</b>	<b>3.071</b>	<b>6.207</b>	<b>6.320</b>	<b>6.320</b>	<b>6.320</b>	<b>6.320</b>	<b>6.320</b>
<b>Total expenditures</b>	<b>243.421</b>	<b>247.567</b>	<b>265.876</b>	<b>279.687</b>	<b>298.863</b>	<b>320.406</b>	<b>344.338</b>
<b>Current expenditures</b>	<b>227.306</b>	<b>223.512</b>	<b>233.286</b>	<b>240.975</b>	<b>251.696</b>	<b>269.593</b>	<b>284.459</b>
Salaries and contributions	29.775	31.394	31.862	31.962	32.062	33.562	34.062
Goods and services	15.423	21.322	22.568	24.418	26.418	29.718	32.718
Transfers to LSGUs	21.373	21.315	21.453	22.184	22.953	25.807	28.671
Subsidies and transfers	34.905	19.351	21.234	22.234	25.734	29.590	33.090
Social contributions	117.799	120.653	126.097	129.803	134.420	139.708	145.176
Interest payments	8.031	9.478	10.072	10.374	10.109	11.208	10.742
Domestic	2.742	3.069	3.603	3.904	4.151	4.471	4.782
Foreign	5.289	6.409	6.469	6.470	5.958	6.737	5.960
<b>Capital expenditures</b>	<b>16.115</b>	<b>24.055</b>	<b>32.590</b>	<b>38.712</b>	<b>47.167</b>	<b>50.813</b>	<b>59.879</b>
<b>Budget balance</b>	<b>-53.867</b>	<b>-34.937</b>	<b>-32.659</b>	<b>-28.414</b>	<b>-25.338</b>	<b>-23.591</b>	<b>-22.494</b>
<b>Primary budget balance</b>	<b>-45.836</b>	<b>-25.459</b>	<b>-22.587</b>	<b>-18.040</b>	<b>-15.229</b>	<b>-12.383</b>	<b>-11.752</b>
<b>Total revenues, % of GDP**</b>	<b>28,5</b>	<b>30,1</b>	<b>31,0</b>	<b>31,1</b>	<b>31,4</b>	<b>31,5</b>	<b>31,6</b>
<b>Total expenditures, % of GDP**</b>	<b>36,7</b>	<b>35,0</b>	<b>35,3</b>	<b>34,6</b>	<b>34,3</b>	<b>34,0</b>	<b>33,8</b>
<b>Budget balance, % of GDP**</b>	<b>-8,1</b>	<b>-4,9</b>	<b>-4,3</b>	<b>-3,5</b>	<b>-2,9</b>	<b>-2,5</b>	<b>-2,2</b>
<b>Primary budget balance, % of GDP**</b>	<b>-6,9</b>	<b>-3,6</b>	<b>-3,0</b>	<b>-2,2</b>	<b>-1,7</b>	<b>-1,3</b>	<b>-1,2</b>

Source: Ministry of Finance and projections of the Ministry of Finance (\*)

When creating the medium-term fiscal framework, a high-quality medium-term budget planning is of great significance therefor. To that end, one should take into account that the medium-term fiscal projections in the next period are based upon the medium-term baseline scenario, according to which fiscal projections are set on the basis of the competences of budget users defined in the existing legislation, the existing obligations and duties, being a result of the already approved multi-year commitments, agreements and on-going projects. Additionally, under the new initiatives, generally pertaining to new projects and new financial liabilities, significant change of the time and financial framework of the

projects, as well as changes in the legislation causing fiscal implications upon the budget, under this Fiscal Strategy, substantial funds have been planned for realising capital investments in the field of road infrastructure.

Expenditures side of the Budget of the Republic of North Macedonia, in the next period, is fully created in terms of achieving the strategic priorities, accelerating the economic growth, as well as the priority EU integration process and the obligations deriving from the NATO membership.

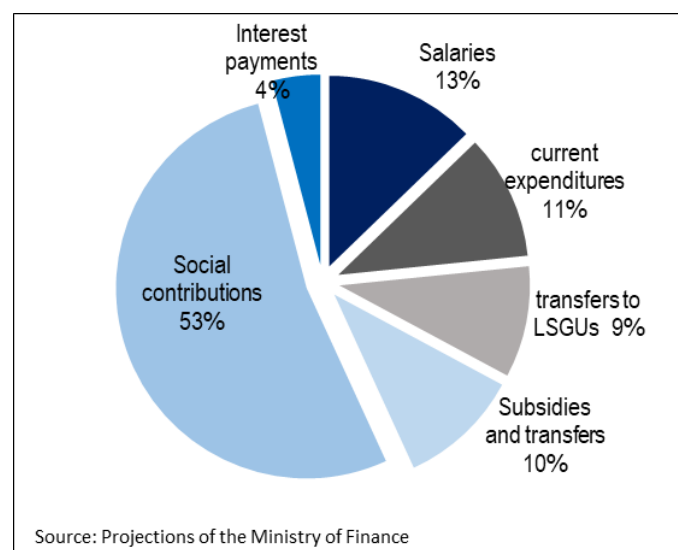
In the period 2022-2026, average share of total expenditures of the Budget of the Republic of North Macedonia accounts for around 34.4% of GDP. Expenditure projections in the state Budget for the next medium-term period are prepared on the basis of three key postulates:

- compliance of the revenue projections with the planned economic activities;
- total budget expenditure projections ensure continuous fiscal consolidation, and
- projected expenditures provide for regular and undisrupted fulfilment of all legal obligations.

When projecting the amount and the structure of the current expenditures for the next period (Figure 13), allocated for regular payment of wages to public sector employees, timely and regular payment of pensions, and other social benefits, payment of agricultural subsidies, support to SMEs, as well as subsidies for innovation activities, following assumptions were taken into account:

- as regards expenditures related to wages and allowances, commitment to continuing the control over new employments for the purpose of optimising the public administration continues, coupled by gradual increase of wages in certain sectors in line with the fiscal possibilities;
- timely payment of pensions by regular indexation of the costs of living, in order to provide for appropriate level of the living standard at the elderly.
- timely payment of social allowances, reformed social protection system (guaranteed minimum income), to the end of ensuring safe well-being of the beneficiaries of these rights
- health protection realised through Health Insurance Fund, mostly refers to the financing of health services for the population.
- implementing the active employment policies and measures, which will be aimed at creating employment programs, measures and services to be carried out for the purpose of improving the functioning of the labour market, supporting job creation, as well as employing young persons - youth guarantee.
- optimal support by providing funds for more efficient use of agricultural subsidies for the purpose of creating sustainable and competitive agricultural production, as well as encouraging employment through agricultural businesses,
- boosting economic growth and development in the Republic of North Macedonia by improving the business environment and creating climate for dynamic and competitive business, support for sustainable and competitive micro, small- and medium-sized enterprises, promotion of entrepreneurship and innovation.

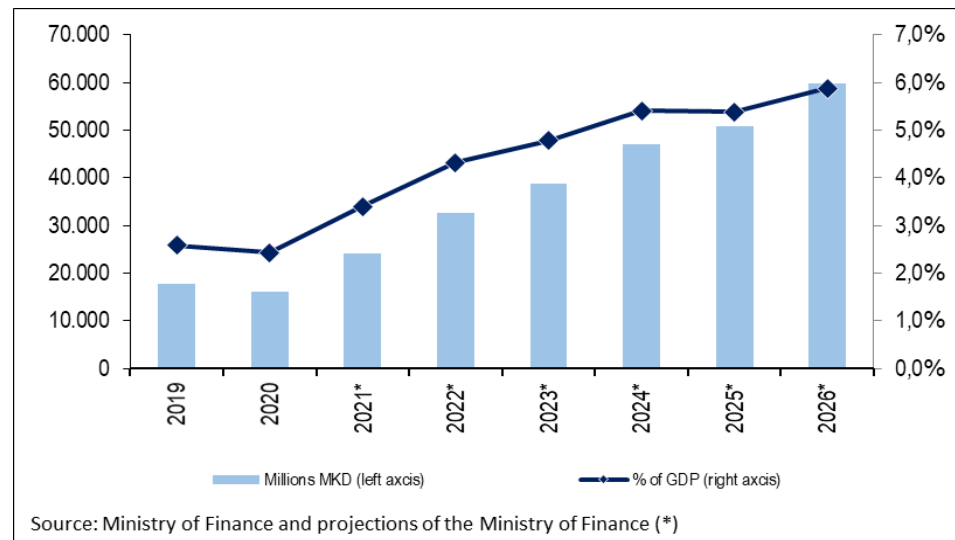
Figure 13. Average structure of current expenditures 2020 - 2022 (%)



In the medium-term period, fiscal policy remains to focus on ensuring substantial public investments, being a precondition for improvement of economic perspectives, as well as better life of the citizens. Related to this, a significant amount of capital investments is projected (Figure 14) by using budget funds, including funds under loans extended from international financial institutions and bilateral creditors. The projected amounts speak of intensification of infrastructure

projects, i.e. investments in road and railway infrastructure, energy and utilities infrastructure, as well as capital investments aimed at improving the conditions in the health, education and social systems, agriculture, culture, sports, environment protection and judiciary.

Figure 14. Capital Expenditures in the Budget of the Republic of North Macedonia



Substantial investments have been planned in the field of road infrastructure, related to the design process, construction and use of Corridor VIII.; Tetovo - Gostivar section/highway extension, construction of new Highway Trebenishta- Struga- Kjafasan, construction of Gostivar-Bukojcani and Bukojcani-Kicevo sections, as well as Corridor Xd, Prilep-Bitola section.

In addition to the Budget, substantial investments in road infrastructure are ongoing through the Public Enterprise for State Roads, such as: "Road Upgrading and Development Project (Kriva Palanka - Rankovce)", financed with a loan from the World Bank. At the same time, construction of Kicevo-Ohrid Highway, financed with loans from Export - Import Bank of China is ongoing. Activities envisaged under the National Roads Programme, funded with EBRD loan, will be intensified in the coming period, envisaging construction of road sections Stip - Kocani and Raec – Drenovo, as well as reconstruction and rehabilitation of 26 road sections in the Republic of North Macedonia, total length of which is around 400 km."Stip – Radovis Road Section Project", also funded with an EBRD loan, is in the process of realisation. In the coming medium-term period, construction of Skopje-Blace highway section is expected to start, which will provide for positive effects on the economic, social and environmental aspects in the region, as well as easier international transportation and trade in the region, particularly between the Republic of North Macedonia and the Republic of Kosovo. As regards rehabilitation and reconstruction of local roads in the country, the implementation of "Local Roads Connectivity Project", financed with a World Bank loan, will continue. At the same time, in 2021, construction of Kriva Palanka - Deve Bair road section (border with Bulgaria) will continue, as well as the second phase of the "Project for Construction and Installation of Electronic Tolling System, along Corridor VIII and Miladinovci - Shtip Motorway".

As for the railway infrastructure, focus will be placed on completion of the implementation of the "Project for Improvement of the Railway Corridor X", as well as intensification of the activities within the Project for Completion of Rail Corridor VIII (section Kicevo-Lin-Border with Republic of Albania), being aimed at connecting the Black Sea with the Adriatic Sea, which speaks about the huge strategic and economic significance of this Project.

Construction of the eastern part of Rail Corridor VIII, i.e. the part towards the Republic of Bulgaria, is carried out in 3 phases. Realisation of the first phase (Kumanovo - Beljakovce section), 30.8 km long, and second phase (Beljakovce - Kriva Palanka section), 34 km long, financed with EBRD loans and WBIF grant funds, will be intensified within the envisaged period. In addition to the WBIF grant funds for technical assistance to the Project, WBIF investment grant in the amount of EUR 68.6 million for financing the second phase has been secured. Preparation of the third phase (Kriva Palanka – Deve Bair section, border towards the Republic of Bulgaria), covering 23.4 km, financed with IPA grants, is completed, and its construction will be financed with loans from the European Investment Bank - EIB and EBRD and grant funds within the national IPA and WBIF.

As regards the transport infrastructure, significant project activities will be financed with a loan under the World Bank regional initiative "Western Balkans Trade and Transport Facilitation Project", aimed at promoting deeper economic integration within the region, reducing the trade costs and enhancing the transport efficiency in the Republic of North Macedonia. In addition, implementation of the Skopje Bus Rapid Transit Project will commence, to be finance with EBRD loan.

By implementing the "Project for Construction of Gas Pipeline System in the Republic of North Macedonia", business sector, public sector and households will be provided supply with cheap and environmentally friendly energy, at the same time reducing the emission of harmful gases. In the envisaged period, realisation of the new "Project on Interconnection Gas Pipeline between the Republic of North Macedonia and the Republic of Greece", is expected to start, which will be financed with EIB loan. At the same time, as regards this filed, implementation of the Project for Construction of National Gas Pipeline Gostivar - Kicevo Section and Sveti Nikole- Veles Section is planned to commence.

Implementation of the "Municipal Services Improvement Project", funded by the World Bank, will continue in the coming period. World Bank loan proceeds are intended for financing infrastructure investment projects in the field of water supply and wastewater drainage, management of solid waste and other investments in municipal services, which have potential for generating revenues, i.e. making savings, or are of high priority for the municipalities.

In addition, Implementation of "North Macedonia Public Sector Energy Efficiency Project", to be financed with a World Bank loan, commenced in 2021. Project will cover making investments in the field of energy efficiency by the municipalities in the Republic of North Macedonia, the City of Skopje and the municipalities in the City of Skopje, as well as the public health institutions, Ministry of Economy, Ministry of Finance and the Development Bank of North Macedonia.

In order to improve the conditions and the quality of life, above all in the rural areas in the country, by supplying clean potable water, "Water Supply and Waste Water Collection Project", financed with EIB (European Investment Bank) loan, will continue to be implemented in the coming period. The Government disburses these funds in the form of grants, which significantly contributes to improving the living conditions of the citizens.

In the period to come, construction of the Regional Clinical Hospital in Shtip will continue, being funded with a loan from the Council of Europe Development Bank - CEB. In the field of education, in the upcoming period, implementation of the "Project for Building Physical Education Facilities in Primary Schools and Rehabilitation of Primary and Secondary Schools", financed with CEB loan and contribution of the Republic of North Macedonia, is expected to continue, aimed at improving the physical education conditions, as well as the overall learning conditions in the primary and the secondary schools.

In the field of education, Project for Reconstruction of Student Dormitories is also being implemented, to be funded with KfW loan, being aimed at implementing the goals and policies geared towards increased energy efficiency, as well as providing basic accommodation conditions in the student dormitories in the Republic of North Macedonia. At the same time, another significant project in this field the Government focuses on is the Primary Education Improvement Project, funded with World Bank loan, geared towards improving the quality of education by making new infrastructure investments in primary schools, carrying out reform for improving and assessing the national learning progress, as well as strengthening the competences of teaching personnel, expert associates and directors of schools. Implementation of the second and the third phases of "Zletovica Water Basin Utilisation Improvement Project" is planned to commence with a support by EIB. Main objective of the second phase is provision of irrigation for 4,570 ha net area in the region of Probistip and Kratovo municipalities. Implementation of the third phase, which includes construction of small hydro power plants along the flow of Zletovica River, will provide for reducing electricity shortage in the region, safe, secure and quality supply of energy for the consumers and increased energy efficiency.

Second phase of the "Irrigation Programme Southern Vardar Valley", which will continue in 2021 as well, will be financed with KfW loan. EUR 4 million has been provided for this Project as a grant from the German Federal Republic through KfW, aimed at supporting the envisaged investment activities, i.e. rehabilitation and modernisation of the irrigation systems in Valandovo region. At the same time, Irrigation Programme North Macedonia will be launched, covering rehabilitation and expansion of 4 irrigation systems along Vardar River Valley (Straishte, Lisiche, Konjsko and Pepelishte), as well as construction of small hydro power plants of the Hydro System Lisiche.

First phase of the "Water and Sewerage Programme Macedonia", financed with KfW loan and SECO grant funds, is expected to be completed in the coming period, providing for sustainable supply of potable water to the population in the municipalities of Gostivar, Kavadarci and Radovich. At the same time, it is expected for the second phase of this Project to commence. This phase will be financed with grant funds in the amount of EUR 5 million, awarded by the German Federal Republic through KfW, for investment activities in the municipalities of Gevgelija and Kavadarci.

"Agriculture Modernisation Project" will be prepared and implemented with the support of the World Bank, which will include establishment of agriculture purchasing and distribution centers, as well as construction of system for disposal of animal by-products.

An important priority which the Government of the Republic of North Macedonia will focus on is the preparation and the implementation of the "Project for Construction of Waste Water Treatment Plant in the City of Skopje", financed with loans from EIB and EBRD, as well as an investment grant within the ERI instrument.

First segment of Prisons Reconstruction Project, i.e. Kumanovo Prison, Tetovo Juvenile Educational Correctional Facility, as well as the first phase of Idrizovo Prison, have been completed. Preparation of project documentation for the second segment of the Project, i.e. phases 2 and 3 of Idrizovo Prison, is ongoing. The Project is financed with a loan from CEB and it contributes a lot to establishing professionally and efficiently organised and managed houses of correction, which continuously ensure re-socialisation and integration of the citizens in the society.

As regards social sector, in 2021, implementation of the Social Services Improvement Project will continue, being financed with World Bank loan, the main goal of which is increasing the access and improving the quality of social services, also including the pre-school services for vulnerable groups, via policy development, setting up a comprehensive system of social services and systematic implementation of the reformed services through an extended network of social service

providers, introducing an integrated information system for administering rights and services, expanding the pre-school care capacities by building new facilities and transformation (or superstructure) of the existing infrastructure of pre-school institutions. At the same time, another significant project in this field is the Social Insurance Administration Project, being aimed at improving the service quality when administering the social insurance and improving the legal framework, regulating issues pertaining to disabled people, as well as the jobs with reduced service years for retirement. This Project is funded with a loan from the World Bank.

For the purpose of overcoming the COVID-19-induced difficulties, all to the end of preventing, detecting and coping with the COVID-19-related threat, as well as strengthening the national public health systems in North Macedonia in terms of their readiness, the Government will continue the implementation of the Emergency COVID-19 Response Project, funded with World Bank loan.

In order to provide fresh capital for small- and medium-sized enterprises, as well as their support to the end of managing COVID-19 pandemic, via support for new projects, job creation, increased liquidity of the economy and higher exports, the sixth EIB credit line for financing small- and medium-sized enterprises, in the amount of EUR 100 million, will be implemented in 2021.

### 2.1.3 Central Government Budget Deficit and Its Financing

During the 2022-2026 period, budget deficit is as follows: Denar 32.7 billion in 2022, Denar 22.5 billion in 2026. This means that gradual fiscal consolidation is projected in this medium-term period, i.e. share of budget deficit in GDP will decrease from 4.3% in 2022 to 2.2% in 2026.

Financing the planned deficit, as well as debt repayment will be ensured via borrowing from foreign and domestic sources (Table 4). In March 2021, the Government issued the Eurobond, amounting to EUR 700 million. Eurobond maturity period is 7 years, while coupon interest rate, upon which it has been issued, accounts for 1.625%, being the lowest interest on the so-far issued Eurobonds. Second tranche under the EU loan for macro-financial assistance, amounting to EUR 80 million, is expected to be disbursed during the second quarter of 2021, whereby the additional Budget financing will be realised via disbursements of loans by international financial institutions, as well as by borrowing on the domestic government securities market. Under such financial structure, the Government can uninterruptedly finance the budget deficit and repay the liabilities on the basis of debt falling due in the course of the year. In the period 2022-2024, foreign borrowing may be realised through issuance of Eurobond on the international capital market and by disbursement of funds under favourable loans from foreign financial institutions and credit lines intended for financing certain projects. Thereby, the choice of a specific external financing source will be based on the ongoing and the expected developments on the international capital market. Furthermore, borrowing on the domestic market will be realised on the basis of issuance of government securities, thus providing for additional financing under favourable terms and conditions, by using the low interest rates and the interest of the investors. For the purpose of optimising the payments and reducing the refinancing risk, Ministry of Finance will continue issuing government securities with longer maturities, thus reducing the debt refinancing risk. To the end of efficiently managing the public debt, Ministry of Finance will also take into account the possibility for early repayment of part of the debt, i.e. determining more favourable debt maturity, currency and interest structure.

Table 4. Deficit and Sources for Its Financing (Denar million)

	Realization 2020	2021*	2022*	2023*	2024*	2025*	2026*
<b>Budget balance</b>	<b>-53.867</b>	<b>-34.937</b>	<b>-32.659</b>	<b>-28.414</b>	<b>-25.338</b>	<b>-23.591</b>	<b>-22.494</b>
<b>Financing of the deficit</b>	<b>53.867</b>	<b>34.937</b>	<b>32.659</b>	<b>28.414</b>	<b>25.338</b>	<b>23.591</b>	<b>22.494</b>
<b>Inflows</b>	<b>95.695</b>	<b>78.290</b>	<b>44.141</b>	<b>77.792</b>	<b>56.153</b>	<b>80.183</b>	<b>105.065</b>
Domestic sources	36.347	23.437	23.903	31.666	40.499	31.402	45.809
Foreign sources	66.207	53.542	18.690	45.091	12.000	49.900	58.050
Deposits ("-" is account accumulation)	-6.859	1.311	1.548	1.035	3.654	-1.119	1.206
<b>Outflows</b>	<b>41.828</b>	<b>43.353</b>	<b>11.482</b>	<b>49.378</b>	<b>30.815</b>	<b>56.592</b>	<b>82.571</b>
Domestic debt repayment	15.261	6.119	5.379	13.103	18.821	9.674	24.526
Foreign debt repayment	26.567	37.234	6.103	36.275	11.994	46.918	58.045
Memorandum:							
Net domestic borrowing	21.086	17.318	18.524	18.563	21.678	21.728	21.283
Net foreign borrowing	39.640	16.308	12.587	8.816	6	2.982	5

Source: Ministry of Finance and projections of the Ministry of Finance (\*)

#### **2.1.4. Economic Measures for Managing COVID-19 Induced Consequences**

Government of the Republic of North Macedonia adopted several sets of economic measures, geared towards coping with the adverse consequences on the economy caused by the health pandemic. Under the first four sets, around 70 various measures were adopted, covering and supporting the entities and the natural persons affected by the pandemic. Fifth set of economic measures comprises total of 29 measures, geared towards the citizens, the companies, well as boosting the liquidity of the economy. Sixth set of measures covers 7 measures, targeting the sectors, being most severely hit by COVID-19-induced crisis.

All sets of anti-crisis measures, aimed at supporting the economy, focus on the citizens, their jobs, social safety, solidarity, creating an environment to easily overcome the economic consequences from the Coronavirus and implementing a rapid exit strategy so as to continue the positive trends of the new Macedonian development economy.

Total amount of the adopted economic measures is estimated at EUR 1.2 billion, i.e. around 10% of GDP, out of which, the first four sets of anti-crisis measures amount to approximately EUR 1.02 billion, i.e. the fourth set of economic measures amount to EUR 470 million, while the total amount of the previous three sets of measures amount to around EUR 555 million. Fifth set of economic measures amount to around EUR 160 million, while the sixth set amounts to EUR 17.8 million, being currently realised. These financial resources are geared towards the citizens and the business sector for the purpose of ensuring stable sustainable economy with a potential for its revitalisation.

All adopted measures may be divided in one of the following 3 groups:

1. Measures causing budget expenditures, i.e. direct fiscal implications,
2. Measures causing reduced budget revenues, and
3. Measures having economic impact, but no fiscal implications

##### **First set**

First set of measures was a prompt response by the Government to the newly occurred situation, aimed at cushioning the blow of the health crisis over the economy. The set comprised urgent measures aimed at protecting liquidity and jobs, targeting citizens and companies the most affected by the health crisis. Total of EUR 12.2 million has been allocated therefor. All spent funds were geared towards the enterprises, also including certain measures intended for the citizens in need therefor.

First set was focused on faster response to the crisis and the adopted measures were mostly from the group of measures causing reduced budget revenues, as well as the group of measures having economic impact, but no fiscal implications. Foregone revenues for the measures under this group are estimated at EUR 5.5 million.

First set of measures included profit tax and personal income tax exemptions for the months from March to July 2020 for entities generating 30% less revenues compared to the previous period, with estimated reduced revenues amounting to EUR 2.1 million, as well as subsidising 50% of the contributions for the months of April, May and June 2020 per employee in the companies operating in the affected sectors, with estimated reduced revenues amounting to EUR 2.5 million. In additions customs duties upon certain grounds have been abolished, and the statutory default interest and the default interest on public duties have been reduced.

As for measures with no fiscal implications, Interest-free credits in the amount of EUR 5.5 million were implemented through the Development Bank, aimed at protecting both the liquidity of micro, small- and medium-sized companies, the economic activity of which is the most affected by the pandemic, as well as the jobs at companies facing difficulties paying the wages, thus providing support to 737 enterprises with 6,509 employees. In addition to the interest-free credits, the first set of measures provided for reducing the policy rate of the National Bank to 1.75%, thus also simplifying the manner of issuance, transmission and receipt of e-invoices.

Under the first set of measures, no funds were spent for measures causing budget expenditures, i.e. direct fiscal implications.

##### **Second set**

The second set of economic measures, comprises precise measures, having direct impact over the real economy, and providing for direct support to every household and individual, separately. The purpose is to provide support to the business sector, keep the jobs, maintain social stability and help the citizens affected by this crisis. Under this set of measures, EUR 332.9 million has been allocated.

Most of the support pertained to measures causing no fiscal implications, primarily the introduced possibility for postponing and restructuring the loan repayments for companies and citizens for a period of 3 to 6 months. In addition, EUR 8 million has been provided for new interest-free credit line from the Development Bank, supporting 639 enterprises with 11,325 people employed therein.

As for measures causing direct budget expenditures, EUR 85.9 million has been allocated. The most important measure under this group was the support for employers aimed at job protection in the amount of Denar 14,500 (minimum



wage level) per employee for payment of wages for the months of April, May and June 2020 for companies and persons performing independent activity generating at least 30% less revenues. EUR 84 million has been allocated for this measures, covering around 120,000 employed persons.

Other such measures were the following:

- unemployment benefit for citizens who lost their job in the amount of 50% of the employee's average wage, with fiscal implications of around EUR 900 thousand;
- relaxing the criteria to the end of expanding the coverage of social assistance beneficiaries with fiscal implications of around EUR 450 thousand
- support for athletes and artists in the amount of Denar 14,500 for the months of April and May 2020, with fiscal implications of around EUR 508 thousand.

The second set of measures cause no reduced budget revenues.

### Third set

The third set of economic measures was aimed at recovery of domestic economy through direct support to the citizens and the business sector. It includes short-term and medium-term measures aimed at revitalising the Macedonian economy.

Third set of measures is aimed at the following:

- stimulating private consumption of citizens, thus creating better living conditions;
- protecting the existing and creating new jobs;
- boosted competitiveness of companies at national, regional and global level;
- urgent encouragement of domestic tourism;
- promoting new agricultural crops and supporting farmers for even greater scope and quality of domestic production;
- developing the economic activities by introducing IT and online activities and tools;
- stimulating and increasing cashless and online payments as an instrument for reducing the grey economy, etc.

As for the third set of measures, total of EUR 229.3 million has been allocated, whereby EUR 122.4 million has been intended for individuals, while EUR 106.9 million has been geared towards legal entities.

With respect to measures causing direct budget expenditures, EUR 143.3 million has been projected. Several measures with significant amount of budget expenditures have been included in this set, above all payment cards amounting to Denar 9,000 for all unemployed persons and payment cards amounting to Denar 3,000 for young people and employed persons with net wage lower than Denar 15,000 per month. EUR 28 million has been spent for this measure alone, whereby payment cards have been allocated to approximately 309,337 citizens.

Other measures under this group are:

- support to the private sector for new markets, competitiveness and modernisation, whereby EUR 20 million has been spent and 400 companies have been supported thereby;
- voucher for domestic tourism of Denar 6,000 for employees receiving a net wage of less than Denar 15,000 monthly, whereby EUR 16 million has been spent therefor;
- payment card for subsidising 50% of the green oil for farmers, with EUR 4.6 million being spent therefor;
- reward for doctors and medical personnel at infectious diseases clinics and units with EUR 890 thousand being spent for 4,260 doctors and medical personnel;
- unemployment benefit for people having lost their job due to COVID-19, with EUR 2.5 million being spent for 3,123 persons;
- financial support for young people up to Denar 3,000 in the form of vouchers for co-financing IT and digital skills trainings with EUR 12 million being spent therefor;
- co-financing the costs for craftsmen for procurement of tools and intermediate goods, whereby EUR 145 thousand has been spent for 225 craftsmen;
- support for development of domestic start-up products and services through the Fund for Innovation and Technological Development, with EUR 1.6 million being sent for 88 projects;
- co-financing of events and conferences with the state covering 50% of the costs up to Denar 30,000 at the most, with EUR 250 thousand spent for that purpose;

As for measures with no fiscal implications, EUR 86 million has been spent under this set. This set provided for extending favourable loans with 1.6% interest rate for companies through the Development Bank within EIB credit line, in the amount of EUR 50.9 million for 186 companies. Moreover, the Development Bank provided for extending interest-free loans for companies in the total amount of around EUR 28 million, by which 2,459 companies with 17,747 employees have been supported. Support to agriculture sector was provided through the Development Bank, amounting to EUR 5 million. The third set of measures cause no reduced budget revenues.



#### Fourth set

Fourth set of measures was designed as a direct assistance for economic and social safety of citizens, as well as for the purpose of encouraging private consumption as a driving force of social growth. Under this set of measures, EUR 472.1 million has been allocated, whereby EUR 293.4 million has been allocated for direct budget expenditures. As for the wage financial support for the months of October, November and December 2020, EUR 70 million has been spent, with 13,042 companies deploying this support. As regards the financial support for vulnerable categories by paying financial resources on transaction account for the purpose of increasing the consumption and developing the domestic economic activities, EUR 27.6 million has been spent for 254,646 beneficiaries. World Bank loan was used as support to the health and social sectors, amounting to EUR 68.4 million.

Other measures causing direct budget expenditures are the following:

- Support to purchase of grape from 2020 harvest, with EUR 7.7 million being spent therefor;
- Grants for 5000 travel agencies, for which EUR 2 million has been spent;
- Grants for restaurants for weddings in the amount from EUR 3 to EUR 10 thousand, with EUR 1 million being spent therefor.
- Grants for kids' play areas, with EUR 2.5 million being deployed therefor;
- Tourist tax refund for 2019 for 4,740 entities with EUR 2 million being spent therefore.
- Wage support for tourist guides for the months of October, November and December 2020, for which EUR 1.6 million has been spent.

Measures causing reduced budget revenues are estimated at around EUR 28 million.

More important measures under this group:

- deferral of profit tax and personal income advance payment by March 2021 for companies and persons performing independent activity experiencing more than 40% decline in their income;
- reduction of VAT rate on restaurant services and serving food and beverages by 10%;
- reduction of import duties on raw materials and intermediate goods;
- VAT-free weekend;
- reduction of daily default interest for public duties;
- extension of renewal of the work licenses for discotheques, night clubs, as well as the companies in the field of transport;
- reduction of VAT rate on craftsman services and products from 18% to 5%;
- recognising private health insurance costs and the costs for COVID-19 testing as an eligible cost and similar.

Out of the measures with no fiscal implications, favourable loans have been allocated by the Development Bank, amounting to EUR 100 million. In addition, grace period for interest-free COVID-19 credit line was extended, also providing for additional extension of the loan repayment by the end of 2020. Deferred payment of VAT within five days upon submitting the VAT return, was allowed.

#### Fifth set of measures

Fifth set of measures is aimed at extending the measures under the previous four sets of measures so as to recover/restart the economy, as well as return the economic growth rates to the pre-crisis level. Fifth set of measures is aimed at providing direct support to the economy and companies, and thus supporting the citizens by having their living standard and working conditions improved.

Fifth set of economic measures comprises total of 29 measures, amounting to around EUR 160 million, out of which around EUR 92 million as direct fiscal implications.

Measures under the fifth set of economic measures are systemised in 4 main pillars:

- Direct financial support for companies aimed at keeping the jobs of citizens, working in sectors that are still affected by the pandemic
- Financial support of the liquidity of citizens and the private sector aimed at keeping and/or increasing the number of workers, as well as recovering the companies
- Creating favourable business environment via systemic redefining of the customs tariff, reduction of other parasfiscal duties and tax relief and postponement of payment of certain public duties
- Support for citizens

More important measures under this group, with higher amount of allocated funds, are the following:

- Wage financial support for employees, scalable support from Denar 14,500 to Denar 21,776 in the months of February and March 2021;

- Loans with 0% interest, made available through the Development Bank geared towards the most severely hit sectors in the field of tourism, craftsmanship, hospitality industry, transport, event planning industry, private health institutions, etc.;
- Credit guarantee scheme through the Development Bank in the period April-October 2021;
- Establishment of Fund for Export Companies Support through the Development Bank;
- Abolishment of customs duties on 71 products and raw materials by end-2021;
- Abolishment and reduction of customs duties on 31 raw materials and meat for export-oriented companies by the end of 2021;
- Support for export-oriented companies by revising the Customs Tariff and harmonising with the rules of the EU market and the markets of the WTO Member States.
- Simplified requirements for 245 companies under active contracts and new potential investors, which will make investments in line with the Law on Financial Support of Investments;
- Co-financed assistance for micro, small- and medium-sized enterprises geared towards technologic development;
- Forgiving the interest on the basis of individuals' debt towards public institutions and enterprises;

### **Sixth set of measures**

Sixth set of measures covers 7 measures, targeting the sectors most severely hit by COVID-19 crisis, amounting to EUR 17.8 million, whereby 10,000 companies will be supported, employing around 60,000 citizens. Sixth set of measures is aimed at supporting the activities being in full-lock down for the purpose of preventing the Coronavirus spread in the course of April 2021, as well as boosting the liquidity of companies making investments throughout 2021. Around EUR 14.8 million of the projected funds have been intended exclusively for the companies operating in the field of hospitality industry and tourism.

Sixth set of measures also targets the following entities:

- Hospitality facilities will be provided with a support of approximately EUR 9.9 million, covering around 6,000 entities employing 17,000 people. This measure will provide for covering 30% of the revenues, an amount to be calculated as an average from the average monthly income generated in 2019 and 2020. In addition, all registered hospitality facilities will be provided with a financial support in the amount of Denar 15,200 per employee, as of 6<sup>th</sup> April 2021 inclusive.
- Categorised restaurants for weddings, event planning industry, kids' play areas, night clubs, private child resorts, fitness centers, photographers and photo studios will receive a support worth EUR 2.5 million. These categories comprise around 1,200 companies, which will provide for covering 30% of the revenues, an amount to be calculated as an average from the average monthly income generated in 2019, also providing a financial support in the amount of Denar 15,200 per employee, as of 31<sup>st</sup> December 2020 inclusive.
- Categorised travel agencies will be supported with EUR 1.4 million. Thereby, travel agencies with "A" license will be extended up to EUR 5,000 each, while travel agencies with B license will be extended up to EUR 2,000 each.
- Musicians, members of the associations of musicians, as well as licensed tourist guides, generating average monthly net income of below Denar 15,000 in the course of 2020, will be provided with a financial support of Denar 30,750.
- Around EUR 2 million will be intended for companies, having reinvested their profit in 2020, a measure to be realised via the Development Bank, which will help companies boost their liquidity, realise their investment plans and continue with their development, by subsidising the interest rates.
- Media broadcasting radio and TV programmes will be supported with interest-free credit line through the Development Bank, amounting to EUR 1 million.
- Foreign tourists, visiting the country, will get 50,000 free PCR tests as additional support and assistance for the domestic tourist and hospitality industry sectors.

### **2.2 Local Government Budget**

Decentralisation of the competences to local government and strengthening its capacity is one of the priorities arising from the Accession Partnership of the Republic of North Macedonia with the EU and the Framework Agreement. Since 2012, all municipalities (except for Plasnica) finance the transferred competence with block grants, when the phased approach for transferring and managing the operating and financial resources for the transferred powers in the field of education, culture, child care and social protection ended.

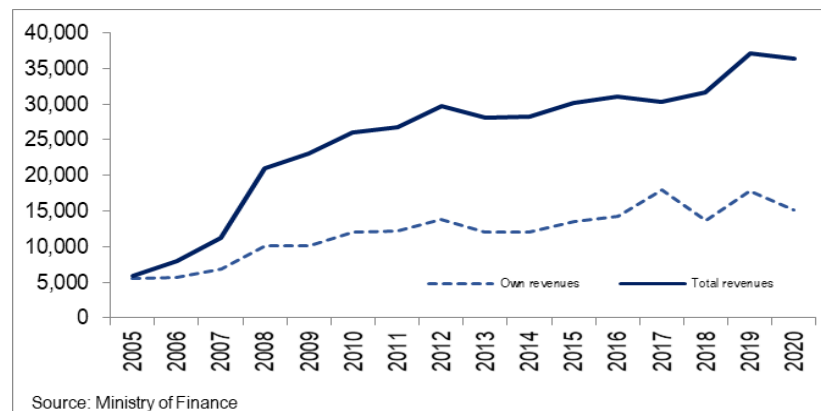
Powers in several sectors assumed by the municipalities increased both the administrative and the fiscal capacities and strengthened the capacities for managing larger amount of funds. Successful administration and collection of own revenues contribute to resuming the process of increased own revenues of municipalities and the strengthened capacities for

fund management, performance of the transferred competences and management of financial and other resources necessary for their realisation. In addition, municipalities successfully administer new powers related to managing construction land, dealing with illegally built facilities with respective revenue collection. Successful implementation of fiscal decentralisation, with fully established legal and institutional framework for local government, provides for developed, responsible and functional local government units and level of local democracy, bringing the citizens closer to the local government institutions. Progress in achieving the decentralisation-related goals is assessed as successful by many international institutions, which assisted with several projects towards improvements in the system for management, control, transparency and coordination in managing local government reforms.

At the same time, access to the capital market has been easier, under more liberal and transparent requirements for borrowing, by which, interest of the municipalities for financing investment projects on the basis of borrowing increased. To that end, the Government has provided credit lines from international financial institutions (World Bank, EIB, KfW and EBRD), which have provided for substantial investments, especially in: reconstruction and rehabilitation of local streets, roads and bridges, construction and reconstruction of water supply and atmospheric water networks, improvement of public hygiene and increasing energy efficiency in municipal public facilities and local spatial landscaping.

As regards the level of decentralisation, Republic of North Macedonia, according to the data on 2020 expenditure execution (around 5.3% of GDP), belongs to the group of medium decentralised countries. Furthermore, when compared to 2005, when the process of transferring the powers and fiscal decentralisation commenced, today, municipal revenues have increased by more than six times (Denar 5.9 billion in 2005, more than Denar 36 billion in 2020). Tax revenues, which the municipalities are authorised to collect, have increased by more than twice during the same period (Figure 15).

Figure 15. Own and Total Revenues in the period 2005 - 2020 (Denar million)



Municipalities in the Republic of North Macedonia are financed from own sources of revenues, grants from the Budget of the Republic of North Macedonia for the competences transferred in the field of education, culture, social protection and fire fighting, revenues determined in separate laws, tax revenues collected at central level, transfers from the Budget of the Republic of North Macedonia and other institutions, revenues collected on the basis of grants, loans and other revenues.

Own revenues of the municipalities are local taxes (property tax, inheritance and gift tax, tax on sales of real estate), local fees prescribed by law (utility fees, administrative fees and other fees stipulated by law), local fees (fee for landscaping of construction land, fees for utility activities, fees for spatial and urban plans), revenues on the basis of ownership and other revenues stipulated by law. Municipalities also receive transferred revenues in the amount of 3% of the collected PIT on the basis of personal earnings from wages of individuals with a permanent address in the respective municipality and 100% of the PIT collected from individuals engaged in craftsmanship activity, registered in the area of the municipality.

Additional revenues are also transferred as grants from the Budget of the Republic of North Macedonia as follows: revenues on the basis of VAT grants (4.5% of collected VAT in the previous fiscal year), capital transfers, earmarked and block grants for the transferred powers in the field of education, culture, social protection and fire fighting. Funds from these grants are distributed on the basis of criteria determined in decrees adopted by the Government of the Republic of North Macedonia.

Unreal projecting of the budgets of the local government units, i.e. the too optimistic projecting of revenues is one of the reasons due to which the local government units accrued outstanding liabilities in the previous years. In order to overcome this situation, under the amendments to the Law in Financing the Local Government Units as of November 2018, fiscal rule has been set out for planning the own revenues of the core budget of local government units, i.e. the planning of own revenues of the core municipal budget is limited with the performance of the collected revenues. According to the amendments to the Law, the own revenues of the municipal core budget in future will be projected with an increase of 10% of averagely collected revenues at the most in the last three years, according to the data from the Treasury records. At the same time, exceptions have been envisaged only if the municipality has provided document for transfer of funds from the respective institution. During 2019, another amendment to the Law on Financing the Local Government Units was adopted,

according to which, upon request by the municipalities, and to the end of greater flexibility when planning the municipal budgets, and thus improving the fiscal position of municipalities, the previous forecast of 10% of revenue growth has been revised to 30%. Under the latest amendment to the Law, the 2021 forecast of revenue growth has been revised to 50%

In the course of 2020, the trend of increasing earmarked and block grants for the transferred powers in the field of education, culture, social protection and fire fighting, was kept.

For the purpose of allocating stable revenues and facilitating the municipal operations in times of COVID-19 crisis in 2021, the Government of the Republic of North Macedonia adopted the measure - Changing the calculation for the base for financing local government units, under which, when allocating funds to the local government units, the calculation of the average VAT collection in the previous three years will be taken into account, instead of the previous year alone as so far. To that end, the Law on Amending the Law on Financing Local Government Units stipulated for the VAT revenues in 2021 to account for 4.5% of the average collected VAT tax in the last three fiscal years.

For the purpose of strengthening the fiscal decentralisation, in the 2021-2024 period, many activities and measures have been envisaged, being grouped in three pillars, as follows: I. Improved fiscal capacity and increased municipal revenues, II. Strengthened fiscal discipline and III. Increased transparency and accountability as regards municipalities' operations. Ultimate goal of this process is achieving better quality of public services, higher economic growth and better living standard.

The first pillar under this reform, or improved fiscal capacity and increased municipal revenues, will be implemented through activities, which envisage increase of the funds distributed to the municipalities on the basis of collected fees in the central Budget, increased own revenues of the municipalities and establishment of funds to support the good performance. To that end, revising the methodology on distribution of funds on the basis of taxes and grants by municipality, will be discussed. It is envisaged for the percentage of PIT revenues distributed to the municipalities, collected from individuals with permanent or temporary place of residence in the respective municipality, to gradually increase. Furthermore, amount of VAT grants will gradually increase in line with the municipalities' performance. Two funds are envisaged to be established – Performance Fund and Equalization Fund.

In fact, it is planned for municipalities showing positive results and higher own revenue collection to be awarded funds from the Performance Fund, while municipalities with lower revenues, but also showing fiscal effort and good results in collecting their own revenues, to be awarded funds from the Equalization Fund.

Activities will be also undertaken towards increased municipal own revenues by improving the efficiency of the administration and determining new local revenues in line with the EU good practices, as well as enhanced criteria on distribution of funds for transferred competences in the field of primary and secondary education, culture, child care and care for elderly and firefighting.

The second pillar, aimed at strengthening the financial discipline of the municipalities, arrears repayment and cost-effective operations, envisages activities aimed at measures for planning the actual revenues and expenditures of the municipalities, rationalising the operations and reducing the unnecessary expenditures, regular servicing of arrears, strengthened financial discipline, procedures on declaring financial instability, issuance of municipal bonds and analysis of the existing arrears of both the municipalities and the public enterprises.

For the purpose of increased transparency and accountability, i.e. within the third pillar of strengthening the fiscal decentralisation, government oversight will be enhanced, in particular by the Department for Public Sector Financial Inspection in terms of the Law on Reporting and Recording Liabilities and reporting non-compliance with the Law on Financial Discipline, measures will be adopted with respect to increased transparency at the municipalities by announcing the financial reports in a transparent and understandable manner, and activities will be undertaken for the purpose of strengthened accountability when using budget funds.

One of the priorities of the Government of the Republic of North Macedonia is continuation of the decentralisation process to the end of greater democratisation, improved (better quality and expanded) public services and intensified local development in the interest of the citizens. Thereby, in the coming period, municipal development policies, i.e. fiscal decentralisation and equal regional development, will continue to be implemented, to the end of strengthening the municipalities' financial sources, at the same time increasing the accountability and the transparency of their operations to the end of bringing the municipalities closer to the citizens.

Following the economic recovery from the consequences caused by COVID-19 pandemic, measures and policies focused on intensified, inclusive and sustainable economic growth have been envisaged, geared towards good governance - rule of law, eradicating corruption and capacity building of institutions, including the measures intended for supporting the fiscal decentralisation, ensuring local and equal regional development, sustainable and healthy environment and digitalisation of the economy and the public services.

### **2.2.1 Revenue Performance and Expenditure Execution in the period January – April 2021**

Performance of revenues and inflows to the budgets of local government units in this period January - April 2021, amounted to Denar 12,580 million and, compared to the same period last year, they significantly grew by 15.8%. Denar 3,130 million out of this amount was tax revenues, being significantly higher by 37.6% compared to last year. In this period of 2021, property tax revenues were collected in the amount of Denar 1,256 million, experiencing 40.1% growth, income tax revenue collection recorded slight increase by 4.2%, revenues on the basis of taxes on specific services experienced

significant growth of 55.1%, while fees for usage or licenses for performing an activity are at approximately the same level compared to the same period last year, i.e. recording a slight growth of 0.5%.

During the analysed period, non-tax revenues were collected in the amount of Denar 363 million, being at approximately the same level compared to the same period in 2020, recording a slight increase by 0.9%. As for non-tax revenues, inflows on the basis of fees and charges predominated, amounting to Denar 227 million, decreasing by 12.3% compared to the revenues collected in the same period last year, while other non-tax revenues amounted to Denar 107 million, recording a 38.9% growth.

In the period January - April 2021, capital revenues were collected in the amount of Denar 657 million, being higher by 80.5% compared to those collected in the previous year. Increase was mostly a result of the COVID-19-induced crisis and the contracted economic activity in the first half of 2020, however, at the same time, in 2021, signs emerged that the economic activity is gradually recovering and that the economy is reviving, thus also resulting in improved revenue collection. As for capital revenues, revenues collected on the basis of sale of land and intangible investments predominated almost on the whole.

In the analysed period of 2021, revenues collected in the basis of grants amounted to Denar 6,365 million, experienced an annual increase of 1.1%. Revenues collected on the basis of transfers in the period January – April 2021 amounted to Denar 1,299.9 million, being higher by 31.8% or by Denar 313 million compared to the revenues collected in the analysed period last year.

In the period January – April 2021, revenues collected on the basis of donations amounted to Denar 415 million, i.e. they were higher by 8.9% compared to last year.

In the period January - April 2021, revenues on the basis of loans were collected in the amount of Denar 351 million, i.e. they significantly increased by 70.7% compared to the same period last year.

In the period January – April 2021, expenditures were executed in the amount of Denar 11,746 million, i.e. execution was higher by 7.8% in relation to the same period last year. These expenditures provided for regular settling of liabilities arising from the transferred powers to the municipalities, necessary for their ongoing operations, implementation of capital projects and principal repayment for the previously taken loans.

Expenditures related to wages and allowances accounted for the most of the expenditures with 52.9%, i.e. Denar 6,216 million. Most of the wages, i.e. 85.4% or Denar 5,354 million was intended for the employees in the institutions at local level, such as primary and secondary education, culture, kindergartens and old people's homes and fire fighting, financed with approximately 99.2% with block grants. Expenditures related to goods and services amounted to Denar 2,250 million, accounting for 19.2% of total expenditures. Capital expenditures accounted for 19.7%, amounting to Denar 2,313 million, being mostly financed, i.e. 79.1% with municipal own funds, while 3.9% was funds on the basis of donations and 14.6 % was funds on the basis of loans. Expenditures related to subsidies and transfers amounted to Denar 684.8 million, accounting for 5.8%, while principal repayment amounted to Denar 225.9 million, i.e. 1.9% of total expenditures. Expenditures executed on the basis of reserves, social benefits and interest payments accounted for around 0.5%.

## **2.2.2 Medium-Term Framework of Local Government Budget**

As one of the priorities indicated in the 2020-2024 Government Programme of the Republic of North Macedonia is also continuation of the decentralisation process. This speaks in favour of the propensity for providing better democracy in the society, more efficient and cost-effective service rendering and delivery, as well as intensified local development.

The objective of the competences is to transfer them to a management level most suitable for the citizens, for the purpose of effective execution, with appropriate financial resources and guaranteed involvement of citizens in the decision-making process. In the coming period, municipal development policies, i.e. fiscal decentralisation and equal regional development, will continue to be implemented, to the end of strengthening the municipalities' financial sources, at the same time increasing the accountability and the transparency of their operations.

In the course of 2021 and in the medium-term, and for the purpose of strengthening the fiscal decentralisation, many activities and measures are envisaged, grouped in three pillars - improved fiscal capacity and increased municipal revenues, strengthened fiscal discipline and transparency and accountability as regards municipalities' operations.

Municipalities are expected to continue the trend of improved collection of own revenues, strengthening the capacities for development of policies for financing the municipalities and enhancing the capacities for financial management. For the purpose of realising the strategic commitments, strong commitment to encouraging sustainable local development, good local governance and creating conditions for more active, more effective and more innovative role of the local authorities in implementing national objectives for growth and development will continue in the next period as well.

To the end of Improved fiscal capacity and increased municipal revenues, many activities activities have been envisaged, which will provide for increase of the funds distributed to the municipalities from the central Budget, increased own revenues of the municipalities and establishment of funds to support the good performance of municipalities. It is envisaged for the percentage of PIT revenues distributed to the municipalities, collected from individuals with permanent or temporary place of residence in the respective municipality, to gradually increase. Furthermore, amount of VAT grants will also gradually increase. By the end of 2021, models for distributing one portion of VAT revenues, distributed to the municipalities and establishing Equity Fund and Performance Fund, will be devised by the end of 2021.

Municipalities showing positive results and higher own revenue collection will be awarded funds from the Performance Fund, while municipalities with lower revenues, but also showing fiscal effort and good results in collecting their own revenues will be awarded funds from the Equalization Fund.

By improving the administration efficiency and finding new local revenues, own revenues will be increased. In cooperation with the competent ministries transferring funds as block and earmarked grants for the transferred competence in the field of primary and secondary education, culture, childcare and care for elderly and fire fighting, activities will be undertaken towards increasing the criteria for distributing the awarded funds and providing better quality of services. Government of the Republic of North Macedonia established Inter-Sectoral Working Group for the purpose of overcoming the issues as regards the fire fighting and analysing the developments in this field, wherein earmarked grant is allocated. In the period to come, activities for amending the Law on Firefighting will commence, in particular as regards the additional regulation of wages and allowances for fire fighters, as well as determination of the required number of firefighters in line with the criteria set under the Law.

What is also envisaged is introducing fiscal decentralisation monitoring indicators, increasing local tax collection efficiency, improving the effectiveness and profitability of public enterprises and the municipalities, as well as increasing the transparency and the accountability of the municipalities.

Strengthening the financial discipline of municipalities, arrears repayment and cost-effective operations will be the priorities in the coming period, whereby measures will be undertaken for the purpose of planning the actual revenues and expenditures of the municipalities, rationalising the operations and reducing the unnecessary expenditures, regular servicing of arrears, strengthened financial discipline, procedures on declaring financial instability and analysis of the existing arrears of both the municipalities and the public enterprises.

For the purpose of increased transparency and accountability and strengthening the fiscal decentralisation, government oversight will be enhanced, in particular by the Department for Public Sector Financial Inspection in terms of the Law on Reporting and Recording Liabilities and reporting non-compliance with the Law on Financial Discipline, measures will be adopted with respect to increased transparency at the municipalities by announcing the financial reports in a transparent and understandable manner, and activities will be undertaken for the purpose of strengthened accountability when using budget funds.

Public consultations and discussions with ALGUs and the other stakeholders on reform proposals have already commenced, in coordination with the Working Group entrusted with the continuation of the decentralisation process, established by the Government, with the Ministry of Political System, Ministry of Finance, Ministry of Local Government and ALGUs as its members. One of the government priorities is continuation of the decentralisation process to the end of greater democratisation, improved public services and intensified local development in the interest of the citizens.

Stable revenues have been provided by allocating funds from lease of state-owned agricultural land to the municipalities, the proportion of which is 50% for the Budget of the Republic of North Macedonia and 50% for the municipalities and the municipalities in the City of Skopje, distributed from 2018, depending on the location of the agricultural land under lease, provided that collection of revenues on the basis of tax on real estate exceeds 80% in relation to the ones projected in the previous year. Municipalities also generate revenues from the fee collected by issuing concession for usage of water resources for electricity generation (50% for the central government budget and 50% for the local authorities), depending on which area the concession activity is performed.

Increase has been recorded at own revenue performance at the municipalities, in particular revenues collected on the basis of taxes on real estate, as a result of greater coverage of the real estate of natural persons and legal entities and re-assessment of the value of real estate. In the coming period, higher revenues are expected to be generated by determining the real market value of the real estate after completing the procedure on treatment of illegally built facilities on construction and agricultural land. Increased property tax rate for higher-value properties could be an additional source of revenues, whereby once the rate is increased, it is of essential importance for assessment and auditing capacities be ensured in order to avoid reporting property at lower value.

In the coming period, higher revenues are expected to be generated by determining the real market value of the real estate after completing the procedure on treatment of illegally built facilities on construction and agricultural land. In addition, municipalities will ensure additional sources of revenues on the basis of performing the transferred competences for management of construction land and treatment of illegally built facilities on construction and agricultural land.

In the upcoming medium-term period, the new Law on Equal Regional Development, as well the 2020-2030 Strategy for Equal Regional Development expected to be implemented. Government of the Republic of North Macedonia will continue to carry out the activities aimed at equal regional development and enhancement of all regions in the country in the next period as well. Implementation of the 2020-2030 Strategy for Equal Regional Development of the Republic of North Macedonia in the eight planning regions (Vardar, East, Southwest, Southeast, Pelagonija, Polog, Northeast and Skopje regions), by better vertical and horizontal coordination of both the national and the local policies and the integrated development projects adjusted to the local needs and conditions, will provide for more balanced local development throughout the country. The Council for Equal Regional Development will continue to play a significant role as promoter of partnership between the regions/the municipalities and the Government, and within it the usage of funds will be coordinated from all sectoral programmes intended for the planning regions and the municipalities. Special efforts will be put at supporting municipalities, by encouraging local development via support geared towards the local projects and their harmonisation with the national ones. Purpose of fiscal harmonisation, in the light of the Strategy for Equal Regional Development, is providing equal offer of public goods and services at all local government units, thereby attaining a

complementary effect in view of achieving greater balance of the development of certain planning regions. By solidly assisting the financially weakest municipalities, i.e. municipalities with lowest capacity for revenue collection, positive effects are yielded on their development, and thus the development of the planning region to which they belong.

2021-2026 Programme on Sustainable Local Development and Decentralisation was adopted, whereby 2021-2023 Action Plan on the 2021-2026 Programme on Sustainable Local Development and Decentralisation is being prepared.

At the same time, Working Sectoral Group for Regional and Local Development is obliged to carry out tasks at expert level, related to the formulating and implementation of the national sectoral policies, including those related to the EU integration and the donors' aid generally, as well as the IPA Programme.

In addition to the support as regards the transfer of competences for collection of part of the public revenues, as well as the Central Budget transfers, support to building municipal capacities is also implemented through projects of the central government funded by international financial institutions.

Municipal Services Improvement Project, being implemented by the Ministry of Finance with support from the World Bank and the European Commission commenced a decade ago, with total fund of more than EUR 100 million, being aimed at improving the municipal services via loans and grants for implementing capital projects such as water supply, sewerage and waste water treatment, energy efficiency (street lighting, insulation of municipal facilities, etc.), local road infrastructure (street and road modernisation and reconstruction), utility services (procurement of vehicles for the public utility enterprises), as well as other municipal services and competences (construction of kindergartens, green markets, infrastructure in the industrial zone, etc.).

Under the Local Roads Connectivity Project, which is part of the ongoing Country Partnership Framework, implemented by the Ministry of Transport and Communications, EUR 70 million is intended to be disbursed to all 80 municipalities for construction and rehabilitation of local roads and streets, as well as other road infrastructure in local government units. Such direct support in the amount of EUR 500,000 up to EUR 2 million per municipality (depending on the project they apply for) provides for improved local infrastructure in the municipalities.

In the upcoming period, realisation of the Public Sector Energy Efficiency Project will commence, to be implemented via the Ministry of Finance with World Bank support with Loan Agreement in the total amount of EUR 10.5 million. Public Sector Energy Efficiency Project will be implemented by the Project Implementation Unit, aimed at improving the municipal services - MSIP. Main objective of this Project is reducing energy consumption in the public sector, at the same time improving the level and the quality of the public buildings and the public lighting. All local government units are eligible to use the funds under this component. Amount of funds per municipality can vary from EUR 50,000 to EUR 750,000 and is dependent on the municipal borrowing capacity and the estimated investment value of the proposed municipal project. By signing a sub-loan agreement with the Ministry of Finance, 80% of the loan funds will be allocated to the municipality as on-lending, with the remaining 20% being allocated as a grant. At the same time, within the funds under this Project, the Ministry of Finance will also cover the expenses for preparation of Energy Audit and technical design.

Another major project implemented in the past ten years, aimed at improvement of the municipal infrastructure, is Water Supply and Wastewater Collection Project, funded by the European Investment Bank (EIB), the World Bank, KfW, IPA and budget funds, implemented by the Ministry of Transport and Communications. Funds in the amount of EUR 100 million are provided to all municipalities, supporting the construction of better water supply infrastructure and wastewater treatment plants. This Project will continue in future as well through the Ministry of Environment and Physical Planning, with additional funds unlocked for supporting the local infrastructure improvement.

Table 5. Medium-Term Projection of Local Government Budget (Denar million)

	2021*	2022*	2023*	2024*	2025*	2026*
<b>Total revenues</b>	<b>42.000</b>	<b>44.920</b>	<b>45.966</b>	<b>47.050</b>	<b>50.944</b>	<b>54.748</b>
Tax revenues	10.905	11.240	11.505	11.770	12.410	12.850
Non-tax revenues	2.466	2.689	2.689	2.689	2.739	2.839
Capital revenues	3.098	3.150	3.200	3.250	3.600	4.000
Transfers	23.666	25.791	26.522	27.291	30.145	33.009
Donations	1.865	2.050	2.050	2.050	2.050	2.050
<b>Total expenditures</b>	<b>43.583</b>	<b>44.920</b>	<b>45.966</b>	<b>47.050</b>	<b>50.944</b>	<b>54.748</b>
Salaries and contributions	19.365	19.284	19.334	19.384	19.434	19.641
Goods and services	10.238	10.470	10.570	10.870	12.170	13.338
Interest payments	61	61	61	61	61	61
Subsidies and transfers	2.810	3.480	3.681	3.681	3.681	3.681
Social transfers	56	61	61	61	61	61
Capital expenditures	11.053	11.564	12.259	12.993	15.537	17.966
<b>Balance</b>	<b>-1.583</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>

Source: Ministry of Finance and projections of the Ministry of Finance (\*)

### 2.3 General Government Budget (Consolidated Budget of the Republic of North Macedonia and Municipal Budget)

General Government Budget includes consolidated data on the Budget of the Republic of North Macedonia and the budgets of the municipalities. Budget of the Republic of North Macedonia comprises the central budget (core budget, self-financing activities budget, donation funds and loan funds) and the budgets of the Pension Insurance Funds, the Health Insurance Fund and the Employment Agency.

Projected revenues of the General Government Budget, as % of GDP, are projected at 32.2% in the next five-year period (Table 6). As a result of the continuous implementation of disciplined budget policy, total expenditures of the consolidated budget in the 2022-2026 period are projected to reduce from 37.8% in 2022 to 36% in 2026. Subsequently, and in line with the gradual fiscal consolidation, the General Government Budget deficit will reduce from 4.3% of GDP in 2022 to 2.2% of GDP in 2026.

Table 6. General Government Budget

	Millions MKD						% of GDP					
	2021*	2022*	2023*	2024*	2025*	2026*	2021	2022	2023	2024	2025	2026
<b>Central budget</b>												
Revenues	118.889	131.948	144.882	161.711	177.214	194.149	16,8	17,5	17,9	18,6	18,8	19,1
Expenditures	153.819	164.600	173.288	187.040	200.797	216.634	21,8	21,8	21,4	21,5	21,3	21,3
Budget balance	-34.930	-32.652	-28.406	-25.329	-23.583	-22.485	-4,9	-4,3	-3,5	-2,9	-2,5	-2,2
<b>Budget funds</b>												
Revenues	70.750	75.778	80.169	84.823	89.756	94.986	10,0	10,1	9,9	9,7	9,5	9,3
Expenditures	70.758	75.786	80.177	84.831	89.764	94.994	10,0	10,1	9,9	9,7	9,5	9,3
Budget balance	-8	-8	-8	-8	-8	-8	0,0	0,0	0,0	0,0	0,0	0,0
<b>Budget of the RNM (Central budget and funds)</b>												
Revenues	189.639	207.726	225.051	246.534	266.970	289.135	26,8	27,6	27,8	28,3	28,3	28,4
Expenditures	224.577	240.386	253.465	271.871	290.561	311.628	31,8	31,9	31,3	31,2	30,8	30,6
Budget balance	-34.938	-32.660	-28.414	-25.337	-23.591	-22.493	-4,9	-4,3	-3,5	-2,9	-2,5	-2,2
<b>Local government</b>												
Revenues	41.086	44.920	45.966	47.050	50.944	54.748	5,8	6,0	5,7	5,4	5,4	5,4
Expenditures	42.859	44.920	45.966	47.050	50.944	54.748	6,1	6,0	5,7	5,4	5,4	5,4
Budget balance	-1.773	0	0	0	0	0	-0,3	0,0	0,0	0,0	0,0	0,0
<b>General government (Consolidated Budget of RNM and Local government)</b>												
Revenues	230.725	252.646	271.017	293.584	317.914	343.883	32,7	33,5	33,5	33,7	33,7	33,8
Expenditures	267.435	285.305	299.430	318.922	341.504	366.376	37,8	37,8	37,0	36,6	36,2	36,0
Budget balance	-36.710	-32.659	-28.413	-25.338	-23.590	-22.493	-5,2	-4,3	-3,5	-2,9	-2,5	-2,2

Source: Ministry of Finance and projections of the Ministry of Finance (\*)



### **3. Other Aspects of Improvement of Public Financial Management**

#### **3.1 Budget Law**

The new Budget Law, pending parliamentary procedure, provides the framework defining the public finance management system in the Republic of North Macedonia.

In the past period, Ministry of Finance, in cooperation with experts from international institutions has paid considerable attention to developing a modern public financial management concept, designed through the new Budget Law.

The Budget is one of the most important instruments of economic policy. Hence, the Budget Law, which defines the procedures for preparation and adoption of this document, is equally significant.

Existing Budget Law dates from 2005, with several additional amendments and clarifications, it regulates the procedures for preparation, adoption and execution of the Budget of the Republic of North Macedonia, and the budgets of the local government units and the City of Skopje, as well as the reporting on the budget execution. However, the new trends, recommendations and directives call for new solutions as regards public financial management, in line with the good practices of the international financial institutions and the EU Directives.

This Law regulates the procedure for preparation, adoption, execution of the Budget of the Republic of North Macedonia and the budgets of the local government units and the City of Skopje and reporting on their execution. This Law regulates the fiscal rules and the fiscal principles, the establishment of the Fiscal Council, the medium-term budget planning, the management of state and municipal funds, as well as the monitoring of financial results of public enterprises and companies established by the state and the municipalities, as well as companies established by such public enterprises and companies, and the financial responsibility and the basis for establishment of an integrated PFM IT system.

Improvement of the public financial management and strengthening the medium-term budget planning in the next 5 years is one of the top priorities of the Government of the Republic of North Macedonia as part of the EU accession process.

Under this legal solution, commitment to strategic planning continues, giving a medium-term public finance framework, i.e. medium-term budget planning and strengthening of the process by introducing fiscal policy statement to be submitted to the Parliament during the Government term of office, which will contain the fiscal strategy guidelines, as well as via realistic macroeconomic and fiscal projections (revenues and expenditures) in line with the most recent available statistical and other relevant data.

Thereby, as regards the process of preparing the Fiscal Strategy, it is envisaged for the existing timeframe to be shifted, i.e. as well as for its structure and contents to be improved.

Some of the Medium-Term Fiscal Strategy postulates for a period of 5 years, containing projections on growth, deficit and capital projects, have already been set in the 2021 Budget.

The Budget will be presented more clearly through plenty of well-structured information, and it will be divided into general, special and development parts. The general part will contain all budget inflows and outflows during the respective fiscal year. The special part will thoroughly present the expenditures of budget users, while the project part will contain information on the public investment projects, with data on the duration and total value of each project, data on the so-far performance and the planned medium-term investments.

New deadlines for the budget preparation process are envisaged, shifting its timeframe, all to the end of greater predictability, public inclusion and transparency.

Under the new Law, Registry of Public Entities, publicly available, has been established for the first time. This Registry will keep records of all legal entities established, directly or indirectly, by the state or the municipalities, thus providing for comprehensives and transparency for all public entities regardless of whether they are at central or local level.

At the same time, the Law includes provisions for introducing numerical fiscal rules, designed in a way, in which they will comply with the EU fiscal rules, thus making the fiscal policy more predictable and more accountable. The Government may apply the escape clauses with respect to the set fiscal rules in case of occurrence of exceptional circumstances:

With respect to the Fiscal Council, it is envisaged to establish an independent body composed of 3 members proposed by the Macedonian Academy of Sciences and Arts, the State Audit Office and the National Bank, who will be elected by the Parliament. Members should be experts in the field of public finances, macroeconomy or economics.

In addition, the Law stipulates general provisions for public debt management and issuance of guarantees, thereby determining the borrowing procedures for the needs of the central and the local government, as well as the issuance of guarantees.

At the same time, reporting quality and quantity are envisaged to be improved.

In the coming period, Ministry of Finance, in cooperation with the World Bank, as well as through the EU IPA Twinning Project "Strengthening Budget Planning, Execution And Internal Control Functions", will continue to work on preparing by-laws, guidelines, manuals, etc., aimed at enforcing the new Budget Law, further improvements of the public financial management system, as well as developing a detailed plan for all working process in the Ministry of Finance. In addition, what is planned to be introduced in the Draft Budget Law, in the coming period, is the introduction of IFMIS – Integrated Financial Management Information System, which will provide for integration and connection with all budget users and systems of the Public Revenue Office, the Customs Administration and other institutions, for the purpose of providing more efficient public financial management. By implementing IFMIS, full compatibility and interoperability with the public

financial systems will be achieved, and their application in accordance with the Public Financial Management Strategy means ensuring availability of the systems and continuous exchange of data 24 hours per day throughout the year.

On the basis of the carried out Public Investment Management Programme (PIMA) by the International Monetary Fund, Ministry of Finance, as process coordinator, prepared Action Plan for preparing the recommendations under PIMA, being adopted by the Government. Action Plan envisages activities, which realisation should commence in 2021 and 2022, to be implemented by the competent national institutions in the next 2021-2024 period to the end of improving the public investment management. More specifically, reforms will be gradually introduced to the end of improving the planning, the allocations and implementation of public infrastructure projects, which will contribute to greater harmonisation of budget allocations with the Government's investment priorities, improvement of the comprehensiveness of the budget documentation so as to include all public expenditures for capital investments and information on the financial needs of ongoing and new projects, introducing supervision over the public investments at national level, including monitoring and management of the overall risks as regards the respective realisation.

### 3.2. Report on the Recorded Liabilities pursuant to the Law on Reporting and Recording the Liabilities

For the purpose of providing and maintaining transparency and accountability and strengthening the accountability when managing public funds, the Law on Reporting and Recording Liabilities regulates the reporting, recording and publication of the data on reported undue liabilities and arrears.

Such legal solution regulates the recording of liabilities on monthly basis in the electronic system by the general government bodies, local government units and institutions performing activities in the field of culture, education, health, child care, social protection, as well as in other activities of public interest determined by Law, established by the Republic of North Macedonia or by the local government units, public enterprises, state-owned companies and other legal entities founded by the Republic of North Macedonia or the local government units.

For the purpose of informing the public and greater transparency, and on the basis of the recorded data on reported liabilities, reporting is carried out on monthly basis through the Electronic System for Reporting and Recording Liabilities, by the 10<sup>th</sup> day in the month for the previous month at the latest, and Ministry of Finance, publishes, on quarterly basis, summary reports on its website.

On the basis of the data recorded in the Electronic System for Reporting and Recording Liabilities, as for the data reported in March 2021, the Report on Reported Liabilities by groups of entities is shown in Table 6.

Table 6. Report on Reported Liabilities by group of entities for 2021 March (Denar million)

No.	Group of subjects	Overdue and unpaid liabilities, 2021	Arrears, 2021	Arrears, 2022	Arrears, 2023
1	First line budget users	693	652	804	403
2	Second line budget users - institutions on national level	191	68	12	2
3	LSGUs	3.833	776	336	413
4	Second line beneficiaries - local institutions financed through block grants	321	45	7	0
5	Public health institutions	3.269	1.540	1	0
6	Public enterprises / Trade companies established by the Republic of North Macedonia	7.557	4.995	5.464	1.078
7	Local enterprises established by municipalities	3.221	637	193	99
8	Regulatory bodies	5	25	0	0
9	Planning regions	94	0	0	0
10	Other entities	4	41	1.221	1.481
<b>Total (1+2+3+4+5+6+7+8+9+10)</b>		<b>19.188</b>	<b>8.779</b>	<b>8.038</b>	<b>3.476</b>

Source: Ministry of Finance - Electronic System for Reporting and Recording Liabilities

### 3.3. Public Enterprises and State-Owned Companies

Operations of public enterprises and state-owned companies is regulated in the Law on Public Enterprises, the Company Law, as well as other laws defining the operations in the specific area (Law on Energy, Law on Railway System, Law on Public Roads, etc.)

Government of the Republic of North Macedonia founded 14 public enterprises, being a single shareholder in 15 companies. These entities are employers of around 15.5 thousand workers, account for a significant part of Macedonian economy.

Total revenues of public enterprises and state-owned companies in 2020 in line with the data from the annual reports, amount to Denar 36.5 billion, total expenditures were executed in the amount of Denar 34.5 billion, whereby as a final result in 2020, gross profit in the amount of approximately Denar 2 billion was realised (Figure 7).

Financial indicators from the operations of public enterprises and companies are shown on accrual basis, in line with the stipulated accounting methodology, differing from the accounting methodology of budget users, whereby financial data are shown on cash basis, thereby taking into account that these entities keep accounting records, prepare and submit the annual account and the financial reports in line with the Company Law and the adopted international accounting standards and the International Financial Reporting Standards, rather than pursuant to the Law on Accounting of Budgets and Budgets Users. The loss presented at certain public enterprises and state-owned companies is a result of the calculated depreciation of fixed assets, which is basically an accrual expense and is presented as an expense of public enterprises. Positive performance recorded in the overall operations of public enterprises and state-owned companies in 2020, will be basis for further improvement of financial performance of these enterprises, along with the efficient improvement of public services they provided to the citizens and the business sector.

Figure 7. Main financial indicators for public enterprises and state-owned companies (Denar million)

No.	Name of Joint Stock Company/ State-Owned Public Enterprise	Total revenues	Total expenditures	loss/profit before taxation	projected revenues	projected expenditures	loss/profit before taxation
		2020			2021		
1	JSC "Power Plants of North Macedonia" - Skopje	12,015.4	13,048.5	-1,033.1	12,434.0	12,421.5	12.5
2	State-Owned Joint Stock Company for Transmission of the Electricity and Management of the Electricity System - Skopje	3,362.1	3,720.0	-357.9	3,193.4	3,860.0	-666.6
3	Public Enterprise for State Roads - Skopje	9,983.4	5,191.8	4,791.6	23,011.5	23,011.5	0.0
4	JSC "Railways of the Republic of North Macedonia Transport" - Skopje	1,235.9	1,620.6	-384.8	1,208.7	1,736.2	-527.5
5	PE "National Forests" - Skopje	1,433.4	1,516.8	-83.4	2,044.5	1,943.3	101.2
6	JSC "National Post Office" Skopje	1,163.8	1,258.8	-94.9	1,181.6	1,341.1	-159.5
7	Public Enterprise for Railway Infrastructure "Railways of the Republic of North Macedonia" - Skopje	780.5	1,103.1	-322.6	1,110.1	1,428.1	-318.0
8	PE for Maintenance and Protection of National and Regional Roads - Skopje	1,197.7	1,194.1	3.6	1,550.0	1,540.0	10.0
9	Public Broadcasting Enterprise "National Radio Television" - Skopje	1,012.2	937.7	74.5	1,022.5	1,022.5	0.0
10	Joint Stock Company for Construction and Management of Business and Housing Premises of Relevance to the Republic of Macedonia - Skopje	1,317.0	1,284.5	32.5	945.3	898.4	46.9

11	JSC Air Navigation Service Provide M-NAV - Skopje	487.4	845.7	-358.3	738.9	777.7	-38.8
12	JSC "Water Economy of Republic of North Macedonia" - Skopje	629.7	657.8	-28.1	796.7	795.2	1.5
13	PE "Strezevo" - Bitola	228.8	464.3	-235.6	244.8	467.6	-222.8
14	JSC TPP "Negotino" - Negotino	187.4	181.8	5.6	195.8	195.8	0.0
15	JSC "State Lottery of Macedonia" - Skopje	673.7	263.0	410.7	641.2	375.5	265.7
16	PE "Zletovica" - Probitip	22.8	163.3	-140.5	25.6	167.2	-141.6
17	PE "National Broadcasting" - Skopje	247.3	202.7	44.6	226.5	225.2	1.2
18	JSC "Airports of North Macedonia" - Skopje	25.2	248.0	-222.8	13.2	122.0	-108.8
19	Single-Member Limited Liability Company "Boris Trajkovski" - Skopje	49.5	99.5	-50.0	116.0	160.0	-44.0
20	PE for Water Economy "Lisice" - Vesles	44.6	85.2	-40.6	47.1	87.8	-40.7
21	JSC for Management of State-Owned Business Premises	87.8	82.3	5.4	90.0	82.9	7.1
22	PE "Official Gazette of the Republic of North Macedonia" - Skopje	88.4	73.1	15.3	118.2	83.2	35.0
23	PE "Studencica" - Drugovo	62.2	65.6	-3.4	69.6	69.6	0.0
24	JSC "Media Information Agency" - Skopje	57.6	56.7	0.9	54.0	54.0	0.0
25	PE "Jasen" - Skopje	37.4	44.9	-7.5	47.6	45.5	2.0
26	PE for Management of Pastures - Skopje	42.6	55.3	-12.7	39.8	34.8	5.0
27	JSC "National Energy Resources"	0.0	20.2	-20.2	3,157.0	44.7	3,112.3
28	PE "Agro - Stock Market" - Skopje	8.6	10.0	-1.4	12.4	12.4	0.0
29	Single-Member Limited Liability Company "Oil Pipeline" - Skopje	0.0	7.0	-7.0	9.3	9.3	0.0
<b>TOTAL:</b>		<b>36,482</b>	<b>34,502</b>	<b>1,980</b>	<b>54,345</b>	<b>53,013</b>	<b>1,332</b>

Source: Annual Reports and Financial Plans of Public Enterprises and State-Owned Companies

Pursuant to the amendments to the Law on Public Enterprises, for the purpose of increasing transparency, public enterprises are obliged to publish the annual and quarterly reports on their websites, thus providing for timely and transparent monitoring of financial operations of these entities, at the same time providing opportunity for more realistic prediction of the fiscal risk in this field and timely reaction and undertaking of appropriate measures. As of 2020, Ministry of Finance, publishes, on its website, consolidated quarterly data on the collected revenues and executed expenditures at the level of public enterprise/state owned-company.

Public enterprises and state-owned companies are obliged, pursuant to the Law on Reporting and Recording of Liabilities, to report, on monthly basis, undue liabilities and arrears in the Electronic System for Reporting and Recording Liabilities, being kept by the Ministry of Finance. On the basis of the recorded data on reported liabilities, Ministry of Finance, in continuity, and on quarterly basis, publishes summary reports on its website, thus additionally contributing to strengthened and increased transparency.

Budget revenues on the basis of payment of dividend by state-owned companies at the end of 2020, amount to Denar 864,554,466.

The obligation for payment of the profit from the Budget-related operations pursuant to the Company Law, while public enterprises according to the Law on Public Enterprises are obliged, to pay the excess of funds generated throughout the operations, into the Budget of the Republic of North Macedonia, in case it is not covered by investments in the public enterprise under the investment programme prepared in accordance with the detailed financial plan. Thereby, the founder of the public enterprise may, as regards the excess funds from the public enterprise operations paid in the Budget of the Republic of North Macedonia, reach a decision to cover the losses of other public enterprise, pay them on special earmarked account pertaining to financial support and development for the purpose of performing an activity of public interest of a legal entity founded by the Republic of North Macedonia or to cover budget liabilities towards the Funds.

In 2020, funds in the total amount of Denar 101,768,517 have been paid in the Budget upon this basis.

Although, the annual Law on Execution of the Budget of the Republic of North Macedonia does not directly cover the public enterprises and state-owned companies, they, via their line ministries, obtain transfers as budget support for the purpose of realizing certain infrastructure projects, given that they perform activities of public interest, i.e. they are entities performing activities essential for Macedonian economy.

In order to better cope with the adverse consequences caused by COVID-19 pandemic, and as per the executive power instructions as founder of these entities, the public enterprises and state-owned companies were obliged to pay the generated profit in the Budget, as well as to revise the financial plans to the end of reducing the non-productive expenditures by 15%.

#### **4. Use of EU Pre-Accession Assistance**

Republic of North Macedonia, as a candidate country for EU membership, has funds under the EU Pre-Accession Assistance (IPA) Instrument available through two financial perspectives: 2007-2013 IPA Financial Perspective (IPA 1) and 2014-2020 IPA Financial Perspective (IPA 2). Projects funded within the 2007-2013 IPA Financial Perspective (IPA 1) finished their implementation, whereby some of the Programmes they were funded with remain to be formally closed.

This section of the document presents only the part of EU Pre-Accession Assistance, which is implemented under the decentralised/indirect management method. IPA decentralised/indirect management method is a management method within which the European Commission (EC) entrusts tasks for implementation of certain IPA programmes to the accredited structure in the Republic of North Macedonia, such as tender procedures, contracting, project monitoring and execution of payments. On the other hand, when it is a matter of centralised management, these are responsibilities of the EC.

Funds for national co-financing intended for projects implemented under the decentralised/indirect management are planned within the budget of the Ministry of Finance, organisational code 09002 - Functions of the State, except for the national co-financing necessary for financing the IPARD projects, which is planned within the budget of the Agency for Financial Support in Agriculture and Rural Development, organisational code 14004, as well as the national co-financing for payment of financial contribution to EC for participation in the Union Programmes, which is planned in the line ministries.

##### **4.1 IPA 1 - 2007-2013 Financial Perspective**

Within IPA 1 - 2007 - 2013 Financial Perspective, Republic of North Macedonia has available, through the five IPA Components, funds in the amount of EUR 614 million (Denar 37.8 billion), around EUR 467 million (Denar 28.7 billion) out of which or around 76% of the total allocations are employed through the decentralised management method (through structures that are accredited by the EC services so as for indirect management of the European funds). As regards IPA 1 programme period 2007-2013, national structures responsible for implementation of the projects are accredited for decentralised management of the following components: IPA Component I - Transition Assistance and Institution Building (TAIB); IPA Component III - Regional Development; IPA Component IV - Human Resources Development and IPA Component V - Rural Development.

Implementation of most of the programmes within IPA 1 was completed at the end of 2019, while the implementation of the projects planned within 2013 TAIB Annual Programme, was completed at the end of 2020.

These IPA Component I Programmes generally provide support to the state administration in order to enhance its capacities at both central and local level, undertake reforms, as well as fulfill the obligations under the membership more quickly and more efficiently.

With respect to National Programme TAIB 2013, contracting rate accounts for around 93%, i.e. total of 52 contracts are concluded, the implementation of which commenced in December 2017. In line with the requirements in the Financing Agreement, contract implementation was completed by October 2020, while final payments under the contracts were made by May 2021 inclusive.

##### **4.2 IPA 2 - 2014-2020 Financial Perspective**

Under IPA 2 2014 - 2020 Financial Perspective, Republic of North Macedonia has EUR 664 million available. With respect to the manner of implementation, around 50% of the total allocations under IPA 2 will be earmarked for projects planned to be implemented through indirect management system, i.e. through accredited IPA structures.

Awarded assistance will be used for financing projects in the following areas: justice and home affairs, road and railway infrastructure, environment protection, education, employment, promotion of gender equality, human resources development and agriculture and rural development

IPA funds that employed through indirect management are the following annual and multi-annual programmes:

- 2014 Action Programme for financing projects in the following areas:  
judiciary,

- disaster recovery system and ensuring business continuity,
- further development of capacities for crime scene investigations,
- entry tickets for the Union Programmes,
- local and regional competitiveness, focusing on tourism, and
- support to EU integration (SEA)
- 2015 Action Programme, 2016 Action Programme, 2018 Action Programme and 2020 Action Programme for financing the entry tickets for EU Programmes;
- 2017 Action Programme for financing projects in the following areas:
  - labour and education,
  - entry tickets for the Union Programmes,
- Multi-Annual Sectoral Operational Programme for Transport 2014 – 2020;
- Multi-Annual Sectoral Operational Programme of the Republic of North Macedonia for Environment and Climate Action 2014 – 2020;
- IPARD 2 Programme.

Under the 2014 Action Programme, total of 26 agreements were concluded, amounting to EUR 14.63 million. As regards the financing of the projects within this Programme, IPA funds in the amount of around EUR 20 million are made available to the Republic of North Macedonia. Significant projects implemented within the Programme are the following:

- construction works for rehabilitation of prisons in Bitola and Skopje,
- construction works for rehabilitation of Public Prosecutor's Office regional offices,
- grant scheme for support to NGO in the area of law,
- service contracts to support judiciary reforms,
- contract for procurement of IT equipment for the needs of the Ministry of Internal Affairs - Disaster Recovery Data Center, etc.

As for this Programme, it is worth mentioning that the deadline for completing the projects, in line with the Financial Agreement between the Republic of North Macedonia and the European Commission is 20<sup>th</sup> November 2021.

Financing of projects in the field of road and rail transport, as well as projects for construction of waste water treatment plants, sewerage networks and waste management and climate changes is envisaged within the Multi-Annual Sectoral Operational Programme of the Republic of North Macedonia for Environment and Climate Action and Multi-Annual Sectoral Operational Programme of the Republic of North Macedonia for Transport.

It is envisaged for around 48 contracts to be financed with EUR 114.96 million as IPA funds within the environment and climate action sector in the period 2014 - 2020. Among the more significant projects envisaged to be financed under the Programme are the following: contracts for construction works related to water treatment stations in Bitola and Tetovo, contracts for construction works related to upgrading the sewerage network in Bitola, Tetovo and Kicevo, contract for construction of wastewater collection infrastructure in Skopje, etc.

It is envisaged for around 22 contracts to be financed within the transport sector in the period 2014 - 2020. IPA funds in the amount of EUR 110.91 million is allocated to the transport sector in the period 2014 - 2019. Among the more significant projects envisaged to be financed under the Programme are the following:

- contract for construction of the rail section from Kriva Palanka to the Republic of Bulgaria,
- contract for construction of Gradsko – Drenovo road section,
- contract for reconstruction of Raec – Prilep road section
- contract for reconstruction of Kumanovo – Rankovce road section, etc.

As of May 2021 inclusive, under the transport sector, 4 (four) contracts have been concluded, in the total amount of EUR 31.98 million, EUR 27.18 million out of which are IPA funds. In the field of environment and climate changes, 9 (nine) contracts have been concluded in the total amount of EUR 25.47 million, EUR 20.53 million out of which are IPA funds. As regards the remaining projects, tender procedures are ongoing.

In line with the signed Financial Agreement for this Programme, deadline for concluding and completing the respective contracts thereunder is 31<sup>st</sup> December 2025.

Around 10 contracts are envisaged to be financed within the 2017 Action Programme, EUR 12.65 million being allocated therefore as IPA funds.

Projects in the field of labour and education are financed within this Programme, the aim of which is to reduce high unemployment rate, increase share on the labour market, in particular the one of young people and women, increase the access to quality education and training, improve the results and the skills and establish a modern and flexible social protection system. In order to achieve the general objective, several projects are envisaged in the following areas:

- institutional strengthening of the capacities for sustainable sectoral reforms;
- improving the quality of education and training;
- promoting the development of skills, employment and working conditions;
- social protection, social inclusion and equal share on the labour market and in the society.

As of May 2021 inclusive, under the 2017 Action Programme, 3 (three) contracts have been concluded, in the total amount of EUR 5.36 million, EUR 5 million out of which are IPA funds.

As for this Programme, it is worth mentioning that in line with the signed Financial Agreement for 2017 Action Programme for Education, Employment and Social Policy, deadline for contract conclusion is 20<sup>th</sup> November 2021.

As regards the funding of entry tickets for Union Programmes, the payment of entry tickets for participation in the appropriate programmes and agencies, should be made through the 2021-2027 IPA 3 Financial Perspective. Funding of entry tickets is implemented on decentralised basis through the National Fund within the Ministry of Finance, whereby IPA share is projected within the budget of the Ministry of Finance, while the respective institutions are in charge of projecting the national share.

Union Programmes cover almost every area of the social and the economic life of European citizens: education, culture, youth, media, social affairs, development of small- and medium-sized enterprises, environment, transport, public health, legal cooperation, fight against violence, crime, terrorism, information society, customs duties and taxes. Legal entities, and in certain cases, natural persons (individuals) participated in the Programmes.

IPARD 2 Programme supports projects that will provide for attaining EU standards introduced in the field of agricultural production, food processing and rural development. In the period 2014-2020, total IPA funds in the amount of EUR 60 million are made available to the Republic of North Macedonia under this Programme.

2014 - 2020 IPARD Programme implementation is launched with 4 measures (Investments in physical assets of agricultural holdings, Investments in physical assets concerning processing and marketing of agricultural and fishery products, Farm diversification and business development and Technical assistance to Programme implementation), while preparation for accreditation of one more measure (Investments in rural public infrastructure) is commenced.

By May 2021, 2043 contracts have been concluded out of six public calls in total.

#### **4.3 IPA 3 - 2021-2027 Financial Perspective**

New 2021-2027 financial package is expected to increase by 6% compared to the previous IPA 2 package. IPA 3 will focus on several funds for investments via grants and loans and greater convergence. In addition, under IPA 3, EU focus is placed on the cooperation with EIB and EBRD, as well as the other international financial institutions, which will offer so-called "leverage" loans. IPA 3 should contribute to implementing "the Economic and Investment Plan for Western Balkans" adopted at the Summit in Zagreb in May 2020, aimed at encouraging intensified medium-term recovery, job creation and increased trade between Western Balkan countries and EU Member States, via funding major infrastructure projects in the field of transport, environment, digitalisation and energy, having regional importance and networking, as well as mature projects to be implemented in the next 4 years.

IPA 3 funds will be absorbed at national and regional level. Usage of funds under the Instrument for Pre-Accession Assistance IPA III for the 2021-2027 period, envisage 5 so-called categories as follows:

- Category 1: Rule of law, fundamental rights and democracy
- Category 2: Rule of law, legislation harmonisation, good neighbouring relations and strategic communication
- Category 3: Green agenda and sustainable connection
- Category 4: Competitiveness and inclusive growth
- Window 5: Territorial and cross-border cooperation

At national level, package of financial resources will range within the so-far EUR 80-100 million on annual basis. Under the national package, focus will remain at the start of the negotiations, adaptation of the administration to the intensive dynamics of reform, and the coordinative mechanisms, which should instigate the negotiating process, in line with the new methodology of accession negotiations, grouping in clusters and harmonisation of the negotiations by using IPA funds for the needs of the process of negotiations and the structural reforms in the whole society. Amount of financial resources at national level will depend on the readiness of the administration to prepare relevant and mature projects arising from the needs of the EU integration process, political commitment to implementing these projects, since IPA 3 is a competition among the beneficiary countries (Western Balkan countries and Turkey) within the so-called fair share.

At regional level, majority of the announced IPA 3 funds will be made available through the regional programmes, intended for providing support to the sectors transport, environment, energy, social support and digitisation. Therefore, what will be important is for these sectors to implement their long-term developed strategies defining the national priorities, as well as the trends arising from the European agenda, such as digitisation, broadband and fast Internet, energy projects and transformation towards decarbonisation, renewable energy sources, gas infrastructure, circular economy, clean environment, private business guarantees and traffic connection, etc. Our country will further have at its disposal of funds under the Western Balkans Investment Framework upon the principle of so-called blending of grants and loans. Mature projects ready for fast implementation will have a priority to be financed. Thereby, the new Fiscal Strategy will be more eased as regards the borrowing of capital from international financial institutions.

## 5. Public Debt

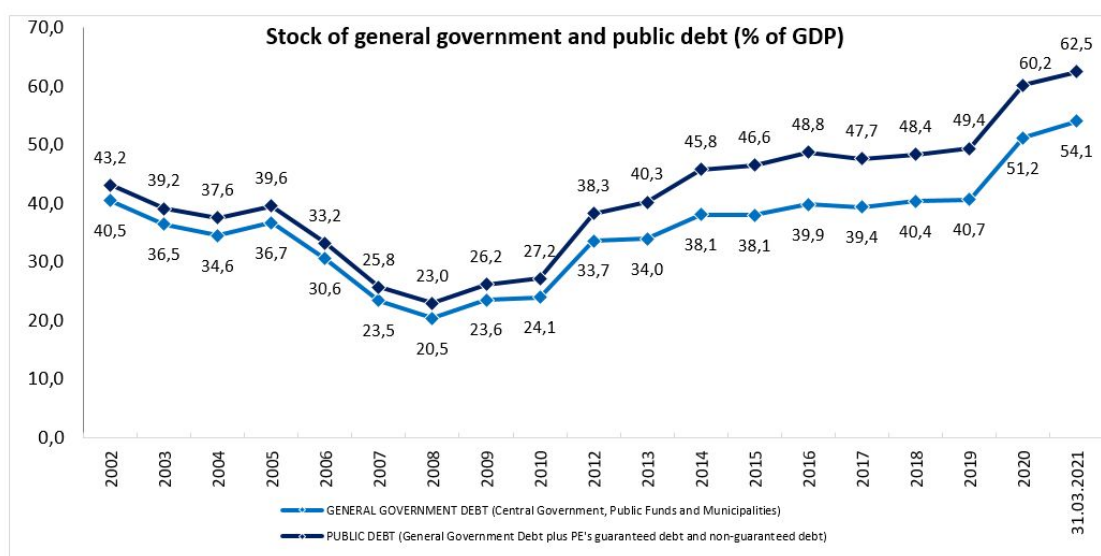
Efficient public debt management is of essential importance, encompassing reduced risks when designing the debt structure and debt management policy, all to the end of avoiding the possible inability to service the debt on regular basis and in a timely manner. The main objective is to ensure the funds necessary to finance the budget deficit and repay the due debt liabilities from the previous years, as well as funds for project financing, thereby not increasing the debt to a level that can jeopardise the stability of the economy and the economic growth of the country. Quality debt management, among other things, is determined on the basis of the institutional framework and the capacity to set and implement the public debt management policy. This implies clear definition of public debt management goals and measures.

In May 2019, the Parliament of the Republic of North Macedonia adopted the Law on Modifications and Amendments to the Law on Public Debt. Legal amendments were aimed at greater transparency, harmonisation with the international practice and greater credibility at international institutions and investors. Under the legal amendments, the public debt management policy has been turned into a separate Public Debt Management Strategy, to be prepared for a three-year medium-term period and adopted by the Government of the Republic of North Macedonia, upon proposal by the Ministry of Finance. Prior to adopting the legal amendments, public debt management policy was part of the Fiscal Strategy.

### 5.1. Amount of public and general government debt

General government debt of the Republic of North Macedonia amounted to EUR 6,207.8 million, i.e. it accounted for 54.1% of GDP on 31<sup>st</sup> March 2021. Central government debt accounts for the most in the general government debt, amounting to EUR 6,191.1 million, while the debt of the municipalities amounts to EUR 16.6 million. Total public debt comprises the general government debt and the debt of public enterprises and companies predominantly or fully owned by the state (guaranteed and non-guarantee debt), amounting to EUR 7,173.6 million on 31st March 2020, accounting for 62.5% of GDP.

Chart 16: Stock of General Government Debt and Public Debt



Central government debt accounted for 86.3% of the total general government debt at the end of the first quarter of 2021 and it is managed directly by the Ministry of Finance. As regards the other levels of debt, such as debt of municipalities and debt of public enterprises and companies predominantly owned by the state of the municipalities, Ministry of Finance participates in the process of borrowing, however, it cannot influence the intensity of withdrawing the funds under the concluded loan agreements.

Upon COVID-19 outbreak, the financing needs have been increased, resulting in larger borrowing on the international capital market. Thereby, the increased financing needs accompanied by reduced economic growth projections, have increased the public debt/GDP indicator. More thorough projections on general government and public debt trends will be presented in the 2022-2024 Public Debt Management Strategy (with prospects until 2026).



## 5.2. Guaranteed Debt and Risk against Calling-Up of Sovereign Guarantees

In order to ensure more favourable financing terms and conditions by the creditors, the state issues a sovereign guarantee, after carrying out analyses of the borrower and its ability to independently service its future liabilities. As for the new borrowings, account is taken of the long-term sustainability of public finance, whereby the process of issuing new guarantees is strictly regulated and subject to the borrowing procedure prescribed in the Public Debt Law, according to which the claimants of guarantees should fulfill certain criteria so as for the country to be able to issue guarantee. According to the latest amendments to the Law on Public Debt, management of contingent liabilities will be improved by strengthening the capacities as regards issuance of borrowing consents. In fact, Ministry of Finance performs credit analysis and assess the creditworthiness of public debt issuers when issuing sovereign guarantee in line with the prescribed assessment methodology. Such approach provides for harmonisation with the international practice on issuance of sovereign guarantees.

As of 31<sup>st</sup> March 2021 inclusive, the issued sovereign guarantees amount to EUR 927.5 million, accounting for 8.1% of GDP.

Although the guaranteed debt is an integral part of the public debt, it is published in a transparent manner, Ministry of Finance takes into account the risk related to contingent liabilities, i.e. the effects on the Budget in case the sovereign guarantees are potentially called up. This segment is more thoroughly explained in the section pertaining to fiscal risks, being an integral part of the Fiscal Strategy.

## 6. Comparative Analysis of Macroeconomic and Fiscal Projections for 2022-2026

### 6.1. Comparison with the Revised 2021-2025 Fiscal Strategy

2022-2026 Fiscal Strategy, compared to the revised 2021-2025 Fiscal Strategy of RNM does not present any deviations as regards the economic growth projections, whereby the deviations with respect to the external positions of the country, are minimal.

With respect to the external environment, gradual stabilisation of the global supply chains, as well as economic activity growth at our major trade partners are expected, which, coupled with the decreased pressures from the pandemic globally, are expected to have positive effect on the domestic economic developments in the coming period, both the foreign trade and the investments and consumption.

Economic growth, as in the previous Fiscal Strategy, is expected to be accompanied by domestic demand, amid positive contribution by both consumption and investments, while net export is expected to have negative contribution, to be gradually narrowed, amid solid growth of export and import.

Significant deviations have been recorded as regards unemployment, i.e. more dynamic drop of unemployment is expected in the medium term in relation to the previous Fiscal Strategy. In fact, by reducing the pressures from the health crisis, restoring of investors' confidence and improved expectations of business entities, labour demand is projected to experience intensified increase in the upcoming period, being also boosted by the support for domestic and foreign enterprises geared towards job creation.

Figure 8. Comparison of macroeconomic projections with the revised 2021-2025 Fiscal Strategy.

Indicators	Revised Fiscal Strategy 2021-2025					Fiscal Strategy 2022-2026				
	2021	2022	2023	2024	2025	2021	2022	2023	2024	2025
GDP, real growth rate (%)	4.1	4.6	5.2	5.6	5.9	4.1	4.6	5.2	5.6	5.9
Inflation rate (average)	1.5	1.8	2.0	2.0	2.2	2.1	1.8	2.0	2.0	2.0
Current account balance (% of GDP)	-2.9	-2.5	-2.0	-1.6	-1.3	-3.0	-2.4	-2.0	-1.6	-1.2
Net wage - nominal growth (%)	3.0	3.5	3.9	4.1	4.4	3.0	3.5	3.8	4.1	4.2
Unemployment rate (average)	15.8	15.0	14.1	13.2	12.4	15.8	14.4	12.9	11.4	9.9
Employment rate (average)	48.3	49.1	50.1	51.1	52.1	47.5	48.6	49.8	51.3	52.8

Source: Projections of Ministry of Finance

During the past period, economic activity was characterised by the implementation of health measures, having an impact on the budget revenue collection, and the expenditure side of the Budget faced increased needs in the field of health and social protection, being also coupled by the need to support the business sector and the citizens, as well as the need for additional targeted measures for revitalisation of the economy amid gradual loosening of the measures aimed at preventing COVID-19 and re-opening the economy.

With the immunisation process and the gradual improvement of the epidemiological situation, the investors' and consumers' confidence will increase, resulting in recovery of both investments and private consumption. With the recovery of the economy and the relaxation of the preventive health measures, the utilisation of the service capacities will be improved, thus contributing to boosted economic activity, economic growth and increased budget revenues.

Compared to the projections on the Budget of the Republic of North Macedonia, the 2022-2026 Fiscal Strategy of RNM indicates deviations in relation to the revised 2021-2025 Fiscal Strategy in relation to the fiscal projections (Table 9). In fact, the budget deficit as the main indicator of fiscal policy (although amended in absolute terms, as well as % of GDP), public finance fiscal consolidation is envisaged in the next period.

Regarding the projections of revenues and expenditures under the 2022-2026 Fiscal Strategy of RNM, projections have been changed in relation to the projections with the revised 2021-2025 Fiscal Strategy of RNM. On the revenue side, appropriate changes have been made in the projections, taking into account the good performance in the period January-April 2021, the expectations for economic growth, as well as maintaining the trend of revenue collection.

As for the expenditures, biggest deviations have been observed as regards subsidies and transfers (with respect to current expenditures) as a result of the undertaken measures for providing funds geared towards implementing the economic measures adopted by the Government of the Republic of North Macedonia, for the purpose of managing COVID-19-induced crisis, as well as the capital expenditures, all to the end of revising the level of funding projects in the field of road infrastructure.

Figure 9. Comparison of the medium-term projections for the Budget of NRM with the revised 2022-2026 Fiscal Strategy (Denar million)

	Revised Fiscal Strategy 2021-2025						Fiscal Strategy 2022-2026						Deviation 2021-2025/ 2022-2026				% of deviation			
Budget of the Republic of North Macedonia	Final account 2020	2021	2022*	2023*	2024*	2025*	2021	2022*	2023*	2024*	2025*	2026*	2022*	2023*	2024*	2025*	2022*	2023*	2024*	2025*
<b>Total revenues</b>	<b>189.554</b>	<b>212.630</b>	<b>223.532</b>	<b>239.216</b>	<b>257.032</b>	<b>278.142</b>	<b>212.630</b>	<b>233.217</b>	<b>251.273</b>	<b>273.525</b>	<b>296.815</b>	<b>321.844</b>	<b>9.685</b>	<b>12.057</b>	<b>16.493</b>	<b>18.673</b>	<b>12</b>	<b>23</b>	<b>18</b>	<b>22</b>
<b>Tax revenues and contributions</b>	<b>173.464</b>	<b>186.282</b>	<b>197.707</b>	<b>212.316</b>	<b>229.432</b>	<b>249.542</b>	<b>186.282</b>	<b>207.047</b>	<b>224.467</b>	<b>246.319</b>	<b>268.909</b>	<b>293.738</b>	<b>9.340</b>	<b>12.151</b>	<b>16.887</b>	<b>19.367</b>	<b>7</b>	<b>19</b>	<b>20</b>	<b>25</b>
Tax revenues	106.900	117.982	126.001	137.032	150.392	166.558	117.982	133.719	146.748	163.946	181.603	201.202	7.718	9.716	13.554	15.045	10	25	24	30
Contributions	66.564	68.300	71.706	75.284	79.040	82.984	68.300	73.328	77.719	82.373	87.306	92.536	1.622	2.435	3.333	4.322	2,3	3,2	4,2	5,2
<b>Non-tax revenues</b>	<b>11.173</b>	<b>16.954</b>	<b>16.317</b>	<b>17.246</b>	<b>17.746</b>	<b>18.246</b>	<b>16.954</b>	<b>16.516</b>	<b>17.152</b>	<b>17.352</b>	<b>17.552</b>	<b>17.752</b>	<b>199</b>	<b>-94</b>	<b>-394</b>	<b>-694</b>	<b>1,2</b>	<b>-0,5</b>	<b>-2,2</b>	<b>-3,8</b>
<b>Capital revenues</b>	<b>1.846</b>	<b>3.187</b>	<b>3.188</b>	<b>3.334</b>	<b>3.534</b>	<b>4.034</b>	<b>3.187</b>	<b>3.334</b>	<b>3.334</b>	<b>3.534</b>	<b>4.034</b>	<b>4.034</b>	<b>146</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>4,6</b>	<b>0,0</b>	<b>0,0</b>	<b>0,0</b>
Donations	3.071	6.207	6.320	6.320	6.320	6.320	6.207	6.320	6.320	6.320	6.320	6.320	0	0	0	0	0,0	0,0	0,0	0,0
<b>Total expenditures</b>	<b>243.421</b>	<b>247.567</b>	<b>252.483</b>	<b>265.172</b>	<b>281.515</b>	<b>297.251</b>	<b>247.567</b>	<b>265.876</b>	<b>279.687</b>	<b>298.863</b>	<b>320.406</b>	<b>344.338</b>	<b>13.393</b>	<b>14.515</b>	<b>17.348</b>	<b>23.155</b>	<b>5,3</b>	<b>5,5</b>	<b>6,2</b>	<b>7,8</b>
<b>Curent expenditures</b>	<b>227.306</b>	<b>223.512</b>	<b>226.593</b>	<b>233.344</b>	<b>245.878</b>	<b>259.270</b>	<b>223.512</b>	<b>233.286</b>	<b>240.975</b>	<b>251.696</b>	<b>269.593</b>	<b>284.459</b>	<b>6.693</b>	<b>7.631</b>	<b>5.818</b>	<b>10.323</b>	<b>3,0</b>	<b>3,3</b>	<b>2,4</b>	<b>4,0</b>
Salaries and contributions	29.775	31.394	31.562	31.662	33.062	34.062	31.394	31.862	31.962	32.062	33.562	34.062	300	300	-1.000	-500	1,0	0,9	-3,0	-1,5
Goods and services	15.423	21.322	22.068	23.418	25.418	27.718	21.322	22.568	24.418	26.418	29.718	32.718	500	1.000	1.000	2.000	2,3	4,3	3,9	7,2
Transfers to LSGUs	21.373	21.315	21.453	22.617	23.744	26.018	21.315	21.453	22.184	22.953	25.807	28.671	0	-433	-791	-211	0,0	-1,9	-3,3	-0,8
Subsidies and transfers	34.905	19.351	17.234	18.234	21.734	24.590	19.351	21.234	22.234	25.734	29.590	33.090	4.000	4.000	4.000	5.000	23,2	21,9	18,4	20,3
Social contributions	117.799	120.653	124.104	126.855	130.981	135.742	120.653	126.097	129.803	134.420	139.708	145.176	1.993	2.948	3.439	3.966	1,6	2,3	2,6	2,9
Interest payments	8.031	9.478	10.172	10.558	10.939	11.140	9.478	10.072	10.374	10.109	11.208	10.742	-100	-184	-830	68	-1,0	-1,7	-7,6	0,6
Domestic	2.742	3.069	3.580	3.938	3.939	3.940	3.069	3.603	3.904	4.151	4.471	4.782	23	-34	212	531	0,6	-0,9	5,4	13,5
Foreign	5.289	6.409	6.592	6.620	7.000	7.200	6.409	6.469	6.470	5.958	6.737	5.960	-123	-150	-1.042	-463	-1,9	-2,3	-14,9	-6,4
<b>Capital expenditures</b>	<b>16.115</b>	<b>24.055</b>	<b>25.890</b>	<b>31.828</b>	<b>35.637</b>	<b>37.981</b>	<b>24.055</b>	<b>32.590</b>	<b>38.712</b>	<b>47.167</b>	<b>50.813</b>	<b>59.879</b>	<b>6.700</b>	<b>6.884</b>	<b>11.530</b>	<b>12.832</b>	<b>25,9</b>	<b>21,6</b>	<b>32,4</b>	<b>33,8</b>
<b>Budget balance</b>	<b>-53.867</b>	<b>-34.937</b>	<b>-28.951</b>	<b>-25.956</b>	<b>-24.483</b>	<b>-19.109</b>	<b>-34.937</b>	<b>-32.659</b>	<b>-28.414</b>	<b>-25.338</b>	<b>-23.591</b>	<b>-22.494</b>	<b>-3.708</b>	<b>-2.458</b>	<b>-855</b>	<b>-4.482</b>	<b>12,8</b>	<b>9,5</b>	<b>3,5</b>	<b>23,5</b>
<b>Primary budget balance</b>	<b>-45.836</b>	<b>-25.459</b>	<b>-18.779</b>	<b>-15.398</b>	<b>-13.544</b>	<b>-7.969</b>	<b>-25.459</b>	<b>-22.587</b>	<b>-18.040</b>	<b>-15.229</b>	<b>-12.383</b>	<b>-11.752</b>	<b>-3.808</b>	<b>-2.642</b>	<b>-1.685</b>	<b>-4.414</b>	<b>20,3</b>	<b>17,2</b>	<b>12,4</b>	<b>55,4</b>
<b>Total revenues, % of GDP</b>	<b>28,5</b>	<b>30,1</b>	<b>29,6</b>	<b>29,6</b>	<b>29,5</b>	<b>29,5</b>	<b>30,1</b>	<b>30,9</b>	<b>31,1</b>	<b>31,4</b>	<b>31,5</b>	<b>31,6</b>					<b>1,3</b>	<b>1,5</b>	<b>1,9</b>	<b>2,0</b>
<b>Total expenditures, % of GDP</b>	<b>36,7</b>	<b>35,0</b>	<b>33,5</b>	<b>32,8</b>	<b>32,3</b>	<b>31,5</b>	<b>35,0</b>	<b>35,3</b>	<b>34,6</b>	<b>34,3</b>	<b>34,0</b>	<b>33,8</b>					<b>1,8</b>	<b>1,8</b>	<b>2,0</b>	<b>2,5</b>
<b>Budget balance, % of GDP</b>	<b>-8,1</b>	<b>-4,9</b>	<b>-3,8</b>	<b>-3,2</b>	<b>-2,8</b>	<b>-2,0</b>	<b>-4,9</b>	<b>-4,3</b>	<b>-3,5</b>	<b>-2,9</b>	<b>-2,5</b>	<b>-2,2</b>					<b>-0,5</b>	<b>-0,3</b>	<b>-0,1</b>	<b>-0,5</b>
<b>Primary budget balance, % of GDP</b>	<b>-6,9</b>	<b>-3,6</b>	<b>-2,5</b>	<b>-1,9</b>	<b>-1,6</b>	<b>-0,8</b>	<b>-3,6</b>	<b>-3,0</b>	<b>-2,2</b>	<b>-1,7</b>	<b>-1,3</b>	<b>-1,2</b>					<b>-0,5</b>	<b>-0,3</b>	<b>-0,2</b>	<b>-0,5</b>

## 6.2. Comparison with the projections of other national and international institutions

Taking into account the uncertainty over the protraction and the consequences of the health crisis, as well as the different assessments of the impact of the economic measures and the policies in the country in the short and medium term, different institutions have different expectations about the economic growth trajectory.

In line with the baseline scenario under the Fiscal Strategy, the economic growth in 2021 is projected at 4.1%, to be followed by growth intensification in the 2022-2026 period, accounting for 5.4% in average and being higher than the expectations of other institutions.

In fact, fiscal policy and redesigned public expenditures, with an emphasis on the public investment cycle, as well as the measures geared towards accelerated, inclusive and sustainable economic growth is expected to have significant impact on the economic activity in the medium term.

In addition, Growth Acceleration Financing Plan will provide for supporting investment activity, intensifying employment growth, boosting the competitiveness of the economy, and thus the potential for economic growth.

Table 10. Comparison of real GDP growth and inflation projections in North Macedonia

Institution	Real GDP growth (%)						Inflation rate (%)					
	2021	2022	2023	2024	2025	2026	2021	2022	2023	2024	2025	2026
IMF	3.8	4.0	3.7	3.5	3.5	3.5	2.0	1.5	1.6	1.9	2.0	2.0
World Bank	3.6	3.5	-	-	-	-	1.6	2.0	-	-	-	-
European Commission	3.7	3.8	-	-	-	-	1.7	1.7	-	-	-	-
NBRNM	3.9	3.9	4.0	-	-	-	2.2	2.0	2.0	-	-	-
Ministry of Finance	4.1	4.6	5.2	5.6	5.9	5.7	2.1	1.8	2.0	2.0	2.0	2.0

Source: IMF (World Economic Outlook, April 2021), World Bank (Western Balkans Regular Economic Report, April 2021), European Commission (European Economic Forecast, May 2021) and NBRNM (Quarterly Report, May 2021).

In addition, there are also differences in the level of budget deficit, with all institutions, as per the projections in the Fiscal Strategy, envisaging certain fiscal consolidation, i.e. gradual reduction of the budget deficit and preservation of government debt sustainability (Table 11).

Figure 11. Comparison of Projections on Budget Deficit and General Government Debt in North Macedonia

Institution	Budget balance (% of GDP)						General government debt (% of GDP)					
	2021	2022	2023	2024	2025	2026	2021	2022	2023	2024	2025	2026
IMF	-5.6	-4.2	-3.6	-3.4	-3.2	-3.0	53.8	54.9	55.5	55.9	56.0	56.0
World Bank	-5.3	-3.9					56.5	57.5				
European Commission	-4.1	-3.4					53.5	54.2				
Ministry of Finance	-4.9	-4.3	-3.5	-2.9	-2.5	-2.2	54.5	55.3	54.9	53.7	52.4	50.7

Source: IMF (World Economic Outlook, April 2021), World Bank (Western Balkans Regular Economic Report, April 2021) and European Commission (European Economic Forecast, May 2021)

## 7. Fiscal Risks and Sensitivity Analysis

Medium-term economic and fiscal projections are always accompanied by certain level of uncertainty and risks. Possible occurrence of these risks, reflecting conditions other than those taken as basis for the medium-term projections mentioned above, would result in deviations from the baseline medium-term scenario, i.e. different effects resulting from the movements of the key fiscal variables. Hence, this section of the Fiscal Strategy analyses the potential effects from the possible occurrence of several main macro-fiscal risks on the budget deficit and the general government debt.

### 7.1 Macro-Fiscal Risks and Sensitivity of Deficit and General Government Debt

This part of the Fiscal Strategy provides review of the results from the sensitivity analyses on sensitivity of budget deficit and level of general government debt to the possible effects of the four main identified risks to fiscal policy in the medium term. Thereby, all risks are analysed separately and all scenarios assume absence of other deviations from the baseline scenario and the effects only of certain risks:

- Scenario 1 - declined economic growth,
- Scenario 2 - lower tax revenues by 5%,
- Scenario 3 - lower execution of capital expenditures by 25% and
- Scenario 4 - servicing the liabilities on the basis of issued guarantees with Budget funds.

Taking into account that baseline medium-term fiscal projection is based on certain macroeconomic assumptions, they are considered to be a primary factor with a potential effect on the fiscal developments. Hence, as a first risk scenario, we assume materialisation of downside risks related to the protraction and the consequences of the health crisis, both in the country and globally, which might have repercussions on global supply chains and external demand, expectations of business entities and households, inflow of investments and foreign remittances and hence adverse consequences on the overall domestic economic activity. According to such scenario, projection on average GDP real growth between 2022 and 2026 is by 0.4 percentage points lower than in the baseline projection. Hence, possible lower economic growth will also imply lower performance of the cyclical component of budget revenues. Therefore, in relation to the baseline projection, this scenario would result in a higher budget deficit by 0.9 percentage points of GDP on average in the period 2022-2026, while the general government debt would be higher by 7 percentage points of GDP at the end of 2026.

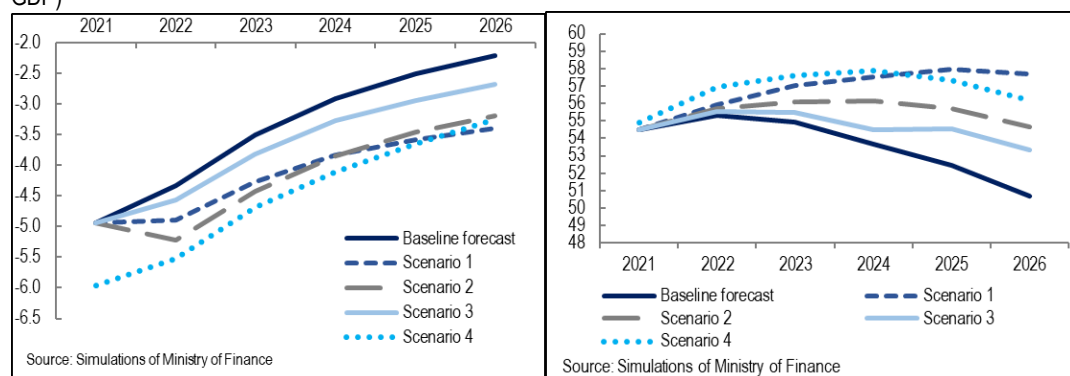
The second scenario assumes lower collection of tax revenues by 5% annually compared to the baseline projection. In conditions of unchanged level of budget expenditures and unchanged economic growth, lower tax revenues would lead to a higher budget deficit by 0.9 p.p. of GDP on average during the 2022-2026 period compared to the baseline projection, while the general government debt would be higher by 3.9 p.p. of GDP at the end of 2026 in relation to the baseline projection.

The third scenario assumes lower execution of capital expenditures, i.e. their execution at the level of 75% of the levels projected in the baseline projection, which is similar to the execution in the past. Reduced execution of capital expenditures would have adverse consequences on the gross investments growths, and respectively the economic activity growth in relation to the baseline scenario by 0.6% percentage points on average annually. This scenario would adversely affect tax revenues as well, which would exceed the effect of the reduced expenditures. Therefore, according to this scenario, budget deficit would be higher by 0.4 p.p. of GDP on average annually in the projection period compared to the baseline projection, while general government debt would be higher by 2.6 p.p. of GDP at the end of 2026 compared to the baseline projection.

The fourth scenario assumes that the liabilities falling due on the basis of principal and interest on loans guaranteed by the state to be fully serviced from the Budget of the Republic of Macedonia, which is an extreme assumption. The possible realisation of this extreme scenario will lead to higher budget expenditures in the period to come. In conditions of unchanged level of budget revenues and unchanged economic growth, this would lead to higher budget deficit by 1.1 p.p. of GDP on average annually in the period 2021-2026 compared to the baseline projection, while the general government debt at the end of 2026 would be higher by 5.4 p.p. compared to the baseline projection. Thereby, the effect of this scenario on the debt would be present throughout the medium-term period.

In summary, the realisation of any of the four risk scenarios, which reflect the main identified macro-fiscal risks in the coming period, would mostly result in relatively limited effects on the budget deficit and the general government debt (Figure 17). More precisely, the sustainability of fiscal policy in the medium run is in no case jeopardised.

Figure 17: Sensitivity Analysis of Budget Deficit (left) and General Government Debt (right) of Main Macro-Fiscal Risks (% of GDP)



In the course of 2021, economy is expected to recover, by carrying out the process of mass immunisation and improving the epidemiologic picture. Main imperative is to overcome the health crisis with least possible consequences on the economy, by which all jobs will be kept, and all those having lost their jobs, will get back on the labour market. If

necessary, additional economic measures geared towards supporting certain activities and sectors affected by the pandemic will be undertaken through an inclusive process, by involving all stakeholders. Additional economic measures would affect the expenditure side of the Budget, as well as increasing the budget deficit.

During the past period, public finance, amid numerous challenges, also including the health and the economic crisis, provided for timely payment of legal rights, i.e. regular and timely settlement of the liabilities of the state via an efficient and public consumption.

In the coming medium-term period, fiscal policy will be focused on consolidation of public expenditures, boosting the economic activity through capital expenditures and infrastructure investments, as well as improving the conditions for doing business and job creation.

Thereby, commitment to disciplined budget spending will continue to be pursued, with an emphasis on restrictiveness and control over less productive costs, on one hand, and increase of investments in capital projects on the other.

Set fundamental postulates of the fiscal policy in the coming period are planned to provide for gradual fiscal consolidation by gradually reducing the deficit level.