



North Macedonia Public Finance Review

Ensuring Stability and Boosting Resilience



Why are public finance reforms important?

Without accelerating structural reforms, with current low productivity and rising public debt, North Macedonia will face stifled prospects for recovery of growth and jobs.

With the right policy actions suggested in this report, North Macedonia has an opportunity to:

- enhance revenue collection and
- improve the efficiency of public spending.

1

Boosting Tax Revenues

North Macedonia's general government tax **revenues** are heavily reliant on indirect taxation and were at



below the

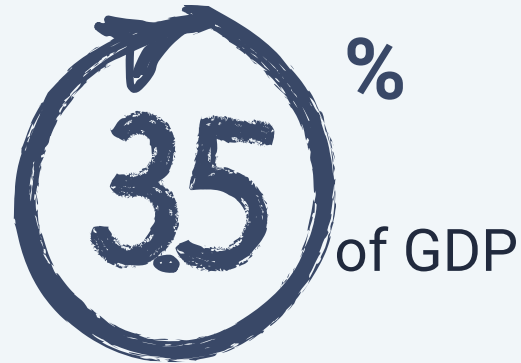
- EU27 average of



- WB6 peer countries average of



World Bank estimates suggest that there is potential to **raise** tax revenues to




to support fiscal consolidation and create fiscal space for more sustainable growth.

HOW:

- Rationalize exemptions
- Introduce taxation progressivity
- Increase environmental, health, and property taxation
- Strengthen tax administration.

2

Enhancing the Effectiveness of Public Administration

At  7.3 % of GDP

North Macedonia spends less on public administration than its EU peers, yet its public sector is comparatively large accounting for close to

 22 % of total employment

and performs poorly on indicators of government effectiveness and the rule of law, while its **productivity** is much lower than of the private sector.

The government could improve operational efficiency and professionalize public administration by:

- **Professionalizing** public and civil service, and introducing **performance-based reward and promotion**.
- **Removing** horizontal **wage inequity** across the administration
- **Investing** in promoting professional and high performing personnel based on strengthened performance management.

3

Rebalancing Local Government Finances

North Macedonia operates under a one-tier subnational government system with many relatively small local government units (LGUs).

Disparities across regions persist, with Skopje's GDP nearly  times higher than that of the Northeast region.

LGUs rely heavily on transfers from the central government, with **two-thirds** of local revenues coming from intergovernmental transfers.

North Macedonia's spending at the local government level stands at 5 percent of GDP.

To address these challenges, it is suggested to:

- **Monitor** the fiscal operations of LGUs to ensure fiscal prudence and alignment with national fiscal rules
- **Redefine** spending responsibilities to avoid duplication and overlap of functions, and to increase the accountability of LGUs
- **Consider** asymmetrical decentralization
- **Promote** greater subnational reliance on own-source revenues, especially property taxes
- **Consolidate and optimize** the structure of LGUs for balanced regional development.

4

Improving the Efficiency, Equity and Delivery of Health Care

Life expectancy at birth is lower than in many peer countries in the region and the EU average.

Public spending on health

5

% of GDP remains among the lowest among aspirational peers.

which contributes to a heavy reliance on out-of-pocket health payments at

42

% of health spending that equity concerns.

Spending efficiency is undermined by high rates of specialist visits and hospital admissions for ambulatory care sensitive conditions.

The following improvements are recommended:

- **Expand** the scope of primary care providers
- **Strengthen** health promotion and prevention including through **health taxes**
- **Improve** coordination across healthcare providers and between the health sector and other sectors
- **Develop** a sustainable system of long-term care services for an aging population
- **Reorganize** the inefficient hospital sector
- Continue to **invest** in the equipment, recruitment, knowledge, and skills of care providers.
- **Ensure** equitable access to healthcare and for medicines, in particular for the poor.

5

Strengthening Social Assistance

North Macedonia's spending on social assistance, at **1.7 % of GDP** in 2023, is **among the lowest** in the region, despite the increase over time .

Without social assistance programs, the **poverty rate would increase by 4** percentage points.

The **social assistance reform**, initiated in 2019, has shown some improvements in coverage and adequacy of benefits. Yet, targeting the poorest quintile **eroded** by 2021.

The following actions are recommended:

- **Sustain and accelerate** the shift towards poverty-targeted programs
- **Use a single, unified set of criteria** to assess eligibility for needs-based social assistance programs
- **Ensure access** to all eligible individuals and limit the error of inclusion.
- **Consider** an increase in coverage to protect households from emerging vulnerabilities
- **Consider** “make-work-pay” benefit reforms and **intensify** activation measures for the long-term unemployed
- **Strengthen** administrative and IT capacity.



Sustainability of the Pension System

North Macedonia's pension system faces:

- large deficits,
- potential erosion of benefit adequacy, and
- uneven benefit levels across generations.

The number of pensioners is projected to surpass the number of contributors by

2053.

Spending on pension benefits increased sharply to **9.3 percent of GDP** in 2023, above the levels of EU and Western Balkan peers.

Three policy proposals have been suggested to reduce the pension deficit in a rapidly aging society:

- **Reverse** the recently introduced price-wage pension indexation pattern back to previous indexation
- Gradually **increase and equalize** retirement ages for men and women
- Gradually **raise** contribution rates.

A combined policy package integrating all three policies could yield more balanced outcomes, preventing the further buildup of pension expenditures and deficits.

7

Financing The Future: Improving the Efficiency of Education Spending

North Macedonia's education spending has **declined to 3.8 percent of GDP** in 2023.

Over **80 percent** of the education budget goes to teachers' salaries, while capital spending remains severely underfunded.

The **student-teacher ratio declined** by 25 percent from 13 in 2009 to **9.7 in 2022**, which is far below the OECD average of **15 students per teacher**.

The current **school network** is costly to maintain and **is not aligned** with demographic and enrollment trends.

To address these challenges, it is essential to:

- **Optimize** the school network
- **Reassess** the student-teacher ratio and class-size requirements
- **Reallocate** resources to non-salary related spending
- **Introduce** new funding formula for primary education
- **Offer** support to families from vulnerable socioeconomic backgrounds to reduce the number of out-of-school children and **introduce** programs for learning recovery to reduce their learning gaps.
- **Expand** access to the internet in schools, **upscale** digital skills of teachers and students, and **increase** the capacity of education institutions to design and implement digital pedagogy.



Improving the Efficiency of Public Procurement

Public procurement in North Macedonia accounted for

11

% of GDP

or around

26

% of total general government spending in 2023.

The e-procurement portal increased transparency and enabled analysis of tendering practices and corruption risks.

However, a significant number of government institutions use procurement practices that create a high risk of corruption.

Recommendations to reduce public spending and increase value for money:

- **Improve** competition by increasing the number of participating bidders
- **Implement** a set of efficiency-enhancing measures within the existing legal framework to save the government 1.6 percent of GDP
- **Streamline** bidding documentation, training and revising guidelines,
- **Set** monitoring and control mechanisms,
- **Reduce** concentration among buyers and suppliers and the prevalence of single-bidder contracts.

9

Rationalizing Agriculture and Rural Development Subsidies

Public spending on agriculture and rural development in North Macedonia **declined to 0.75 percent of GDP**, but remains **double the EU average**.

Direct farm subsidies, often coupled with production, amounted to 83 percent of the agricultural support envelope.

Only 16 percent of the support envelope was directed to rural development.

The economic performance of subsidized farms lags behind that of non-subsidized ones, implying that the agricultural support policy mix needs to be revised.

The following actions are proposed:

- **Align** agricultural policies with the EU's Common Agricultural Policy
- **Eliminate** direct payment support to tobacco
- **Allocate** farm support towards high-value crops
- **Shift** to decoupled payments
- **Ensure** a just transition for vulnerable farmers
- **Support** farm agglomeration
- **Repurpose** rural development support towards capital investment and the adoption of innovative technologies
- **Remove** structural difficulties that hinder the clustering of very small farms into more efficient, larger units.