

Adjusting to Shocks, Mobilizing Untapped Potential



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Adjusting to Shocks, Mobilizing Untapped Potential

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Contents

Acknowledgments	iii
Abbreviations and Acronyms	ix
Overview	1
Recent Economic Developments	1
Outlook and Risks	4
Spotlight: Mobilizing Underutilized Human Capital	5
Chapter 1: Economic Update and Outlook	9
Growth slowed down amid weakening domestic demand and a subdued external environment	9
Employment gains slowed as labor demand eased and supply constraints tightened	13
Rising domestic cost pressures and local supply shocks pushed inflation higher across the region	16
Private sector credit expansion remained strong across the region, underpinned by robust banking sector resilience	20
External vulnerabilities increased, driven by strong domestic demand compounded by the still weak external environment	22
Expansionary fiscal policy has helped sustain economic activity but limited rebuilding of buffers	33
While medium-term outlook remains cautiously positive, external pressures cloud the short-term development agenda	38
Chapter 2: Spotlight: Mobilizing Underutilized Human Capital	48
The human capital of women is significantly underutilized	50
Youth struggle to translate human capital into employment due to skill mismatches	51
Gaps in job quality and pay are shaped by sectoral and occupational allocations	53
Enforcement of legal frameworks can promote women's economic participation	57
Labor market policies can be strengthened to incentivize employment among vulnerable individuals	62
Labor market policies targeting youth can improve education-to-work transitions	66
Expanded childcare services will be crucial to alleviate constraints on labor-force participation	68
Eldercare services are increasingly important to support labor force participation	72
Gig work can provide flexible job opportunities for economically inactive or unemployed workers	76
Enabling inactive workers to enter and thrive in the labor market	79

Country Notes	85
Albania	86
Bosnia and Herzegovina	90
Kosovo	94
Montenegro	98
North Macedonia	102
Serbia	105

Figures

Figure 1.1	Global growth remained resilient despite persisting geopolitical and trade tensions...	10
Figure 1.2	...while weakening domestic demand weighed on WB6 growth in 2025	10
Figure 1.3	Domestic demand continued support growth in 2025 although its contribution is weakening...	11
Figure 1.4	...while the contribution of net exports improved in selected economies	11
Figure 1.5	Services continued to drive growth in 2025...	12
Figure 1.6	...with sector-specific industry developments in some of the countries	12
Figure 1.7	Agriculture and services remain drag on employment from the demand side...	13
Figure 1.8	...while outmigration among other reasons intensifying supply side constraints	13
Figure 1.9	While growth in real average wages is strong in the region...	15
Figure 1.10	...productivity growth has started to outpace unit labor costs growth in several countries strengthening competitiveness	15
Figure 1.11	The pace of poverty reduction continues to slow	16
Figure 1.12	Global food prices edged up during the second half of 2025...	17
Figure 1.13	...as average headline and core inflation inch closer together	17
Figure 1.14	Policy rates	20
Figure 1.15	Exchange rate dynamics	20
Figure 1.16	Credit growth remained strong in 2025 with households continuing to outperform corporates	21
Figure 1.17	Banks remain well-capitalized with capital adequacy ratio above minimum requirements...	22
Figure 1.18	...with non-performing loan ratios at multi-year lows	22
Figure 1.19	Current account deficits widened in all countries except for Albania...	23
Figure 1.20	...as strong goods import growth outpaced export in 2025	23
Figure 1.21	Net FDI declined across the region with the largest drop in North Macedonia and Serbia...	24
Figure 1.22	...while remaining an important source of CAD financing	24

Figure 1.23	Total foreign investment annual inflows* by countries and years	25
Figure 1.24	Share of FDI inflows* in GDP	25
Figure 1.25	Trends in number of jobs created by the new FDI in the Western Balkans, 2010–2025	25
Figure 1.26	Capital expenditure per job, growth rates	26
Figure 1.27	Sectoral shift of new FDI-created jobs	27
Figure 1.28	The WB6 consistently invest more than they save, relying on external financing	29
Figure 1.29	More Diversified Exporters Are More Volatile, But Diversification Itself Is Not the Cause	31
Figure 1.30	Fewer Than 1 in 4 New WB6 Export Relationships Survive the First Year	32
Figure 1.31	Better logistics are associated with higher export survival	32
Figure 1.32	Average budgetary expenditures increased across the region...	34
Figure 1.33	...due mainly to higher spending on social benefits and wages	34
Figure 1.34	Elevated spending led to an increase in fiscal deficits for the second consecutive year...	35
Figure 1.35	...but this did not translate into increased PPG debt	35
Figure 1.36	Rising deficits narrowed fiscal buffers in selected countries...	37
Figure 1.37	...and the deficit coverage of government deposits varied across countries	37
Figure 1.38	The share of interest payments is set to increase in all countries except North Macedonia...	37
Figure 1.39	...due in part to a decline in concessional borrowing	37
Figure 1.40	GDP growth is expected to strengthen in the medium-term amid a more favorable external environment	38
Figure 1.41	As external conditions improve over the medium term, both current accounts and fiscal deficit are expected to narrow	40
Figure 1.42	Inflation is expected to remain elevated in 2026 with price pressures easing over the medium term	40
Figure 1.43	Iron and steel and electricity account for most CBAM exposure in the Western Balkans	46
Figure 1.44	Emissions intensity drives large differences in CBAM-related carbon costs for iron and steel	46
Figure 2.1	Unemployment remains high among women, youth and the low-educated...	49
Figure 2.2	...and labor-force participation rates are persistently low	49
Figure 2.3	Human capital outcomes in ECA	50
Figure 2.4	Men have higher expected lifetime productivity and earnings potential than women	51
Figure 2.5	Women substantially underperform in employment outcomes across the WB6	51
Figure 2.6	NEET rates remain high across WB6, especially among women...	52
Figure 2.7	...and tertiary-educated youth	52

Figure 2.8	Multidimensional job-quality indicators have improved due to rising formal employment	54
Figure 2.9	Pay gap is wide in market-oriented sectors	55
Figure 2.10	Pay gap persists across occupations	55
Figure 2.11	Female graduates exhibit slower transition to work and below average earnings	56
Figure 2.12	Transition quality varies depending on the field of study	56
Figure 2.13	Supportive framework to promote gender equality needs to be strengthened	57
Figure 2.14	Share of total compensation by firms' trading status	60
Figure 2.15	Labor earnings premium of trading firms relative to domestic-only firms	61
Figure 2.16	Distribution of compensation by gender ownership	61
Figure 2.17	The cost of formalization is high across the WB6	63
Figure 2.18	Wealthier and urban households use childcare more than poorer and rural households	70
Figure 2.19	Private childcare fees can consume a significant share of household income	70
Figure 2.20	Strong preference for in-home care of young children	70
Figure 2.21	LTC needs among the elderly are high...	73
Figure 2.22	...and the elderly population is rapidly increasing	73
Figure 2.23	Access to residential and home-based care is extremely limited in most WB6 countries	73
Figure 2.24	The share of women in online gig work varies across the WB6	76
Figure 2.25	A three-pillar strategy to mobilize untapped human capital in the Western Balkans	80

Boxes

Box 1.1	What are the drivers of inflation in the Western Balkans?	18
Box 1.2	Improving quality of foreign direct investments in the Western Balkans	24
Box 1.3	Export Diversification and Volatility in the Western Balkans: Firm-Level Evidence	31
Box 1.4	Regional Trade Exposure to the CBAM	44
Box 2.1	The Graduate Tracer Survey in North Macedonia	56
Box 2.2	Trading Firms and Job Creation for Women and Youth in WB6	60
Box 2.3	The FTR Methodology	64
Box 2.4	ALMP Pilots in the Western Balkans	65
Box 2.5	Private Sector Participation in LTC in North Macedonia	75

Tables

Table O.1	Western Balkans Economic Outlook (2022–2028)	7
Table 1	Across the region, short-term fiscal measures were introduced to mitigate the impact of the conflict in the Middle East on households and firms	42

Abbreviations and Acronyms

AEs	Advanced Economies
CAD	Current Account Deficit
BAM	Bosnia and Herzegovina Convertible Mark
CBAM	Carbon Border Adjustment Mechanism
CPI	Consumer Price Index
ECB	European Central Bank
ETS	Emissions Trading System
FDI	Foreign Direct Investment
GDP	Gross Domestic Product
HICP	Harmonized Index of Consumer Prices
ICT	Information and Communication Technology
IMF	International Monetary Fund
LEK	Albanian Lek
LFS	Labour Force Survey
MRV/MRVA	Monitoring, Reporting, and Verification / and Accreditation
NEET	Not in Education, Employment, or Training
NPL	Non-Performing Loan
NTM	Non-Tariff Measures
PPG	Public and Publicly Guaranteed Debt
PPI	Producer Price Index
PPP	Purchasing Power Parity
RER	Regular Economic Report
RGF	Reform and Growth Facility
RRF	Recovery and Resilience Facility
SME	Small and Medium-sized Enterprise
SOE	State-Owned Enterprise
VAT	Value Added Tax

Western Balkan Country Abbreviations

ALB	Albania
BiH	Bosnia and Herzegovina
KOS	Kosovo
MKD	North Macedonia
MNE	Montenegro
SRB	Serbia
WB6	The six countries collectively grouped as the Western Balkans

Note: All comparisons are year-on-year unless otherwise stated.

Overview

Overview

Recent Economic Developments

Prior to the outbreak of the current conflict in the Middle East, the six Western Balkan economies (WB6) had been expecting a relatively benign 2026; however, those expectations have now changed, as ongoing geopolitical shocks are likely to result in weaker growth, higher inflation, and amplified uncertainty. Growth forecasts for 2026 have been revised downward across all WB6 since the Fall 2025 edition of the RER from 3.1 percent to 2.8 percent, reflecting the impact of the conflict in the Middle East, as assessed in late March, and country-specific domestic developments. However, the situation has continued to evolve since then and may lead to further revisions. The impact of the conflict is expected to come primarily through rising imports costs, especially for fuel and fertilizers, which are expected to push up inflation and thereby weigh on private consumption, and to widen the current account deficit, alongside additional pressure from weaker euro area demand for exports. Investment will also be affected owing to the tighter financing conditions and weaker investor sentiment.

Reflecting global and regional dynamics, aggregate growth in the WB6 slowed from 3.7 percent in 2024 to an estimated 2.6 percent in 2025.¹ Serbia experienced the sharpest deceleration, driven by a poor agricultural season, sanctions in the oil sector, lower private investments, and

domestic political volatility. Growth also slowed in Bosnia and Herzegovina and in Montenegro, due largely to the poor performance of the industrial sector, while in Kosovo domestic political uncertainty weighed on investment activity and weakened reform momentum. By contrast, growth held broadly stable in Albania and accelerated in North Macedonia, driven by rising household consumption and public infrastructure investment. Both countries also made important progress on their EU accession efforts during the year.

Slowing growth in the WB6 reflects a broader shift in the drivers of economic activity. Consumption continued to be the primary source of growth across much of the region in 2025, while investment and exports were relatively subdued. Consumption was underpinned by continuing wage growth and sustained credit expansion, though its contribution declined as rising prices exerted pressure on real incomes. Investment supported growth more modestly in 2025 compared to 2024, as public investment only partially offset modest levels of private investment. Net exports were negative overall, due to subdued external demand, though export flows increased in several countries.

Employment growth in the WB6 slowed sharply in 2025, reflecting weaker economic activity, downturns in specific sectors, and persistent structural constraints on job creation. Average

¹ | Comparisons are year-on-year unless stated otherwise.

employment growth slowed from 1.8 percent in 2024 to just 0.1 percent in 2025. Agriculture and industry were the primary drag on employment, with an unfavorable agricultural season compounded by contracting private investment. While services emerged as the main source of employment growth, supported by robust tourism and other service exports, the sector was unable to compensate for the broader slowdown in job creation. Meanwhile, demographic pressures, emigration, high youth unemployment rates, and persistent gender gaps in labor force participation increasingly constrained the labor supply. Youth unemployment rate remained high at 25 percent, well above EU average of 14.7 percent with Bosnia and Herzegovina reporting the highest rate in the region at 32.8 percent, and Kosovo recorded lowest rate at 18.4 percent. Gender gaps in labor force participation ranging from 13.3 ppts in Albania to approximately 34 ppts in Kosovo, point to significant underutilized labor potential across the region. In this context, supporting job creation and realizing the potential of the region's human capital, particularly women, youth, and other groups facing barriers to work, will be essential to ease structural labor constraints, sustain economic growth, and safeguard long-term fiscal and social sustainability (see Chapter 2).

Poverty continued to fall, supported by higher real incomes and credit growth, although the pace of poverty reduction also continued to slow down. The poverty rate, measured at the \$8.3/day (2021 PPP) line is estimated to be 14.1 percent of the population in 2025. Real wages across the region continued to rise in

2025, although at slower pace compared to a year before, driven by minimum wage increases and tightening labor markets in several countries. Rising wages contributed to higher unit labor costs across most of the region in 2025, although the pace of increase moderated compared to 2024.

Following a sharp decline in 2024, the regional headline inflation across the Western Balkans picked up to 3.7 percent in 2025, driven by higher food prices, as well as rising services and utility prices.

All countries in the region experienced a faster rate of inflation in 2025 compared to the year before. Growth in incomes, supported by increases in minimum wages, social transfers, pensions, and consumer credit, as well as rising utilities prices in several countries and food prices due to local shocks, including droughts, floods, and a poor agricultural season contributed to broad-based inflationary pressures across the region. Core inflation for the Western Balkans declined from 4.3 percent in 2024 to 3.8 percent in 2025, slightly above headline inflation.

Sustained consumer confidence, a buoyant housing market, and strong corporate credit demand supported the growth of private-sector credit in 2025.

Household credit expanded by an average of 16.9 percent at the regional level, outpacing corporate lending, as demand for mortgage loans and consumer credit remained robust. Corporate lending grew by 12.5 percent, underpinned by rising fixed investment, increased working-capital financing, and positive developments in the small and medium enterprise (SME) sector. Increased lending has not undermined

credit quality. Across the region, capital adequacy ratios remain robust and well above regulatory minimums at an average of about 19.6 percent, underscoring the sector's strong loss-absorption capacity.

A combination of weak external demand and expansionary domestic policies put pressure on the external accounts, and the regional current account deficit widened from 6.4 percent of GDP in 2024 to 7.3 percent in 2025. Heightened trade policy uncertainty, increased trade barriers and import tariffs, and disruptions in global value chains weighed on the economic performance of key external partners, particularly EU economies. Montenegro, North Macedonia, and Kosovo registered the largest increases in their current account deficits, as higher demand for construction and consumption goods boosted imports while merchandise exports grew marginally or declined. Net services exports, including tourism, continued to bolster current accounts across the region, though the average services trade surplus narrowed slightly by 0.2 percentage points (ppts) of GDP in 2025. Net foreign direct investment (FDI) inflows fell from 5.4 percent of GDP in 2024 to 4.0 percent in 2025, with North Macedonia and Serbia recording the sharpest declines. Nevertheless, positive net FDI continued to finance a meaningful share of current account deficits across the region, ranging from about 32 percent in Montenegro and North Macedonia to around 80 percent in Bosnia and Herzegovina.

On the fiscal side, governments across the region actively supported economic activity through higher public spending

in 2025, which, despite robust revenue growth, pushed fiscal deficits wider.

Revenues reached 36.2 percent of GDP, the region's strongest revenue performance since 2012, supported by buoyant value-added tax (VAT) and personal income tax (PIT) collection. Public spending increased by 0.8 ppts of GDP to 38.8 percent in 2025, as governments implemented policies to support household incomes while increasing capital expenditures. As a result, the average fiscal deficit for the WB6 widened from 2.1 percent of GDP in 2024 to 2.6 percent in 2025. This trend was most pronounced in Montenegro and Albania, which saw their fiscal deficits widen by about 1 ppt of GDP to 4.3 and 1.7 percent, respectively. North Macedonia was the only country to narrow its fiscal deficit, which shrank from 4.5 percent of GDP in 2024 to 4 percent in 2025. Primary fiscal balance remained negative across all countries except Albania, which recorded a surplus for the third consecutive year, albeit modest at 0.3 percent of GDP in 2025, down from 1.4 percent of GDP in 2024.

Despite wider deficits, regional public and publicly guaranteed (PPG) debt continued to fall across most WB6 countries.

Regional PPG debt levels have declined steadily since 2020 and reached 44.4 percent of GDP in 2025. Albania, North Macedonia and Serbia recorded the steepest declines, driven by faster nominal GDP growth, the use of government deposits to cover financing needs and by exchange rate appreciation in Albania. Only Montenegro bucked the regional trend: its PPG debt stock rose by 4.1 ppts of GDP to 63.9 percent as the government attempted

to build a liquidity buffer ahead of an upcoming external debt repayment.

Financial market conditions were relatively favorable in 2025 but started to tighten in 2026. Albania, Bosnia and Herzegovina, and Montenegro all placed Eurobonds in 2025, while North Macedonia tapped external markets in January 2026, and Serbia focused on domestic borrowing for 2025 deficit financing. However, rising geopolitical tensions in early 2026 have already begun to affect financing costs for the WB6. Between September 2025 and end-March 2026, yields in all WB6 countries rose by about 0.6 to 1.4 ppts, reflecting a higher risk premium on developing country debt.

Outlook and Risks

Regional GDP growth is projected to slow to 2.8 percent in 2026, amid heightened uncertainty and the adverse impact of the conflict in the Middle East, before gradually recovering to 3.2 percent in 2027 and 3.7 percent in 2028. The near-term outlook has weakened, largely reflecting geopolitical tensions, external pressures which have driven up import prices and are expected to weigh on euro area demand and country-specific developments, which raises risks of slower-than-expected pace of reforms implementation.

Economic performance is projected to vary significantly across the WB6. Kosovo is expected to post the region's highest growth rate at about 3.7 percent in 2026, supported by more stable political conditions. Serbia, the region's largest

economy, is expected to see its growth 0.3 ppts lower in 2026 compared to the fall 2025 forecast due to continued problems in SOEs, lack of progress in the next stage of structural reforms, and global and domestic uncertainty. Bosnia and Herzegovina is projected to record the lowest growth rate in the region at 2.5 percent, driven by weaker export performance on the back of adverse impact from the EU Carbon Border Adjustment Mechanism (CBAM), and limited political momentum to advance the reform agenda. Growth in Albania is projected at 3.4 percent, bolstered by the continued expansion of tourism, unless the conflict raises travel costs and disrupts routes, while Montenegro and North Macedonia are expected to post growth rates slightly above the regional average at 2.9 percent. Inflation across the region is projected to rise to an average of 3.9 percent in 2026, driven by higher energy and food prices alongside continued demand-supporting fiscal policies, with higher inflation rates in four of the six countries. Over 2027–28, regional growth is expected to strengthen gradually and remain above the euro area's projected growth rate of 1.3–1.4 percent, implying that convergence will continue over the forecast period.

Risks to the outlook remain heavily tilted to the downside, reflecting a combination of domestic and external factors. Upcoming elections in Bosnia and Herzegovina, North Macedonia, and Serbia could increase policy uncertainty, delay investments, or slow the implementation of EU-aligned reforms under the Reform and Growth Facility (RGF). Contingent liabilities from state-owned enterprises (SOEs) and public-private partnerships

(PPPs) could limit fiscal flexibility, especially in Kosovo, Montenegro, and Serbia. External headwinds, including a weaker-than-expected euro area recovery and higher global uncertainty, could weigh on exports and investment, particularly in manufacturing-intensive economies. A significant escalation of geopolitical tensions stemming from the conflict in the Middle East—with more severe shipping disruptions through the Strait of Hormuz—could push energy and food prices higher for longer, amplify financial market volatility, and raise borrowing costs. Finally, the EU CBAM, which has taken effect in 2026, represents an additional source of cost and competitiveness risk for carbon-intensive exports in the WB6.

On the upside, WB6 growth could benefit from faster reform implementation, stronger institutional capacity, and greater policy stability. Effective execution of the RGF could enhance investment efficiency, reduce regulatory bottlenecks, and support competitiveness. Reduced domestic uncertainty in Bosnia and Herzegovina, Kosovo, and Serbia could significantly improve the business climate and strengthen private-sector confidence. Externally, a stronger-than-anticipated performance in the euro area would support exports, investment, and remittances in the WB6. Easing geopolitical tensions could lower energy prices, reduce volatility and risk premia, strengthen investor confidence, and ease inflationary pressures, supporting regional economic activity. The CBAM could also spur investment in decarbonization and energy efficiency in the WB6, helping firms in carbon-intensive

manufacturing sectors strengthen their competitiveness over the medium term.

Sustaining growth in the WB6 over the medium term will require faster reform implementation and stronger institutions, complemented by decisive action to unlock the region's human capital potential. Structural constraints continue to weigh on the region's competitiveness: unit labor costs outpace productivity growth, employment remains concentrated in low-productivity sectors, and labor markets face a central paradox where labor shortages coexist with high unemployment, low participation, and sustained outmigration. Tapping into the potential of underrepresented groups, particularly women and youth, will be essential to easing these constraints and safeguarding long-term growth and fiscal sustainability.

Spotlight: Mobilizing Underutilized Human Capital

Despite rising education levels, the countries of the Western Balkans continue to underutilize their human capital. Widespread inactivity, high unemployment rates, and pervasive underemployment persist across the region, especially for women and youth. Low labor-force participation and employment rates among these groups represent not only an equity challenge but also a missed opportunity to boost productivity, resilience, and growth.

Rapid population aging, along with continued outmigration, compounds these challenges. The WB6 countries are

among the most rapidly aging in Europe and are projected to become super-aged (defined as having at least one-fifth of the population aged 65 and above) within the next decade, intensifying labor shortages that are already emerging in several sectors. These pressures are further intensified by sustained outmigration of working age populations across skill levels and by reported labor shortages, even as unemployment and inactivity remain high.

However, capitalizing on the full and untapped potential of the workforce, especially women and youth, provides the region with a development opportunity.

In this context, realizing the potential of the region's human capital—particularly women, youth, and other groups facing barriers to work—will be vital to mitigate labor constraints, sustain economic growth, and support long-term fiscal and social sustainability. Raising participation rates to the same level as comparators in the EU would add over 2.8 million people to the regional labor market. Under assumptions of sufficient labor demand and no labor market frictions, a comparable increase in female participation could raise the region's annual GDP growth by about 0.35 ppts.

Mobilizing underutilized human capital in the WB6 will require a comprehensive and coordinated reform agenda.

Key priorities include: (i) reducing labor-market disincentives through targeted reforms to tax and social benefit systems and alleviating constraints linked to childcare and eldercare responsibilities; (ii) aligning skills with employer demand while supporting vulnerable jobseekers and youth not in employment, education, or training (NEET) through strengthened activation, guidance, and employment services; and (iii) expanding access to inclusive, high-quality job opportunities by promoting nondiscriminatory, flexible, and decent work environments, including for platform-based gig workers.

Table O.1 Western Balkans Economic Outlook (2022–2028)

	2022	2023	2024	2025e	2026f	2027f	2028f
Real GDP growth (percent)							
Albania	4.8	4.0	4.0	3.9	3.4	3.7	3.6
Bosnia and Herzegovina	4.2	2.0	3.2	2.1	2.5	3.0	3.2
Kosovo	4.3	4.1	4.6	3.6	3.7	3.9	4.0
North Macedonia	2.8	2.6	3.0	3.5	2.9	3.0	3.0
Montenegro	7.7	6.5	3.2	2.7	2.9	3.1	3.1
Serbia	2.7	3.7	3.9	2.0	2.7	3.0	4.0
WB6	3.6	3.5	3.7	2.6	2.8	3.2	3.7
Contribution to real GDP growth (ppts)							
Consumption	2.9	1.0	3.2	2.7	2.4	2.6	2.9
Investment	1.1	-0.1	1.8	1.5	1.1	1.3	1.2
Net exports	-1.1	2.4	-2.0	-1.7	-0.7	-0.7	-0.5
Exports	6.5	1.3	1.3	2.7	2.4	2.7	2.7
Imports (-)	7.6	-1.1	3.3	4.4	3.1	3.4	3.2
Consumer price inflation (percent, period average)	11.9	9.1	3.3	3.7	3.9	3.2	2.6
External sector (percent of GDP)							
Goods exports	27.9	24.1	21.9	21.1	20.9	20.9	20.7
Trade balance	-19.3	-14.7	-15.9	-16.3	-17.3	-16.9	-16.5
Current account balance	-7.5	-4.0	-6.4	-7.3	-7.6	-7.2	-6.8
Foreign direct investment	6.8	5.2	5.4	4.0	4.4	4.6	4.6
External debt	75.1	66.5	64.9	47.5	47.5	47.0	46.4
Public sector (percent of GDP)							
Public revenues	34.4	35.1	35.9	36.2	36.3	36.3	36.3
Public expenditures	37.0	36.5	38.0	38.8	38.9	38.6	38.3
Fiscal balance	-2.7	-1.4	-2.1	-2.6	-2.6	-2.4	-2.1
Public and publicly guaranteed debt	49.5	44.9	44.8	44.4	44.7	44.3	44.0

Sources: National statistical offices; Ministries of Finance; central banks; World Bank staff estimates.

Note: e = estimate; f = forecast. World Bank projections with cut-off date of March 25, 2026.

Chapter 1: Economic Update and Outlook

Chapter 1: Economic Update and Outlook

Growth slowed down amid weakening domestic demand and a subdued external environment

Global growth remained subdued but more resilient than expected in 2025 amid persistent geopolitical tensions, rising trade barriers, and elevated policy uncertainty. At 2.8 percent², global growth exceeded expectations, supported by front-loading of trade ahead of expected tariff increases, easier global financial conditions, and a surge in AI-related investment (Figure 1.1). Growth in advanced economies remained broadly steady despite higher trade tensions and policy uncertainty, with the immediate drag proving less pronounced than expected. Activity, however, remained modest. The euro area is estimated to have grown by 1.4 percent, surprising to the upside, supported by easing financing conditions, the continued rollout of the Recovery and Resilience Facility (RRF) in the EU, relatively steady labor markets, export front-loading, and the timing of tariff increases. Growth in EMDEs was stronger than expected, with activity in China more robust than anticipated, supported by fiscal stimulus and increased shipments to non-U.S. markets, including Europe. Many other EMDEs also benefited from stronger net exports and firmer investment. Global headline inflation increased slightly to 2.8 percent while moving closer to central bank targets, reflecting firmer inflation in some advanced economies, and particularly in goods prices in the United States. In

contrast, goods inflation eased in many EMDEs as demand for tradables softened following earlier stock-building. Overall, tariff pass-through to goods prices has so far been more limited than initially anticipated.

The outbreak of the Middle East conflict in early 2026 has shifted global economic risks to the downside. Disruptions in commodity markets have pushed energy prices higher and triggered significant volatility across financial markets, while elevated geopolitical and trade uncertainty and disrupted supply chains continue to weigh on global economic prospects. Weaker cross-border investment and rising financing costs add further pressure, constraining growth and complicating borrowing conditions. The euro area, the primary trading partner of the WB6, is particularly exposed, given its reliance on imported oil and gas, with additional headwinds expected from weaker external demand and subdued private investment.

Growth in the Western Balkan countries (WB6) slowed down sharply from 3.7 percent in 2024 to 2.6 percent in 2025, driven by weakening domestic demand despite better performance of net exports (Figure 1.2). The moderation in domestic demand reflected the combined impact of rising inflationary pressures, heightened domestic political uncertainty, and labor supply constraints. The sharpest growth slowdown is estimated in Serbia, where political developments weighted on

² Growth numbers based on consensus forecast as of April 13, 2026.

Figure 1.1 Global growth remained resilient despite persisting geopolitical and trade tensions...

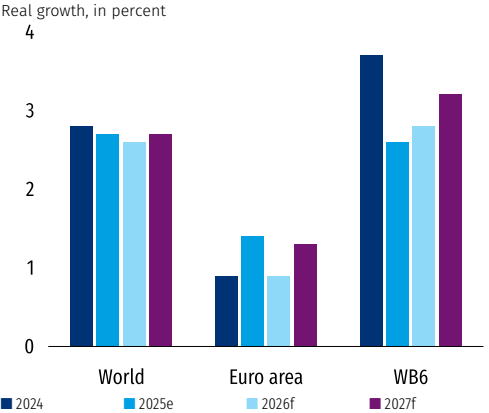
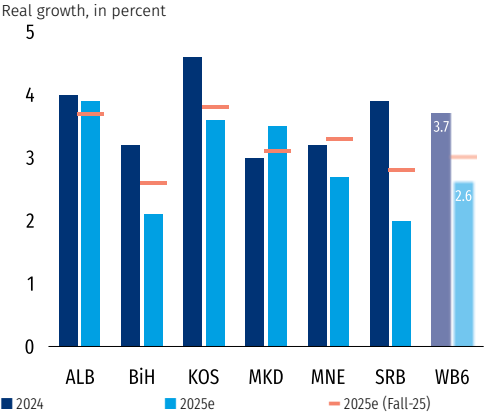


Figure 1.2 ...while weakening domestic demand weighed on WB6 growth in 2025



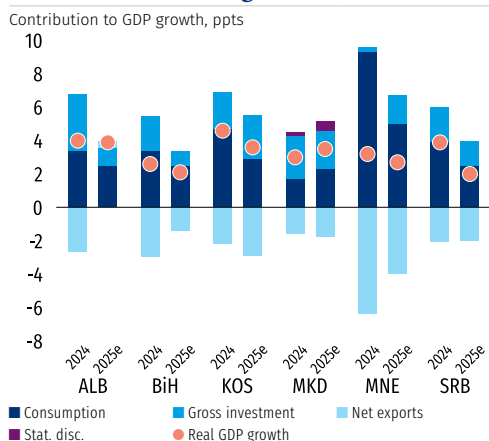
consumption and investment decisions, in particular in private sector, pushing growth down by 1.9 ppts compared to 2024. In Bosnia and Herzegovina and Kosovo growth also decelerated by 1.1 and 1 ppts, respectively, reflecting weaker domestic demand in Bosnia and Herzegovina and higher political uncertainty that weighed on investment activity and reform momentum in Kosovo. In contrast, growth in North Macedonia is estimated to have accelerated by 0.5 ppts, driven by public infrastructure investments, household consumption, as well as some export improvements.

While consumption continued to drive regional growth in 2025, its contribution weakened year-on-year, which accounted for a significant share of the overall growth slowdown. On average, consumption contributed 2.7 ppts to regional growth in 2025, down from 3.2 ppts in 2024, with five of the six economies recording a lower contribution (Figure 1.3). A rise in inflation eroded real incomes, partly offsetting the positive impact of continued wage growth, an accelerating expansion in

private credit, and rising levels of public current spending. Private credit grew by an average of 16.9 percent, with rates ranging from 10.9 percent in North Macedonia and 12.2 percent in Bosnia and Herzegovina to above 19 percent elsewhere. Public current spending increased as a share of GDP in all countries except Montenegro, where it remained stable. Nevertheless, the contribution of consumption to growth declined in five of the six economies. These dynamics were further compounded by near-negligible employment growth, declining remittances, and a contracting labor force, all of which weighed on consumption across the region helping to explain why consumption, while still the dominant growth driver, made a smaller contribution to growth in 2025.

Along with consumption, investment continued to support growth in 2025, but its contribution weakened as public investment only partly compensated for declines in private investment. The contribution of investment to average regional growth declined from 1.8 ppts in

Figure 1.3 Domestic demand continued support growth in 2025 although its contribution is weakening...

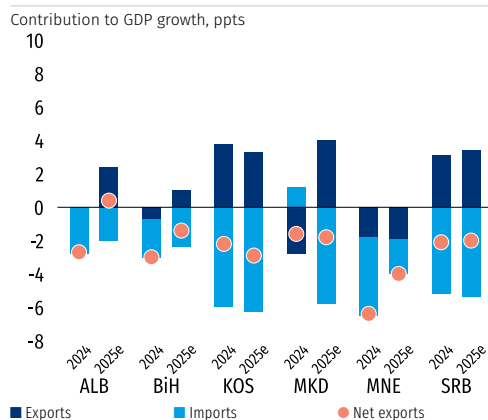


Source: Regional statistics offices, World Bank staff estimates.

Note: Data for BiH by expenditure side revised in 2026 for entire series.

2024 to 1.5 ppts in 2025 (Figure 1.3). This trend occurred despite several supportive factors, including double-digit corporate credit growth rates in Serbia, Montenegro, and North Macedonia; robust construction activity in Albania and Kosovo; and higher public capital spending in the energy and transport sectors in Montenegro and North Macedonia, respectively. In addition to supporting investment activity, these factors contributed to higher imports and a widening trade deficit. In Bosnia and Herzegovina, the positive contribution of investment was largely driven by inventory accumulation, likely reflecting firms' anticipation of the EU's continued implementation of the CBAM, which is weakening the competitiveness of carbon-intensive exports such as aluminum, steel, and electricity. At the same time, investment conditions were less supportive in several countries, as reflected in a sharp decline in FDI inflows. In Serbia, FDI fell by about 50 percent in euro terms (3 ppts of GDP) due to lower equity investment,

Figure 1.4 ...while the contribution of net exports improved in selected economies



and in North Macedonia FDI declined by around 60 percent (5.2 ppts of GDP), reflecting reduced debt and equity inflows.

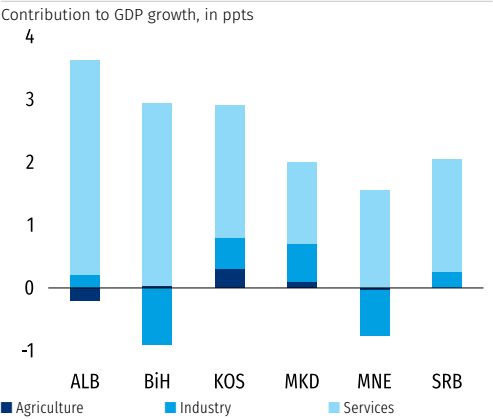
Although the contribution of net exports to growth remained negative amid subdued external demand, total exports increased in several countries. On average, net exports reduced regional growth by an estimated 1.7 ppts in 2025, down from 2 ppts in 2024, as a gradual export recovery partially offset rising imports. Meanwhile, the contribution of total exports to regional growth rose from 1.3 ppts in 2024 to 2.7 ppts in 2025: a rebound in automotive production linked to the European market boosted merchandise exports in Serbia and North Macedonia; a stable tourism season increased service exports in Albania and Montenegro; and the strong performance of travel, information technology, and business services bolstered service exports in Kosovo. In Montenegro, net exports were a drag on growth, as electricity exports plunged due to the nine-month closure of

the Pljevlja power plant for upgrades, which compounded an existing merchandise trade deficit and outweighed robust growth in the service sector (Figure 1.4). At the regional level, total imports slashed growth by an estimated 4.4 ppts, up from 3.3 ppts in 2024, due to strong investment-related demand and higher food imports in a weak agricultural year.

On the supply side, growth in 2025 was increasingly driven by services and construction, while agriculture and parts of industry faced headwinds. Services continued to drive growth in the WB6, with gains in tourism, transportation, administrative support, and information technology. Travel and tourism were key contributors to growth in Albania, Kosovo, and Montenegro. The construction sector’s performance was strong in Albania, Kosovo,

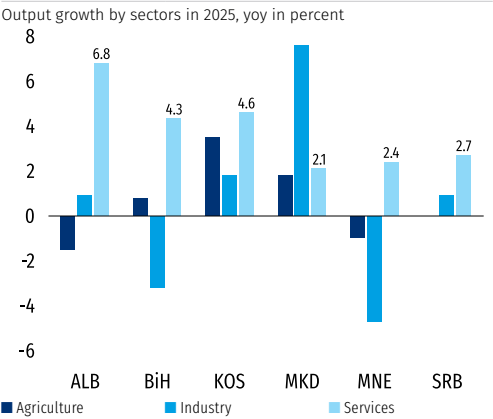
and North Macedonia, with the latter’s gains closely tied to ongoing highway investments. Bosnia and Herzegovina recorded the greatest negative industrial contribution to growth, reflecting persistently weak demand among its main trading partners, primarily key EU markets, while reduced electricity generation hampered the performance of Montenegro’s industrial sector. Industrial production rebounded modestly in North Macedonia, albeit from a low base year-on-year, while in Serbia scaled up FIAT production at the Kragujevac automotive plant supported overall industrial performance. Adverse weather conditions weakened agricultural output in Albania, Montenegro, and Serbia in 2025 compounded by food supply vulnerabilities in addition to existing structural challenges³ (Figure 1.5 and 1.6).

Figure 1.5 Services continued to drive growth in 2025...



Source: World Bank staff estimates.

Figure 1.6 ...with sector-specific industry developments in some of the countries



3 The latest Serbia Policy Notes suggest that the major issues impacting agricultural sector development include an aging farm labor force, high labor intensity, low efficiency and use of technology, a poorly functioning land market, low financial liquidity, low access to credit, and underinvestment, as well as the limited participation of very small and fragmented landholders (78 percent of them operate on less than 5ha) in higher value agri-food value chains. Other challenges include inadequate irrigation systems,11 advisory services, phytosanitary controls, low institutional capacity, and weak linkages among agri-food value chain actors. <https://documents.worldbank.org/en/publication/documents-reports/documentdetail/099827004062638439>.

Employment gains slowed as labor demand eased and supply constraints tightened

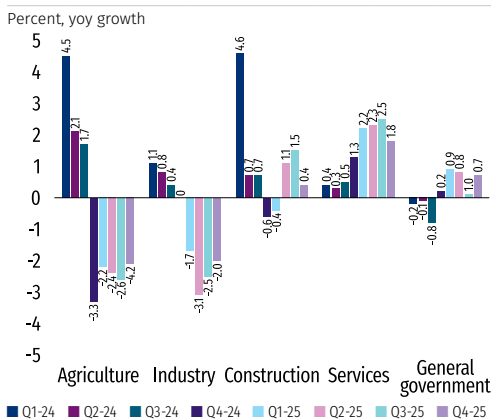
Employment growth in the Western Balkans slowed sharply in 2025, reflecting weaker economic activity and sectoral downturns, with limited offset from services. Job creation fell sharply in 2025, with regional average employment growth declining to a negligible 0.1 percent from 1.8 percent in 2024. Agriculture and industry were largest drag on employment growth, reflecting an unfavorable agricultural season and contracting private investment, while robust tourism and other service exports drove employment growth (Figure 1.7). Construction and the public sector also contributed positively to employment growth, particularly in Kosovo. After increasing for several consecutive years, employment in Serbia stagnated in 2025, while Albania posted a modest contraction. Kosovo had the region's highest employment growth rate at

2.9 percent, followed by North Macedonia and Bosnia and Herzegovina at 1.5 and 1.1 percent, respectively.

Slowing rates of job creation reflected both weaker labor demand and intensifying supply-side constraints, with demographic pressures and emigration increasingly limiting the available human capital. As employment growth slowed, the region's average employment rate remained broadly unchanged at 48.9 percent in 2025. This reflects not only low employment growth but also shrinking working age population including declining labor force and inactive population. Over the last five years working age population dropped by 4.5 percent in the region highlighting mountain pressures from population aging and outmigration (Figure 1.8).

The regional unemployment rate edged down only marginally from 10.8 percent in 2024 to 10.6 percent in 2025 compared to earlier years mirroring

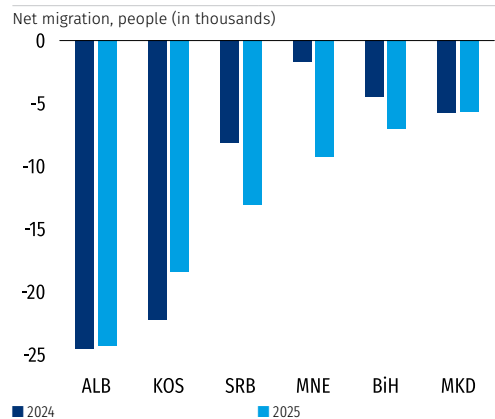
Figure 1.7 Agriculture and services remain drag on employment from the demand side...



Source: National statistical offices, World Bank staff calculations.

Note: (i) Albania does not report employment by disaggregated services sectors; (ii) Trade and hospitality includes wholesale and retail trade, accommodation and food sectors. Other services include administrative and support services, professional, scientific and technical activities, entertainment, recreation, and other services.

Figure 1.8 ...while outmigration among other reasons intensifying supply side constraints



Source: World Bank Data Bank.

the broader economic slowdown in the region. Bosnia and Herzegovina and North Macedonia recorded the greatest declines in unemployment, with rates falling from 13.1 percent to 12.2 percent in the former and from 11.9 percent to 11.5 percent in the latter, alongside declining inactivity rates, suggesting tighter labor market conditions. These trends are broadly consistent with some growth acceleration in North Macedonia and relatively smaller GDP growth slowdown in Bosnia and Herzegovina. By contrast, Kosovo and Serbia saw their unemployment rates rise to 12.4 and 8.7 percent, respectively, as they suffered the sharpest economic slowdowns in the region. Improvements in headline unemployment did not fully extend to vulnerable groups, particularly youth. Youth unemployment rose in several countries, especially Bosnia and Herzegovina, where job losses among young workers outpaced new hiring, pushing the youth unemployment rate to 32.8 percent, the highest level in the region. North Macedonia posted the second highest youth unemployment rate at 29.3 percent. Youth unemployment rates were lowest in Albania and Kosovo at 21.5 and 18.4 percent, respectively, though both remain far above the EU average of 14.7 percent.

High headline and youth unemployment rates and wide gender gaps in labor-force participation compound structural constraints while highlighting the underutilization of human capital across

the region. In most countries, the female labor-force participation rate increased only marginally in 2025, and gender gaps remained wide: 13.3 percent in Albania, 13.5 percent in Serbia, 18.3 percent in North Macedonia, 22.9 percent in Bosnia and Herzegovina, and 34 percent in Kosovo. In a context of high emigration and rapid demographic aging, leveraging the full potential of the region's human capital, particularly women, youth, and other groups facing barriers to work, will be essential to ease structural labor constraints, sustain economic growth, and safeguard long-term fiscal and social sustainability (see Chapter 2).

Despite weak employment growth, real wages continued to rise across the WB6 in 2025, driven by minimum-wage increases and tightening labor markets. Real wage growth remained robust across the region, albeit with considerable variation between countries. Bosnia and Herzegovina recorded the highest real increase in average gross wages at 9.6 percent, up from 8 percent in 2024, supported by substantial increases in minimum wages in both entities⁴. Average real wage growth in North Macedonia plunged from 9.1 percent in 2024 to just 0.6 percent in 2025, the lowest rate in the region. Average wages in Albania rose by 6.2 percent despite a modest decline in the real minimum wage, reflecting strong labor demand in the service sectors and a tightening labor supply. Minimum-wage increases were similarly varied, ranging from

⁴ In the Federation of Bosnia and Herzegovina, the minimum wage rose by approximately 73 percent in real terms. In Republika Srpska, the government introduced a differentiated minimum wage structure from 2025, based on employees' level of education, spanning four tiers (adding one more tier from 2026). As a result, changes in real minimum wage relative to 2024 ranged from -3.8 percent for level 1, to 2.0 percent for level 2, 7.9 percent for level 3, and 43.1 percent for level 4.

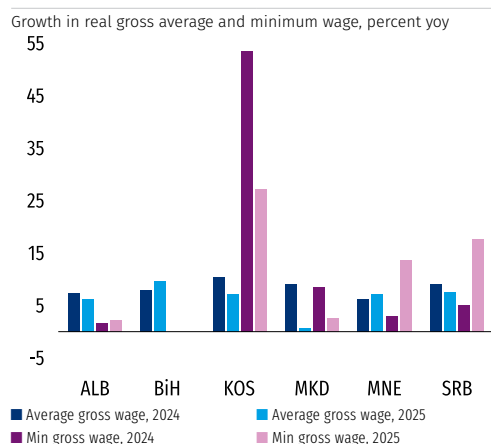
27.1 percent in Kosovo to 10.9 percent in North Macedonia. Rising minimum wages pushed replacement rates upward in five of the six countries, compressing the gap between the minimum and average wages. Replacement rates⁵ were highest in Montenegro at 55.2 percent and lowest in Albania at 47.6 percent, where the rate also declined by 4 ppts compared to 2024.

Rising wages contributed to higher unit labor costs across most of the region in 2025, although the pace of the increase slowed compared to 2024. Bosnia and Herzegovina and Kosovo registered the largest annual increases in real unit labor costs at 4.5 and 4.6 percent, respectively. These countries had the slowest labor productivity growth and fastest real wage growth, especially Bosnia and Herzegovina, where average real wages grew by 9.6 percent while

labor productivity grew by just 1.7 percent. In contrast, unit labor cost growth rates fell markedly in Serbia and Albania, to 2.5 and 1.7 percent, respectively, as labor productivity improved. North Macedonia was the only economy in the region in which unit labor costs declined, as rising labor productivity growth more than offset wage increases, indicating an improvement in cost competitiveness (Figure 1.10). While wage growth in the region represents in part a degree of catching up relative to earlier price increases, deeper efforts will be needed to strengthen productivity so that higher wages do not erode the region's relative competitiveness in key export sectors.

Poverty continued to fall, supported by real incomes and credit growth, although the pace of poverty reduction continues to slow. The poverty rate, measured at

Figure 1.9 While growth in real average wages is strong in the region...

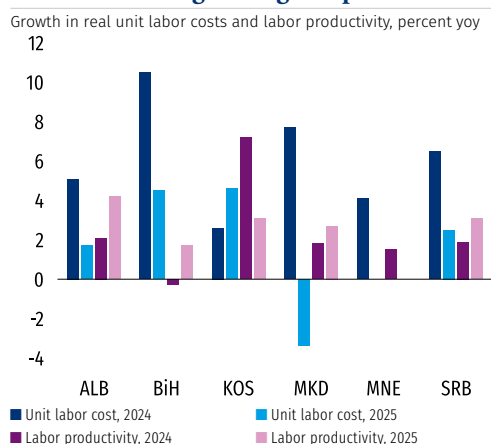


Source: National statistical offices, World Bank staff calculations.

Note: Kosovo data on average gross wage was not available at the time of report preparation.

⁵ Replacement rate defined as the ratio of the minimum gross wage to the nominal average gross wage. In Montenegro, the minimum wage corresponds to the rate set for low-skilled workers. In Republika Srpska, the replacement rate ranges between 55.2 percent for low-skilled workers and 82.1 percent for high-skilled workers. In the Federation of Bosnia and Herzegovina, the replacement rate stood at 64.1 percent.

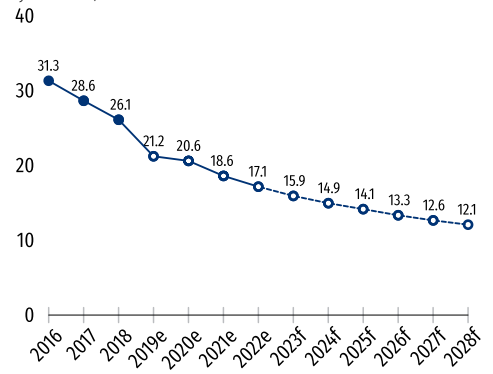
Figure 1.10 ...productivity growth has started to outpace unit labor costs growth in several countries strengthening competitiveness



the \$8.3/day (2021 PPP) line, declined from 31.3 percent in 2016 to a forecasted 14.1 percent in 2025 (Figure 1.11). Improvements in living standards have been supported by rising transfers and real wage increases, particularly in sectors such as wholesale and retail trade, construction, and food services and accommodation, which tend to employ a relatively high share of low-skilled workers. However, uneven labor-market gains limit the poverty-reducing impact of growth. Across the region, labor-force participation rates among youth, women, and individuals with low levels of formal education remained low or deteriorated. As a result, poverty is increasingly associated with structural barriers to employment and inclusion, limiting the extent to which continued growth alone can sustain rapid poverty reduction.

Figure 1.11 The pace of poverty reduction continues to slow

Poverty headcount (percent of population living on less than \$8.3/day 2021 PPP)



Source: World Bank staff estimates.

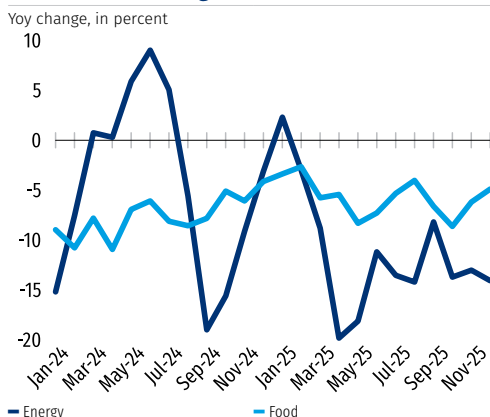
Rising domestic cost pressures and local supply shocks pushed inflation higher across the region

Following a sharp decline in 2024, regional headline inflation rebounded moderately to 3.7 percent in 2025, driven by higher food, services, and utility prices. While global prices eased, domestic factors boosted inflation across all WB6 countries (Figure 1.12). Growth in real incomes, supported by increases in minimum wages, social transfers, pensions, and consumer credit, contributed to broad-based inflationary pressures across the region. Additional local shocks, including droughts, floods, and a poor agricultural season, pushed up food prices in Bosnia and Herzegovina and drove a midyear spike in food-price inflation to about 8 percent in Serbia. In response, the Serbian government temporarily capped retail margins, which contributed to a significant drop in average regional food inflation in the second half of 2025. However, this measure expired in February 2026, leaving the trajectory of food prices uncertain. Higher housing, utility, and electricity prices added to inflationary pressures in Montenegro, Bosnia and Herzegovina, and Kosovo. Bosnia and Herzegovina and Kosovo recorded the sharpest increase in inflation between 2024 and 2025, with headline rates in each country rising by 2.3 ppts to 4 percent and 3.9 percent, respectively. Despite strong demand and rising wages, Albania maintained the region's lowest and most stable inflation rate at 2.2 percent, mainly supported by exchange-rate appreciation.

Average core inflation in the WB6 slowed from 4.3 percent in 2024 to 3.8 percent in 2025, remaining slightly above headline inflation on average (Figure 1.13). Core inflation exceeded headline inflation in Albania, Montenegro, and Serbia, where real wage growth continued to outpace labor productivity growth, keeping upward cost pressure on prices and widening the gap between core and headline inflation. In North Macedonia, labor productivity growth exceeded real wage growth, leading to a decline in unit labor costs in 2025, which helped narrow the gap between core and headline inflation. In Bosnia and Herzegovina and Kosovo, headline inflation exceeded core inflation, driven by sharp increases in food and utility prices coupled with continued pressures from rising wages and unit labor costs. Overall, the varying intensity of core inflation across countries largely reflected differences in wage-growth dynamics, a trend that has become the defining feature of inflation in the WB6 in recent years (see Box 1.1).

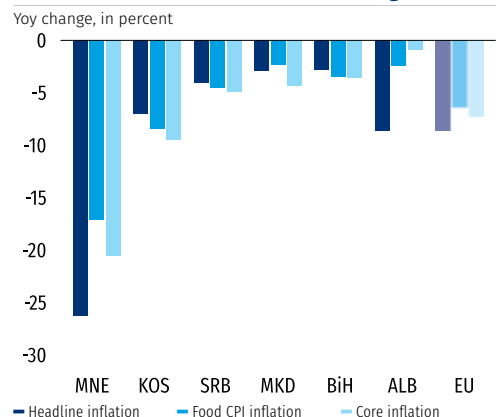
Food and energy prices remained volatile across the region in 2025, while domestic cost pressures were moderate despite strong wage growth and rising prices for non-tradables. Following an initial increase in the Producer Price Index (PPI) in early 2025, the headline Consumer Price Index (CPI) and PPI converged in most countries toward the fourth quarter of the year. This trend may indicate that the pass-through to consumer prices was weaker than initially expected, even as imported inflation rebounded in the second half of the year amid higher food and commodity prices. While the average PPI for the region declined from 3.7 percent in the first half of 2025 to 2.8 percent for the full year, strong wage growth, elevated energy costs, and rising service prices may indicate that cost-push pressures remain a regional concern.

Figure 1.12 Global food prices edged up during the second half of 2025...



Source: World Bank Pink Sheets, country Central Banks and Statistical Offices, World Bank staff calculations.

Figure 1.13 ...as average headline and core inflation inch closer together



Box 1.1 What are the drivers of inflation in the Western Balkans?

As inflation in the Western Balkans remains above EU levels, identifying inflation drivers continues to be highly relevant. Following the approach of the ECB⁶ and IMF⁷, this analysis decomposes GDP deflator growth—a measure of domestic price pressures—into a weighted sum of unit labor costs (divided into wages and productivity), unit profits, and unit taxes, all of which are measured per unit of real GDP. Importantly, GDP deflator growth only covers price changes in domestic production, so that levels and trends may somewhat differ from the CPI inflation which also covers imported consumption goods' price movements. Also, since no Western Balkan country publishes timely, high-frequency GDP income approach data, this analysis relies on proxies. Total labor costs are estimated by multiplying the number of employees by the average cost per employee, which includes gross wages and employers' social security contributions. Profits, specifically gross operating surplus and mixed income, are calculated as the difference between gross value added and labor costs. Net taxes on production are retrieved from GDP production approach data.

In the Western Balkans, wages have surpassed profits as the primary driver of inflation since 2023. Until the end of 2022, profits were the dominant inflation driver. As firms benefited from short-term supply inelasticities during the post-COVID demand recovery, profits raised inflation by more than 4 ppts in 2022. As supply capacity improved and demand patterns normalized, profit margins declined, resulting in lower inflationary pressures. By 2024, falling profits had reduced inflation by an average of 1.9 ppts. In contrast, wage pressures intensified amid the onset of the cost-of-living crisis, persistent labor shortages, and rising minimum as well as public sector wages. In 2024, wage growth increased inflation by 5 ppts on average, and such trends intensified in 2025 with wages adding 5.3 ppts to inflation on average.

The relative importance of wage and profit dynamics differs by country, resulting in varying inflation outcomes. Albania, Bosnia and Herzegovina and North Macedonia have experienced the most pronounced shift from profit-led to wage-led inflation. Falling profit rates contributed most to the mitigation of inflationary pressures in Bosnia and Herzegovina and Kosovo. Unit labor costs have been rising across the region, but more moderately in Albania and Kosovo. This might change in the future as both Albania and Kosovo increased their minimum wages to LEK 50,000 and EUR 425, respectively, in January 2026, with Kosovo planning to increase it further to EUR 500 in July 2026.

Changes in productivity and net taxes play an important yet minor role in recent inflation dynamics. In 2025, net taxes increased the GDP deflator growth rate by about 0.7 ppts in the Western Balkans, ranging from 0.1 ppts in North Macedonia to 2.4 ppts in Montenegro. Meanwhile, in 2025, improvements in labor productivity reduced inflation by about 1.5 ppts, which was still insufficient to offset the pressure from wage growth. Therefore, falling profit rates contributed to moderating domestic production prices.

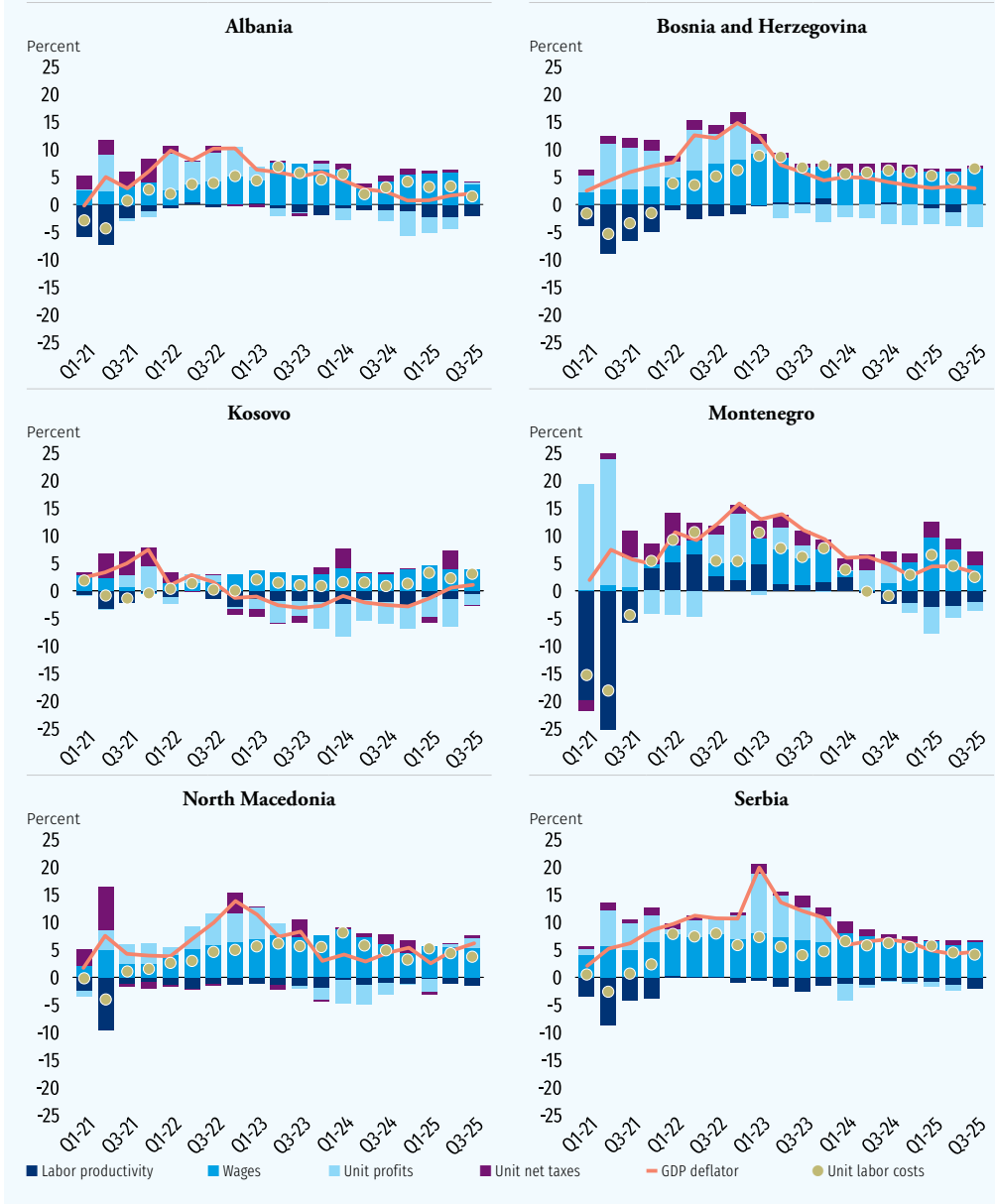
Although inflation levels have stabilized in the Western Balkans, structural barriers, particularly in labor markets, continue to prevent convergence toward EU-level inflation rates.⁸ In the short term, a close coordination between restrictive monetary and prudent fiscal policies is essential to avoid reigniting demand pressures. In this context, increases in minimum

6 <https://www.ecb.europa.eu/press/blog/date/2023/html/ecb.blog.230330-00e522ecb5.en.html>.

7 Hansen, Toscani, Zhou (2023): *Euro Area Inflation after the Pandemic and Energy Shock: Import Prices, Profits and Wages*. IMF Working Paper. WP/23/131.

8 European Investment Bank (2025). Central, Eastern and South-Eastern Europe (CESEE) Bank Lending Survey: Second half of 2025.

wages, public sector wages, and tax burdens must be carefully balanced against their potential inflationary impact, particularly through higher unit labor costs and increased domestic demand. In the medium term, structural reforms aimed at raising labor productivity are crucial for offsetting the inflationary pressure of inevitable wage increases. Particular caution is warranted in Bosnia and Herzegovina, where unit labor costs increased by far the most in 2025, adding 7.4 ppts to the inflation rise.



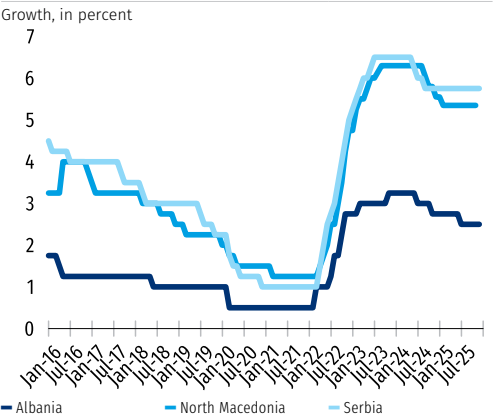
In countries with independent monetary policy, central banks maintained a cautious stance, seeking to balance inflation control with slowing growth.

In Albania, where inflation was the lowest in the region, the central bank cut its key policy rate by 250 basis points to 2.5 percent during the year, with the aim of bringing inflation in line with its 3 percent target. In North Macedonia, the central bank relied on macroprudential measures to support price and exchange rate stability, keeping the policy rate unchanged at 5.35 percent (Figure 1.14). In Serbia, following a cumulative easing of 75 basis points in 2024, the National Bank of Serbia held the rate steady at 5.75 percent throughout 2025, even as inflation rose to 4.9 percent by mid-year. In Bosnia and Herzegovina, a currency board arrangement, and in Kosovo and Montenegro euroization, constrain monetary policy, shifting the burden of adjustment toward fiscal, administrative, and structural measures.

Private sector credit expansion remained strong across the region, underpinned by robust banking sector resilience

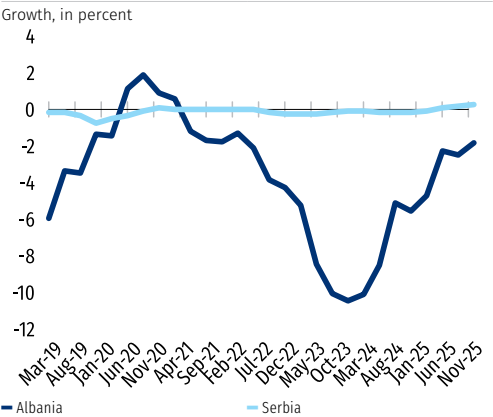
Sustained consumer confidence, a buoyant housing market, and strong corporate credit demand supported private-sector credit growth across the WB6 in 2025.⁹ Household credit expanded by an average of 16.9 percent, up from 13.4 percent in 2024. The growth of corporate lending accelerated more modestly, rising from 11.7 percent to 12.5 percent, underpinned by rising fixed investment, working capital needs, and positive developments in the small and medium-sized enterprise sector. Strong household credit growth in 2025 coexisted with moderating consumption growth, reflecting a shift in borrowing toward housing (asset acquisition) and balance-sheet smoothing rather than consumption expansion. Montenegro and Kosovo led the growth of household credit, with lending rising by 19.8 and 19.7 percent, respectively, while Montenegro and North

Figure 1.14 Policy rates



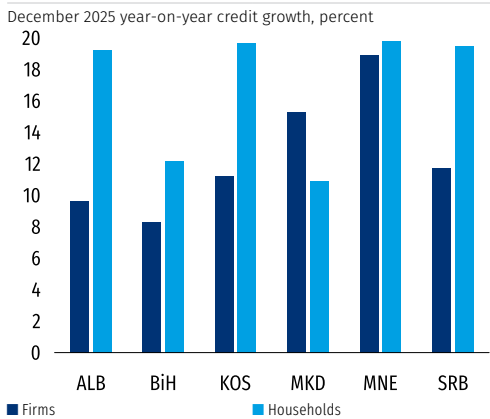
Source: Countries' Central Banks.

Figure 1.15 Exchange rate dynamics



⁹ European Investment Bank (2025). Central, Eastern and South-Eastern Europe (CESEE) Bank Lending Survey: Second half of 2025.

Figure 1.16 Credit growth remained strong in 2025 with households continuing to outperform corporates



Source: Regional Central Banks and World Bank staff calculations.

Macedonia recorded the highest corporate credit growth rates at 18.9 and 15.3 percent, respectively (Figure 1.16).

Mortgage lending drove household credit growth in most WB6 countries, supported by targeted policy measures and evolving market conditions. In Serbia, the central bank aimed to create more favorable borrowing conditions for lower-income households. In Montenegro, bank credit terms eased in the third quarter of 2025 amid improved economic growth and increased competition in the banking sector, which facilitate household borrowing.¹⁰ Similarly, in Bosnia and Herzegovina,

heightened competition among lenders contributed to more favorable conditions for housing loans.¹¹

While credit growth did not reignite broad inflationary pressures, it underscores the importance of macroprudential policy in containing housing-related risks and preventing a delayed pass-through to services inflation. Amid ongoing credit growth and an expanding housing market, Montenegro increased its countercyclical capital buffer to 1 percent in 2024, effective in January 2026.¹² In North Macedonia, new macroprudential measures that took effect in December 2025 increased the minimum down payment requirement from 15 to 25 percent, with an exception for first-time homebuyers, who are subject to a lower threshold of 10 percent.¹³ In Albania, to address groups with higher debt relative to their income or with smaller down payments, the authorities introduced binding limits from mid-2025 on how much of a home's value can be financed by a loan and on how large monthly payments can be relative to a borrower's income.¹⁴ In Kosovo, the central bank implemented a countercyclical capital buffer in late 2024. These measures indicate a tightening of mortgage-credit supply conditions driven by increased bank caution and, in some

10 Central Bank of Montenegro (2025). Report on Bank Lending Survey Results: Third Quarter 2025 (https://www.cbcg.me/slike_i_fajlovi/eng/fajlovi/fajlovi_publikacije/izv_rez_ankete/rep_on_bank_lending_survey_results_q3_2025.pdf).

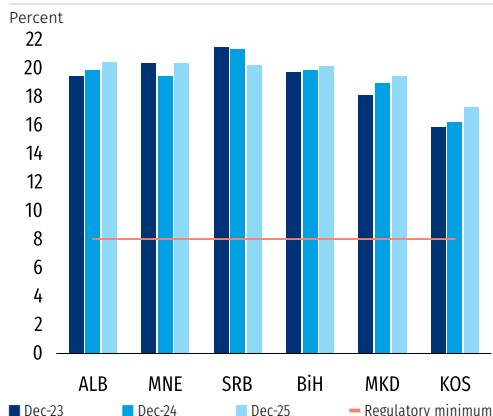
11 Central Bank of Bosnia and Herzegovina (2025). Bank Lending Survey Q3 2025 (<https://cbbh.ba/search/results?searchTerm=lending%20survey>).

12 OeNB (2025). OeNB Report 2025/10: Economic trends in EU candidates and Russia (<https://www.oenb.at/en/Publications/Economics/reports/2025/report-2025-10-economic-trends-in-cesee/html-version.html>).

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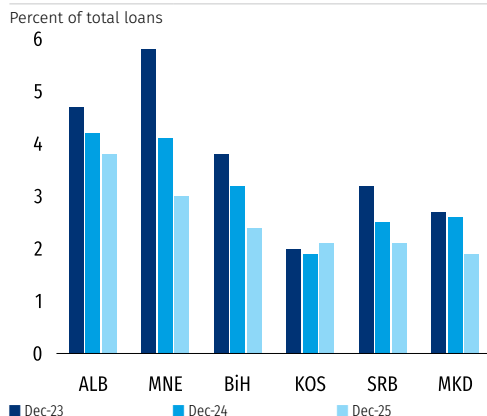
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Figure 1.17 Banks remain well-capitalized with capital adequacy ratio above minimum requirements...



Source: Central Banks of Western Balkan economies; International Monetary Fund.

Figure 1.18 ...with non-performing loan ratios at multi-year lows



cases, macroprudential measures on real estate lending.¹⁵

Credit quality has continued to improve.

Capital adequacy ratios remain robust and well above regulatory minimums at an average of about 19.6 percent across the region, underscoring the sector's strong loss-absorption capacity. Asset quality remains solid and has continued to improve, with non-performing loan ratios falling to historical lows across the region, from 2.1 percent in Kosovo and Serbia to 3.8 percent in Albania as of December 2025, with a WB6 average of 2.8 percent (Figure 1.17 and Figure 1.18).

External vulnerabilities increased, driven by strong domestic demand compounded by the still weak external environment

External demand remains weak, while domestic demand—though easing—

is still strong. These factors exerted pressure on the external accounts of the WB6 in 2025, with the average current account deficit widening by 0.9 ppts to 7.3 percent of GDP. Heightened trade-policy uncertainty, increased trade barriers and import tariffs, and disruptions in global value chains weighed on the economic performance of key external partners, particularly EU economies. While EU markets proved resilient to external shocks, growth remained sluggish, dampening demand for WB6 exports. Meanwhile, buoyant domestic demand and rising energy needs contributed to strong import growth in the region, widening the average current account deficit from 6.4 percent of GDP in 2024 to 7.3 percent in 2025 (Figure 1.19). Montenegro's current account deficit widened the most, reaching 20.5 percent of GDP, followed by North Macedonia (4.3 percent of GDP), and Kosovo (9.5 percent of GDP). In all three economies, merchandise imports

¹⁵ Bank of Albania (2025). Quarterly Monetary Policy Report (https://www.bankofalbania.org/rc/doc/RPM_2025_IV_ENG_32643.pdf), 2025/IV; Central Bank of the Republic of Kosovo (2026). Quarterly Assessment of the Economy Q III/2025 (https://bqk-kos.org/wp-content/uploads/2026/02/CBK_QAE_Q3_2025.pdf?lang=en).

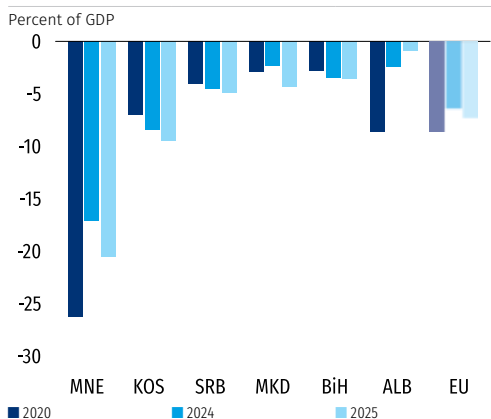
rose sharply, reflecting higher demand for construction and consumption goods, while merchandise exports grew only marginally or, as in Montenegro, declined—contributing to the expansion of trade deficit. In Serbia, however, merchandise exports grew faster than imports on the back of stronger manufacturing performance and rising automotive exports to EU countries and the wider Balkan region. In Albania, by contrast, the current account deficit narrowed by 1.5 ppts to 0.9 percent of GDP, supported by a strong expansion in net services exports (Figure 1.20).

Net service exports continued to support current account balances across the WB6, though the average services trade surplus narrowed marginally by 0.2 ppts of GDP in 2025. Overall, service exports proved resilient, accounting for 11.8 percent of regional GDP in 2025. Strong tourism receipts in Albania, Montenegro, and Kosovo, expanding information and communication technology services in Kosovo, and growing business services in

Kosovo and Montenegro helped contain current account deficits in these economies. Although exports of construction services declined in Montenegro and slowed in Serbia, the region maintained a sizeable services trade surplus that partially offset the merchandise trade deficit.

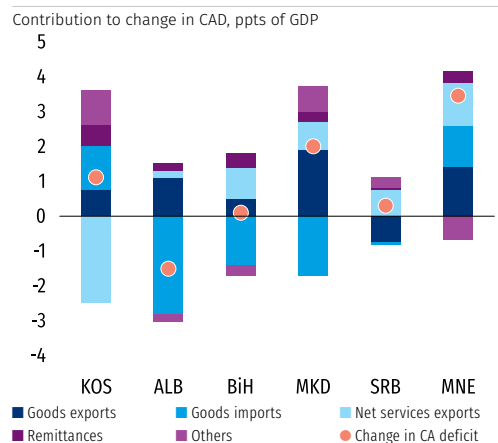
Net FDI inflows in the WB6 declined from 5.4 percent of GDP in 2024 to 4.0 percent in 2025. The sharpest drops were recorded in North Macedonia, where net FDI fell by 5.2 ppts to 1.4 percent of GDP, and in Serbia, where it declined by 3.0 ppts to 2.6 percent of GDP (Figure 1.21). In North Macedonia, subdued EU growth and heightened global trade volatility resulted in weaker equity-investment and debt-instrument inflows in the automotive despite a 67 percent rise in reinvested earnings, which accounted for about 70 percent of total inflows. In Serbia, FDI declined across all instruments, especially equity (-72 percent), with the sharpest contractions in mining, automotive manufacturing, electricity, construction,

Figure 1.19 Current account deficits widened in all countries except for Albania...



Source: World Bank staff calculations based on Central Banks data.

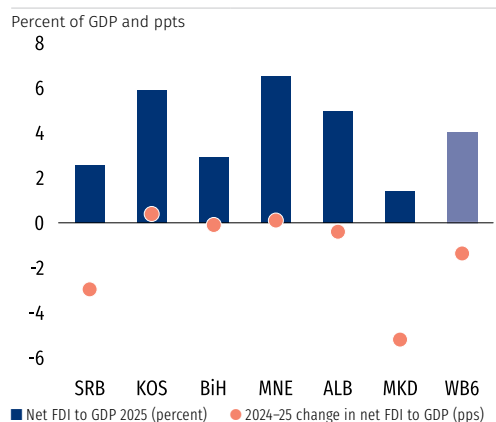
Figure 1.20 ...as strong goods import growth outpaced export in 2025



and real estate, driven by weaker investment from both China and the EU. Kosovo and Montenegro recorded modest FDI increases of 0.4 and 0.1 ppts of GDP, respectively. Overall, investment momentum was dampened by global economic uncertainty, political risk, and uneven progress on structural reforms across the region. Despite

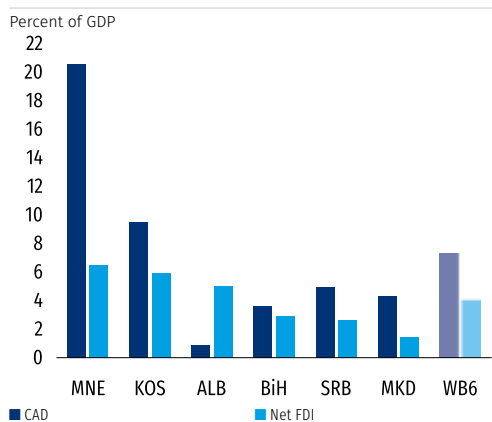
the slowdown, FDI remained an important source of external financing, covering about 32 percent of current account deficits in Montenegro and North Macedonia and nearly 80 percent in Bosnia and Herzegovina (Figure 1.22). FDI also plays a key role in facilitating technology transfer and job creation (Box 1.2).

Figure 1.21 Net FDI declined across the region with the largest drop in North Macedonia and Serbia...



Source: World Bank staff calculation based on Central Banks data.

Figure 1.22 ...while remaining an important source of CAD financing



Box 1.2 Improving quality of foreign direct investments in the Western Balkans

Foreign direct investment (FDI) inflows into the region have been robust over the past decade, despite impacts of successive external shocks. Inflows grew steadily through 2019, with average annual inflows of EUR 5.2 billion, led by Serbia (Figure 1.23). The COVID-19 shock in 2020 caused a dip in regional FDI, with the largest declines recorded in North Macedonia and Serbia, at 49 and 20 percent, respectively. Kosovo and Montenegro were exceptions, recording increases in total inflows driven by a rise in debt instruments. A strong recovery followed over 2021–2024, with inflows reaching a peak annual average of EUR 8.8 billion, largely driven by Serbia but supported by broad-based regional improvements. This was followed by a second dip in 2025 on the back of external trade volatility. While Serbia leads the region in absolute annual terms, Montenegro, Kosovo, and Albania record the highest FDI inflows as a share of GDP (Figure 1.24).

More importantly than levels, FDI across WB6 has undergone a notable structural shift. The region's economies can be broadly grouped into manufacturing oriented destinations—Serbia, North Macedonia, and Bosnia and Herzegovina—and service-oriented destinations—Albania, Kosovo, and Montenegro, where tourism and real estate dominate. Beyond the post-pandemic recovery in nominal FDI inflows into the region, which may partly reflect efforts

to shorten supply chain distances, there is encouraging evidence of early stage qualitative, upgrading within manufacturing. Bosnia and Herzegovina has shifted from food and beverages toward automotive and transport equipment, North Macedonia has moved into higher-tech machinery and equipment, and Albania has seen electrical equipment displace textiles as its leading FDI subsector.

Figure 1.23 Total foreign investment annual inflows* by countries and years

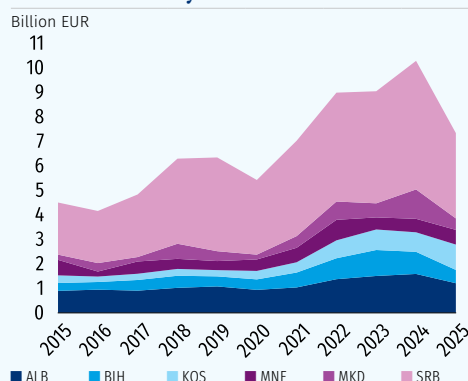


Figure 1.24 Share of FDI inflows* in GDP

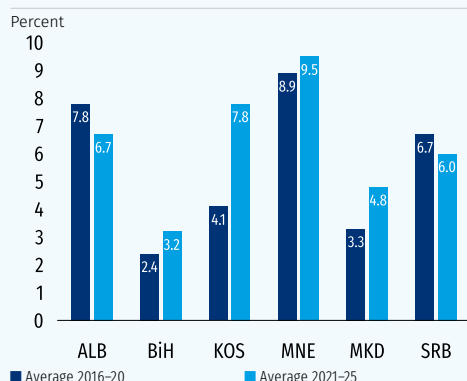
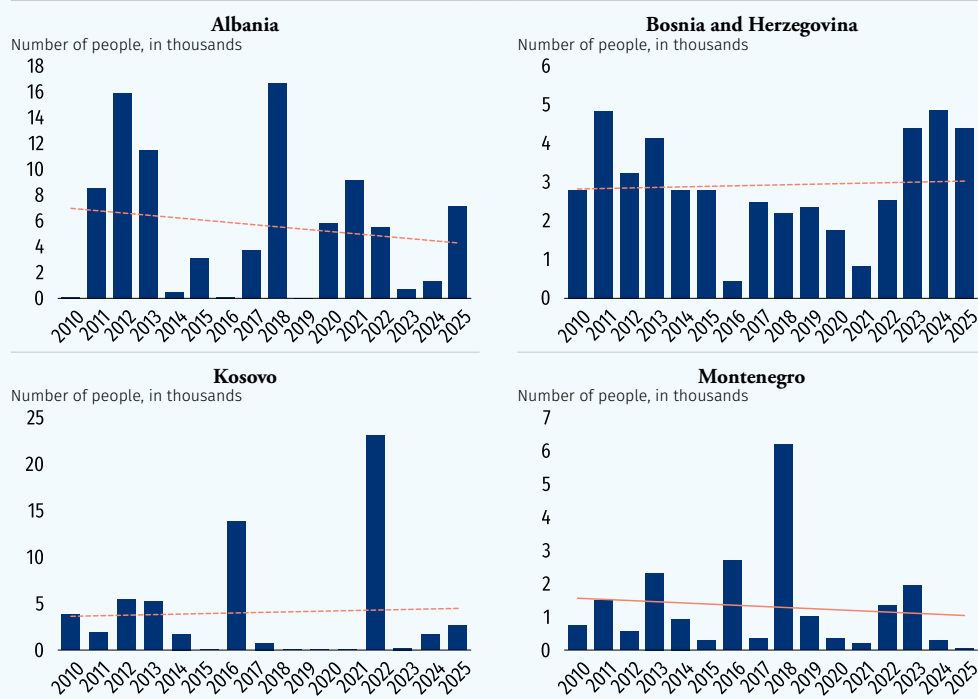
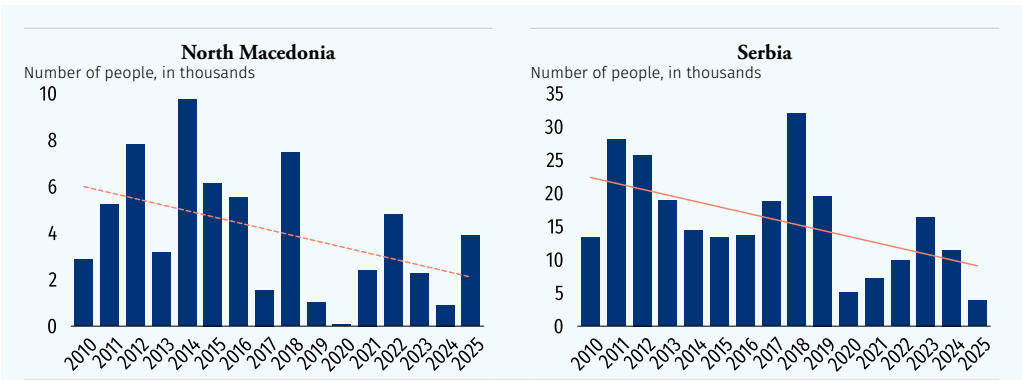


Figure 1.25 Trends in number of jobs created by the new FDI in the Western Balkans, 2010–2025



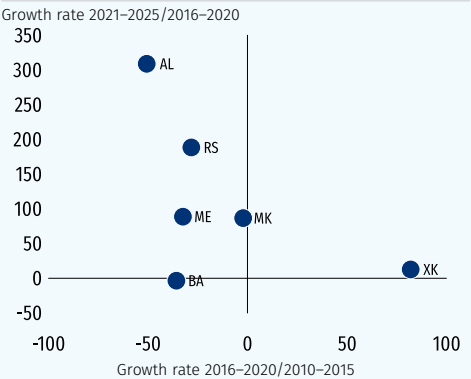


Source: wiw calculations using data from the fDI Markets database and wiw FDI database.

Yet, the number of jobs created by new FDI projects has trended downward in most economies—with only Bosnia and Herzegovina and Kosovo registering marginal gains. In Albania, for example, annual job creation was close to 9,000 between 2010 and 2014, while in 2022–2025 it was around 3,700. In Serbia, the average number of new FDI jobs fell from around 21,000 per year in 2010–2013 to about 10,000 in 2022–2025. In North Macedonia, the annual average declined from around 5,800 in 2010–2016 to roughly 2,200 in 2019–2025 (Figure 1.25).¹⁶ These patterns may reflect the gradual saturation of Western Balkan labour markets, where unemployment has declined substantially over the past two decades, but also reducing job intensity of FDI may be linked to an ongoing sectoral shift, with a growing share of investment directed towards higher-productivity, higher value-added activities. While in the Western Balkans FDI has historically been driven largely by low-cost advantages, especially labor, there is evidence that some countries are gradually moving towards other factors that help seek efficiency, alongside a partial shift towards market-seeking and nearshoring-driven investment. This transition away from labor-cost-based competitiveness may also help explain weaker job creation effects.

At the same time, capital intensity has risen steadily, pointing to a move toward larger, more capital-heavy investments. The size of investment projects increased between 2010 and 2025 in most countries, except Bosnia and Herzegovina and Montenegro. Project sizes rose notably in Albania from 2020 onward and in North Macedonia and Kosovo from 2018. Overall, project sizes were largest in Montenegro, followed by Serbia. Capital expenditure per job increased after pandemic, with strongest increase in Albania and Serbia, while it remained flat in Bosnia and Herzegovina (Figure 1.26). This pattern suggests a higher capital intensity relative to

Figure 1.26 Capital expenditure per job, growth rates



Source: wiw calculations using data from FT the fDI Markets database and wiw FDI database.

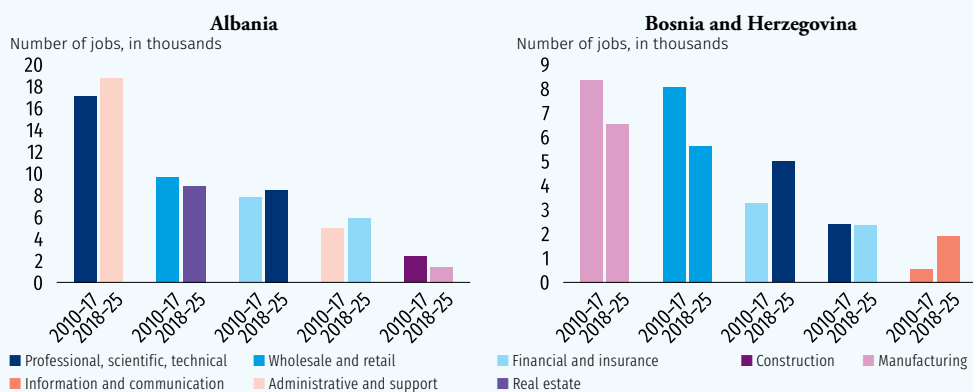
16 The number of jobs created by new FDI in the region, and specifically changes in the sectoral composition, capital intensity and value-added of the new jobs have been estimated by combining project-level FDI data from the FT fDi Markets database with official macro-level FDI statistics. This is done at the NACE 2-digit level for the period 2010–2025, subject to data availability.

labor from 2020 onward, indicating potential upgrading in Albania, Serbia, Montenegro, and North Macedonia. In the latter, the trend appears more stable, with fewer fluctuations over time.

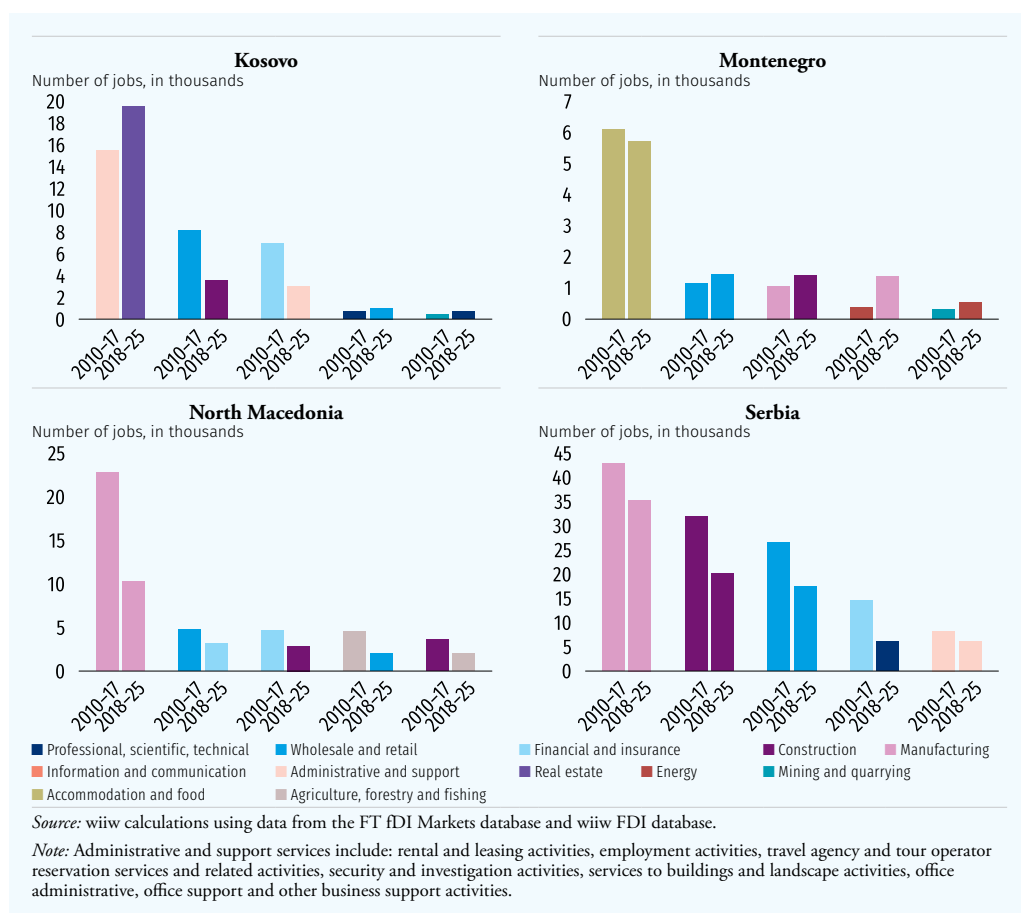
Jobs created through new greenfield FDI were concentrated in high value-added and medium value-added sectors.¹⁷ This trend became particularly pronounced from 2021 onward, suggesting that while FDI is generating fewer jobs, the foreign investment projects themselves are of greater scale and sophistication. Serbia and Albania have approximately 80 percent of FDI jobs in high value-added sectors, while Bosnia and Herzegovina, North Macedonia, and Kosovo around 75 percent. Montenegro is a notable outlier, with only 37 percent of FDI jobs in high value-added activities and a larger share in medium value-added sectors, though it has shown signs of improvement in the most recent period. Some economies, including Albania and Bosnia and Herzegovina, have also exhibited a recent shift toward medium value-added sectors, underscoring the importance of continued investment promotion strategies that prioritize quality over volume.

The sectoral analysis of new jobs reveals evidence of upgrading in Bosnia and Herzegovina and North Macedonia largely in manufacturing industries (Figure 1.27). In 2010–2017, the top manufacturing sector in Bosnia and Herzegovina was food and beverages, while in 2018–2025, motor vehicles and transport equipment, indicating a move towards more complex manufacturing activities. Chemicals and metals, which were among the top five manufacturing sectors in the first period, were replaced by machinery and electrical equipment in the latter, again pointing to a gradual upgrading of the manufacturing structure towards more technology-intensive activities. In North Macedonia manufacturing remains by far the dominant sector of FDI-related job creation in both sub-periods, despite a marked decline in absolute numbers. However, there was a shift towards higher-tech sectors: while motor vehicles and transport equipment remained the leading sub-sector in both periods, metals and textiles were replaced by machinery and equipment and rubber and plastic products in the ranking, while computers and electronics and furniture remained among top industries. Kosovo and Montenegro observed a strong concentration of FDI in non-tradable sectors, while Serbia has manufacturing (motor vehicles and transport equipment), construction, and trade remaining the three dominant sectors of FDI-related job creation in both sub-periods, though with a decline in absolute numbers.

Figure 1.27 Sectoral shift of new FDI-created jobs



¹⁷ NACE sectors were divided into low-, medium- and high-value added according to their value added per employee. Sectors with value added per employee below the 33rd percentile were classified as low-value added, sectors with value added per employee above the 67th percentile as high-value added, and the rest as medium-value added. This was done on the average value for the 2010–2024 period, for each of the individual economies.



Persistent current account deficits across the WB6 reflect a structural imbalance between investment needs and domestic savings, resulting in a sustained reliance on external financing. High consumption levels, low domestic savings, and strong dependence on imported energy, capital goods, and intermediate products have created an enduring gap between investment requirements and available domestic resources. In all six economies, investment as a share of GDP consistently exceeded domestic savings over the past decade, and while both variables fluctuated over time, the structural pattern of investment outpacing savings confirms the region's continued reliance on external financing to support

growth (Figure 1.28). At the sectoral level, the general government is typically a net borrower, while households are generally net lenders, with precautionary savings and remittances playing an important role. Corporations also tend to be net borrowers, due largely to weak profitability and limited retained earnings.

Country-level trends reveal variations both in the magnitude and persistence of savings-investment gaps. Montenegro and Kosovo display the largest and most persistent deficits, with current account imbalances being particularly pronounced during periods when investment surged. Bosnia and Herzegovina and Serbia showed

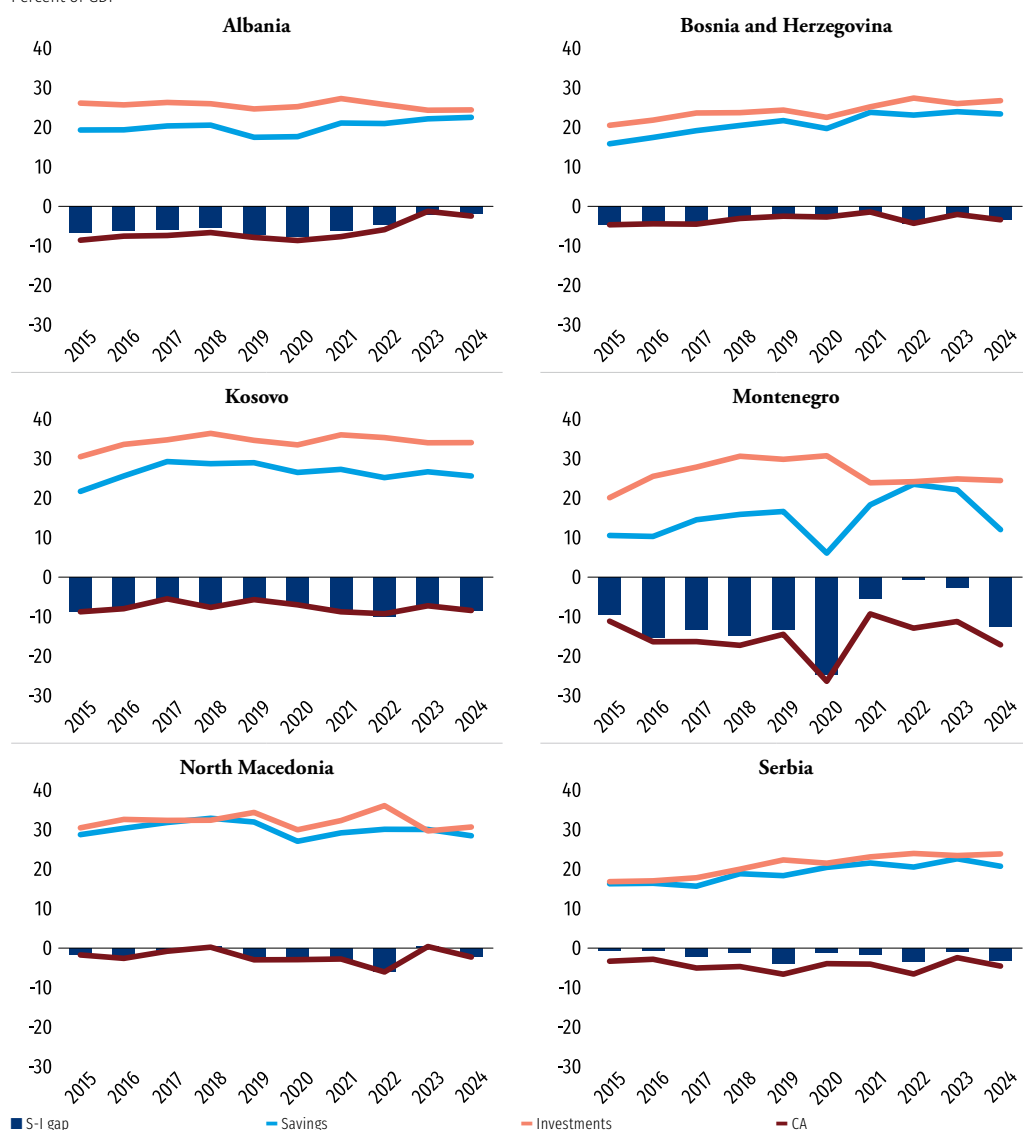
more moderate but still negative gaps, with modest improvements in certain years. Albania and North Macedonia experienced episodes of narrowing deficits, particularly after 2020, though the underlying imbalance remained. Despite short-term adjustments, especially around 2020–22, the broader regional pattern points to structurally limited domestic savings capacity relative

to investment needs, underscoring the persistent external vulnerabilities of the WB6.

External inflows are necessary to finance the region's persistent savings-investment gaps, but the composition and implications of these flows differ markedly across countries. Remittances

Figure 1.28 The WB6 consistently invest more than they save, relying on external financing

Percent of GDP



Source: National accounts, Central Banks data and World Bank staff calculation.

play a dominant role in Bosnia and Herzegovina and Kosovo, accounting for 7.4 and 12.1 percent of GDP, respectively, the largest shares in the region. Remittances help contain current account pressures, but they also reflect weak domestic production and investment capacity. Albania and Montenegro rely heavily on tourism receipts, which generate foreign exchange but expose them to external demand shocks, with Montenegro also facing the region's largest structural deficits due to high import dependence and infrastructure-driven investment. By contrast, Serbia and North Macedonia benefit from stronger FDI inflows into manufacturing and deeper integration into European value chains, which support exports and partially offset deficits. Despite these diverse buffers, all countries remain vulnerable to global commodity price fluctuations and weaker EU demand, underscoring the need for country-specific strategies to strengthen resilience and achieve more sustainable improvements in their external balances.

At the same time, the persistence of sizeable current account deficits raises concerns about emerging external financial risks and the buildup of external debt. These issues are particularly pronounced in Montenegro, where the external debt stock remained exceptionally high at 126.3 percent of GDP in 2025, only marginally lower than in 2024, heightening exposure to refinancing risks in an increasingly restrictive global financial environment. In Albania and Kosovo, external debt levels are lower but rising: Albania's external debt increased from 40.6 percent of GDP in 2024 to 46 percent in 2025, while Kosovo's external debt edged

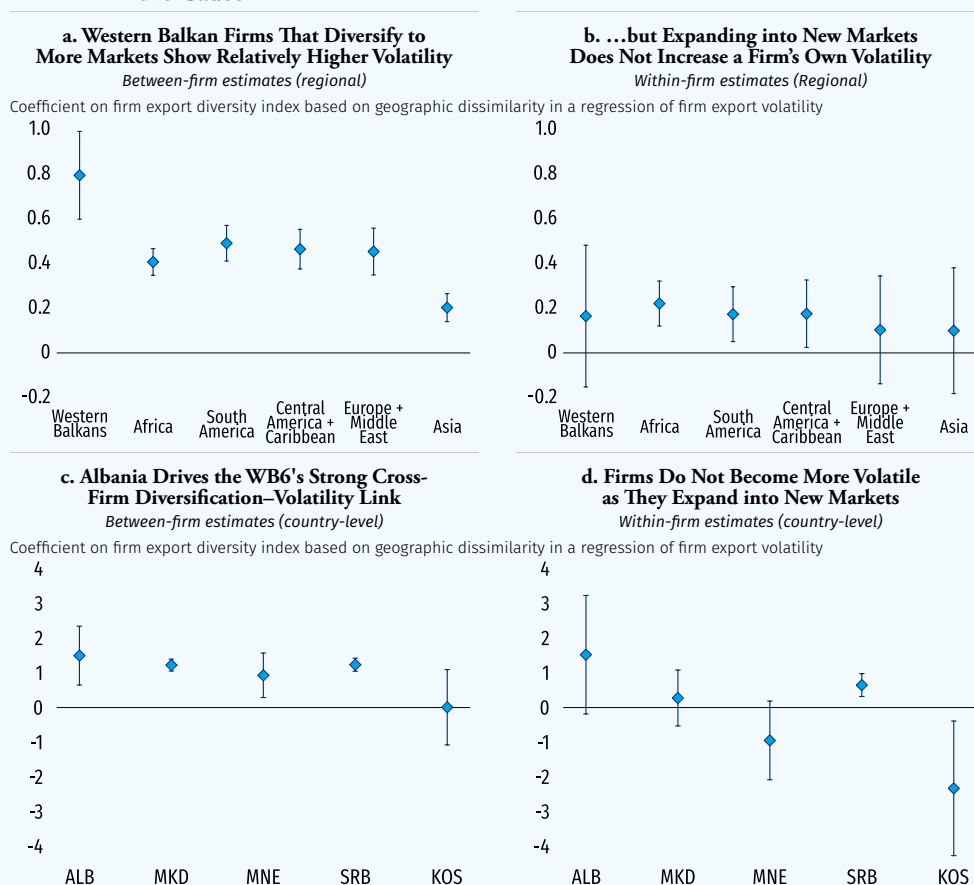
up from 40.6 percent to 40.7 percent, reflecting the cumulative impact of sustained external deficits. Serbia's external debt stock remained broadly unchanged at 58.6 percent of GDP in 2025, suggesting more stable external financing conditions. Despite these differences in buffers and debt trajectories, all countries remain vulnerable to global commodity-price volatility and weaker EU demand, underscoring the need for country-specific strategies to strengthen resilience and achieve more sustainable improvements in external balances.

In a context of heightened global volatility and mounting energy-related inflationary pressures, these vulnerabilities underscore the need for WB6 countries to strengthen competitiveness, diversify exports, and enhance productivity to support sustainable and inclusive growth. A more restrictive international financial environment, shifting supply-chain dynamics, and ongoing geopolitical uncertainty continue to disrupt global trade and investment flows. Strengthening competitiveness, diversifying exports, and improving the efficiency and productivity of public investment are critical priorities, as addressing these constraints is essential to reduce external imbalances, mitigate macroeconomic vulnerabilities, and deepen integration with EU markets in an increasingly unstable global environment (Box 1.3).

Box 1.3 Export Diversification and Volatility in the Western Balkans: Firm-Level Evidence

Export diversification in the Western Balkans directly shapes external vulnerability. When export earnings are volatile, the trade balance (and therefore the current account) becomes harder to stabilize. In economies where investment persistently exceeds domestic savings, this volatility can widen the savings–investment gap (see external sector) and raise reliance on external inflows (remittances, tourism receipts, and FDI) to finance deficits. Real exchange rate (RER) movements can help absorb shocks, but RER adjustment alone cannot substitute for structural competitiveness and resilience. This places the focus on the microeconomic foundations of export performance: for the Western Balkans, the key question is not only whether exports grow, but whether the way firms diversify products and markets reduces, or inadvertently increases, export volatility.

Figure 1.29 More Diversified Exporters Are More Volatile, But Diversification Itself Is Not the Cause



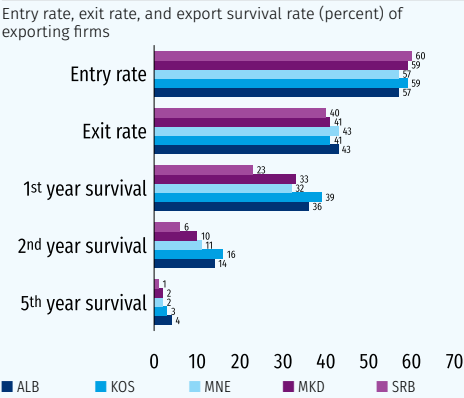
Source: Matthieu Crozet, Ana Margarida Fernandes, Thierry Mayer, Emmanuel Milet and Daria Taglioni (2026), forthcoming.

Notes: Each dot shows the estimated relationship between diversification and volatility. If a dot is above zero, diversification is associated with higher volatility. Between firms: Do firms that are more diversified than others also have more volatile exports? Within firms: When a given firm becomes more diversified over time, do its exports become more volatile?

Western Balkan exporters tend to diversify into more distant and economically dissimilar markets. New research drawing on firm-level data across 63 developing countries finds that Western Balkan exporters tend to expand into markets that are geographically distant or whose economic cycles move differently from their own, reaching, for instance, into Asian economies, North American or African markets. At first glance, this sounds like smart risk-spreading. But the data tell a more nuanced story.

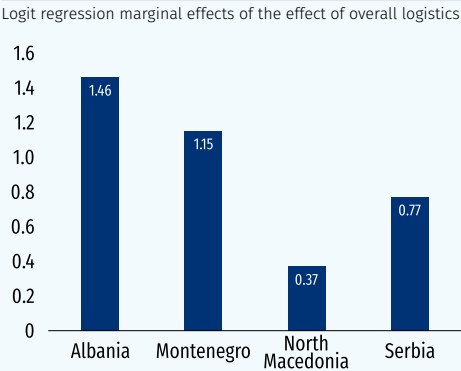
Highly diversified exporters appear more volatile, but this instability reflects who diversifies rather than diversification itself. Between-firm results compare different firms at a single point in time. Estimates show that those that sell to more and more distant markets tend to have more volatile and less predictable export revenues than firms that focus on fewer, closer markets, this effect that is stronger in the Western Balkans than in most other regions (Figure 1.29a) and most pronounced in Albania (Figure 1.29c). The elevated instability reflects who is doing the diversifying and into which markets—often smaller or experimental firms entering distant destinations—rather than diversification per se. This interpretation is reinforced by within-firm evidence: when the same firm is followed over time, expanding into new markets does not cause that firm’s revenues to become more volatile (Figure 1.29b and 1.29d), pointing to firm fragility, not market spread, as the source of instability. Accordingly, the higher volatility observed among highly diversified exporters in the region appears to reflect firm characteristics of the firms doing the diversifying, notably their size, age, or market sophistication, rather than a structural effect of diversification itself.

Figure 1.30 Fewer Than 1 in 4 New WB6 Export Relationships Survive the First Year



Source: Albania Trade Competitiveness Diagnostics 2026 (Forthcoming).
Note: All analyses are at the firm-product-partner country-year level.

Figure 1.31 Better logistics are associated with higher export survival



Source: Albania Trade Competitiveness Diagnostics 2026 (Forthcoming).
Note: Industry fixed effects are at the 2-digit HS level. A positive coefficient indicates an increase in the probability of export survival.

A defining feature of export activity across Western Balkan economies is how fragile it is, characterized by a rate of churning that is exceptionally high even when compared to other emerging markets. Entry rates range from approximately 57 to 60 percent, while exit rates range from 40 to 43 percent annually (Figure 1.30). While high entry into export markets is common in emerging economies, the Western Balkans combine very high entry rates exceeding other countries which average about 30 percent annually, with exceptionally rapid exit. First-

year survival rates are strikingly low: only 23 to 39 percent of new export relationships survive beyond the first year, fall well below the 38 to 47 percent recorded across comparable emerging market regions and by the fifth year, fewer than 4 percent remain active. This pattern of high entry coupled with rapid exit means that a considerable share of observed diversification reflects short-lived, experimental market forays rather than durable expansion of the export base.

Better logistics, alongside firm-level capabilities and regulatory compliance, help firms stay in export markets longer. One foundational factor that meaningfully improves a firm's chances of surviving as an exporter is the quality of logistics. A one unit improvement in overall logistics performance (both physical such as transport and ports, and procedural such as customs, border management) is associated with a measurably higher probability that a firm keeps exporting year after year (Figure 1.31). The effect is largest in Albania and Montenegro, and smaller but still positive in Serbia and North Macedonia. Strengthening competitiveness at the firm level complements RER based adjustment and reduce the risk that external shocks lead to persistent external imbalances. However, logistics alone is not sufficient. Firm-level characteristics play a central role in shaping export survival. Firms that enter export markets at higher initial scale, that trade multiple products or destinations, or that are simultaneously exporters and importers exhibit significantly higher survival rates, pointing to the importance of underlying firm capabilities and experience. Trade costs and market access conditions also matter: distance, tariffs, non-tariff measures and trade integration matter for survival, while shared borders and trade agreements improve persistence. Together, these results indicate that durable export performance requires a combination of efficient logistics and stronger firm-level competitiveness, all of which complement RER-based adjustment and reduce the risk that external shocks translate into persistent external imbalances.

The takeaway is not that firms should stop diversifying, but that diversification needs to be matched with the right capabilities. Policies oriented primarily toward stimulating new entry into export markets without addressing the structural conditions that determine whether firms can sustain those relationships, risk generating a revolving door of short-lived export attempts that contribute little to stable earnings. Improving logistics and trade facilitation infrastructure, strengthening firm-level productivity and financial resilience, and reducing NTM compliance costs, offer a concrete lever for raising export survival rates and reducing volatility.

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Expansionary fiscal policy has helped sustain economic activity but limited rebuilding of buffers

The Western Balkans recorded robust revenue growth in 2025, driven by buoyant VAT and personal income tax collection, reflecting solid household

demand underpinned by rising wages and social transfers. Revenues rose from 35.9 percent of GDP in 2024 to 36.2 percent in 2025. While this was the region's strongest revenue performance since 2012, gains were uneven across countries. Bosnia and Herzegovina was the standout performer: revenues increased by 2 ppts of

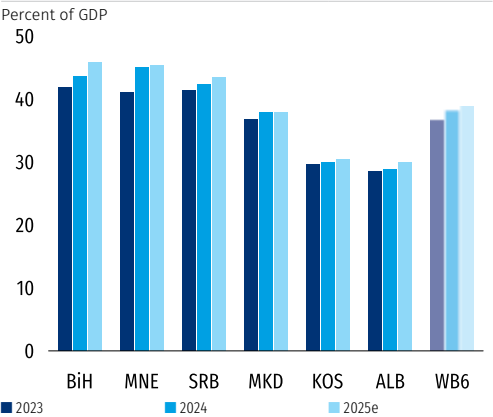
GDP, buoyed by higher VAT collection and social security contributions, both reflecting significant nominal wage growth in 2025. North Macedonia and Serbia also posted more modest revenue gains of 0.5 ppts of GDP each. By contrast, revenues in Montenegro and Kosovo ticked down by 0.6 and 0.1 ppts of GDP, respectively. Montenegro's drop was largely attributable to the government's 2024 decision to reduce pension contribution rates, which caused social contributions to fall by 28.1 percent between 2024 and 2025.

Rising public spending outpaced revenue growth as governments attempted to bolster household incomes. Fiscal policy remained expansionary, with regional public spending rising from 38 percent of GDP in 2024 to 38.8 percent in 2025, about 1.7 ppts above the preceding ten-year average (Figure 1.32).¹⁸ Social benefits and the public sector wage bill drove expenditure growth. Spending on social benefits increased in four of the six Western Balkan countries and exceeded 2024 levels by an average of

0.7 ppts of GDP. The sharpest rise occurred in Bosnia and Herzegovina, where social spending jumped from 16.2 to 20.3 percent of GDP, due largely to a 10 percent increase in pensions, though disability assistance, newborn benefits, and other social transfers also rose across the region. Bosnia and Herzegovina and Serbia recorded the most significant wage-bill increases, 0.9 and 0.6 ppts of GDP, respectively, and both posed the highest public sector wage bills in the region at 11.4 and 9.9 percent of GDP, respectively (Figure 1.33).

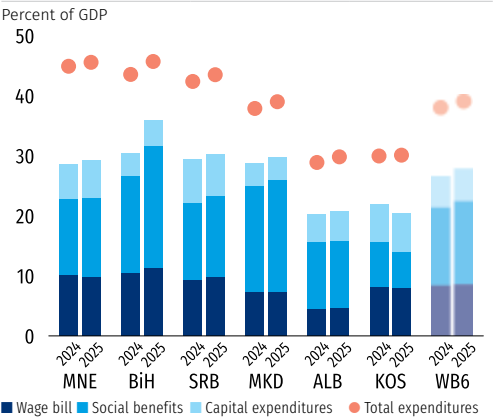
Capital spending also supported economic activity across most of the region. Public investment levels rose in four of the six countries, with the most notable increases in Bosnia and Herzegovina (0.5 ppts of GDP), Montenegro (0.4 ppts), and Albania (0.3ppts) financing upgrades in core transport and energy infrastructure. North Macedonia and Serbia were the only two countries in which capital spending declined, falling by 0.4 and 0.3 ppts of GDP, respectively. In North Macedonia,

Figure 1.32 Average budgetary expenditures increased across the region...



Source: World Bank staff calculations.

Figure 1.33 ...due mainly to higher spending on social benefits and wages



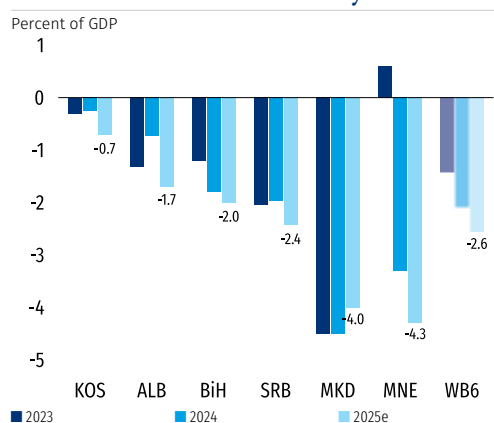
Source: World Bank staff calculations.

18 This calculation excludes year 2020 as it was a year with extraordinary high expenditures due to the COVID-19 crisis.

this change reflected persistently low budget execution rates, with less than 60 percent of the capital budget disbursed, while Serbia's decline was driven by a modest nominal increase against a high base in 2024.

Higher spending widened fiscal deficits for a second consecutive year, though they remained below 3 percent in most countries. The average fiscal deficit for the Western Balkans reached 2.6 percent of GDP in 2025, up 0.5 ppts from 2024 (Figure 1.34). Montenegro and Albania each saw their deficits increase by 1 percentage point of GDP, the former due to lower social security contribution revenues and the latter due to higher expenditures on public investment and the wage bill. North Macedonia was the only country to narrow its fiscal deficit in 2025, from 4.5 to 4.0 percent of GDP, as revenue gains offset a decline in capital expenditure, but its deficit remained the second largest in the region. Montenegro's deficit was the largest at 4.3 percent of GDP, while Kosovo's was the smallest at 0.7 percent.

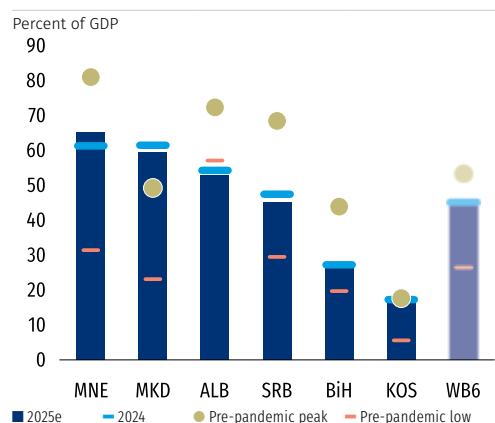
Figure 1.34 Elevated spending led to an increase in fiscal deficits for the second consecutive year...



Source: World Bank staff calculations.

Financial market conditions were relatively favorable for deficit financing, with four of the six countries successfully accessing international capital markets through Eurobond issuances. Albania, Bosnia and Herzegovina entities, and Montenegro placed Eurobonds in 2025 for €650, €350, and €850 million respectively, while North Macedonia tapped external markets in January 2026, raising two tranches of €500 million at interest rates of 3.875 and 4.750 percent, slightly more expansive than the previous issuance in March 2025. Separately, Republika Srpska, one of Bosnia and Herzegovina's two entities, issued €500 million in five-year bonds in March 2026 to refinance €300 million in debt maturing in April 2026. The new debt was issued at an interest rate of 6.25 percent, approximately 2 ppts above the previous issuance in 2021, due to elevated political risks and weak investor confidence. By contrast, the Federation of Bosnia and Herzegovina accessed international capital markets earlier, placing a €350 million debut Eurobond in July 2025, which was significantly oversubscribed and helped

Figure 1.35 ...but this did not translate into increased PPG debt



Source: World Bank staff calculations.

diversify financing sources and extend debt maturities. Serbia focused on domestic borrowing to finance the 2025 deficit and raised the equivalent of about €3 million (3.4 percent of GDP).

Rising geopolitical tensions in early 2026 have already begun to affect financing costs, and yields on sovereign Eurobonds have risen across the Western Balkans.

Between September 2025 and end-March 2026, Eurobond yields increased for all countries in the region by approximately 0.6–1.4 ppts, reflecting increased investor risk aversion and a higher risk premium demanded on developing-country debt. The average yield on regional Eurobonds maturing in 2027–28 stood at about 4.7 percent, up from around 3.9 percent six months earlier. Albania and Montenegro recorded the smallest increases, with yields hovering between 4.2 and 4.6 percent, while North Macedonia and Serbia traded at 5.3 and 5.7 percent, respectively.

Despite wider deficits in 2025, average public and publicly guaranteed (PPG) debt levels have declined steadily across the Western Balkans since 2020. Regional PPG debt fell to 44.4 percent of GDP in 2025, declining by 1.3–2.3 ppts of GDP in Albania, North Macedonia, and Serbia as nominal GDP growth outpaced debt issuance and the use of government deposits to cover financing needs (Figure 1.35). Only Montenegro bucked the regional trend, with PPG debt rising from 61.2 to 65.2 percent of GDP, due mainly to the government's decision to build a liquidity buffer ahead of an anticipated external debt repayment. At end-2025, PPG debt levels in five of the six countries remained

below their pre-pandemic peaks. North Macedonia was the only exception, with PPG debt at 59.3 percent of GDP. Albania was the strongest performer in terms of debt consolidation, with PPG debt falling to a record low of 52.3 percent of GDP. Bosnia and Herzegovina, Kosovo, and Serbia all had public debt levels below the 45 percent of GDP threshold specified in the EU's Maastricht criteria.

Government deposits represent an additional source of deficit financing and serve as important fiscal buffers across the Western Balkans.

Sizeable deposits enabled several governments to limit new borrowing in 2025, which in turn helped to lower their public-debt-to-GDP ratios despite widening deficits. Serbia's deposits were highest at about 8 percent of GDP, though they fell significantly over the year as the government drew them down to cover the deficit. Albania and Montenegro continued to rebuild their deposit buffers to approach pre-pandemic levels, while Kosovo continued to draw down its deposits to finance the deficit—a move coupled with IFI borrowing. In Bosnia and Herzegovina government deposits strengthened in 2025, largely reflecting normalization following the inflationary period (Figure 1.36). When assessed against actual 2025 deficit levels, Montenegro, which posted the highest deficit and debt levels in the region, has government deposits sufficient to cover approximately 1.5 years of its annual deficit, the region's lowest coverage ratio. Kosovo, by contrast, holds the smallest deposits as a share of GDP, yet its buffers are sufficient to cover 4.5 years of its annual deficit (Figure 1.37).

Figure 1.36 Rising deficits narrowed fiscal buffers in selected countries...

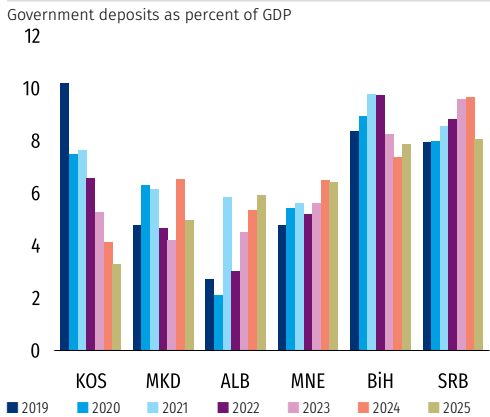


Figure 1.37 ...and the deficit coverage of government deposits varied across countries

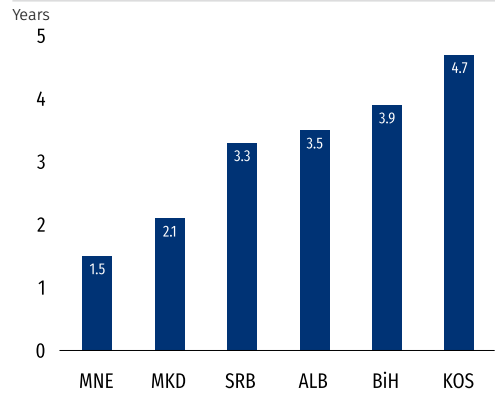


Figure 1.38 The share of interest payments is set to increase in all countries except North Macedonia...

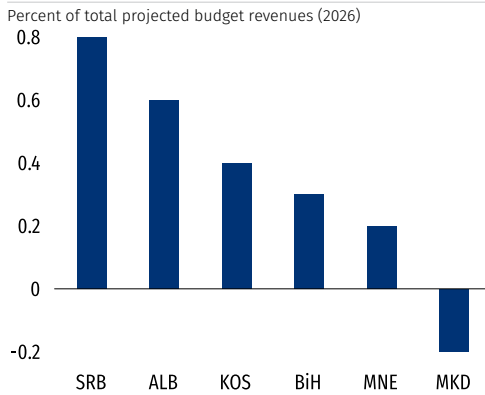
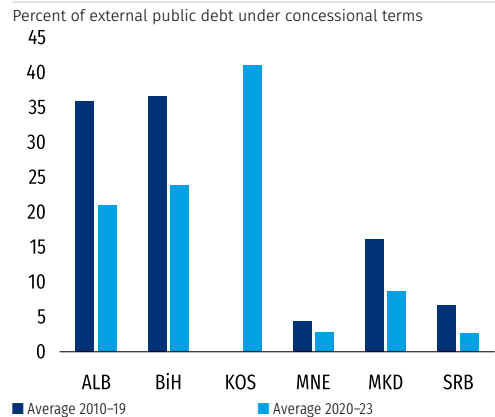


Figure 1.39 ...due in part to a decline in concessional borrowing



While PPG debt declined in four of the six economies, primary fiscal deficit dynamics suggest that fiscal space remains limited. The primary fiscal balance remained negative in 2025 across all countries except Albania, which recorded a modest surplus of 0.3 percent of GDP, down from 1.4 percent of GDP in 2024. This was Albania's third consecutive year

with surplus, consistent with its fiscal rule requiring a non-negative primary balance. Montenegro and North Macedonia posted the largest primary deficits in the region at 2.3 and 2.1 percent of GDP, respectively, followed by Bosnia and Herzegovina, Serbia, and Kosovo. In these five countries, primary deficits widened compared to the previous year, most notably in Montenegro,

where the deficit expanded by 1 ppts of GDP, while Kosovo shifted from a surplus to a deficit.

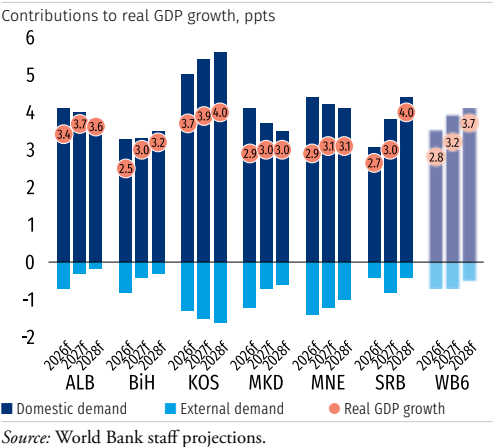
Widening deficits, coupled with mounting interest payments, are progressively narrowing the available fiscal space. Serbia and Albania will lose the most fiscal space due to higher upcoming spending on interest payments, while a similar but less pronounced trend is evident in other countries (Figure 1.38). These trends are partly explained by the maturation of past debts and partly by increased non-concessional borrowing. Concessional external public debt as a share of total external public debt is still relatively high in Kosovo, and to a lesser extent in Albania and Bosnia and Herzegovina, while it is low and declining in Montenegro, North Macedonia and Serbia (Figure 1.39).

While medium-term outlook remains cautiously positive, external pressures cloud the short-term development agenda

GDP growth in the Western Balkans is projected to remain subdued in 2026, as elevated geopolitical tensions and spillovers from the conflict in the Middle East are expected to weigh on domestic and external demand. In this context, energy and fertilizer prices have already pushed up inflation and are expected to dampen demand in the euro area. Growth forecasts for 2026 have been revised downward across all six Western Balkan economies since the fall 2025 edition of the RER from 3.1 percent to 2.8 percent, reflecting the impact of the conflict in the

Middle East and country-specific domestic developments. The largest downgrades are in Bosnia and Herzegovina and Serbia, reflecting notably a slower-than-expected pace of reforms implementation and strongly increasing headwinds from CBAM’s impact on carbon-intensive export sectors in Bosnia and Herzegovina, as well as strong inflationary pressures stemming from higher energy prices, given the elevated energy intensity and reliance on energy imports in both countries. Montenegro and North Macedonia are particularly vulnerable to the conflict, with transmission through higher inflation and external pressures amid constrained policy space. Amid the challenging external environment and elevated uncertainty, domestic demand is expected to continue to drive growth in the WB6 but be constrained by higher inflation, while net exports’ contribution is expected to remain negative (Figure 1.40).

Figure 1.40 GDP growth is expected to strengthen in the medium-term amid a more favorable external environment

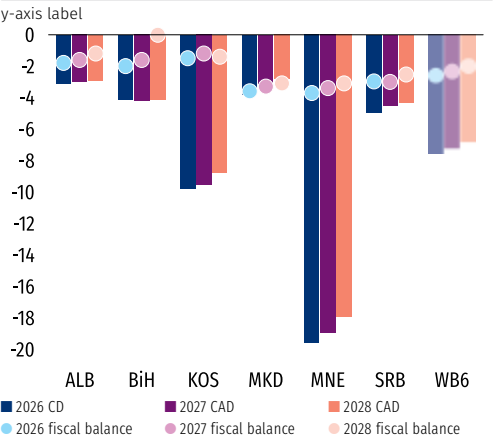


Growth in WB6 is projected to remain weak in 2026, gradually recovering in the medium term, supported by easing inflation, firming domestic demand, and an improving external environment. Kosovo's projected growth rate for 2026 is the fastest in the region at about 3.7 percent, as some of the political uncertainty from 2025 subsides. Serbia, the region's largest economy, is expected to see growth at 2.7 percent in 2026, 0.3 pts lower compared to the Fall 2025 forecast due to continued problems in SOEs, lack of progress in the next stage of structural reforms, and global and domestic uncertainty. Bosnia and Herzegovina is projected to record the lowest growth rate in the region at 2.5 percent, reflecting weaker export performance on the back of adverse impact from CBAM, delays in structural reforms and, limited political momentum to advance the reform agenda. In the medium term, regional growth is expected to strengthen gradually to 3.2 percent in 2027 and 3.7 percent in 2028, remaining above the euro area projections, as inflation is expected to ease, domestic demand to firm up, and external demand to improve. However, uncertainty remains elevated and the outlook is contingent on evolving external conditions and progress on domestic reforms. Convergence towards EU per-capita income level will hinge on sustained reforms to lift productivity, strengthen health and education outcomes, raise labor force participation, and improve investment efficiency.

Rising energy costs and a significant slowdown in the euro area will put pressure on external balances in the WB6 in 2026, though increased tourism and continued EU integration will provide partial support. The ongoing conflict in the Middle East is likely to widen external imbalances by driving up oil, gas, and fertilizer prices and increasing global risk premia through 2026, which will rise import bills across the region, as all WB6 economies are net energy importers. Kosovo and Montenegro are the most vulnerable to further deterioration in terms-of-trade due to their elevated current-account deficits, and North Macedonia is also highly exposed, with energy imports covering around 60 percent of its needs. In addition, growth in the euro area is projected to decline from 1.4 percent in 2025 to just 0.9 percent¹⁹ in 2026. This slowdown is expected to continue shaping the region's export and investment dynamics and will likely limit manufacturing exports—particularly in Bosnia and Herzegovina, North Macedonia, and Serbia. By contrast, more tourism-oriented economies such as Albania and Montenegro are anticipated to benefit from relatively resilient services exports, though not enough to offset import pressures—unless the conflict raises travel costs and disrupts routes. External conditions are expected to improve in 2027–28, with softer commodity prices and a gradual recovery of the euro area. As a result, the aggregate WB6 trade deficit is projected to widen in 2026 to about 17.3 percent of GDP before narrowing gradually to 16.5 percent by 2028, while the regional current-account deficit is

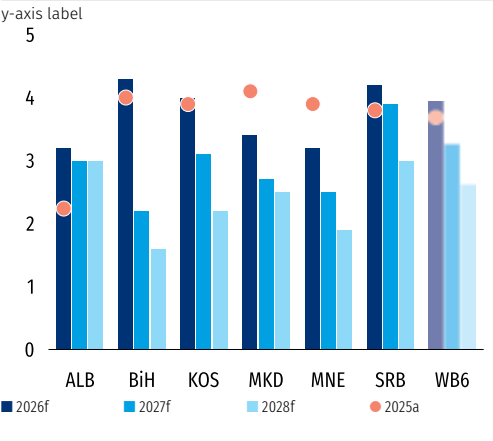
¹⁹ Consensus forecast as of April 13, 2026.

Figure 1.41 As external conditions improve over the medium term, both current accounts and fiscal deficit are expected to narrow



Source: World Bank staff projections.

Figure 1.42 Inflation is expected to remain elevated in 2026 with price pressures easing over the medium term



Source: World Bank staff projections.

Note: f=forecast, a=actual.

expected to deteriorate to 7.6 percent of GDP in 2026 and then improve modestly to 6.8 percent by 2028 (Figure 1.41). Amid elevated uncertainty, FDI in the WB6 is expected to remain constrained and uneven over the medium term, averaging about 4.5 percent of GDP. While still below pre-pandemic levels, FDI will continue to play an important role in financing external balances in the region and catalyzing international economic integration.

Regional inflation is projected to rise to an average of 3.9 percent in 2026, driven by higher energy and food prices, as well as continued demand-supporting fiscal policies (Figure 1.42). Inflation is expected to rise, year-on-year, in four of the six countries in 2026, due to the pass-through effect of higher energy and fertilizer prices, compounded by robust domestic wage growth and social support measures. Bosnia and Herzegovina is expected to record the region’s highest inflation rate, followed by Serbia and Kosovo, reflecting their greater

exposure to food- and energy-price shocks. Albania’s inflation rate is projected to rise but remain comparatively lower, driven by rising food prices and domestic pressures, including wage and rent increases, while the dominance of hydropower in the country’s energy mix limits the pass-through effect of higher global hydrocarbon costs. Inflation in North Macedonia and Montenegro is projected to ease but remain above 3 percent despite rising energy and food prices, reflecting base effects from the previous year, a lower energy component in the CPI relative to other WB6 countries, and in Montenegro, the influence of euro area monetary conditions due to euroization. Across the region, inflation is projected to ease by 2028 and fall to at or below 3 percent, as conflict-related external commodity pressures subside, with the sharpest decline expected in Bosnia and Herzegovina to 1.6 percent where faster disinflation relative to regional peers is supported by the currency board, which allows for a quicker pass-through of euro

area disinflation. In addition, domestic demand pressures are expected to ease as the effects of earlier increases in public wages and pensions fade and are unlikely to be repeated at the same scale.

To cushion the impact of rising energy prices and limit the pass-through to food and consumer prices, governments have begun introducing short-term support measures. Starting in the second half of March, governments in all WB6 countries implemented temporary fiscal measures and price controls designed to limit the impact of higher international energy prices. These policies are expected to remain in place until late April or end-May 2026, depending on the country. They include: (i) lower excise and/or VAT rates for fuel (Albania, Montenegro, North Macedonia, and Serbia); (ii) caps on profit margins for fuel (Albania, Bosnia and Herzegovina, and Kosovo), and (iii) caps on profit margins for essential food items (Bosnia and Herzegovina) (Table 1).

Untargeted support may be easier to roll out, but past energy and food price shocks show that targeted measures are more effective and more cost-efficient in protecting the most vulnerable. Continued reliance on administered prices risks compressing margins in fuel distribution and food retail, weakening VAT and corporate income tax performance in an already low-growth environment. By contrast, time-bound targeted support is generally more cost-effective, easier to unwind, and less distortionary, preserving fiscal space for further policy action without over-stimulating aggregate demand. Such measures could include targeted social

assistance and shock-responsive safety nets, while reducing inefficient tax expenditures and streamlining non-essential programs could free up additional fiscal resources. On the supply side, more flexible access to micro-credit, optimized agricultural support programs, and streamlined trade and investment policies could help mitigate the impact of external shocks on firms.

As external headwinds are expected to continue, supportive fiscal policies are anticipated to remain in place in 2026, with only moderate consolidation by 2028. The policy responses to the February 2026 energy price shock have increased fiscal pressures through higher subsidies and forgone revenues from tax relief and are likely to weigh on public finances in an environment of moderate growth and higher inflation. Absent the shock, fiscal balances would have been somewhat stronger. Instead, the regional fiscal deficit is projected to remain broadly unchanged from 2024 at about 2.6 percent of GDP in 2026, reflecting election cycles and expenditure rigidities, especially related to wages, pensions, social transfers, defense, and energy-related support measures. Fiscal positions are set to diverge across countries: Kosovo, Serbia, and Albania are expected to see their fiscal positions deteriorate temporarily in 2026. In Kosovo, the fiscal deficit is projected to widen, driven by expanded transfer schemes, higher pensions and child-benefit outlays, and structural changes to wage policy, though it should remain within the legally binding ceiling of 2 percent of GDP. Deficits are projected to rise in Serbia and Albania due to high levels of public investment and defense spending in the former and elevated pension

Table 1 Across the region, short-term fiscal measures were introduced to mitigate the impact of the conflict in the Middle East on households and firms

Albania	Fuel excise duty reduced by 20 percent when the fuel price exceeds 220 ALL per liter. Cap on wholesale and retail fuel prices.	Measures established by the Transparency Board
Bosnia and Herzegovina	Fuel margin caps set at 0.25 to 0.30 BAM per liter (in place and reaffirmed in 2026). Profit margin caps on 20 to 30 essential food products at the entity level. Maximum margins: up to 6–8 percent at the wholesale level and up to 8–12 percent at the retail level.	Price caps remain in force until May 1, 2026, in FBiH and until June 1, 2026, in RS.
Kosovo	Daily price-setting decisions for fuel based on the average cost of the last (previous day) 10 million liters of imported diesel and 1 million liters of imported non-diesel fuel products, while allowing a profit margin of up to 2 cents for wholesale and 12 cents for retail.	Supersedes previous decision on price caps.
Montenegro	Excise duties reduced by 50 percent on unleaded petrol and by 25 percent on gas oils used as motor fuel.	24 March–21 April 2026
North Macedonia	VAT on petrol and diesel reduced from 18 to 10 percent. Excise duties on diesel reduced by 4 denars and on gasoline 95 and 98 octanes by 2 denars per liter.	March 22–April 20 2026
Serbia	Fuel excise duty reduced by about €0.12 per liter.	In place until April 24, 2026

spending, wage indexation, defense outlays, and capital expenditures in the latter. North Macedonia and Montenegro are the only two countries expected to narrow their deficits, reflecting commitments to stronger revenue collection in the former and expenditure consolidation in the latter. Gradual fiscal consolidation over 2027–28 should bring the average regional deficit to 2.1 percent of GDP, assuming that temporary spending measures are unwound, revenue strategies take effect, EU funding absorption improves, and political constraints ease.

Downside risks dominate, but reform progress offers upside potential

The Western Balkans are expected to face a period of heightened uncertainty in 2026, with limited policy space to absorb further shocks. This constrained policy space reflects a broader erosion of the region's resilience, extending beyond fiscal space alone and encompassing limited room for monetary policy, weak external buffers, and exposure through the financial sector. While regional public and publicly guaranteed debt has continued its uninterrupted decline since 2020 and is expected to reach 44.7 percent of GDP

in 2026, primary deficits remain negative across all countries except Albania and projected to widen in several countries. Government deposits provide only a partial buffer, while rising interest payments are gradually eroding available fiscal space, particularly in Serbia and Albania. North Macedonia and Montenegro remain the most exposed to a tightening of financing conditions due to high public debt—a risk that financial markets have already begun to price in, as reflected in rising yields on sovereign Eurobonds, increased investor risk aversion, and higher borrowing costs. Constraints are further compounded by limited monetary and external adjustment capacity in parts of the region. Montenegro and Kosovo remain the most vulnerable to external shocks owing to their unilateral euroization. With such arrangements, external shocks such as commodity price surges, terms of trade deterioration, or shifts in global financial conditions must be absorbed through domestic price and wage adjustments or fiscal measures, both of which tend to be slower and more costly. Montenegro's high current account deficit and elevated public debt, and Kosovo's low reserve coverage at just 1.7 months of imports, and limited market access, leave both countries particularly exposed in the current environment.

Risks to the outlook remain tilted to the downside, as domestic and external factors could weigh on the region's recovery. Bosnia and Herzegovina, North Macedonia, and Serbia will all hold elections over 2026–28, and the resulting policy uncertainty could delay investment and slow the implementation of EU-aligned reforms under the Reform and Growth Facility

(RGF). Contingent liabilities arising from SOEs and public-private partnerships could further increase fiscal rigidity, especially in Kosovo, Montenegro, and Serbia. External headwinds, including a weaker-than-expected recovery in the euro area and/or additional geopolitical shocks, could depress exports and investment, particularly in manufacturing-intensive economies. A significant escalation of the conflict in the Middle East could result in the protracted disruption of shipping through the Strait of Hormuz and substantial damage to oil and gas production capacity, leading to persistently higher energy prices. Meanwhile, additional spillover effects from Russia's invasion of Ukraine could drive up energy and food prices, amplify financial market volatility, and raise borrowing costs. Policy measures could mitigate the pass-through effect of imported inflation but would impose additional fiscal costs. With the highest gross financing needs and some of the largest public debt ratios in the region, Albania, Montenegro, and North Macedonia would be particularly exposed to tighter financial conditions. Heightened rollover risks, diminished investment, and pressures on real incomes could reinforce downside risks across the WB6. The EU CBAM has taken an effect in 2026, introducing an additional source of cost and competitiveness risk for carbon-intensive exporters in the WB6, particularly aluminum, iron and steel, and electricity exports from Bosnia and Herzegovina and Montenegro, as well as iron and steel exports from North Macedonia and Serbia (Box 1.4).

Accelerated reform implementation, stronger institutional capacity, and greater policy stability all present upside risks to the regional outlook. Effective RGF implementation—particularly in Albania, Kosovo, Montenegro, Serbia, and North Macedonia—could enhance investment efficiency, reduce regulatory bottlenecks, and support competitiveness, while progress in Bosnia and Herzegovina would hinge on easing institutional constraints. Reduced domestic uncertainty in Bosnia and Herzegovina, Kosovo, and Serbia could significantly improve the business climate and strengthen private-sector confidence. On the external front, stronger-than-anticipated growth in the euro area would boost exports, investments, remittances, and tourism in the WB6. Easing geopolitical tensions would result in lower energy prices, reduced volatility, diminished risk premia, stronger investor confidence, and greater price stability, supporting the regional recovery. The adoption of the CBAM could also spur investment in decarbonization and energy efficiency in the WB6, helping firms—especially in carbon-intensive manufacturing sectors—adapt to

EU market requirements and strengthening competitiveness over the medium term.

Sustaining growth in the Western Balkans over the medium term will require faster reform implementation and stronger institutions, complemented by decisive action to unlock the region's human capital potential. Structural constraints in the region continue to weigh on competitiveness: unit labor costs are outpacing productivity growth, employment remains concentrated in low-productivity sectors, and skills mismatches limit integration into global value chains. At the same time, Western Balkan labor markets face a central paradox: labor shortages coexist with high unemployment and low participation, particularly among women and youth, while sustained outmigration drains the human capital base underpinning long-term productivity growth. In this context, realizing the potential of available human capital, particularly women, youth, and others facing barriers to employment will be essential to easing labor constraints, sustaining growth, and safeguarding long-term fiscal and social sustainability.

Box 1.4 Regional Trade Exposure to the CBAM

The CBAM is intended to align the carbon cost of certain imported goods with the carbon cost faced by EU producers under the EU Emissions Trading System (ETS).²⁰ The CBAM requires importers of covered goods to measure and report the emissions embedded in their production and to pay a carbon price based on those emissions comparable to the carbon costs faced by EU producers under the EU ETS. After a transition period from 2023 to 2025, which focused on emissions reporting, the CBAM's financial obligations entered into force in January 2026. The WB6 is closely integrated with the EU market and exports carbon-intensive products—such as iron and steel, aluminum, cement, and electricity—that fall directly within the CBAM's Phase 1 coverage. Starting in 2028, the CBAM will be extended to over 180 additional downstream products from the sectors already covered.

²⁰ https://ec.europa.eu/commission/presscorner/api/files/document/print/en/ip_25_3088/IP_25_3088_EN.pdf.

CBAM exposure across the WB6 is uneven, reflecting differences in export composition, economic size, and reliance on the EU market. Iron and steel account for a large share of CBAM-covered exports in Bosnia and Herzegovina, Kosovo, North Macedonia, and Serbia, while electricity dominates the exposure profile in Montenegro and represents a significant share in Albania, Kosovo, and North Macedonia. Aluminum contributes across all WB6 economies, with particularly large shares in Bosnia and Herzegovina and Serbia, while cement appears only marginally in Albania and Bosnia and Herzegovina. Fertilizers are negligible across the region and appear only in North Macedonia, where they represent a small share of total CBAM-covered exports.

The economic impact of the CBAM depends not only on the scale of exports but also on how emissions-intensive production is relative to EU producers. Estimates of “excess carbon payments”—the implied CBAM carbon cost relative to the EU—illustrate this point. While iron and steel and electricity account for a large share of CBAM-covered exports in several WB6 economies, other covered sectors such as cement and fertilizers can also generate non-negligible excess carbon payments when emissions intensity exceeds EU reference levels, even if export shares are smaller. For example, estimated CBAM payments for cement exports to the EU amount to roughly 2.9 percent of (2024) of cement export values in Serbia, around 2 percent in Bosnia and Herzegovina, and about 1.1 percent in Albania.²¹ For iron and steel exports, excess carbon payments range from zero in North Macedonia to around 4 percent in Albania, with levels in Serbia and Kosovo in between. These differences reflect variations in production technologies and energy inputs, highlighting the fact that countries with similar trade exposure can face different competitive pressures depending on their emissions intensity.

Reducing CBAM compliance costs hinges on the availability of verified emissions data and the presence of domestic carbon pricing. When facility-level data are not reported, CBAM regulations require the use of default emissions values, which include a conservative markup that may lead to higher measured carbon costs than those implied by actual performance. At the same time, domestic carbon pricing affects where and how carbon costs are paid: when a domestic carbon price is in place, part of the carbon cost is paid domestically rather than at the EU border, allowing revenues to accrue at home and potentially reducing residual CBAM payments, depending on the difference between EU carbon prices and those applied in exporting countries.

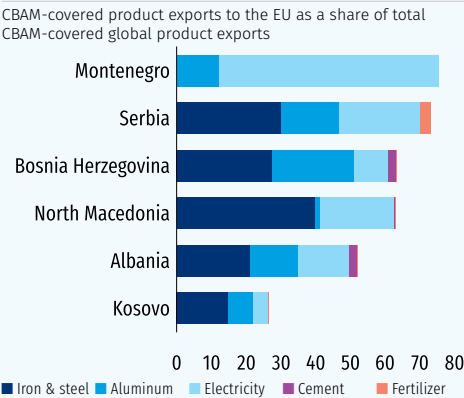
WB6 countries vary in terms of their readiness to address the impact of the CBAM. Montenegro has an emissions-trading system, but it is currently very limited in practice, with only one remaining covered operator, and a coal tax. Serbia has taken steps to establish both the necessary pricing and infrastructure systems, including a national carbon-emissions tax (albeit set at a low level) that entered into force on 1 January 2026 and an EU-aligned monitoring, reporting, verification, and accreditation framework.²² Albania has begun a phased reform of its carbon tax on coal, and its climate law forms the basis for strengthening climate-related monitoring, reporting, and verification (MRV) arrangements. Kosovo has adopted a Law on Climate Change that explicitly references alignment with key EU climate governance and MRV instruments. North Macedonia has developed national MRV diagnostics and documentation standards and continues to work on enhancing transparency in line with international and

21 World Bank staff calculations based on Maliszewska, M., C. Fischer, E. Jung, and M. Chepeliev. 2025. Carbon Border Adjustment Mechanism (CBAM) Exposure Indices: Methodological Note. Prosperity Notes Series. Washington, DC: World Bank.

22 MRVA - refers to the framework required for tracking and verifying greenhouse gas emissions, a foundational building block for carbon pricing systems and compliance with CBAM requirements.

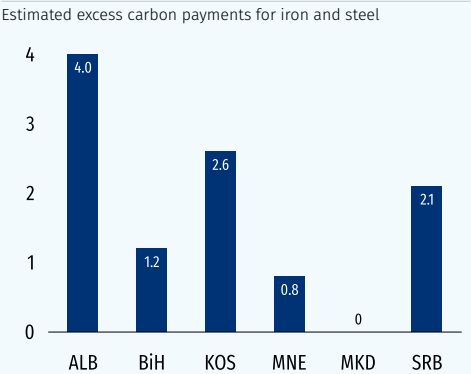
EU-accession obligations, but its flagship climate law is still pending adoption. Bosnia and Herzegovina is engaged in ongoing institution-building efforts, including workstreams supported through EU programs and an initiative to develop MRV frameworks.

Figure 1.43 Iron and steel and electricity account for most CBAM exposure in the Western Balkans



Source: WITS trade data 2024 (Kosovo sourced from BACI and is 2023, WB/IMF GDP data.

Figure 1.44 Emissions intensity drives large differences in CBAM-related carbon costs for iron and steel



Source: World Bank staff calculation using the methodology from Maliszewska et al (2025).

Readiness for potential CBAM-related electricity exemptions remains limited across the WB6. Under the CBAM rules, a time-bounded exemption for electricity is linked primarily to integration with the EU internal electricity market, as well as additional criteria monitored by the Energy Community, including progress on climate and carbon-pricing frameworks. The latest Energy Community CBAM Readiness Tracker found that no WB6 economy currently qualifies for an electricity exemption, implying that CBAM-related carbon costs are likely to apply to all electricity exports from the region in the near term. Urgent policy priorities for the WB6 include strengthening MRV systems, advancing credible carbon-pricing pathways, accelerating electricity-market integration, and implementing sectoral reforms, particularly in countries where CBAM exposure is driven by electricity and other energy-intensive exports.

The CBAM poses important compliance and competitiveness challenges, but it also presents opportunities, both of which are concentrated in a narrow range of energy-intensive sectors and countries. For the WB6, the impact will depend not only on emissions intensity in key industries but also on policy readiness—particularly the development of credible MRV systems and progress in industrial decarbonization and cleaner energy, which will shape firms’ ability to comply with EU requirements and maintain market access. While shifting exports away from the EU market is possible, high shipping costs and policy constraints limit the scope to diversify export destinations.

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Chapter 2: Spotlight: Mobilizing Underutilized Human Capital

Chapter 2: Spotlight: Mobilizing Underutilized Human Capital

Although educational attainment is steadily increasing in the Western Balkans, the countries of the Western Balkans continue to underutilize their human capital. Many individuals, especially women and youth, are poised to make valuable contributions to the workforce. Their current lower participation and employment rates highlight not only an opportunity to enhance equity, but also a chance to drive productivity, resilience, and economic growth. By expanding access to affordable, high-quality childcare and long-term care services, the region can empower more caregivers—who are often women—to pursue meaningful employment. Furthermore, the growing gig and platform economy provides flexible work options for those with caregiving and other responsibilities. With supportive regulatory frameworks in place, these opportunities can foster secure, decent jobs and help unlock the full potential of the workforce.

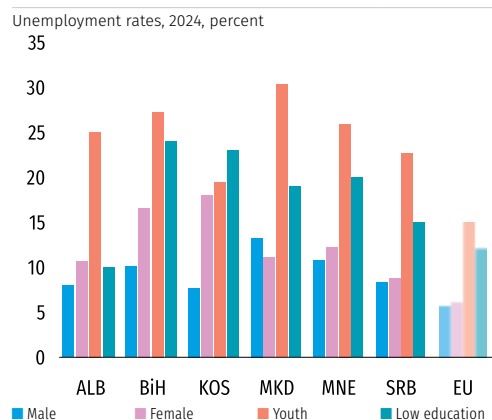
Rapid population aging compounds these challenges. Western Balkan countries are among the most rapidly aging in Europe and are projected to become super-aged²³ within the next decade, intensifying labor shortages that are already emerging in several sectors. In this context, realizing the potential of the region's human capital—particularly women, youth, and other groups facing barriers to work—will be vital to mitigate labor constraints, sustain economic growth, and support long-term fiscal and social sustainability. These pressures are further intensified by sustained outmigration of working age populations across skill levels and by reported labor shortages, even as unemployment and inactivity remain high.

Mobilizing underutilized human capital in the Western Balkans will require a comprehensive and coordinated reform agenda. Key priorities include: (i) reducing labor-market disincentives through targeted reforms to tax and social benefit systems and alleviating constraints linked to childcare and eldercare responsibilities; (ii) aligning skills with employer demand while supporting vulnerable jobseekers and youth not in employment, education, or training (NEET) through strengthened activation, guidance, and employment services; and (iii) expanding access to inclusive, high-quality job opportunities by promoting nondiscriminatory, flexible, and decent work environments, including for platform-based gig workers.

²³ Superaged is defined as having at least one fifth of the population aged 65 and above.

Mobilizing the underutilized labor potential of the Western Balkans will be vital to sustain economic growth across the region and offset the increasingly acute labor shortage expected from 2030 onward. The Fall 2025 Regional Economic Report highlighted a central paradox in the Western Balkan labor markets: labor shortages coexist with persistently high unemployment (Figure 2.1) and low rates of labor-force participation (Figure 2.2), especially among women and youth, despite rising levels of educational attainment. This disconnect points to structural constraints that prevent large segments of the population from contributing productively to the economy. Raising participation rates to the same level as comparators in the EU would add over 2.8 million people to the regional labor market. Under assumptions of sufficient labor demand and no labor market frictions, a comparable increase in female participation could raise the region's annual GDP growth by about 0.35 percentage points.

Figure 2.1 Unemployment remains high among women, youth and the low-educated...

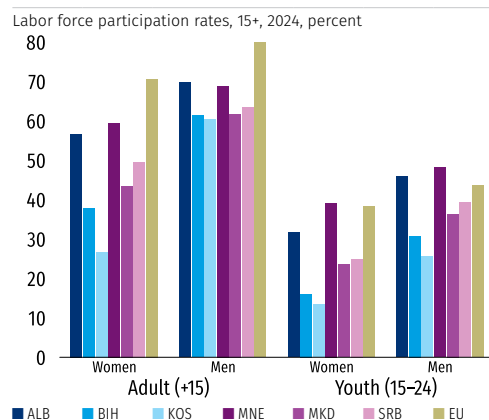


Source: Labor Force Survey (LFS) 2024 (Albania: 2023); low education data for 2023.

Note: Low-educated means less than secondary education.

In the Western Balkans, underemployment among women and youth does not reflect widespread part time or temporary work as in many EU countries, but a broader pattern of underutilization. Compared to the EU, gaps are driven mainly by low labor force participation, constrained working hours due to care responsibilities, difficulties translating education into employment, and limited participation in entrepreneurship and higher productivity occupations. These forms of underutilization are closely linked to deficits in childcare and eldercare coverage, skills mismatches, and weak transitions from education to work, rather than to an excess of non standard jobs. Recognizing these structural differences is essential for identifying policies that can effectively mobilize the region's untapped human capital.

Figure 2.2 ...and labor-force participation rates are persistently low



Source: World Bank staff calculations based on LFS and Eurostat.

The human capital of women is significantly underutilized

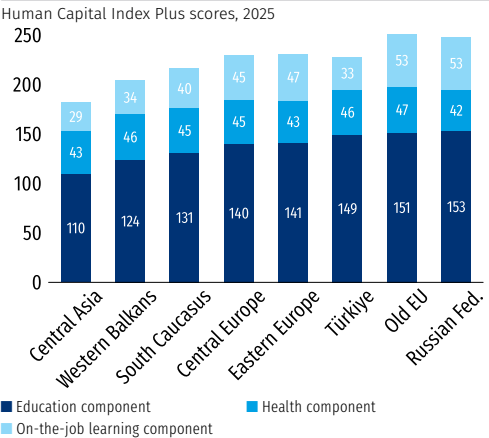
Workers in the Western Balkans face substantially lower lifetime productivity and earnings potential than those in the European Union.²⁴ The Human Capital Index Plus (HCI+), which measures the human capital a child born today can expect to accumulate over their working life based on current levels of health, education, and employment, places the WB6 average at 203 out of 325—over 40 points below the EU average and well below those of other middle income regions in Europe (Figure 2.3). As each point on the index corresponds to approximately a 1 percent difference in expected lifetime labor earnings, this gap is consistent with earnings potential in the Western Balkans being roughly 40 percent lower than in the EU, associated with significantly lower levels of human capital.²⁵ Substantial variation was also observed

within the WB6, with Kosovo scoring lowest and trailing the top performer, Serbia, by around 60 points. The gap mainly reflects differences in educational attainment due to lower school quality, limited access to pre-primary education, and lower tertiary completion rates in several countries. While the expected years of schooling in the Western Balkans are similar to the EU average, international test scores point to weaker learning outcomes. Limited preschool enrollment in Bosnia and Herzegovina, Kosovo, and North Macedonia further undermines early skill formation.²⁶

Gender gaps in earnings-potential persist across all WB6 countries and are particularly pronounced in Kosovo and Bosnia and Herzegovina. In most WB6 countries, human capital indicators for women are equal to or higher than those for men, driven by better health indicators and greater educational attainment, especially at the tertiary level. However, women’s human capital does not translate into commensurate employment outcomes (Figure 2.4). Serbia is the only WB6 country where women’s expected lifetime earnings exceed those of men.

Gender gaps in employment outcomes are equally sizeable and are driven mainly by low female labor force participation. The employment pillar of the HCI+ reveals the stark underutilization of women’s human capital (Figure 2.5). Gender gaps in

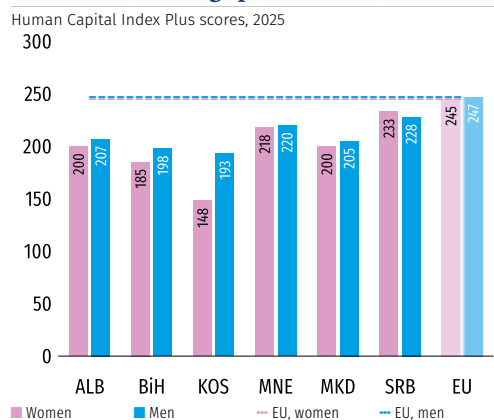
Figure 2.3 Human capital outcomes in ECA



Source: Human Capital Index Plus 2025.

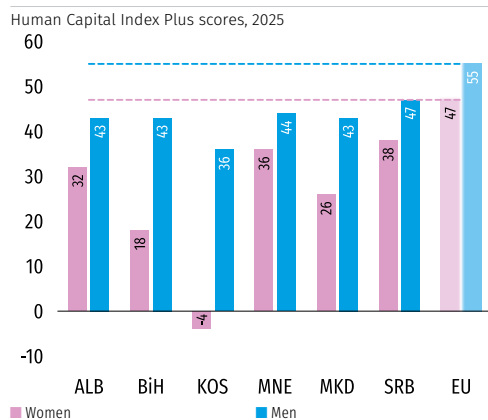
24 Human Capital Index Plus <https://humancapital.worldbank.org/hcplus/>.
25 World Bank. 2026. The Human Capital Index Plus 2026: Findings Brief. World Bank. <http://hdl.handle.net/10986/44305>.
26 Western Balkans Regular Economic Report No. 28, Fall 2025: Towards Better Jobs. World Bank (2025). <http://documents.worldbank.org/curated/en/099100625100539134>.

Figure 2.4 Men have higher expected lifetime productivity and earnings potential than women



employment outcomes reached 40 points in Kosovo²⁷ and 25 points in Bosnia and Herzegovina, with sizable disparities also observed in North Macedonia and Albania. On average, the male labor-force participation rate exceeds the female rate by 18 percentage points across the WB6 and is exceptionally low in Kosovo. Youth outcomes are similarly weak: labor-force participation among those aged 15–24 lags the EU average by 6 percentage points among men and 13 percentage points among women, resulting in lost early-career learning and professional development, skills erosion, and forgone productivity.

Figure 2.5 Women substantially underperform in employment outcomes across the WB6



Youth struggle to translate human capital into employment due to skill mismatches

Despite rising educational attainment, youth in the Western Balkans, including highly educated, continue to face difficulties translating their human capital into positive labor-market outcomes. While NEET²⁸ rates among those aged 15–29 have declined since 2015, they remain elevated at 22.5 percent on average, nearly twice the EU level. Young women consistently experience higher NEET rates than men across the region, with gender gaps reaching 8.5 percentage points in Kosovo (Figure 2.6). Youth with tertiary education face persistent barriers in several countries. In 2023, NEET rates among tertiary-educated youth ranged from 16 percent in Serbia to nearly 40 percent

27 Kosovo's HCI+ employment pillar score for women is negative as the level of skills depreciation among women not working exceeds the level of human capital utilization and further accumulation at work among working women, due to very low female labor force participation. HCI+ measures the negative impact of not working on log earnings as "skills depreciation," capturing the scarring effect on wages. The assumption is that productivity drops by 1.25 percent per year when individuals do not work. Details of HCI+ methodology can be found in its Methodology Note <https://openknowledge.worldbank.org/entities/publication/8c011df6-2134-4da6-8f40-160ce2cf37a4>.

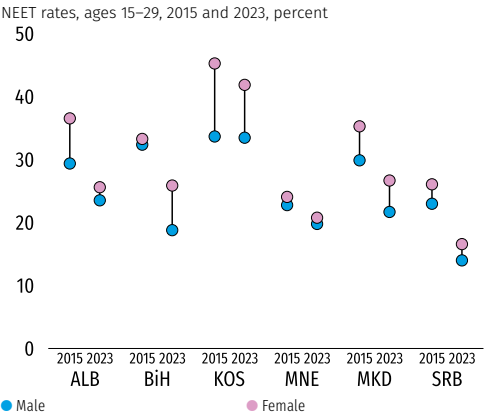
28 NEET stands for not in employment, education, or training.

in Kosovo, compared to just 8 percent in the EU (Figure 2.7). In Bosnia and Herzegovina, Kosovo, and Serbia, tertiary-educated women are 6–10 percentage points more likely to be NEET than men, pointing to structural barriers beyond education attainment.

These outcomes reflect constraints on both the supply and demand sides of the labor market: low-quality skills due to learning deficits, and limited high-skill job opportunities. The region has seen a significant rise in educational attainment over recent decades, yet more schooling has not meant better schooling—gains in attainment have not translated into commensurate gains in skill quality or

relevance. International test scores have stagnated or declined since 2020,²⁹ and employers frequently report difficulty finding workers with the skills their businesses need. In OECD surveys, nearly one in four firms identify workforce skills as a major constraint on competitiveness.³⁰ At the same time, slow structural transformation has limited the creation of high-skill jobs, and labor demand remains skewed toward medium- and low-skill routine tasks. Only around 39 percent of tasks performed by tertiary-educated workers in the region involve non-routine analytical skills, resulting in widespread vertical skills mismatches that diminish earnings and raise the risk of skill erosion.³¹

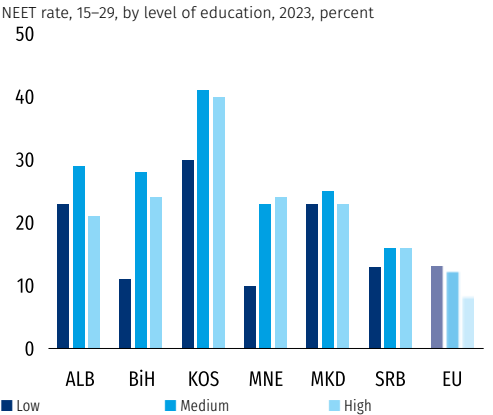
Figure 2.6 NEET rates remain high across WB6, especially among women...



Source: Jobs Gateway.

Note: Indicators showing educational attainment are based on the International Standard Classification of Education (ISCED 1997 or ISCED 2011). In the following tables, as well as in the SEE Jobs Gateway Database, the definition of low-educated (level 0–2), medium-educated (level 3–4), and high-educated (level 5–8) refers to ISCED 2011. Any deviations (application of ISCED 1997) are described in the metadata. Detailed ISCED 2011 levels of education: 0 = early childhood education, 1 = primary education, 2 = lower secondary education, 3 = upper secondary education, 4 = post-secondary non-tertiary education, 5 = short-cycle tertiary education, 6 = bachelor's or equivalent, 7 = master's or equivalent, 8 = doctorate or equivalent.

Figure 2.7 ...and tertiary-educated youth



29 Harmonized Test Scores - Human Capital Data Portal, World Bank https://humancapital.worldbank.org/en/indicator/HD_HCIP_HLOS.

30 Western Balkans Competitiveness Outlook 2024: Regional Profile, OCED (2024) https://www.oecd.org/content/dam/oecd/en/publications/reports/2024/06/western-balkans-competitiveness-outlook-2024-regional-profile_359dd5b9/170b0e53-en.pdf.

31 World Bank Western Balkans Regular Economic Report, Fall 2025.

Compounding these mismatches, informal employment represents a further dimension of human capital under-utilization. Low wages can push workers toward informal arrangements where, despite marginally higher disposable income in the absence of tax obligations, opportunities for on-the-job skill development and productivity increases remain severely limited. Informality thus reinforces the low-skill equilibrium, trapping workers from a young age outside the structures that foster productivity growth and keep skills current. Available estimates confirm that informal employment remains widespread across the region, with shares reaching 34.2 percent in Albania and 30.5 percent in Kosovo, and somewhat lower but still notable levels in Serbia (11 percent) and North Macedonia (10 percent).

Young women face additional school-to-work transition barriers linked to social norms, care responsibilities, and field-of-study choices. Evidence from a graduate tracer survey in North Macedonia indicates that care responsibilities are a leading reason for economic inactivity even among highly educated women, while employment outcomes vary sharply by field of study.³² ICT and engineering graduates exhibit relatively strong employment outcomes, yet women remain underrepresented in these fields³³ and overrepresented in disciplines such as education, health, arts, and humanities, which are associated with weaker labor-market returns (Box 2.1). This pattern highlights a misalignment

between students' field of study choices and labor market demand, particularly among young women, and underscores the need to support informed study and career decisions using up to date labor market information.

Gaps in job quality and pay are shaped by sectoral and occupational allocations

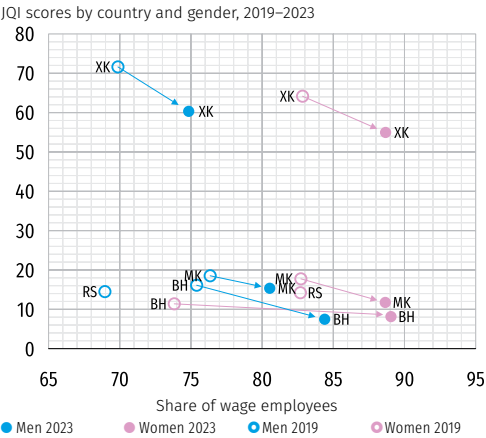
Gender differences in job quality in the Western Balkans are generally modest and reflect primarily the sorting of women and men into different sectors and occupations, rather than systematic within-job disparities. Job quality, measured using the Multidimensional Job Quality Index (JQI), which captures labor income, access to benefits, job stability, and working conditions, has improved for both women and men since 2019, driven largely by a rising share of wage (and thus more formal) employment and a declining share of poor-quality jobs (Figure 2.8). These aggregate gains, however, mask important structural differences in sectoral employment. Women are disproportionately concentrated in the public sector and heavily regulated sectors such as education, health, and certain services, while men dominate construction, manufacturing, transport, energy, and extractive industries. Construction alone accounts for around 10–15 percent of male employment but only 1–2 percent of female employment, while education and health absorb one-quarter to one-third of female

32 Brodmann, S., Naceva, B., von Lenthe, C. and Vadle, Z. 2025. Education-to-Work Transition in North Macedonia: Insights from the 2025 Graduate Tracer Survey.

33 Tertiary education statistics, Eurostat, (2025) https://ec.europa.eu/eurostat/statistics-explained/index.php?title=tertiary_education_statistics.

employment across the region—reaching nearly 40 percent in Kosovo. Because male-dominated sectors tend to be more cyclical, informal, and weakly protected, men in several countries exhibit a slightly higher incidence and intensity of low-quality employment. Taken together, these patterns indicate that gender differences in job quality are driven mainly by sectoral allocation and that recent improvements—associated mainly with policy-driven formalization and minimum-wage increases rather than productivity-led improvements—will need to be complemented by reforms that promote firm upgrading and the creation of higher-quality jobs.³⁴

Figure 2.8 Multidimensional job-quality indicators have improved due to rising formal employment



Source: Author’s calculations based on Labor Force Surveys.

Note: The JQI headcount refers to a share of the workforce employed in jobs that fail to meet acceptable quality thresholds across the JQI dimensions (labor income, access to benefits, job stability, and working conditions).

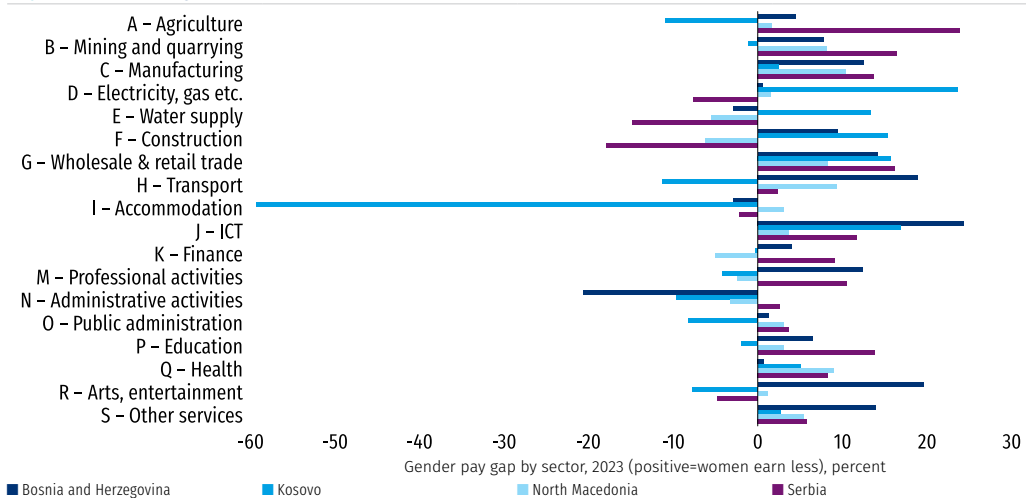
Women tend to face persistent pay penalties in market-oriented sectors such as manufacturing, trade, and ICT, while education, health, and public administration display smaller, zero, or

even reversed gaps. This contrast reflects sector-specific wage-setting mechanisms: the trade sector exhibits consistent female pay penalties across countries, whereas institutional wage-setting and pay compression mitigate gaps in public services (Figure 2.9). Overall, gender pay inequality is concentrated in competitive private-sector activities, while regulated sectors provide partial protection.

Gender differences are more pronounced between occupations than between sectors.

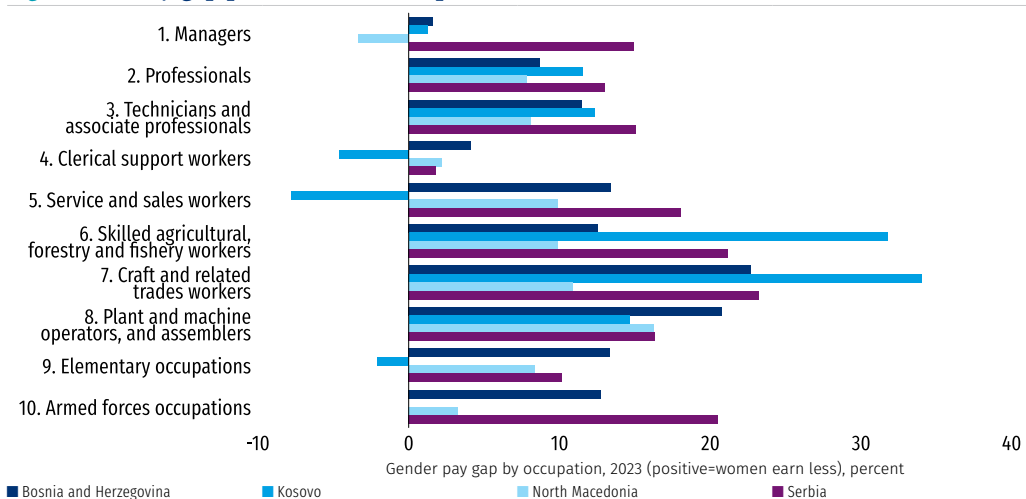
Women are heavily concentrated in professional, clerical, service, and sales occupations, while men dominate craft trades, plant and machine operation, and other production-oriented roles. About 25–36 percent of employed women are professionals, compared to 13–17 percent of men, highlighting women’s strong presence in education and health. By contrast, craft and machine-operator occupations account for 35–45 percent of male employment but rarely more than 5–15 percent for women. These patterns reinforce women’s concentration in occupations with compressed pay structures and limited advancement, while men cluster in occupations with greater wage dispersion and bargaining power. Gender gaps are largest in manual labor and production, often exceeding 20 percent (Figure 2.10). Professional and technical roles exhibit moderate but persistent gender gaps, while clerical, service, and sales occupations tend to have smaller gaps, reflecting standardized pay-setting structures.

³⁴ World Bank Western Balkans Regular Economic Report, Fall 2025.

Figure 2.9 Pay gap is wide in market-oriented sectors

Source: Author's calculation based on Labor Force Surveys.

Note: L – Real estate; T – Activities of households as employers; and U – Activities of extraterritorial organizations and bodies are excluded sectors due to sizes below 1 percent. Gender pay gap refers to the raw difference between average wages of men and women expressed as percentage of men's average wage.

Figure 2.10 Pay gap persists across occupations

Source: Author's calculation based on Labor Force Surveys.

Job-quality and pay-gap analyses reveal a structural interaction between sectoral and occupational allocation, job quality, and earnings that underscores the importance of promoting pay equity and career pathways for women, especially in male-dominated sectors and occupations (Box 2.1). Women's disadvantages in the labor market largely

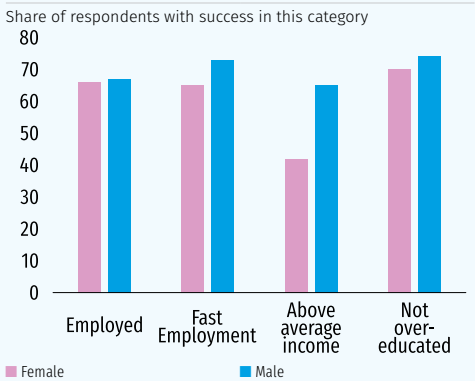
reflect their concentration in a narrow set of regulated sectors and occupations rather than systematic discrimination within sectors or occupations. However, within-sector and -occupation discrimination still exists, mainly in male-dominated and market-oriented sectors and occupations that employ a small share of female workers. Enhancing women's career opportunities

Box 2.1 The Graduate Tracer Survey in North Macedonia

Most Bachelor graduates in North Macedonia transition into work or further studies, but a sizable minority remains disconnected from the labor market. The Ministry of Education and Science conducted a graduate tracer survey in 2025 covering Bachelor graduates from public universities approximately one and a half years after graduation. The survey finds that around 70 percent of graduates had transitioned into employment or further studies, while about 15 percent were neither in employment, education, nor training (NEET), with no marked gender differences in NEET status.

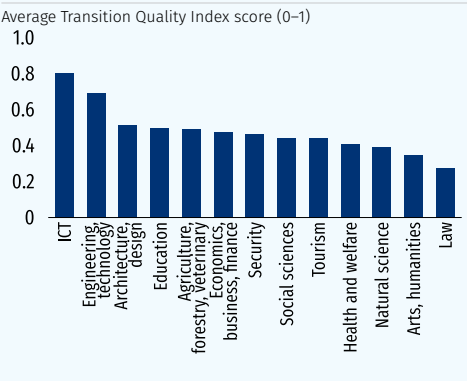
Gender gaps in the education to work transition emerge primarily in job quality rather than in employment rates. Beyond employment status, the survey allows assessment of the quality of the transition along multiple dimensions. Figure 2.11 presents four indicators for graduates who are no longer studying: (i) being employed, (ii) securing a first job within one month, (iii) earning above average wages, and (iv) having a vertical skills match. While overall employment rates are similar for men and women, female graduates perform worse on several quality dimensions, particularly in earnings and speed of labor-market entry, pointing to gender-specific barriers beyond access to jobs.

Figure 2.11 Female graduates exhibit slower transition to work and below average earnings



Source: Authors' calculations based on Graduate Tracer Survey.
Note: Bars represent the share of graduates that are currently not studying, for which the given dimension is considered a success.

Figure 2.12 Transition quality varies depending on the field of study



Source: Authors' calculations based on Graduate Tracer Survey.
Note: Results for some fields should be interpreted with caution due to small sample sizes.

Labor market transition quality varies sharply by field of study, reflecting large differences in demand for graduates' skills. Figure 2.12 shows that graduates from ICT and Engineering perform strongly across all four dimensions, suggesting robust demand for technical skills. By contrast, employment rates and transition quality are substantially lower in Law, Arts and Humanities, and Natural Sciences, indicating weaker labor demand or a greater need for further qualifications.

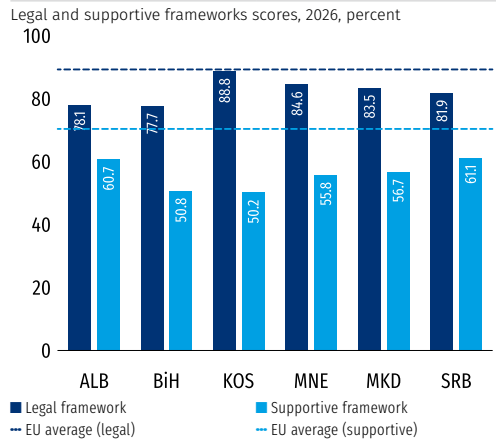
Differences in the field of study explain an important share of gender gaps in transition outcomes, but do not account for them fully. A Blinder-Oaxaca decomposition reveals that roughly half of the gap in transition quality between men and women can be explained by observable characteristics such as field of study, age, educational institution, and ethnicity, while the remaining half is unexplained. Moreover, gender disparities within fields of study indicate that other structural labor-market obstacles persist.

and progression in market-oriented sectors and occupations requires targeted skills development, apprenticeships, and employer engagement, coupled with stronger policies to support women's career advancement, by alleviating constraints such as care responsibilities, and reducing discrimination by employers in recruitment, pay, and promotion.

Enforcement of legal frameworks can promote women's economic participation

Western Balkan countries are relatively close to EU averages in terms of legal protections for women's economic participation, but supportive frameworks lag. In the 2026 Women, Business, and the Law (WBL) index, Western Balkan countries scored an average of 82 points out of 100 on indicators of the legal framework for women's economic participation (below the EU average of 89), with Kosovo scoring highest and Albania and Bosnia and Herzegovina scoring lowest (Figure 2.13). By contrast, WBL scores for supportive frameworks—capturing policies, implementing institutions, guidelines, programs, budgets, and monitoring systems—averaged only 56 points across the Western Balkans, well below EU levels; even the highest-scoring country, Serbia, reached only 61 points, underscoring persistent implementation gaps.

Figure 2.13 Supportive framework to promote gender equality needs to be strengthened



Source: Women, Business, and Law 2026.

Formal protections against workplace discrimination exist, but weak implementation and limited support for flexible work reduce their effectiveness. All WB6 countries prohibit gender discrimination in employment, and most also ban recruitment discrimination based on marital or parental status, yet guidance, monitoring, and employer awareness-raising measures to ensure fair recruitment and equal treatment are largely absent. Gaps are particularly evident in flexible work policies: while some countries recognize a right to request flexibility in work location, none provide legal recognition of flexibility in working time, and practical guidance to support employers remains minimal. These shortcomings matter because international evidence shows that access to flexible work arrangements can raise women's labor-force participation and retention by helping reconcile paid work with caregiving responsibilities.³⁵

³⁵ Women, Business and the Law 2024, World Bank (2024) <https://openknowledge.worldbank.org/entities/publication/853a55af-f1ba-4979-949c-61979af2fbb9>.

The design of social insurance and labor taxation further constrains flexible employment arrangements. In most WB6 countries (except Montenegro), social security contributions are levied on a relatively high minimum contribution base rather than on actual earnings, requiring employers hiring part-time or low-wage workers to pay contributions close to those for full-time earners and making part-time employment disproportionately costly. Legal recognition and guidance alone are therefore insufficient without fiscal and social security reforms that reduce disincentives for flexible work.

Equal pay frameworks remain weak in parts of the region, with limited transparency and enforcement. Bosnia and Herzegovina, Montenegro, and North Macedonia do not mandate equal remuneration for work of equal value, and several countries continue to restrict women's employment in certain sectors or conditions, reinforcing sectoral and occupational segregation. Compensation-related transparency and enforcement mechanisms are largely absent, and Serbia is the only WB6 country with a formal body empowered to address wage discrimination.³⁶ Evidence from the EU suggests that mandatory employer reporting of compensation and other transparency measures can significantly

reduce gender pay gaps;³⁷ for instance, a Danish reform requiring companies to disclose compensation reduced the gender gap by an estimated 13 percent.³⁸

Women's entrepreneurship is not restricted by law, but proactive measures are needed to close large participation and finance gaps. Across the region, women have equal rights to sign contracts, open bank accounts, register businesses, and access credit, and gender discrimination in lending decisions is prohibited; nevertheless, women remain significantly underrepresented in entrepreneurship, with only about 13 percent of firms on average being majority women-owned.³⁹ More advanced legal instruments—such as gender quotas and gender-responsive procurement—could strengthen women's leadership and business development: only Kosovo has introduced a legal gender quota for corporate boards, and only Kosovo and Montenegro have established gender-sensitive provisions in public procurement legislation. Worldwide, public procurement totals nearly US\$9.5 trillion annually, yet women-owned businesses receive only 1 percent of procurement contracts, suggesting substantial untapped potential in expanding access across the WB6.⁴⁰ Financial inclusion gaps persist: roughly 54 percent of women hold an account at a formal financial institution, with an

36 Commissioner for Protection of Equality in Serbia (accessed on 20 February 2026) <https://ravnopravnost.gov.rs/en/discrimination/legal-protection-misdemeanor-matters/>.

37 Pay transparency in the EU, European Council (accessed on 20 February 2026) <https://www.consilium.europa.eu/en/policies/pay-transparency/>.

38 Women, Business and the Law 2025: Methodology Handbook, World Bank (2025) <https://openknowledge.worldbank.org/entities/publication/41c18d3e-383a-47ec-b625-619a7bfaf25b>.

39 World Bank Enterprise Survey (Albania and Kosovo from 2025; Serbia from 2024; Bosnia Herzegovina, Montenegro, and North Macedonia from 2023). <https://www.enterprisesurveys.org/en/data>.

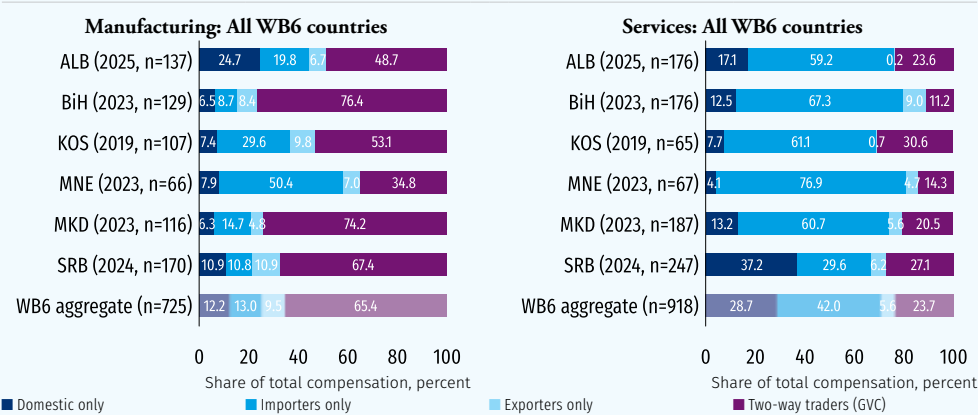
40 Women, Business and the Law 2024, World Bank (2024) <https://openknowledge.worldbank.org/entities/publication/853a55af-f1ba-4979-949c-61979af2fbb9>.

Box 2.2 Trading Firms and Job Creation for Women and Youth in WB6

Deeper trade integration is closely linked to higher labor compensation and better job outcomes, but these gains remain uneven across workers and firms. Women and female owned firms, especially in services, capture a smaller share of these benefits, pointing to constraints related to firm size, productivity, and skills. Policies that support firms’ integration into trade, while simultaneously investing in skills development, workforce upgrading, and targeted support for women led businesses, can help ensure that the job and wage gains from trade translate into more inclusive opportunities for women and young workers across the Western Balkans.⁴⁷

GVC firms account, on average, for 65.1 percent of female manufacturing income and revenues across the WB6. Importers’ share of female compensation (16.3 percent) is slightly higher than their overall contribution, while domestic firms account for a smaller share (9.3 percent). This is similar to the average pattern (Figure 2.14, left panel). Focusing on skilled workers—captured by their qualification and occupational role (for manufacturing) and educational achievement (for services)—yields similar results, with GVC firms accounting for 65.7 percent of compensation, indicating that trade integration benefits workers broadly rather than disproportionately favoring skilled labor. By contrast, GVC firms account for a smaller share of services compensation (23.7 percent), and an even lower share of female compensation (17.3 percent) (Figure 2.14, right panel). Serbia stands out as an outlier, where domestic firms contribute a larger share of services compensation (37.2 percent) than the WB6 average (28.7 percent), while the role of importers is more limited at 29.6 percent.

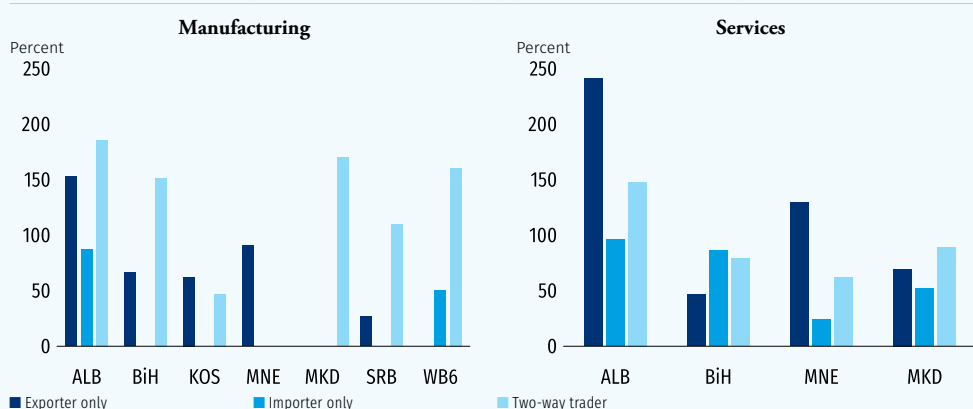
Figure 2.14 Share of total compensation by firms’ trading status



Source: World Bank Enterprise Surveys.

Note: Total compensation in constant 2009 USD.

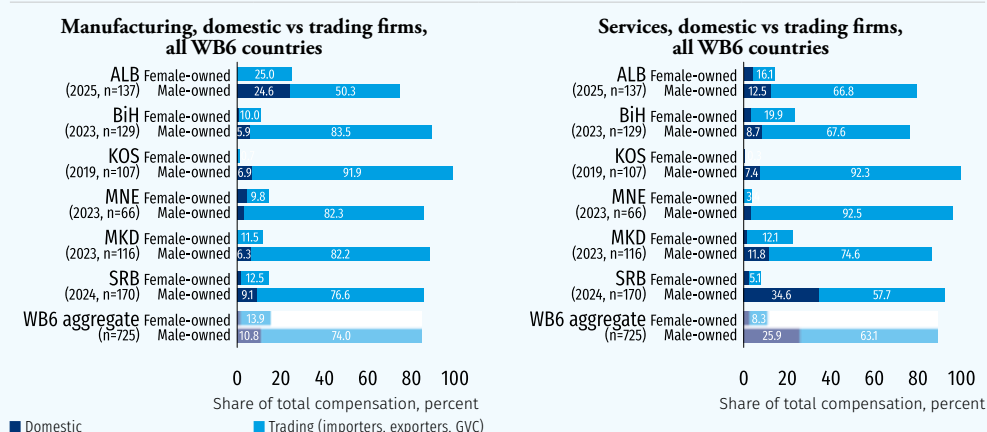
⁴⁷ Drawing on Enterprise Survey data from all WB6 countries, this analysis examines how firms’ trading status relates to the creation of more and better jobs, with particular attention to women. It quantifies the contribution of trading firms to total labor compensation, separately for manufacturing and services, and assesses econometrically whether trading firms earn a labor compensation premium after controlling for sectoral and regional characteristics. Labor compensation serves as a proxy for job quantity and quality, reflecting both employment levels and wage rates. Firms are classified into four groups: exporter-only (with exports accounting for at least 10 percent of sales), importer-only (with imported inputs accounting for at least 10 percent of total inputs), two-way traders (GVC participants), and non-trading domestic firms. The analysis also explores outcomes for female workers and firms with majority female ownership (at least 50 percent).

Figure 2.15 Labor earnings premium of trading firms relative to domestic-only firms

Source: World Bank Enterprise Surveys.

Note: The analysis for services includes the two most recent available years for all countries. For manufacturing, all available years are included (four years total), apart from Albania, which has three years of data available. The figures report the estimated premium in the labor earnings (in logs) in percent for trading firms relative to domestic firms. The regressions include the trade indicators, region and sector fixed effects. All reported results are statistically significant at the 10-percent level.

GVC firms in manufacturing hold a significant labor compensation premium of 160 percent over firms that do not trade at all (Figure 2.15, left panel). However, these gains are not uniform across the region. The labor compensation premium observed in manufacturing is also evident in services (Figure 2.15, right panel). While no premium is found in Kosovo or Serbia, GVC firms in the remaining WB6 countries offer a substantial earnings advantage, with labor compensation on average 89 percent higher than in domestic firms. Exporter-only and importer-only firms also earn premia in services, averaging 69 percent and 52 percent, respectively, with Albania consistently reporting the highest returns to trading.

Figure 2.16 Distribution of compensation by gender ownership

Source: World Bank Enterprise Surveys.

Note: Latest available year per country. Female-owned = majority female ownership (b4a ≥ 50 percent). Bar length reflects share of total.

Female firm ownership is modest in manufacturing and trailing in services. Female-owned firms account for less than one sixth of total manufacturing labor compensation across the WB6 (Figure 2.16, left panel). On average, female-owned manufacturing firms contribute 15.3 percent

of total compensation, of which 1.4 percent comes from domestic firms and 13.9 percent from trading firms. This broadly mirrors their presence in the sector, as female-owned firms represent 13.8 percent of manufacturing firms overall (1.9 percent domestic and 11.9 percent trading), suggesting roughly proportionate compensation on average. Cross-country variation, however, is substantial. In Albania, female-owned trading firms account for 25 percent of manufacturing compensation despite representing just 13.1 percent of firms, while in Kosovo female-owned manufacturing firms are virtually absent. In services, on average, female-owned firms contribute 11.1 percent of services compensation despite representing 18.2 percent of all services firms (Figure 2.16, right panel). This implies average compensation per female-owned firm of roughly 61 percent of the sector average. The gap is most pronounced in Serbia, where female-owned firms account for 7.8 percent of compensation but 18.2 percent of firms, and in Montenegro (3.9 percent from 14.9 percent).

Labor market policies can be strengthened to incentivize employment among vulnerable individuals

Reducing policy induced disincentives to formal employment is critical to mobilize underutilized labor in the Western Balkans. Despite progress on legal and institutional frameworks, labor taxes and social benefits still discourage formal work at low-income levels. High labor taxes—especially social security contributions (SSCs)—remain a key barrier to formalization for workers and employers. In most Western Balkan countries, labor taxation is regressive, with higher effective tax rates for low-income earners, including part-time workers.⁴⁸ This is largely driven by minimum SSC bases that are weakly linked to hours worked or earnings, making formal part time jobs expensive and scarce. The resulting lack of flexible jobs disproportionately affects people with time constraints—especially women with care responsibilities—and can push work into informality without protections. Kosovo

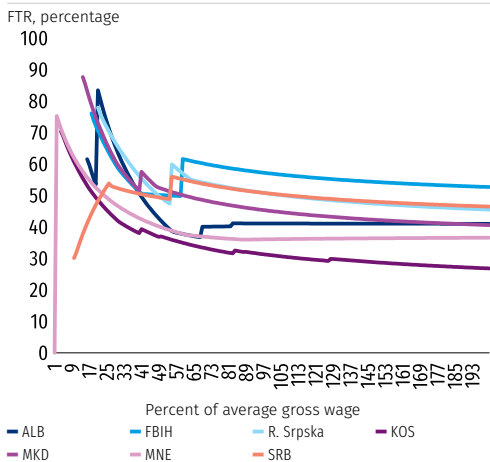
(low minimum base) and Montenegro (no minimum base) are notable exceptions. Announced SSC rate reductions in 2025 are unlikely to materially change incentives because minimum contribution bases—the main source of regressivity—remain unchanged.

The design of social assistance systems creates further disincentives to formal employment. In most Western Balkan countries, reporting any labor income triggers ineligibility for poverty-targeted benefits, which can make low-paid and part-time formal work financially unattractive. Serbia and Albania partially mitigate this: Serbia phases benefits out as earnings rise, and Albania applies a formula-based eligibility system, though low thresholds still exclude many households once formal income is earned. Kosovo introduced an income-disregard mechanism in 2025–26, but only as a pilot. Elsewhere, abrupt benefit withdrawal continues to reduce incentives to take up formal employment at the bottom of the wage distribution.

⁴⁸ Western Balkans Labor Market Brief 2022, World Bank and wiiw (2024) <https://documents.worldbank.org/pt/publication/documents-reports/documentdetail/099082824082013360>.

Simulations confirm the negative impact of benefit withdrawal on formal employment. The formalization tax rate (FTR)—the share of income lost when moving from informal to formal work—is highest at the bottom of the wage distribution because labor taxes rise while benefits fall. Although FTRs decline as earnings increase, they often remain elevated until earnings reach about two thirds of the average wage. In several Western Balkan countries, FTRs reach 70–80 percent at low-income levels, compared with around 30–40 percent in some OECD countries at comparable income levels (Figure 2.17).

Figure 2.17 The cost of formalization is high across the WB6



Source: Western Balkans Labor Market Brief 2023, World Bank & wiiw (2025).

International experience shows that tax-and-contribution design can shape formal labor market participation, especially at the lower end of the wage distribution. Germany’s “mini-job” and “midi-job” schemes illustrate how differentiated contribution treatment can facilitate

entry into formal employment, including for women.⁴⁹ While context-specific and not without risks (e.g., labor market segmentation), these schemes underscore a broader principle: reducing steep marginal costs of low-wage formal employment can lower barriers to formalization. Any reforms would need to be assessed for revenue implications and broader labor market effects, alongside complementary efforts on job creation, skills matching, enforcement, and social protection design.

In 2024, Kosovo piloted a nationwide reform that shifted social assistance eligibility from categorical criteria to poverty-based targeting. The pilot introduced an income-disregard mechanism that phases out benefits as labor income rises: households below the base threshold receive the full benefit, while benefits are reduced gradually once income exceeds the threshold according to a formula. Under the pilot, the FTR remains below 10 percent for wages up to 30 percent of the average, compared with consistently above 40 percent under the normal scheme—suggesting substantially smaller disincentives to formal work at low-income levels, while disincentives remain similar at higher incomes.

In-work benefits (IWB) are another option to support low-wage workers without raising employer labor costs. Through cash transfers, wage supplements, or tax credits that phase out gradually as earnings rise, IWBs can strengthen work incentives and reduce reliance on social assistance. The Earned Income Tax Credit

49 Konle-Seidl, R. (2021). Precarious but popular? The German mini-job scheme in comparative research on work and welfare. *Journal of International and Comparative Social Policy*, 37(3), 293–306. & Herget, A. & Riphahn, R. T. (2022). The untold story of midijobs. *Journal of Economics and Statistics*, 242(3), 309–341.

Box 2.3 The FTR Methodology

The FTR is calculated as a difference between “net total income” and “income if informal,” as a percentage of the latter. It consists of the labor taxes and SSCs that must be paid by a household when one or more of its members enters formal employment as well as the social benefits that are lost. At each level of gross wages, the model calculates the net total income that the household would receive if that gross wage were earned through either formal or informal employment. The resulting “net total income” for formal employment is the sum of the net wages and social benefits that the household retains when working formally, while “income if informal” is the sum of the net wage plus unpaid labor taxes and all applicable social benefits.

The representative household consists of two working-age adults and two preschool-age children, as this is the most typical household in the region. It is assumed that both adults are able to work and that the household does not receive disability benefits, pensions, or other special assistance. While the findings are most precise for the representative household, the main issues identified in the analysis apply to all households.

The social benefits included in the analysis are non-contributory means-tested programs that cover a significant share of the population. In the Western Balkans, these include: (i) a poverty-alleviation program; (ii) a winter energy allowance or subsidy; and (iii) an allowance to support families with children. Insurance-based schemes (e.g., pensions and unemployment insurance) as well as specialized programs (e.g., disability support or war veterans’ benefits) are excluded from the analysis, as these are targeted at specific population groups based on personal characteristics or past circumstances.

While the FTR model provides valuable insights, it also suffers from important limitations. First, the model uses a representative household that may not fully reflect the conditions faced by all real-world households. Second, the model omits certain types of income and social benefits (e.g., veteran pensions, disability benefits, and income from service contracts or other non-standard forms of work), even though these may be sizeable and can significantly influence household income and decisions regarding formal employment. Third, the model does not account for the likelihood that informal workers will be identified and sanctioned by the authorities, which may deter informality. Fourth, the model is static and does not consider dynamic effects.

Source: Western Balkans Labor Market Brief 2023, World Bank and wiiw (2025).

(EITC) in the United States is a prominent example, with evidence of increased labor force participation, particularly among women.

Beyond labor tax and benefit reforms, active labor market policies (ALMPs) can help motivate and support hard-to-employ individuals and even elderly.

Western Balkan countries offer training, wage subsidies, internships, public works, and self-employment support, but coverage remains low (typically 5–9 percent of registered unemployed).⁵⁰ Spending is also far below EU averages, ranging from 0.02 percent of GDP in Albania to 0.23 percent in Bosnia and Herzegovina (about half the EU level).⁵¹

50 Advancing Social Protection in the Western Balkans: Opportunities for Reform, World Bank (2024) <https://openknowledge.worldbank.org/entities/publication/dc99ba75-a35a-40ca-bb14-3360dbf67d0f>.

51 <https://openknowledge.worldbank.org/entities/publication/dc99ba75-a35a-40ca-bb14-3360dbf67d0f>.

Weak employer engagement and limited adaptation to vulnerable groups often undermine effectiveness. ALMPs can also offer upskilling, re-skilling and employment services tailored to older workers which would want to remain longer on the labor market.

Evidence from the region suggests ALMPs work best when tailored to participants and paired with stronger employer engagement. A Discrete Choice Experiment (DCE) in Serbia finds that around half of registered women disengaged from formal programs would participate if suitable options were available, with preferences for programs closer to home and opportunities emphasizing workplace-relevant, hands-on skills. Rigorous evaluations also show potential impacts:

in North Macedonia, a wage subsidy and training program for social assistance beneficiaries increased employment by 87 percent and wages by 93 percent relative to non-participants.⁵² Albania implemented a similar program placing unemployed youth and low-educated adults in firms for four months of on-the-job training with wages and social security contributions fully covered; evaluation results show positive employment effects, though wage impacts are less conclusive.⁵³ More recent pilots point to promising approaches that combine individualized counseling/mentoring, training, employer engagement, and post-placement follow-up (Box 2.4), and scaling these models will require adequate resources and stronger public employment service capacity.

Box 2.4 ALMP Pilots in the Western Balkans

In Bosnia and Herzegovina, a gender-sensitive counseling training module was developed to strengthen the capacity of public employment counselors to support female jobseekers, particularly long unemployed and vulnerable women. Qualitative evidence showed that counselors faced challenges related to low motivation and self-confidence among clients, limited gender-equality awareness among employers, and insufficient links to complementary services, such as psychological support.⁵² The World Bank-supported training equipped counselors with gender-sensitive knowledge and techniques, including active listening, empathetic communication, and effective approaches for addressing gender-based violence and other sensitive issues. The pilot demonstrated improvements in counselors' knowledge of the legal framework, issues around workplace discrimination, and methods for supporting vulnerable groups.

In North Macedonia, a pilot mentorship program supported Roma women's entry into formal employment in the care sector through individualized guidance and psychosocial support. The program addressed persistently low enrollment and high dropout rates among

52 What Works for Work: A Guidebook to Proven and Promising Employment Solutions, World Bank (2026) <https://openknowledge.worldbank.org/entities/publication/d57b125e-e41a-4bec-93cf-02b32ccc6165> based on Armand, Alex, Pedro Carneiro, Federico Tagliati, and Yiming Xia. 2026. "Can Subsidized Employment Tackle Long-Term Unemployment? Experimental Evidence from North Macedonia." *Journal of Development Economics* 178.

53 Impact Assessment Employment Promotion Programmes in Albania 2021-2024, unpublished.

54 Kapo, Amra, Gender-sensitive support for PES counselors in Bosnia and Herzegovina (2025, unpublished).

Roma women in care training and employment programs. Mentors provided continual support from onboarding and training to job placement and early employment in coordination with training providers and employers. The program also engaged families to address restrictive gender norms. Over 90 percent of the 121 mentees completed the training, and a follow-up survey one year later found that 47 percent were employed. The program is being piloted for social assistance beneficiaries and is expected to inform the design of additional policy measures.

In Kosovo, a results-based financing approach was introduced for a program that offered training vouchers to social assistance beneficiaries registered with the PES. Beneficiaries may redeem vouchers with private training providers, who are reimbursed in phases based on attendance, certification, and employment outcomes. Providers receive an additional performance-based payment if beneficiaries obtain formal employment and remain employed for six months. By linking payments to results, the scheme incentivizes providers to reduce the dropout rate, improve training quality, and strengthen job intermediation.

In Serbia, a pilot post-placement support program provides six months of follow-up to long-term unemployed individuals, including social assistance beneficiaries, Roma women and men, and youth. The program combines regular engagement between employment counsellors, participants, and employers with tailored counseling and referrals to complementary social protection, health, or rehabilitation services. Employer engagement is a key element of the pilot, helping to address biases and support workplace adaptation. Post-placement support aims to reduce early job attrition and stabilize employment relationships.

Labor market policies targeting youth can improve education-to-work transitions

Improving the quality and relevance of education is central to strengthening youth employability in the Western Balkans, and closer employer engagement can help reduce skills mismatches.

Addressing learning gaps requires sustained investments in curriculum reform, instructional time, teacher training and coaching, as well as measures to reduce absenteeism.⁵⁵ Enrollment in pre-primary education remains well below EU levels, and expanding access would strengthen

foundational skills and improve long-term labor-market outcomes. Employers across the region frequently report that graduates lack relevant skills.⁵⁶ Including employers on educational boards and advisory bodies, expanding internships/apprenticeships or subsidized placements, and using labor-market observatories to bring private-sector data into curriculum design can improve work-based learning, career guidance, and school-to-work transitions.

Access to high-quality career guidance remains uneven. The European Training Foundation reports progress in developing career guidance frameworks at the

55 Unlocking Potential: Enhancing Education Quality in the Western Balkans Based on Insights from the PIRLS 2021 and PISA 2022 Studies, World Bank (2025) <https://openknowledge.worldbank.org/entities/publication/359a1f97-7f94-4421-9d9d-d782b3ec6701>.

56 World Bank Enterprise Surveys, *Workforce* topic data. Available at: <https://www.enterprisesurveys.org/en/data/exploretopics/workforce?subGroup=-1&subtopic=73> (accessed February 2026).

secondary and tertiary level across the region, but implementation gaps persist.⁵⁷ In North Macedonia, for example, donor-supported career centers have largely disappeared, and schools are not required to employ dedicated career counselors.⁵⁸ As a result, many students lack structured support in choosing fields of study aligned with employer demand. Enhanced career guidance services, supported by data on graduate outcomes and employment prospects, can improve education choices and support smoother transitions into higher-quality jobs.

The Youth Guarantee (YG) provides a key policy framework for strengthening youth employment services and activation measures, but progress varies and common constraints persist. Since 2021, all Western Balkans countries have committed to implementing the YG, which aims to ensure that young people under 30 receive a quality offer of employment, education, or training within four months of unemployment or leaving education. North Macedonia has fully rolled out a national YG scheme and reports that more than 100,000 young people were reached, with around 40 percent transitioning to

employment, education, or training within four months.⁵⁹ Albania's pilot program (2023–25) enrolled 1,255 applicants in 2023–24, with 847 positive outcomes.⁶⁰ Kosovo's municipal pilots achieved transition rates above 60 percent,⁶¹ while Serbia's pilot reached over 8,700 young people, with more than three-quarters of positive exits meeting the EU's four-month benchmark.⁶² In contrast, YG programs in Bosnia and Herzegovina and Montenegro remain in the early stages, with pilots only recently launched.⁶³ Across the region, geographic coverage remains limited (pilots concentrated in urban areas), outreach to hard-to-employ groups (including Roma youth and long term NEETs) is weak, and monitoring and evaluation systems are underdeveloped: few countries track outcomes beyond immediate exits, and none has yet conducted a national level counterfactual impact evaluation. Institutional challenges further complicate implementation, including the declining functionality of Local Youth Councils in North Macedonia, procurement and funding delays affecting outreach in Serbia, and weak interinstitutional coordination and employer engagement in Albania and Kosovo.

57 A review of national career development support systems in the Western Balkans, European Training Foundation (2022) <https://www.etf.europa.eu/en/publications-and-resources/publications/review-national-career-development-support-systems-western>.

58 Understanding Training Pathways into in-Demand Engineering Technician in North Macedonia. World Bank (2025) Forthcoming.

59 <https://www.rcc.int/download/docs/Performance-of-Western-Balkan-economies-regarding-the-European-Pillar-of-Social-Rights-North-Macedonia.pdf/27a146c62ecf1ac0ca147996dc3ebd10.pdf>.

60 <https://www.rcc.int/download/docs/Performance-of-Western-Balkan-Six-regarding-the-European-Pillar-of-Social-Rights-WB-29102025A.pdf/e0bdbc27f44521a05ed60b81e545e0d5.pdf>.

61 <https://www.rcc.int/download/docs/Performance-of-Western-Balkan-Six-regarding-the-European-Pillar-of-Social-Rights-WB-29102025A.pdf/e0bdbc27f44521a05ed60b81e545e0d5.pdf>.

62 Youth Guarantee Implementation Plan (2023–2026). First report (2023–2024). Conclusion note of the Government of Serbia (2025).

63 <https://www.rcc.int/download/docs/Performance-of-Western-Balkan-Six-regarding-the-European-Pillar-of-Social-Rights-WB-29102025A.pdf/e0bdbc27f44521a05ed60b81e545e0d5.pdf>.

In addition to YG programs, Western Balkan countries deploy a range of youth-targeted ALMPs. These include internships and targeted counselling in Albania;⁶⁴ first job placements and youth entrepreneurship grants in Bosnia and Herzegovina;⁶⁵ the SuperPuna digital wage-subsidy platform in Kosovo;⁶⁶ Montenegro's large-scale Professional Training Program for graduates;⁶⁷ North Macedonia's portfolio of internships, wage subsidies, and youth allowances;⁶⁸ and Serbia's My First Salary program, which offers mentored work placements.⁶⁹ These measures have broadened the reach of youth activation policies, but low ALMP spending and administrative bottlenecks weaken their impact.⁷⁰ Systematic monitoring and evaluation of youth-related and first-job ALMPs in the Western Balkans remain very limited, with scarce information available on program take-up and on impacts across countries. The only robust evidence identified consists of administrative reporting that Montenegro's Professional Training for Graduates program generated about 15,300 placement opportunities as of 2024⁷¹, and experimental evidence

from North Macedonia showing significant long-term employment effects of a subsidized employment scheme.⁷²

Effective youth activation policies ultimately depend on the capacity of public employment services (PES).

Across the Western Balkans, PES face limited funding, staffing shortages, and high caseloads, which undermine the scale and effectiveness of youth-focused interventions. Strengthening PES capacity through increased resources, digitalization, improved profiling tools, stronger labor-market intelligence, and enhanced employer outreach will be essential to support successful education-to-work transitions.

Expanded childcare services will be crucial to alleviate constraints on labor-force participation

Participation in early childhood education and care (ECEC) remains limited across the Western Balkans, especially among children under three. Average preschool enrollment is about

64 <https://www.rcc.int/pubs/271/rcc-esap-3-performance-of-the-western-balkan-six-regarding-the-european-pillar-of-social-rights-2025-review-on-albania>.

65 <https://national-policies.eacea.ec.europa.eu/youthwiki/chapters/bosnia-and-herzegovina/36-integration-of-young-people-in-the-labour-market>.

66 <https://www.rcc.int/pubs/273/rcc-esap-3-performance-of-the-western-balkan-six-regarding-the-european-pillar-of-social-rights-2025-review-on-kosovo>.

67 <https://www.rcc.int/pubs/274/rcc-esap-3-performance-of-the-western-balkan-six-regarding-the-european-pillar-of-social-rights-2025-review-on-montenegro>.

68 <https://national-policies.eacea.ec.europa.eu/youthwiki/chapters/republic-of-north-macedonia/36-integration-of-young-people-in-the-labour-market>.

69 <https://national-policies.eacea.ec.europa.eu/youthwiki/chapters/serbia/36-integration-of-young-people-in-the-labour-market>.

70 <https://www.rcc.int/download/docs/Performance-of-Western-Balkan-Six-regarding-the-European-Pillar-of-Social-Rights-WB-29102025A.pdf/f44521a05ed60b81e545e0d5.pdf>.

71 Regional Cooperation Council | RCC ESAP 3: Performance of the Western Balkan Six Regarding the European Pillar of Social Rights – 2025 Review on Montenegro (<https://www.rcc.int/pubs/274/rcc-esap-3-performance-of-the-western-balkan-six-regarding-the-european-pillar-of-social-rights-2025-review-on-montenegro>).

72 Armand, Alex, Pedro Carneiro, Federico Tagliati, and Yiming Xia. 2026. "Can Subsidized Employment Tackle Long-Term Unemployment? Experimental Evidence from North Macedonia." *Journal of Development Economics* 178.

51 percent.⁷³ While Albania and Montenegro are approaching the OECD average of 84 percent, enrollment rates in Kosovo, North Macedonia, and Bosnia and Herzegovina are less than half the level of their regional counterparts.⁷⁴ Only in Kosovo, Bosnia and Herzegovina, and Serbia is the last year of preschool mandatory. For children under three, enrollment across WB6 is far below the OECD average of 32 percent; many children remain at home because they are perceived as too young for kindergarten.⁷⁵ Childcare and other care responsibilities are the most commonly cited reason for women's absence from the labor force, particularly among mothers ages 25–34.⁷⁶

Although the number of nurseries, preschools, and kindergartens has increased, overall coverage remains low—especially in rural areas—and supply often does not keep up with demand. In Serbia, major cities such as Belgrade and Novi Sad have historically had thousands of children on waiting lists, though the situation has improved with new construction. In Bosnia and Herzegovina, children on preschool waiting lists in 2022 equaled 17 percent of all children enrolled in preschool.⁷⁷ Kosovo's ECEC infrastructure meets only about 30 percent of total childcare demand, with rural areas especially disadvantaged. On average, 58 percent of urban households with children under age six use childcare services, compared with 30 percent of rural

households (Figure 2.18). Coverage is also low among vulnerable groups (e.g., ethnic minorities, children with disabilities, and low-income households with unemployed parents) due to limited infrastructure in marginalized areas, documentation and language barriers, social norms, and discriminatory practices.

When access to public institutions is limited, families often must bear the high cost of private childcare. Across the region, private fees are significantly higher than public fees—around double in Bosnia and Herzegovina and as much as 16 times higher in North Macedonia (Figure 2.19). For households with two children and only one employed parent, private childcare costs range from 30 percent of household income in Serbia to 63 percent in North Macedonia; by contrast, public childcare costs are 10 percent and 6 percent of household income, respectively. Childcare use is also unequal by income: among higher-income families, 54 percent of those with children under age six and 36 percent with children under three use childcare, compared with 42 percent and 35 percent, respectively, among households in the bottom 40 percent of the income distribution (Figure 2.18).

Quality is mixed and, together with social norms, may suppress demand for formal ECEC—especially for children under three. Despite progress on standards and

73 OECD. 2024. Western Balkans Competitiveness Outlook 2024: Regional Profile. OECD: Paris.

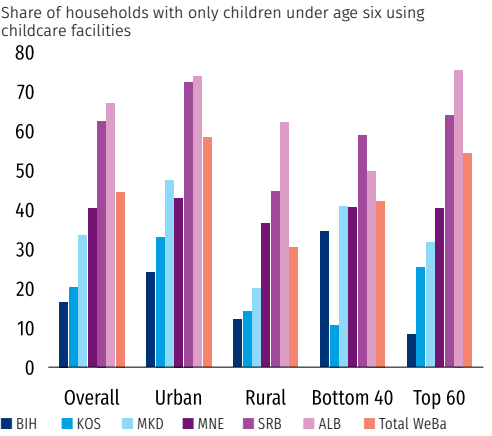
74 Early Childhood Education and Care in the Western Balkans: Investing in children, families and jobs, World Bank (2026) forthcoming. based on the Agency for Statistics of each country for 2023 and UN/UNESCO data.

75 Gomez Tamayo, S., & Shmis, T. (2026). Investing in Early Years: Evidence, Challenges, and Policy Directions for Early Childhood Education and Care in Kosovo, forthcoming.

76 Care Responsibilities and Female Employment in the Western Balkans, World Bank (2026) forthcoming.

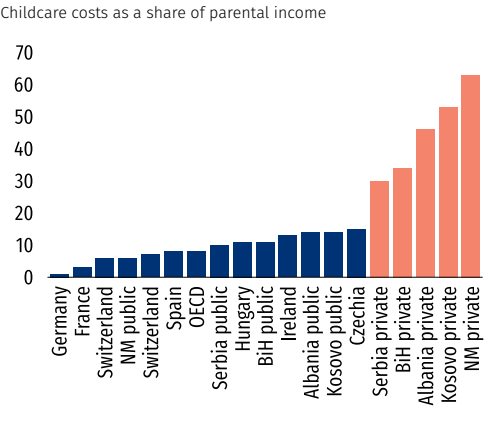
77 Agency for Statistics of Bosnia and Herzegovina, Pre-school upbringing and education in the school year 2022/2023, 2023, available at [https://bhas.gov.ba/data/Publikacije/Saopstenja/2023/EDU_07_2022_Y2_0_BS.pdf](https://bhas.gov.ba/data/Publikacije/Saopštenja/2023/EDU_07_2022_Y2_0_BS.pdf).

Figure 2.18 Wealthier and urban households use childcare more than poorer and rural households



Source: Fruttero et al., forthcoming, based on the Life in Transition Survey IV by EBRD (2023).

Figure 2.19 Private childcare fees can consume a significant share of household income

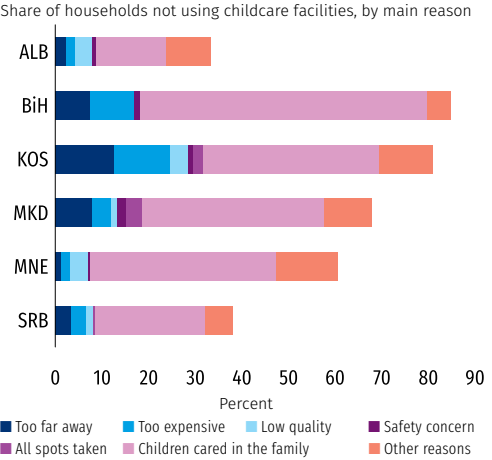


Source: Early Childhood Education and Care in the Western Balkans: Investing in children, families and jobs, World Bank (2026) forthcoming, based on OECD Education at a Glance 2025 and wage data from wiiw institute.

Note: The prices for the Western Balkan countries are calculated based on the lowest end of the fee ranges.

curricula, quality-assurance frameworks are often not fully operational; implementation is inconsistent; inspections are infrequent; and monitoring systems are weak. The sector also faces labor shortages—particularly in rural and underserved areas—linked to low wages, limited career progression, and inadequate training, alongside insufficient pedagogical support and limited use of systematic monitoring and evaluation (e.g., ratings systems, inspections, mentoring, and coaching). In parallel, many families cite in-home care as a reason not to enroll: on average, 36 percent of households report not using childcare facilities because children are cared for at home (Figure 2.20), reflecting expectations that women assume primary responsibility for childrearing and uncertainty about external care arrangements.⁷⁸ These expectations can hinder women’s labor market participation

Figure 2.20 Strong preference for in-home care of young children



Source: Fruttero et al., forthcoming, based on the Life in Transition Survey IV by EBRD (2023).

78 Early Childhood Education and Care in the Western Balkans: Investing in children, families and jobs, World Bank (2026) forthcoming.

or push them into less productive but more flexible employment.

Given the scale and urgency of unmet childcare needs, expanding ECEC will require more public and private provision alongside stronger quality-management systems. Public provision can be expanded by repurposing public spaces, integrating childcare into schools, and supporting flexible models (e.g., mobile units). Home-based childcare networks can complement traditional services by training and certifying local providers to care for small groups within the official system (as in Austria, France, and Canada). In parallel, countries can strengthen quality management by fully operationalizing existing standards (e.g., training inspectors, increasing inspection frequency, undertaking mentoring and coaching visits, and institutionalizing robust monitoring and evaluation for all provider types), and by improving compensation, training opportunities, and career pathways for staff. While all WB6 countries allow private ECEC centers to varying extents, boosting private participation—through public-private partnerships, voucher schemes with strong quality and equity safeguards, and financial incentives (e.g., tax relief, favorable loans, subsidies for service providers, employers, or parents)—can help expand access in poorer communities and rural areas; countries such as Germany and Japan have used tax incentives to boost

employer contributions, and several large companies in Serbia and North Macedonia have established on-site daycare for employees' children.

Expanding affordable ECEC will also require more public funding, better spending efficiency, and efforts to address information gaps and trust.

Available indicators suggest WB6 countries typically spend 0.2–0.4 percent of GDP on preprimary education—less than half the OECD average.⁷⁹ ECEC is among the highest-return investments in human capital: high-quality preschool generates durable gains in skills, productivity, and lifetime earnings, with benefit-to-cost ratios ranking above most other education and labor market interventions.⁸⁰ Returns can be raised further by improving how resources are used (e.g., centralized or bulk procurement) and by exploring complementary financing (e.g., social impact funds or public-private investment funds) with public oversight. To encourage take-up, authorities should communicate ECEC's developmental benefits and address quality concerns; evidence from the United Kingdom shows that exposure to positive feedback from parents using ECEC services increased enrollment among other families.⁸¹

79 Early Childhood Education and Care in the Western Balkans: Investing in children, families and jobs, World Bank (2026) forthcoming, based on Our World in Data, 2025; UNESCO, 2024; UNICEF, 2023; World Bank, 2023; Ministry of Finance, Labor and Transfers of Kosovo, 2024; OECD, 2023b.

80 Elder, Leslie Kennedy; Kataoka, Naoko; Naudeau, Sophie; Neuman, Michelle J.; Valerio, Alexandria. Investing in young children: an early childhood development guide for policy dialogue and project preparation (English). Africa regional educational publications |Directions in development. Human development Washington, DC: World Bank. <http://documents.worldbank.org/curated/en/691411468153855017>.

81 Increasing the uptake of government childcare offers: A report from the Behavioural Insights, HM Revenue and Customs UK (2018).

Expanding ECEC services would not only enable more parents to enter and remain in the labor market but would also generate substantial job creation in the care economy itself. Bringing enrollment closer to OECD levels (32 percent for children under three and 86 percent for children ages three to the minimum age for compulsory education) could create an estimated 24,000 additional jobs—around 16,000 teaching positions and 8,000 administrative and support roles—and could raise female employment by over 1 percent.⁸² Evidence from high-income countries similarly links greater ECEC investment to higher maternal employment.⁸³

Eldercare services are increasingly important to support labor force participation

While childcare remains the dominant care-related constraint to female labor force participation among prime-aged women, responsibilities for caring for older family members are

rising as populations age.⁸⁴ Women disproportionately shoulder eldercare during mid and later working ages, often at critical career points. Because eldercare is time-intensive and long-lasting, it is difficult to reconcile with paid work; as demographic aging accelerates and family sizes shrink, pressure on women's labor supply will grow unless accessible and affordable formal care expands.

Demand for long-term care (LTC) services is already high in the Western Balkans and will rise rapidly as populations continue to age.⁸⁵ LTC refers to services and benefits for people who, due to physical or mental limitations over an extended period, need support with daily activities or ongoing care; definitions vary across international organizations and countries in scope, medical versus social orientation, age coverage, and the role of informal care.⁸⁶ In WB6, about 16 percent of people aged 65+ report severe difficulty with basic daily activities, and an additional 32 percent report some difficulties (Figure 2.21).⁸⁷ Older adults already account for

82 Early Childhood Education and Care in the Western Balkans: Investing in children, families and jobs, World Bank (2026) forthcoming, based on employment data taken from ILOSTAT (2025).

83 Olivetti, C. and B. Petrongolo. "The Economic Consequences of Family Policies: Lessons from a Century of Legislation in High-Income Countries." *Journal of Economic Perspectives* 31(1): 205-230; and Halim, D., E. Perova and S. Reynolds. 2023. "Childcare and Mothers' Labor Market Outcomes in Lower- and Middle-Income Countries." *The World Bank Research Observer* 38(1): 73-114.

84 World Bank, 2026. *Mend the Gap, Unleash Potential. Addressing Barriers in Women's Economic Opportunities in Europe and Central Asia*. World Bank.

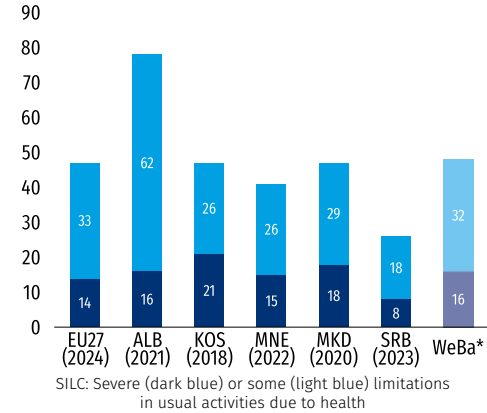
85 European Commission defines LTC as "the range of services and assistance for people who, as a result of mental and/or physical frailty and/or disability over an extended period of time, depend on help with daily living activities and/or need some permanent nursing care" Details found in the Long-term care page of European Commission.

86 Frisina Doetter, Lorraine; Hamandi, Ali; Coll-Black, Sarah; Grigoras, Vlad. *The ABCs of Long-Term Care: A Functional Framework for Building System Capacity*. Washington, D.C.: World Bank Group. <http://documents.worldbank.org/curated/en/099112425122032004>.

87 Long-Term Care Report – Trends, challenges and opportunities in an ageing society, Volume I, European Commission (2021) Note: EU Statistics on Income and Living Conditions (EU-SILC) uses the Global Activity Limitation Indicator (GALI), designed to measure the presence of long-standing limitations in usual activities due to health problems (Eurostat). The survey asks respondents: are you limited because of a health problem in activities people usually do? Would you say you are severely limited, limited but not severely, or not limited at all? The EU tends to consider "severe limitations" as a proxy for LTC needs (see, e.g., European Commission). As these are self-reported measures rather than assessments, the numbers should be interpreted with caution as measurement is subjective and potentially affected by cultural factors as well as personal beliefs and circumstances.

Figure 2.21 LTC needs among the elderly are high...

Share of the population aged 65 and above reported limitations in activities of daily living



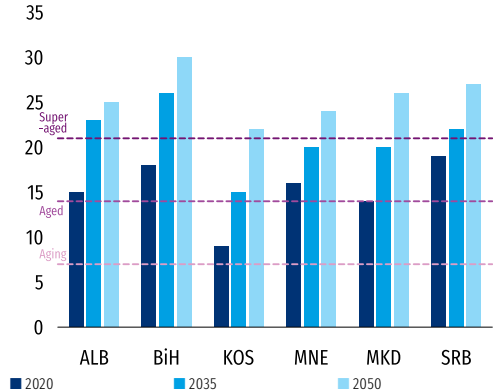
Source: Long-term Care in the Western Balkans: Investing in Better Lives and More Jobs, World Bank (2026) Forthcoming, based on Eurostat and Dakić, B., Veljković, T., Vuković, O., Todorović, N. and Vračević, M. (2023). Long-Term Care of Older Persons and Persons with Disabilities in the Western Balkans. Red Cross Serbia.

9–19 percent of national populations; within the next decade, Albania, Bosnia and Herzegovina, and Serbia are projected to become “super-aged” (with at least 20 percent of population aged 65+), and by 2050 Kosovo, Montenegro, and North Macedonia are expected to follow (Figure 2.22).

Despite these trends, the coverage of formal LTC services and benefits remains extremely limited across the region, resulting in heavy reliance on informal family care. Available evidence suggests that only a small share of older adults receive publicly financed in-kind services—well below EU levels (Figure 2.23). Public support tends to focus on residential care and cash allowances for informal caregivers, while home- and community-based services remain underdeveloped and are often donor/NGO financed on a project basis rather than embedded in sustainable public systems.

Figure 2.22 ...and the elderly population is rapidly increasing

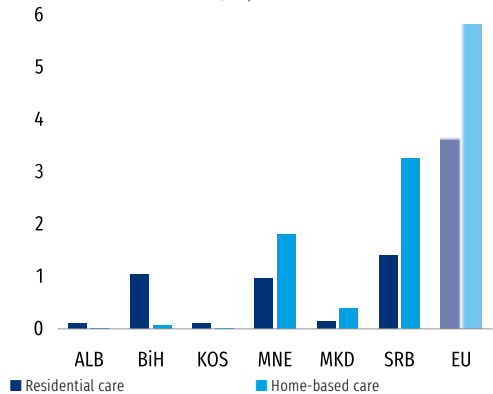
Demographic aging, recent and projected



Source: Long-term Care in the Western Balkans: Investing in Better Lives and More Jobs, World Bank (2026) Forthcoming, based on based on UN 2024, Kosovo Statistical Agency (2017, 2024).

Figure 2.23 Access to residential and home-based care is extremely limited in most WB6 countries

The share of population +65 covered by publicly financed residential and home-based LTC services, in percent



Source: Long-term Care in the Western Balkans: Investing in Better Lives and More Jobs, World Bank (2026) Forthcoming, World Bank (2025): Assessing current and future expenditure on Long-Term Care in North Macedonia, and Background paper for the “Promoting Jobs and the Care Economy in the Western Balkans” reports, financed by the European Commission.

Affordability constraints and social norms further limit access to LTC and shape labor-market outcomes. Public spending on LTC is far lower than in the EU, contributing to high out-of-pocket costs; cost is frequently cited as the main barrier to using formal services, even

where availability and quality are not the primary concern.⁸⁸ At the same time, norms of filial responsibility—reinforced by legislation that assigns eldercare duties to adult children—discourage the use of external services; survey evidence shows that families most commonly report providing care within the household even when older relatives have significant needs.⁸⁹ These dynamics affect women's labor supply: in Bosnia and Herzegovina, 24 percent of unemployed women and 11 percent of economically inactive women with eldercare responsibilities report they would consider joining the labor force or increasing working hours if affordable, high-quality eldercare were available.⁹⁰

Expanding LTC services—especially home- and community-based options—is critical to reduce family care burdens and support labor-market participation.

Community care, respite care, and home-based support remain minimal across much of the region, even though international evidence suggests they can cost-effectively complement or substitute for informal care and delay institutionalization. Broadening care options would give households services tailored to different levels of need; Albania, North Macedonia, and Serbia have begun developing home- and community-based care models, reflecting a shift toward service diversification.

Given limited public-sector capacity, scaling up LTC will require greater reliance on non-state providers, alongside stronger quality assurance to build public trust. Governments have often relied on ad hoc outsourcing or private markets for residential care; more systematic contracting for defined services (home care, day care, respite) can expand coverage without creating parallel public delivery systems. Because private provision tends to concentrate in urban areas, targeted interventions are needed for rural communities (for example, differentiated contracting incentives, mobile care units, support for community volunteer networks, and digital/telecare solutions). As services expand, enforcement of minimum standards through licensing and inspections should be strengthened and complemented over time with better administrative data, user feedback, peer learning through professional associations, and transparent reporting.

Sustainable financing, coherent governance, and integration between social protection and healthcare are prerequisites for scaling quality LTC—alongside workforce investment that can deliver jobs and support labor supply. Public spending on LTC in the Western Balkans averages around 0.4 percent of GDP versus the EU average of 1.7 percent,⁹¹ and North Macedonia projections show that even with constant coverage, aging alone could raise spending from 0.39 percent of GDP in

88 Simmons, C. and Lorenz-Dant, K. (2023). Systems in transition: Responding to changing attitudes, expectations and preferences on long-term care in the Balkans, Research note 2023/03, European Centre for Social Policy and Research.

89 Life in Transition Surveys, EBRD (2023).

90 World Bank-administered household survey (2025).

91 Long-term Care in the Western Balkans: Investing in Better Lives and More Jobs, World Bank (2026) Forthcoming.

Box 2.5 Private Sector Participation in LTC in North Macedonia

Recent analytical work and implementation experience from North Macedonia provide concrete evidence that systematically engaging nonstate providers can expand LTC services while supporting job creation. A recent World Bank assessment of private-sector participation in LTC found that nonstate actors—mainly nonprofit providers but also private operators—already deliver residential, day, and home-based care services, particularly in areas where public provision is limited, and they can scale relatively quickly when supported by predictable financing, clear contracting arrangements, and minimum quality standards.* Experience from the Social Services Improvement Project further demonstrates the potential of this type of mixed-delivery model. By contracting non-public providers to deliver home-based care services in 43 municipalities, the government expanded access to care for more than 1,600 older persons while creating 773 formal jobs, including for women, Roma, and Guaranteed Minimum Assistance beneficiaries, equivalent to 0.48 jobs per client served. Building on this model, the second iteration of the project is extending community-based and home-based services to additional municipalities, complemented by improvements in licensing, pricing, quality assurance, and information systems. This experience suggests that public financing combined with regulated non-state service provision can expand LTC coverage, reduce unpaid family care burdens, and boost labor-market participation.

* O'Hanlon, Barbara; Coll-Black, Sarah; Hamandi, Ali; Ngwashi, Christabel Apholung. An Assessment of Private Sector Engagement in Long-Term Care for the Elderly in North Macedonia. Washington, D.C.: World Bank Group. <http://documents.worldbank.org/curated/en/099022426123517759>.

2023 to 0.56 percent by 2042.⁹² Mobilizing complementary private financing matters; in well-developed OECD systems, around 20 percent of total LTC spending is privately financed,⁹³ suggesting potential roles for tax incentives, tax-advantaged savings, or public-private co-financing under public oversight. At the system level, responsibilities remain fragmented with incomplete data and weak performance and quality monitoring;⁹⁴ establishing workable institutional arrangements, standardized

needs assessment, integrated information systems, and clearer referral pathways between health and social services can reduce fragmentation, avoid inefficiencies (such as avoidable admissions and delayed discharges), and support home- and community-based transitions. Formal LTC employment is extremely low: Serbia employs about 0.3 formal LTC workers per 100 people aged 65+, compared with around five per 100 in OECD countries;^{95,96} targeted training and hiring incentives

92 Coll-Black, Sarah; Hamandi, Ali; Shimbov, Bojan; Wiener, Mitch. Assessing Current and Future Expenditure on Long-Term Care in North Macedonia. Washington, D.C.: World Bank Group. <https://documents.worldbank.org/pt/publication/documents-reports/documentdetail/099030926105526980>.

93 Health at glance 2025, OECD (2025) https://www.oecd.org/content/dam/oecd/en/publications/reports/2025/11/health-at-a-glance-2025_a894f72e/8f9e3f98-en.pdf.

94 Dakić, B., Veljković, T., Vuković, O., Todorović, N. and Vračević, M. (2023). Long-Term Care of Older Persons and Persons with Disabilities in the Western Balkans. Red Cross Serbia.

95 Long-term Care in the Western Balkans: Investing in Better Lives and More Jobs, World Bank (2026) Forthcoming, based on information on home-based and residential staff from Todorović, N., and Vračević, M. (2024). Long-term care system profile: Serbia. Global Observatory of Long-Term Care, LSE. Available at: <https://goltc.org/system-profile/serbia/>, and population data from United Nations 2022.

96 OECD. (2020). Who cares? Attracting and retaining care workers for the elderly. Paris: OECD Publishing.

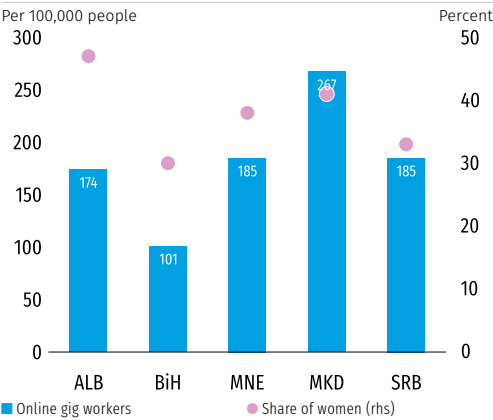
can help mobilize underutilized labor. World Bank estimates suggest that raising the LTC workforce toward the current EU average could create around 110,000 additional jobs (nearly 2 percent of total employment in 2023),⁹⁷ and international evidence indicates that expanding access to formal LTC can increase female labor-force participation, particularly among women aged 40+.⁹⁸

Gig work can provide flexible job opportunities for economically inactive or unemployed workers

Short-term and task-based work (“gig work”) can provide flexible earning opportunities for workers with time and location constraints, including women with care responsibilities. Even with rapid expansion of childcare and eldercare services, some care constraints will remain, and gig work (and other flexible arrangements) can help workers earn additional income and enter the labor market, including women, youth, the long-term unemployed, and others who face barriers to traditional employment.⁹⁹ The gig economy is expanding quickly as digital platforms (e.g., ride-hailing, food delivery, and online freelancing) scale up, but data on gig work in the Western Balkans remain limited; in the region, high unemployment

(especially among youth), bureaucratic hurdles to formal entrepreneurship, and skills mismatches are contributing to growth in platform-based work.¹⁰⁰

Figure 2.24 The share of women in online gig work varies across the WB6



Source: Gigmeter, May 2025.

Available estimates suggest Western Balkan countries employ about 182 online gig workers per 100,000 people—above the average for four neighboring EU countries (Romania, Bulgaria, Hungary, and Croatia) at 60.6 per 100,000—though the Western Balkan figure is likely underestimated due to data constraints (Figure 2.24). For comparison, more reliable EU figures indicate an average of 6,300 gig workers per 100,000 people in 2022.¹⁰¹ Platform-mediated gig work is either location-based (e.g., ride-hailing and delivery apps) or

97 Long-term Care in the Western Balkans: Investing in Better Lives and More Jobs, World Bank (2026) Forthcoming.
98 Saraceno, C. and Keck, W. (2010). Can we identify intergenerational policy regimes in Europe? European Societies, 12(5), 675–696. Available at: <https://doi.org/10.1080/14616696.2010.483006>.
99 Gender differences in motivation to engage in platform work, EIGE and Eurofound (2023) <https://www.eurofound.europa.eu/en/publications/all/gender-differences-motivation-engage-platform-work>.
100 The Platform Revolution: Shaping the Fair Future of Platform Work in the EU and Western Balkans EUROPEUM (2025) <https://www.europeum.org/en/articles-and-publications/final-report-the-platform-revolution-shaping-the-fair-future-of-platform-work-in-the-eu-and-western-balkans/>.
101 Gig economy: how the EU improves platform workers’ rights, European Parliament (2019) <https://www.europarl.europa.eu/topics/en/article/20190404STO35070/gig-economy-how-the-eu-improves-platform-workers-rights>.

remote (e.g., freelancing).¹⁰² Data from Gigmeter (freelancing platforms such as Upwork, Freelancer, and Guru) show that 38 percent of active freelancers were women in 2025 (the same as in the four EU member states), but the average hourly rate for female freelancers was US\$4.20 lower than for men, unchanged since 2020.¹⁰³

Online gig platforms combine high-skill opportunities with entry-level tasks, while location-based platform work in the region appears more limited and male dominated. More than half of registered gig workers engage in creative, multimedia, or software development and technology roles; at the same time, about 10 percent perform clerical work and data entry and another 10 percent work in sales and marketing support, creating entry points for hard-to-employ workers. In Kosovo, the World Bank-supported Women in Online Work pilot trained 100 young unemployed women from two rural areas; within three months of completion, participants earned twice the average national hourly wage in Kosovo, supporting plans to expand the pilot.¹⁰⁴ While the number of location-based platform workers is difficult to estimate, a cross-country study reports that ride-hailing, food delivery, and similar activities

are dominated by young men.¹⁰⁵ A study in Albania and Bosnia and Herzegovina found these workers are mainly young people with primary and secondary education seeking temporary employment rather than long-term careers.¹⁰⁶ In WB6, location-based work remains relatively limited compared to online platform work (the opposite pattern from many European countries), reflecting international demand for the region's low-cost freelancing workforce.¹⁰⁷

Despite flexibility, gig workers often face precarious conditions and limited legal and social protection; aligning regulation with emerging EU standards and simplifying formalization could help the Western Balkans better leverage platform work. The WB6 lack comprehensive legal frameworks for gig work, and unclear employment status can deprive workers of rights such as employer social security contributions (SSCs), sick leave, family leave, union organization, and occupational health and safety standards. Fairwork's 2023 evaluation of 17 major location-based platforms in Albania, Bosnia and Herzegovina, and Serbia found that more than half failed to ensure workers received the local minimum wage after costs, and only a few provided clear terms and

102 Working Without Borders: The Promise and Peril of Online Gig Work, World Bank (2024) <http://hdl.handle.net/10986/40066>.

103 Gigmeter, Public Policy Research Center (accessed on December 2025) <http://gigmetar.publicpolicy.rs/en/2586-2/>.

104 Working Without Borders: The Promise and Peril of Online Gig Work, World Bank (2024) <http://hdl.handle.net/10986/40066>.

105 Gender and Platform Work: Beyond Techno-Solutionism, Fairwork (2023) <https://fair.work/en/fw/publications/gender-and-platform-work-beyond-techno-solutionism/>.

106 <https://fair.work/en/fw/publications/fairwork-albania-ratings-2023-assessing-work-in-the-albanian-platform-economy/> and <https://fair.work/en/fw/publications/fairwork-bosnia-and-herzegovina-ratings-2023-labour-standards-in-the-platform-economy/>.

107 <https://www.europeum.org/en/articles-and-publications/final-report-the-platform-revolution-shaping-the-fair-future-of-platform-work-in-the-eu-and-western-balkans/>.

conditions or task-specific risk-mitigation measures.¹⁰⁸ In Bosnia and Herzegovina, workers reported low awareness of their rights and benefits (including uncertainty about contract type), and platforms lacked mechanisms to ensure collective worker voice. In Serbia in 2023, couriers protested changes to the pay formula on Wolt and Glovo, and in 2024 Albanian Wolt workers demonstrated against fee reductions, underscoring the importance of collective organization and representation.

Social insurance coverage is uneven: some gig workers with formal contracts are covered, but those with service contracts or without contracts may be partially covered or excluded. In North Macedonia, self-employed workers must register with labor associations that lack representative bodies for platform work, limiting access to health and pension benefits.¹⁰⁹ Many location-based and online gig workers operate informally without contracts and are not covered by social insurance.¹¹⁰ Instead, they typically operate under service contracts that are subject to tax, but the contracting entities are not obliged to pay SSCs. Another increasingly

popular form of contract is “employer of record,” which entitles platform-based workers to pension benefits and health insurance, but these contracts are limited to freelancers working in foreign markets. While the sample is not representative and the result cannot be generalized, a survey of freelancers in four countries in the region found that only a quarter of respondents had health insurance,¹¹¹ and pension coverage was especially limited in Bosnia and Herzegovina (8 percent) and Serbia (16 percent). In the EU, the 2024 Platform Work Directive set minimum standards for working conditions, including determining correct employment status and strengthening transparency, fairness, and accountability in algorithmic management of platform work.¹¹² As of 2025, six member states had established a legal presumption of employment for platform-based gig workers;¹¹³ examples include Spain’s 2021 Rider Law (recognizing delivery couriers as employees and requiring monthly SSCs),¹¹⁴ and Belgium’s 2023 presumption of employment and requirement for work-related accident insurance for qualifying platform workers.¹¹⁵

¹⁰⁸ <https://fair.work/en/fw/ratings/>.

¹⁰⁹ The Platform Revolution: Shaping the Fair Future of Platform Work in the EU and Western Balkans EUROPEUM (2025) <https://www.europeum.org/en/articles-and-publications/final-report-the-platform-revolution-shaping-the-fair-future-of-platform-work-in-the-eu-and-western-balkans/>.

¹¹⁰ Embracing the digital age: The future of work in the Western Balkans – North Macedonia, European Training Foundation (2022) <https://www.etf.europa.eu/en/document-attachments/embracing-digital-age-future-work-western-balkans-north-macedonia>.

¹¹¹ Freelance in Four Countries of the Western Balkans, Đukanović Borislav; Marković Dušan; Krivokapić Nataša; and Banović, Silva (2022) https://www.researchgate.net/publication/361741285_Freelance_In_Four_Countries_of_Western_Balkan.

¹¹² Directive of the European Parliament and of the council on improving working conditions in platform work, European Union (2024) <https://data.consilium.europa.eu/doc/document/PE-89-2024-INIT/en/pdf>.

¹¹³ Working conditions of online platform workers: the complex legal landscape, Eurofound (2025) <https://www.eurofound.europa.eu/en/publications/all/working-conditions-of-online-platform-workers-the-complex-legal-landscape>.

¹¹⁴ Platform economy database, Eurofound, (accessed in December 2025) <https://apps.eurofound.europa.eu/platformeconomydb/riders-law-105142>.

¹¹⁵ <https://apps.eurofound.europa.eu/platformeconomydb/riders-law-105142>.

In the Western Balkans, legislation is under discussion in several countries.¹¹⁶

The Federation of Bosnia and Herzegovina drafted a new Labor Law in 2024 (under Parliamentary review) that would define platform work, mandate platform registration, and establish protections consistent with the EU directive; Kosovo is pursuing reforms to clarify employment status and labor rights including access to social security; Albania's Employment and Skills Strategy (2023–2030) highlights the need to accommodate new forms of employment and develop contractual tools for short-term and occasional jobs;¹¹⁷ and North Macedonia's 2025 Law on Work Engagement of Persons aims to formalize unregistered seasonal and casual workers and enable access to social security through a digital platform, including allowing pensioners, students, and social assistance beneficiaries to work formally without losing benefits.¹¹⁸

Simplifying registration, taxation, and SSC processes for gig workers while raising awareness of their legal rights would further leverage the potential of gig-work platforms to support sustainable employment growth. In Albania, freelancers registered as sole proprietors can pay taxes and SSCs through an online platform, and some platforms, such as Freelance and Nativeteams, provide freelancers with guidance on taxes and social contributions.

In addition to offering stronger worker protections, clear legal classifications for gig workers will enable Western Balkan governments to understand the size of gig economy and the characteristics of gig workers. Social dialogue is also crucial to ensure that gig workers have input into new or revised legislation. The EU's Directive on Platform Work offers valuable guidance that will enable Western Balkan countries to address critical issues facing platform-based gig workers.

Enabling inactive workers to enter and thrive in the labor market

Mobilizing underutilized human capital, especially youth, women, and vulnerable groups, will be vital for the WB6 economies to sustain growth amid mounting demographic pressures.

Despite progress on workforce education and improvements in job quality, large shares of workers remain unemployed, underemployed, or economically inactive across the region. To enable these groups to maximize their potential, governments will need to: (i) reduce disincentives and constraints to work; (ii) equip workers with in-demand skills and facilitate entry into the labor market; and (iii) expand the range of inclusive job opportunities.

116 Performance of the Western Balkan Six Regarding the European Pillar of Social Rights 2025, Regional Review, Regional Cooperation Council (2025) <https://www.esap.online/docs/236/rcc-esap-3-performance-of-the-western-balkan-six-regarding-the-european-pillar-of-social-rights-2025-regional-review>.

117 National Employment and Skills Strategy 2023–2030, Albania <https://ageing-policies.unece.org/api/public/attachments/view/56e00f58-84d4-448d-b3f2-d42616a972e8>.

118 New Law on Work Engagement of Persons – Providing Path to Legal and Social Protection for Informal Workers, Center for Research and Policy Making (2025) <https://crpm.org.mk/new-law-on-work-engagement-of-persons-providing-path-to-legal-and-social-protection-for-informal-workers/>.

Together, while these actions can help the region unlock its human capital, driving stronger and more inclusive economic growth, they will need to be complemented with demand-side reforms that create jobs. The Fall 2025 RER points to a combination of weak institutions, burdensome regulation, infrastructure gaps, limited access to finance, and an uneven playing field shaped by the outsized role of state-owned enterprises—that keep firms small, less competitive, and unable to generate quality jobs at scale. In a region where labor shortages are already reported as a constraint by firms in parallel with high unemployment rates, mobilizing

more workers alone does not solve the challenge; the countries must also ensure that productive and quality jobs exist to absorb them.

The recommendations below focus on high impact supply-side reforms that can be sequenced over time and implemented through a combination of public action, expenditure reprioritization, and greater private sector participation. While all the relevant policy areas are outlined for comprehensiveness, the report acknowledges the progress in certain areas by specific countries.

Figure 2.25 **A three-pillar strategy to mobilize untapped human capital in the Western Balkans**

Reducing disincentives and constraints to work	Equipping workers with in-demand skills and facilitate entry into the labor market	Expanding the range of inclusive job opportunities
» Lower policy-induced disincentives to formal employment » Expand access to quality childcare and elderly care services, including by private-sector participation » Promote a more equal sharing of care responsibilities	» Improve education quality to strengthen labor market relevance » Strengthen career guidance and school-to-work transitions » Strengthen PES capacity, services, and programs to provide tailored support to vulnerable groups, such as youth, women, the long-term unemployed, and social assistance beneficiaries	» Reduce labor market discrimination and segregation » Promote entrepreneurship and financial inclusion, especially for women » Enable flexible and new forms of work, including platform-based gig work » Facilitate the labor market integration of migrants and returnees

1. Reduce disincentives and constraints to work

- › Lower policy-induced disincentives to formal employment
 - i. Reduce minimum SSC bases to lower the effective tax burden on low-income workers and part-time workers.
 - ii. Introduce income-disregard provisions and in-work benefits to smooth transitions from social assistance into formal employment and strengthen work incentives.
- › Expand access to quality childcare services.
 - i. Increase public service provision using cost-efficient delivery models (repurposing public spaces, integrating childcare into schools, mobile units).
 - ii. Leverage private and home-based providers through streamlined licensing, training and certification, voucher schemes, and public-private partnerships – especially in underserved areas.
 - iii. Offer financial incentives for childcare services, including tax relief, favorable loan terms, and subsidies for providers, employers, and parents, especially in vulnerable households. In parallel, establish clear procedures and guidelines for families and childcare providers to apply for financial support.
 - iv. Strengthen the quality-management framework for childcare services by training inspectors, increasing inspection frequency, introducing mentoring and coaching visits, and institutionalizing robust monitoring and evaluation systems.
 - v. Improve the working conditions and career prospects of the ECEC workforce by expanding professional training opportunities, increasing compensation, and expanding career pathways.
 - vi. Increase ECEC funding gradually toward EU benchmarks, combining public resources with innovative and private financing mechanisms. Shift social attitudes toward formal childcare services by communicating ECEC benefits with families and by publishing data and reports on service quality to help families with informed decisions when choosing providers.
- › Expand access to quality elderly care services.
 - i. Scale-up home-based, community-based and residential LTC services, prioritizing individuals with highest care needs.
 - ii. Contract non-state providers and use digital and community-based solutions to extend coverage, particularly in rural areas.
 - iii. Define and enforce minimum quality standards through licensing and inspections and gradually introduce more proactive quality-management tools for LTC service providers (e.g., user-feedback and complaint mechanisms, peer-driven quality controls, and learning-oriented support).
 - iv. Gradually increase funding levels through budget reprioritization and complimentary private financing.

- v. Establish clear and workable institutional governance arrangements for LTC, with a clear strategic direction for services and benefits, regular assessments of LTC needs, and robust data collection and information systems.
- › Promote a more equal sharing of care responsibilities
 - i. Improve data on unpaid care work and strengthen incentives for men's take-up of parental leave.

2. Equip workers with in-demand skills and facilitate entry into the labor market

- › Improve education quality to strengthen labor market relevance
 - i. Focus on curricula modernization, teacher training, attendance policies, and expanded pre-primary enrollment to improve foundational and job-relevant skills.
- › Strengthen career guidance and school-to-work transitions
 - i. Expand access to high-quality career guidance secondary and tertiary levels, using data on graduate outcomes and labor demand.
 - ii. Strengthen links between education providers and employers through internships, apprenticeships, and work-based learning, and with employers playing a greater role in curriculum design.
- › Strengthen PES capacity, services, and programs to provide tailored support to vulnerable groups, such as youth, women, the long-term unemployed, and social assistance beneficiaries.
 - i. Increase PES funding and staffing, invest in the digitalization of services and processes, and introduce advanced profiling tools and labor-market intelligence to boost PES capacity and efficiency.
 - ii. Provide capacity-building opportunities for PES staff to better engage with employers, vulnerable individuals, NEET youth, and those not registered with public institutions.
 - iii. Increase the effectiveness of programs and services targeting vulnerable groups by training PES staff in gender- and vulnerable populations-sensitive counseling techniques, establishing a mentorship program, introducing performance-based financing for vocational training, helping vulnerable workers gain experience through public works, social services, and community development projects, and strengthening coordination with employers in offering post-placement support for vulnerable workers.
 - iv. Accelerate the implementation of the Youth Guarantee by allocating sufficient funding, establishing institutional coordination mechanisms, investing in public outreach, increasing employer engagement, and improving monitoring and evaluation systems.

3. Expand the range of inclusive job opportunities

- › Reduce labor market discrimination and segregation
 - i. Strengthen enforcement mechanisms to address discrimination in recruitment, pay, and promotions, including pay transparency and reporting requirements.
 - ii. Facilitate women's entry into higher productivity, market-oriented sectors through targeted activation and skills pathways.
 - iii. Extend working lives by aligning retirement ages with EU benchmarks and gradually increase statutory ages, especially for women; promoting flexible and part-time jobs for older workers beyond the retirement age; and offering upskilling, and skills training and employment services tailored to older workers.
- › Promote entrepreneurship and financial inclusion, especially for women
 - i. Scale support for female entrepreneurship through improved access to finance, business services, and networks.
 - ii. Use corporate governance measures and gender-sensitive procurement to expand market opportunities, while avoiding distortionary blanketed subsidies.
- › Enable flexible and new forms of work, including platform-based gig work
 - i. Recognize workers' rights to request flexible working arrangements and provide practical guidance to employers.
 - ii. Clarify the legal status, rights, and obligations of gig workers in line with the EU Platform Work Directive.
 - iii. Simplify taxes and SSC compliance for non-standard workers through digital, low-cost administrative systems and monitor implementation.
- › Facilitate the labor market integration of migrants and returnees
 - i. Streamline the recognition of foreign qualifications and prior learning, including through mutual recognition agreements with key destination countries.
 - ii. Establish one-stop-shop service centers that integrate employment counseling, skills training, legal information, and social services for both incoming migrants and returnees, leveraging digital platforms to reduce administrative barriers and improve access.

Translating these recommendations into action will require careful prioritization and a strategic mobilization of both public and private resources, given the limited fiscal space in the region.

Not all measures outlined above can be implemented simultaneously or financed through additional public spending alone. Public resources need not bear the full burden of reform. As discussed throughout, greater private sector participation—through public-private partnerships, private savings mechanisms, and stronger employer engagement in school-to-work transitions, vocational training, employment services, and care provision—can significantly extend the reach of reform without equivalent fiscal cost. Governments should sequence reforms strategically, prioritizing interventions with the highest impact relative to their cost, while gradually building the fiscal and institutional foundations needed for more resource-intensive investments over time.

Beyond short-term fiscal trade-offs, the reforms above should be understood as long-term fiscal and human capital investments. By raising labor force participation among women and youth and improving access to education, skills, and care services, these reforms increase human capital accumulation, productivity, and lifetime earnings. In turn, higher participation and productivity broaden the tax base, reduce reliance on social transfers, and ultimately creates the fiscal space needed to sustain further reform. The long-term dividends of stronger human capital and higher participation therefore reinforce the case for early, well-targeted action.

Country Notes

Albania

- Albania's economy sustained positive momentum through September 2025, supported by private consumption, tourism and construction.
- GDP grew by 3.7 percent in Q3 2025, y-o-y.
- Inflation remained contained, below the 3 percent target, while poverty declined amid a tightening labor market and rapid wage growth, which boosted incomes but added to price pressures.
- Growth is expected to moderate to 3.6 percent per annum in the medium term, reflecting a maturing tourism sector.

Key conditions and challenges

Albania's post-pandemic rebound has been supported by tourism and stronger trade and services linkages with the EU, helping growth average about 4.2 percent in 2022–25. Tourism remains an important contributor to growth, bolstering economic performance but increasing exposure to external shocks and highlighting the need for diversification.

Albania's economy continues to face structural constraints that weigh on its ability to converge to the EU average per capita income (currently at one third). These include low productivity in agriculture and services, a narrow export base, and a business environment affected by regulatory barriers, informality, and institutional weaknesses.

Skills mismatches, migration and aging continue to constrain human capital availability. Demographic and climate pressures, alongside higher spending needs, underscore the importance of safeguarding fiscal buffers through revenue mobilization and spending efficiency. Adoption of EU acquis-consistent reforms can raise productivity, deepen market integration, and ensure that gains are inclusive.

Recent Developments

Albania's economy grew by 3.7 percent y-o-y in Q3 2025, following 4.0 percent growth in 2024. Growth was supported by net exports, while domestic demand was broadly steady, with a slight increase in private investment. Looking at the supply side, services and construction drove economic activity in 2025, offsetting continued declines in agriculture, manufacturing and extractive industries, alongside a tapering of tourism growth.

Unemployment fell to 8.1 percent in Q3 2025, despite unchanged employment levels, reflecting labor force contraction driven by emigration and aging, alongside sectoral shifts toward services. Wage growth remained strong in 2025 (10.2 percent y-o-y through Q3), with public wage increases initially outpacing the private sector and supporting consumption. Sustained solid growth is estimated to have reduced poverty by 1.6 percentage points, bringing it down to 23.4 percent in 2025.

Inflation averaged 2.2 percent in 2025 remaining below BoA target. Despite strong demand and rising wages, inflation remained contained overall, while core inflation was higher, mainly reflecting services and rent, though imported inflation continued to ease.

Financing conditions remained favorable in 2025 and, together with strong demand, supported rapid private-sector credit growth (13.2 percent). Real-estate lending, particularly mortgages to households (16.7 percent), was the main driver, while a further increase in the share of lek-denominated credit supported monetary policy transmission and financial stability. Credit quality improved further, with the NPL ratio falling to 3.8 percent in December 2025 (from 4.2 percent in December 2024).

Albania had mixed results in its fiscal accounts in 2025. The fiscal balance and the primary balance deteriorated, owing to spending increases (public wages, pensions, and investment) that outpaced revenue growth (driven by higher social security contributions and personal income tax on the back of rapid wage growth). Yet, public debt dropped to 52.9 percent of GDP at end-2025, from 54.2 percent in 2024, aided by the positive primary balance, the appreciation of the Lek, and solid GDP growth.

Albania's external position strengthened significantly, with the current account shifting to a surplus of 0.25 percent of GDP in the first three quarters of 2025 (from a 1.26 percent deficit a year earlier), marking the first surplus on record. Strong services exports, led by tourism, offset weaker goods exports amid exchange rate appreciation and rising labor costs. FX purchases reached 3.0 percent of GDP in the first three quarters of 2025, reflecting primarily discretionary interventions rather than reserve accumulation that helped temper the Lek's appreciation, while raising external reserves to 7.7 months of imports.

Outlook

Albania's economic growth is forecast to slow as tourism matures. Consumption will get a temporary lift in 2026 from fiscal transfers and wage hikes, but rising prices will partly offset some gains. By 2027-2028, consumption growth is expected to ease with stable inflation near 3 percent, while government spending supports investment, especially for infrastructure. Wage growth may continue outpacing productivity, fueling inflation, while higher global energy prices and trade disruptions linked to the conflict in the Middle East are expected to add to domestic price pressures in 2026 and weaken household purchasing power. Despite these factors, employment and wage increases should help reduce poverty to 19.4 percent by 2028.

The fiscal deficit will rise to 1.8 percent of GDP in 2026 due to pension bonuses, defense spending, wage indexation, and capital investments. Through 2028, the deficit should shrink as GDP grows, the revenue strategy takes effect, and EU fund absorption increases, lowering public debt to about 51 percent of GDP.

The current account deficit will stay below historical levels despite strong demand owing to increased import-heavy public investment, although a larger fuel and energy import bill related to the Middle East conflict could widen the deficit.

Risks include global uncertainty and domestic pressures that may dampen confidence or reform pace. Positive outcomes are possible through faster EU accession and stronger reforms, leading to higher investment and productivity.

Albania - Selected Economic Indicators	2023	2024	2025e	2026f	2027f	2028f
Real GDP growth (percent)	4.0	4.0	3.9	3.4	3.7	3.6
Composition (percentage points):						
Consumption	2.5	3.4	2.5	2.4	2.2	1.8
Investment	-1.4	3.4	1.1	1.8	1.8	2.0
Net exports	2.9	-2.7	0.4	-0.7	-0.3	-0.2
Exports	3.0	0.0	2.4	2.5	2.8	2.9
Imports (-)	0.1	2.8	2.0	3.2	3.1	3.1
Consumer price inflation (percent, period average)	4.8	2.2	2.2	3.2	3.0	3.0
Public revenues (percent of GDP)	27.2	28.2	28.2	29.8	29.8	29.9
Public expenditures (percent of GDP)	28.5	28.9	29.9	31.6	31.4	31.1
<i>Of which:</i>						
Wage bill (percent of GDP)	4.2	4.5	4.7	4.6	4.5	4.4
Social benefits (percent of GDP)	10.9	11.2	11.2	11.4	11.3	11.3
Capital expenditures (percent of GDP)	5.1	4.6	4.9	5.3	5.5	5.7
Fiscal balance (percent of GDP)	-1.3	-0.7	-1.7	-1.8	-1.6	-1.2
Primary fiscal balance (percent of GDP)	0.7	1.4	0.3	0.5	0.7	1.1
Public debt (percent of GDP)	55.9	52.9	51.7	51.5	50.9	49.7
Public and publicly guaranteed debt (percent of GDP)	57.6	54.2	52.9	52.7	52.1	50.9
<i>Of which:</i> External (percent of GDP)	26.3	22.9	29.8	28.7	27.9	27.0
Goods exports (percent of GDP)	8.3	6.6	5.5	5.5	5.5	5.5
Goods imports (percent of GDP)	29.1	29.1	26.3	26.7	26.5	26.3
Net services exports (percent of GDP)	15.4	15.6	15.4	14.1	13.8	13.6
Trade balance (percent of GDP)	-5.4	-6.9	-5.4	-7.1	-7.2	-7.2
Net remittance inflows (percent of GDP)	4.2	4.2	4.0	3.8	3.8	3.8
Current account balance (percent of GDP)	-1.2	-2.4	-0.9	-3.1	-3.0	-2.9
Net foreign direct investment inflows (percent of GDP)	5.7	5.4	5.0	5.0	5.1	5.1
External debt (percent of GDP)	45.9	40.6	46.0	47.1	46.2	45.2
Real private credit growth (percent, period average)	-1.7	7.8	10.6	-	-	-
Nonperforming loans (percent of gross loans, end of period)	4.7	4.2	3.8	-	-	-
Unemployment rate (percent, period average)	9.5	8.5	8.4	-	-	-
Youth unemployment rate (percent, period average)	24.5	22.8	21.5	-	-	-
Labor force participation rate (percent, period average)	62.4	63.7	63.8	-	-	-
GDP per capita, PPP (current international \$)	21,208	22,066	22,927	23,709	24,587	25,472
Upper middle-income poverty rate (\$8.30 in 2021 PPP)	27.1	25.0	23.4	22.0	20.7	19.4

Sources: Country authorities, World Bank estimates and projections.

Bosnia and Herzegovina

- GDP growth slowed to 2.1 percent in 2025, down from 3.2 percent a year earlier, as momentum in private consumption and investment softened amid elevated inflation and political uncertainty. Industrial weakness persists.
- General elections could keep the fiscal deficit elevated in the near term, although public debt remains moderate.
- Growth is projected to gradually recover toward potential, reaching 3.2 percent by 2028.

Key conditions and challenges

Despite three decades of peace in Bosnia and Herzegovina, the path to sustainable growth remains challenging. The country has rebuilt its infrastructure and maintained macroeconomic stability despite the highly fragmented political system.

Convergence with the EU has been slow: average yearly real income growth of just 3 percent since 2015 has left BiH's per capita GDP at only about one-third of the EU average in 2024. As a result, progress in reducing poverty has been slow, and economic vulnerability persists—40 percent of adults reported in 2023 not being able to cover expenses for more than a month if their main income is lost.

Structural economic weaknesses weigh on long-term growth and add fiscal pressure. Outmigration and aging are shrinking the workforce and tax base while raising demand for public services. Low productivity, skills mismatches, high unemployment (especially among youth and women), and informality constrain growth and revenues. Reliance on coal-based energy, and low carbon pricing, keep production carbon-intensive and increase exposure to competitiveness losses under the EU's CBAM. Administrative burdens, governance challenges, and a weak business climate further slow reforms and EU accession progress.

Recent Developments

Real GDP growth slowed to 2.1 percent in 2025 from 3.2 percent in 2024, as private consumption and investment continued to expand at a more moderate pace. External demand remains a drag on growth due to continued import growth relative to exports. On the production side, services improved but industrial production maintained its negative trend.

Inflation increased to 4.0 percent in 2025, up from 1.7 percent the year before, driven by higher prices for food and utility bills, mainly water, electricity, and gas. Businesses and households faced rising costs, service sector prices increased after minimum wage hikes, and energy prices went up. More recently, conflict in the Middle East pushed up global oil prices, feeding through to higher gasoline prices and adding to inflationary pressures. Nevertheless, wages in the economy rose by 9 percent in real terms, bolstering the purchasing power of the population. The minimum wage increased by 55 percent in real terms in FBiH, which has impacted sectors with higher shares of low-wage workers, such as hospitality, construction, or food processing.

Despite the growth slowdown, labor market indicators showed an improvement, albeit uneven. The overall employment rate (LFS) increased to 44.5 percent in Q3 2025 from

43.6 percent in Q3 of 2024, notably among those with tertiary education (+2pp), while falling by 0.5pp among those with secondary education. The unemployment rate fell by 1pp to 11.2 percent during the same period. Against this background, the PPP \$8.3/day poverty rate was projected to decline by 0.4pp to 8.1 percent in 2025.

In 2025, higher government spending on wages, social benefits, and transfers widened the fiscal deficit of 2.0 percent of GDP, up from 1.8 percent in 2024. Despite this, BiH's public debt remains modest at approximately 28 percent of GDP.

The current account deficit slightly widened to 3.6 percent of GDP in 2025, with 80 percent of the external gap financed by FDI inflows, mainly into the foreign-owned banking sector.

With the attention of policy makers on the general elections in October 2026 and on meeting the legislative requirements to initiate EU accession negotiations, substantive progress on key structural reforms in 2026 could prove to be challenging.

Outlook

In the medium term, GDP growth is expected to remain moderate, with a projected rise close to its potential at 3.2 percent by 2028. Inflation is expected to decline to less than 2 percent. The fiscal deficit is expected to narrow as wage and pension hikes are embedded into the budget, and additional increases are not anticipated. The poverty rate is projected to decrease gradually by 1.7pp during the forecast period. Progress on EU accession will depend on political reforms following the 2026 elections. Although the Reform Agenda has been adopted, several essential laws for negotiations remain unresolved,

making significant advancements less likely during the election year. EU funds are thus expected to have a limited impact on growth. Exports will face increasing headwinds from CBAM's impact on carbon-intensive sectors (electricity, iron and steel, and aluminum), exacerbated by a lack of energy sector reform. The forecast is cautiously optimistic, driven mainly by domestic consumption, while industrial output, exports, and structural reforms lag behind. The forecast includes the impact of the conflict in the Middle East on the country, which is mainly through inflation and the current account. It highlights the need for persistent policy efforts to strengthen economic resilience and accelerate EU convergence.

However, significant downside risks remain. Persistent geopolitical tensions and further market disruptions could reignite inflation and undermine the fragile recovery in the EU—a key trading partner. Reduced demand there could further weaken BiH's exports. Geopolitical challenges may intensify domestic political divisions, making it even harder to advance crucial structural reforms.

Bosnia and Herzegovina - Selected Economic Indicators	2023	2024	2025e	2026f	2027f	2028f
Real GDP growth (percent)	2.0	3.2	2.1	2.5	3.0	3.2
Composition (percentage points):						
Consumption	-	-	2.5	2.3	2.7	2.7
Investment	-	-	0.9	1.0	0.6	0.8
Net exports	-	-	-1.4	-0.8	-0.4	-0.3
Exports	-	-	1.0	0.3	0.2	0.2
Imports (-)	-	-	2.4	1.0	0.6	0.5
Consumer price inflation (percent, period average)	6.1	1.7	4.0	4.3	2.2	1.6
Public revenues (percent of GDP)	40.7	41.7	43.7	43.3	43.0	43.0
Public expenditures (percent of GDP)	41.9	43.6	45.8	45.3	44.6	43.9
<i>Of which:</i>						
Wage bill (percent of GDP)	10.4	10.5	11.4	11.6	11.5	11.3
Social benefits (percent of GDP)	15.8	16.2	20.3	19.9	19.7	19.5
Capital expenditures (percent of GDP)	3.4	3.7	4.2	4.0	4.0	4.0
Fiscal balance (percent of GDP)	-1.2	-1.8	-2.0	-2.0	-1.6	-0.9
Primary fiscal balance (percent of GDP)	-0.4	-0.8	-1.1	-1.0	-0.6	0.0
Public debt (percent of GDP)	26.4	26.1	25.8	25.4	24.8	25.4
Public and publicly guaranteed debt (percent of GDP)	28.5	27.2	26.8	26.1	26.0	26.4
Of which: External (percent of GDP)	21.1	19.9	18.2	17.9	17.4	17.8
Goods exports (percent of GDP)	31.1	28.1	27.6	27.4	27.0	26.6
Goods imports (percent of GDP)	51.6	49.8	48.4	48.1	47.3	46.5
Net services exports (percent of GDP)	8.8	8.3	7.4	7.1	6.7	6.4
Trade balance (percent of GDP)	-11.7	-13.4	-13.4	-13.6	-13.6	-13.5
Net remittance inflows (percent of GDP)	7.6	7.8	7.4	7.2	7.1	6.9
Current account balance (percent of GDP)	-2.1	-3.5	-3.6	-4.1	-4.2	-4.1
Net foreign direct investment inflows (percent of GDP)	3.7	3.0	2.9	2.8	3.0	2.9
External debt (percent of GDP)	47.3	47.5	44.7	43.0	41.4	39.9
Real private credit growth (percent, period average)	-0.7	7.2	5.0	-	-	-
Nonperforming loans (percent of gross loans, end of period)	3.8	3.2	2.4	-	-	-
Unemployment rate (percent, period average)	13.2	12.6	12.2	-	-	-
Youth unemployment rate (percent, period average)	30.1	30.2	32.5	-	-	-
Labor force participation rate (percent, period average)	47.8	49.1	49.5	-	-	-
GDP per capita, PPP (current international \$)	18,256	18,842	19,237	19,717	20,307	20,956
Upper middle-income poverty rate (\$8.30 in 2021 PPP)	9.3	8.5	8.1	7.6	7.0	6.5

Sources: Country authorities, World Bank estimates and projections.

Kosovo

- Although growth decelerated in 2025, the economy showed resilience amid heightened uncertainty.
- Intensifying price pressures weighed on activity, while a widening merchandise trade gap further strained the current account.
- The outlook is subject to downside risk, including uncertainty stemming from the impact of the Middle East conflict.
- Prudent fiscal management is key to maintain strong fiscal buffers and prioritize growth-enhancing spending.

Key conditions and challenges

Kosovo, an economy in transition, has made significant improvements in socio-economic development allowing its transition to middle-income status in 2008. Over the past decade, it moved away from a growth model with high dependence on foreign aid toward a model characterized by rising consumption, sustained investment in infrastructure, and deeper financial intermediation. In 2025, growth remained resilient despite elevated domestic uncertainty. Although higher inflation tempered the pace of poverty reduction, the \$8.30 (2021 PPP) headcount kept edging down, aided by wage growth and labor-market formalization amid tightening conditions.

Macroeconomic stability rests on a prudent, rule-based fiscal framework and improving revenue performance. However, faster convergence with the EU will require stronger revenue mobilization, more effective public financial management, and expanded resources to meet substantial investment needs in energy, infrastructure, and human capital.

Persistent structural labor market constraints limit the breadth and durability of welfare gains. Expanding childcare to raise female participation and strengthening education

and training, especially for lower educated workers, could support better quality jobs and reduce persistent disparities across regions and households with children.

Energy vulnerabilities linked to aging lignite-based generation underscore the need to accelerate the shift to renewables and enhance energy efficiency. Investments in core infrastructure would improve water security, digitalization, and connectivity. Convergence to the EU will require an acceleration in reform implementation to strengthen trade integration, attract productive foreign direct investment (FDI) and improve governance.

Recent Developments

After a 3-year period of above 4 percent average growth, Kosovo's economy slowed to 3.1 percent in the third quarter of 2025, as private consumption softened and imports picked up, while investment activity strengthens gradually. Higher wages and transfers, alongside robust credit growth, supported private consumption. By end-2025, the contribution of trade to growth remained negative. Goods exports remained weak amid subdued external demand, while services exports growth, dominated by travel, ICT, and other business services, helped offset the impact of rising imports to a degree. Remittances and FDI inflows

continued to provide support covering more than half of the CAD. Rising energy and food prices contributed to higher inflation in 2025, continuing in 2026 as recent global developments worsen the outlook, with potential disproportionate negative impacts on the poor and vulnerable. The consumer price index reached 5.3 percent by December 2025, bringing annual inflation to 3.9 percent. In addition to higher food and energy prices, domestic inflationary pressures have also been picking up, as reflected in the Producer Price Index for the first three quarters of 2025 reaching 8.5 percent. Data from administrative sources on wages for 2025 indicates that inflation has been exerting a drag on household incomes.

The fiscal outturn during 2025 reflected an increase in spending, matched by sustained revenue mobilization. Preliminary data for 2025 indicate that the fiscal position continues to be supported by strong tax revenue growth (8.5 percent in 2025 in nominal terms), driven by consumption, and continued formalization. At the same time, expenditure increased by 9.8 percent, driven by spending on wages, pensions and social transfers. The financial sector remains stable amid continued financial deepening, although recent trends in credit growth call for stronger oversight and risk monitoring.

Outlook

The medium-term outlook is expected to firm only modestly in 2026 due to a combination of domestic and external factors and converge close to its potential at 3.8 for the period.

Price increases in energy and food following the conflict in the Middle East are expected to exacerbate an already difficult external demand sector, and the current account deficit is expected to hover above 9 percent

on average, reflecting more expensive imports alongside a gradual rebound in exports. In addition, higher energy prices, domestic pressures, and an expansionary fiscal policy during a period of near-potential growth are likely to be fueling inflation. As a result, growth is projected to be driven by domestic demand, particularly consumption, as investment will be subject to costlier goods imports.

Higher wages and elevated public and private transfers are expected to support private consumption and further reduce poverty, even as inflationary pressures are likely to persist throughout the period. The upward risk on poverty from a possible increase in food prices is significant, as food represents 64 percent of total consumption for the bottom decile.

The 2026 Budget foresees an increase in existing transfer schemes, pensions and child benefits, as well as structural changes to wage policy. While the fiscal deficit is budgeted within the legally binding rule of 2 percent of GDP, policy adjustments are warranted to contain current spending growth and reorient expenditures toward high-quality public investment and stronger fiscal risk management.

This reprioritization would help accelerate implementation of the EU Growth Plan, address longstanding development constraints, and lift growth beyond current trends. Structurally high poverty rates necessitate a policy agenda that reforms social assistance and focuses on participation, skills, and firm dynamism.

Kosovo - Selected Economic Indicators	2023	2024	2025e	2026f	2027f	2028f
Real GDP growth (percent)	4.1	4.6	3.6	3.7	3.9	4.0
Composition (percentage points):						
Consumption	3.3	4.7	3.9	3.9	4.0	3.9
Investment	1.2	2.2	2.6	1.1	1.4	1.7
Net exports	-0.4	-2.2	-2.9	-1.3	-1.5	-1.6
Exports	2.8	3.8	3.3	2.6	3.2	3.3
Imports (-)	3.2	6.0	6.3	3.9	4.6	4.9
Consumer price inflation (percent, period average)	4.9	1.6	3.9	4.0	3.1	2.2
Public revenues (percent of GDP)	29.3	29.7	29.6	29.0	29.1	28.7
Public expenditures (percent of GDP)	29.6	30.0	30.4	30.5	30.2	30.1
<i>Of which:</i>						
Wage bill (percent of GDP)	7.9	8.1	8.1	8.2	8.2	8.2
Social benefits (percent of GDP)	7.0	7.6	6.1	6.6	6.5	6.4
Capital expenditures (percent of GDP)	5.7	6.3	6.4	6.2	6.4	6.8
Fiscal balance (percent of GDP)	-0.3	-0.2	-0.7	-1.5	-1.2	-1.4
Primary fiscal balance (percent of GDP)	0.1	0.1	-0.4	-1.1	-0.8	-1.1
Public debt (percent of GDP)	17.2	16.8	16.9	17.5	17.7	17.0
Public and publicly guaranteed debt (percent of GDP)	17.5	17.2	17.1	17.5	17.8	17.1
<i>Of which: External (percent of GDP)</i>	7.2	7.5	9.3	11.6	13.0	13.6
Goods exports (percent of GDP)	8.9	9.1	8.3	8.3	8.2	8.0
Goods imports (percent of GDP)	61.1	61.2	62.5	64.6	65.5	65.9
Net services exports (percent of GDP)	16.8	17.3	19.8	19.4	20.4	21.4
Trade balance (percent of GDP)	-35.3	-34.8	-34.3	-36.9	-36.9	-36.5
Net remittance inflows (percent of GDP)	13.4	12.7	12.1	11.9	11.5	11.1
Current account balance (percent of GDP)	-7.2	-8.4	-9.6	-9.8	-9.6	-8.8
Net foreign direct investment inflows (percent of GDP)	6.7	5.5	5.8	5.6	5.7	5.7
External debt (percent of GDP)	39.6	40.7	40.8	42.0	42.9	43.6
Real private credit growth (percent, period average)	8.8	12.2	14.9	-	-	-
Nonperforming loans (percent of gross loans, end of period)	2.0	1.9	2.1	-	-	-
Unemployment rate (percent, period average)	10.9	10.8	-	-	-	-
Youth unemployment rate (percent, period average)	17.3	19.5	-	-	-	-
Labor force participation rate (percent, period average)	40.7	43.2	-	-	-	-
GDP per capita (US\$)	6,159	6,647	7,613	8,378	8,935	9,563
Upper middle-income poverty rate (\$8.30 in 2021 PPP)	37.2	36.6	33.7	31.9	30.3	29.9

Sources: Country authorities, World Bank estimates and projections.

Montenegro

- Growth slowed to 2.7 percent in 2025, reflecting lower electricity production and softer tourism.
- The fiscal deficit widened from 3.3 to 4.3 percent of GDP in 2025, reducing policy space and increasing financing needs. Public debt is about 64 percent of GDP amid sizable upcoming repayments.
- As European Union (EU) accession advances, stronger fiscal discipline and rebuilding buffers will be key to safeguarding stability and supporting growth.

Key conditions and challenges

Montenegro's small, highly open, and euroized economy is structurally exposed to external shocks. Without independent monetary policy, fiscal policy is the main macroeconomic instrument, increasing the importance of prudent budgeting, credible medium-term frameworks, and reform implementation. Heavy reliance on tourism, foreign investment, and external financing further heightens vulnerability to shifts in global demand and financial conditions amid elevated geopolitical uncertainty.

After a sharp pandemic contraction, Montenegro recorded a strong rebound, with growth averaging 9.1 percent in 2021–23. As external momentum softened and base effects faded, growth moderated to 3.2 percent in 2024. The Europe Now reform agenda, expanded in 2024 through “Europe Now 2,” significantly increased net wages and pensions and reduced labor taxation, supporting household incomes and formal employment. While supporting living standards, these measures, implemented amid slowing growth, have widened the fiscal deficit in 2025. The poverty rate, measured at the at the purchasing power parity (PPP) \$8.3/day threshold, has been declining steadily since the peak in 2020.

EU accession remains Montenegro's central policy anchor, shaping its fiscal and growth agenda. All 33 negotiating

chapters have been opened and 14 provisionally closed, with membership targeted for 2028, contingent on sustained reform progress. Alignment with the EU acquis—particularly under Chapter 17 (Economic and Monetary Policy)—requires strengthening fiscal governance, improving medium-term budgeting, and enhancing debt management. An important pending reform is the operationalization of an independent Fiscal Council, which would reinforce fiscal discipline and policy credibility. EU integration, supported by pre-accession funds and the Growth Plan, provides both financing and reform incentives, linking stronger institutions with more sustainable growth.

Recent Developments

Growth moderated further in 2025, estimated at 2.7 percent, extending the gradual slowdown observed since 2024 and reflecting significantly weaker net exports. Industrial production declined by 9.2 percent, largely due to reduced electricity output following the temporary closure of the Pljevlja thermal power plant for environmental upgrades. Tourism remained broadly stable: total arrivals increased by 4.7 percent, while overnight stays declined by 1.5 percent, pointing to shorter average stays. At the same time, retail trade and credit growth reflected resilient domestic demand.

Inflation increased to 3.9 percent in 2025, driven mainly by housing and utilities. Strong wage growth supported household purchasing power, with average net wages rising by 11.3 percent in real terms, reflecting the minimum wage increase and reduced pension contributions. Registered unemployment fell 14.3 percent by end-2025, while employment rose nearly 5 percent, pointing to still-favorable labor market conditions. Supported by positive employment and wage dynamics, the PPP \$8.3/day poverty rate declined 0.8 percentage points (pp) to 7.7 percent in 2025.

External imbalances widened significantly. The current account deficit reached 20.5 percent of GDP in 2025, driven by a large goods trade deficit (around 46 percent of GDP), only partly offset by a sizeable services surplus. Net foreign direct investment covered roughly a third of the external gap, with the remaining part financed primarily through other capital inflows.

The fiscal position weakened, with the overall deficit widening from 3.3 percent of GDP in 2024 to 4.3 percent in 2025. Higher spending, particularly on social transfers, capital investment, and interest, together with lower social contribution revenues, outweighed strong tax performance. Public debt rose to 63.9 percent of GDP, partly reflecting liability management operations to strengthen liquidity buffers ahead of large, uneven repayments. These operations also point to debt management risks and reliance on foreign financing.

Outlook

Economic activity is projected to expand at about 3 percent annually over 2026–28. Domestic demand is expected to remain the main engine of growth, reflecting steady household spending, broadly stable

tourism, and a pipeline of capital projects, amid heightened global uncertainty. Public investment in transport and renewable energy—together with continued nonresident interest in property—should support medium-term prospects by easing infrastructure bottlenecks and advancing decarbonization. Outcomes will, however, depend critically on implementation capacity. As investments are import dependent, external imbalances are likely to persist, with the current account deficit averaging 18–19 percent of GDP in 2026–28.

Early-March Middle East conflict pushed up oil and gasoline prices, lifting the inflation projection to an estimated 3.2 percent in 2026 before it eases to 1.9 percent by 2028.

The PPP \$8.3/day poverty rate is projected to decline by a further 1.4pp during 2026–2028, but the pace of poverty reduction is tapering off, as labor market absorption lags for low-skilled workers. Higher prices driven by the Middle East conflict are expected to put additional strain on the purchasing power of households.

The fiscal deficit is expected to decline gradually from 3.7 percent of GDP in 2026 to about 3.1 percent by 2028. Public debt is projected to hover around 64 percent of GDP, although amortization pressures will intensify in 2027. Considering sizable gross financing needs, a robust fiscal framework—grounded in debt sustainability, aligned with EU requirements, and capable of addressing fiscal risks while supporting development objectives—will be essential to safeguard investor confidence and underpin durable growth.

Downside risks stem from financing and geopolitical pressures, including prolonged conflict in the Middle East; faster EU accession could improve the outlook.

Montenegro - Selected Economic Indicators	2023	2024	2025e	2026f	2027f	2028f
Real GDP growth (percent)	6.5	3.2	2.7	2.9	3.1	3.1
Composition (percentage points):						
Consumption	6.7	9.3	5.1	3.1	2.9	2.8
Investment	2.4	0.3	1.7	1.3	1.3	1.3
Net exports	-2.5	-6.5	-4.0	-1.4	-1.2	-1.0
Exports	4.0	-1.8	-1.9	0.8	1.1	1.2
Imports (-)	6.5	4.7	2.1	2.2	2.3	2.2
Consumer price inflation (percent, period average)	8.6	3.3	3.9	3.2	2.5	1.9
Public revenues (percent of GDP)	41.6	41.7	41.1	41.1	41.3	41.6
Public expenditures (percent of GDP)	41.0	45.0	45.4	44.8	44.7	44.7
<i>Of which:</i>						
Wage bill (percent of GDP)	10.5	10.2	9.8	9.8	9.7	9.7
Social benefits (percent of GDP)	11.2	12.7	13.1	13.0	13.0	12.9
Capital expenditures (percent of GDP)	4.8	5.8	6.2	6.0	6.0	6.0
Fiscal balance (percent of GDP)	0.6	-3.3	-4.3	-3.7	-3.4	-3.1
Primary fiscal balance (percent of GDP)	2.4	-1.3	-2.3	-1.6	-1.3	-1.0
Public debt (percent of GDP)	58.4	59.8	63.9	66.4	64.2	64.1
Public and publicly guaranteed debt (percent of GDP)	59.9	61.2	65.2	67.5	65.3	65.2
<i>Of which:</i> External (percent of GDP)	50.2	55.1	60.7	63.1	61.5	60.6
Goods exports (percent of GDP)	10.1	8.6	7.2	7.5	7.5	7.7
Goods imports (percent of GDP)	52.4	51.8	53.0	52.8	52.2	51.6
Net services exports (percent of GDP)	23.9	20.7	19.5	19.2	19.3	19.3
Trade balance (percent of GDP)	-18.3	-22.5	-26.3	-26.1	-25.4	-24.6
Net remittance inflows (percent of GDP)	4.7	4.5	4.2	4.2	4.1	4.1
Current account balance (percent of GDP)	-11.2	-17.1	-20.5	-19.6	-18.9	-17.9
Net foreign direct investment inflows (percent of GDP)	6.1	6.4	6.5	6.5	6.5	6.5
External debt (percent of GDP)	128.2	126.5	126.3	..	..	..
Real private credit growth (percent, period average)	-2.3	7.2	14.0	-	-	-
Nonperforming loans (percent of gross loans, end of period)	5.8	4.1	3.0	-	-	-
Unemployment rate (percent, period average)	13.1	11.4	10.7	-	-	-
Youth unemployment rate (percent, period average)	23.3	26.0	23.9	-	-	-
Labor force participation rate (percent, period average)	63.9	63.7	60.7	-	-	-
GDP per capita, PPP (current international \$)	31,863	34,063	38,960	42,518	44,828	47,170
Upper middle-income poverty rate (\$8.30 in 2021 PPP)	10.2	8.5	7.7	7.1	6.8	6.3

Sources: Country authorities, World Bank estimates and projections.

North Macedonia

- Growth strengthened in 2025, driven by highway construction and services.
- Rising wages, together with food and services price increases kept inflationary pressures elevated.
- Revenue shortfalls and an increasing debt stock highlight the need for timely fiscal consolidation.
- Outlook projections are contingent on sustained reform implementation and subject to significant downside risks, including uncertainty stemming from the Middle East conflict.

Key conditions and challenges

Growth accelerated in 2025, with output rising by an average 3.5 percent, underpinned by robust investment and consumption. Poverty, measured by the US\$ 8.30 per day poverty line, is declining slowly, reflecting wage growth, but structural labor market weaknesses remain due to youth unemployment, low participation of women in labor markets and a high degree of informality. Medium-term prospects hinge on tackling persistent structural constraints that limit productivity, inclusive growth, and convergence with EU living standards. Weak competitive dynamics, reflected in market barriers to entry and exit, informal sector practices, and a weak competition landscape, increase risks for businesses and discourage innovation and investment. A high level of state presence in the economy creates market distortions and limits the effectiveness of public support measures. Fiscal governance and public administration reforms are a key priority to safeguarding macroeconomic stability and creating space for growth-enhancing spending.

Fiscal consolidation plans have been postponed, and the fiscal deficit in 2025 is above limits set by the fiscal rule. Persistent weaknesses in expenditure management and medium-term budgeting together

with structural challenges in revenue administration, reduce the ability of fiscal policy to support growth. Strengthening public financial management, reprioritizing expenditure toward human capital and infrastructure, and improving SOE management are critical to improve the effectiveness of fiscal policy. Indicators of human capital development are among the lowest in the region, pointing to efficiency and quality issues, especially in the education and health sectors. Reforms in the areas of energy, digitalization, connectivity and labor markets remain a priority for the growth agenda. Anchoring reforms in the EU Growth Plan, with credible implementation and monitoring, could promote private investment, and sustain poverty reduction.

Recent Developments

Output growth accelerated in 2025, reaching 3.5 percent, propelled by gross investments which also dragged imports up, amid growing consumption and a higher trade deficit. On the production side, growth was led by construction, largely highway-related, and services. In line with stronger investment-led demand, external balances deteriorated. By end 2025, the current account deficit deepened to 4.3 percent of GDP on the back of a higher merchandise trade deficit and

narrower services surplus. Net FDI, a large portion of which consists of reinvested earnings, decelerated in 2025 to its lowest level since 2020. Labor market conditions for those aged 15+ continued to improve in 2025 alongside output growth, but gains were uneven across age groups and favored men. The unemployment rate decreased to 11.5 percent, with a sharper decline for men, reflecting the chronic underutilization of the country's human capital. These developments preceded the escalation of the Middle East conflict, which has since emerged as a source of heightened global uncertainty. Poverty, as measured by the US\$ 8.30 per day poverty line, is estimated to have marginally declined by 0.5p.p. in 2025, helped by a 5.3 percent increase in real wages during 2025, partly driven by labor shortages. Robust wage gains, coupled with strong credit growth, and persistent food and services price increases weighed on inflation (4.1 percent in 2025). To strengthen monetary policy transmission, the Central Bank adjusted its operational framework by shortening the maturity of the main policy instrument and introducing a symmetric interest rate corridor. Although robust growth and rising inflation bolstered revenues, revenue collection fell short of the revised 2025 target, reflecting broad-based shortfalls. Combined with increased spending on social and municipal transfers, these revenue gaps contributed to a larger than planned fiscal deficit of 4 percent of GDP in 2025.

Outlook

Growth is projected to average around 3 percent in 2026–2028 driven primarily by domestic demand. However, this trajectory

faces downside risks. Increased uncertainty associated with the conflict in the Middle East poses risks to the inflation outlook, although targeted measures could help cushion the impact of inflation in 2026. Higher commodity prices and supply chain disruptions could also drive-up import costs in 2026, putting additional pressure on the current account. A slowdown in key trading partners, particularly in the EU, could weigh on export demand and remittances. The US\$ 8.30 poverty rate is projected to decline a further 1.7pp between 2025 and 2028. Rebuilding fiscal buffers and ensuring compliance with the fiscal rule will be critical to strengthen resilience against shocks. Accelerating convergence toward EU living standards will require stronger reform efforts to advance the structural transformation of the economy. Priority should be given to reforms that enhance competitiveness, crowd-in investment toward higher value-added sectors, and expand opportunities for more and better jobs. Effective and timely implementation of reforms under the EU Growth Plan, including reforms in public administration, the energy sector, digitalization and human capital can further catalyze the country's long term growth agenda.

North Macedonia - Selected Economic Indicators	2023	2024	2025e	2026f	2027f	2028f
Real GDP growth (percent)	2.6	3.0	3.5	2.9	3.0	3.0
Composition (percentage points):						
Consumption	1.2	1.7	2.3	1.8	1.6	1.5
Investment	-5.6	1.5	2.3	2.3	2.1	2.0
Net exports	8.4	-1.6	-1.8	-1.2	-0.7	-0.6
Exports	-2.2	-2.8	4.0	2.4	3.0	3.2
Imports (-)	-10.6	-1.2	5.8	3.6	3.7	3.8
Consumer price inflation (percent, period average)	9.4	3.5	4.1	3.4	2.7	2.5
Public revenues (percent of GDP)	32.5	33.4	33.9	34.1	34.3	34.5
Public expenditures (percent of GDP)	36.8	37.9	37.9	37.7	37.7	37.7
<i>Of which:</i>						
Wage bill (percent of GDP)	6.7	7.4	7.5	7.5	7.5	7.5
Social benefits (percent of GDP)	16.5	17.7	18.3	18.4	18.4	18.4
Capital expenditures (percent of GDP)	5.3	3.8	3.4	3.8	3.8	3.9
Fiscal balance (percent of GDP)	-4.3	-4.5	-4.0	-3.6	-3.3	-3.1
Overall fiscal balance with the Public Enterprise for State Roads included (percent of GDP)	-4.6	-4.9	-4.5	-4.1	-3.8	-3.6
Primary fiscal balance (percent of GDP)	-2.9	-2.6	-2.1	-2.2	-1.9	-1.7
Public and publicly guaranteed debt (percent of GDP)	57.8	61.4	59.3	59.4	59.8	60.0
<i>Of which:</i> External (percent of GDP)	39.1	37.8	38.0	-	-	-
Goods exports (percent of GDP)	49.3	43.1	41.2	42.4	42.5	43.1
Goods imports (percent of GDP)	67.3	62.8	61.1	61.5	61.3	61.6
Net services exports (percent of GDP)	5.0	6.8	6.0	5.0	5.4	5.7
Trade balance (percent of GDP)	-13.0	-12.9	-13.9	-14.1	-13.4	-12.8
Net remittance inflows (percent of GDP)	2.2	2.0	1.7	1.8	1.9	1.8
Current account balance (percent of GDP)	0.3	-2.1	-4.3	-3.8	-3.1	-2.8
Net foreign direct investment inflows (percent of GDP)	3.3	6.6	1.4	2.1	2.6	3.1
External debt (percent of GDP)	79.1	75.3	-	-	-	-
Real private credit growth (percent, period average)	-2.9	3.5	7.6	-	-	-
Nonperforming loans (percent of gross loans, end of period)	2.7	2.6	1.9	-	-	-
Unemployment rate (percent, period average)	13.1	12.4	11.5	-	-	-
Youth unemployment rate (percent, period average)	29.3	28.9	29.3	-	-	-
Labor force participation rate (percent, period average)	52.3	52.3	52.5	-	-	-
GDP per capita, (current international \$)	8,675	9,280	10,492	10,643	11,255	11,834
Upper middle-income poverty rate (\$8.30 in 2021 PPP)	18.9	17.9	17.4	16.5	16.0	15.6

Sources: Country authorities, World Bank estimates and projections.

Serbia

- Growth slowed to 2 percent in 2025 amid internal and external pressures.
- It is projected to recover to 2.7 percent in 2026, as consumption and investment rebound gradually although external uncertainty persists, including due to the conflict in the Middle East.
- The incidence of poverty remained broadly flat at 7.8 percent in 2025 and is projected to continue falling, albeit at slower rate, as the remaining poor are often characterized by chronic unemployment.

Key conditions and challenges

GDP growth slowed to an estimated 2 percent in 2025, reflecting relatively weak consumption amid stubbornly high inflation and significantly lower investment. Exports, however, contributed positively to growth. Looking at the production side, services sectors were the only significant drivers of growth. The construction posted the largest drag on growth (of 0.7 pp), while adverse weather conditions had a notable effect on agriculture. Manufacturing had only a marginally positive contribution to growth.

Serbia continues to demonstrate a strong fiscal performance, and the economic slowdown of 2025 did not affect the collection of revenues, which together with the underperformance of expenditures, led to a lower-than-expected fiscal deficit. Domestic political uncertainty has, however, disrupted policy dialogue and implementation of key structural reforms which is inter alia reflected in slower than expected progress with the EU accession process.

Recent Developments

After a strong 2024, Serbia's economy lost momentum in 2025. A series of domestic and external events led to this economic underperformance. The resignation of the

Prime Minister and the delayed formation of the government, Russia-related sanctions impacted the oil sector, another poor agriculture season led to a significant increase in food prices and slower than expected GDP growth, and the year was characterized by repeated political protests. All these factors, together with a continued weak external economic environment, led to a drop in net FDI inflows by about 50 percent in euro terms and some decline in employment in the manufacturing sector. A notable positive development was the pickup in operations of the Stellantis (FIAT) factory in Kragujevac, which contributed significantly to a good export performance in 2025. Exports increased by 8.4 percent in 2025, largely driven by higher exports to the EU and the Balkans region. Despite the slowdown, private consumption remained resilient, supported by wage growth of 11.5 percent (7.4 percent in real terms) and continuous increase in short-term consumption loans.

While the unemployment rate stabilized at around 8.7 percent (practically at the same level as in 2024), the youth unemployment remained at over 23 percent, due to skills mismatches and limited job opportunities. Consequently, many young Serbian citizens migrate abroad, fueling brain drain and a shrinking workforce. While regional disparities are severe, there is very little internal labor mobility. Reflecting these

labor market pressures and inflation eroding incomes, the poverty level (based on the upper-middle income line of \$8.30/day in 2021 PPP) was at an estimated 7.8 percent in 2025.

Inflation rose in early 2025, peaking at 4.9 percent in July, slightly above the target the upper bound of the target range ($3\pm 1.5\text{pp}$). This increase was largely driven by food prices, which were 7.4 percent higher in July than a year ago affected by the poor agriculture season. In response, the government decided to introduce an administrative control of margins in the retail sector, which contributed to lower inflation in the second half of 2025. However, it remains to be seen whether prices will rebound as these measures expired in February 2026.

Against the backdrop of slower growth, weaker domestic demand, and somewhat higher inflation in 2025, government revenues performed well in 2025. They increased by 7.9 percent in nominal terms, year-over-year, thanks to a higher-than-planned collection of contributions for social insurance, VAT, and PIT. However, expenditures increased by 9 percent in nominal terms, driven by higher spending on wages and pensions, pushing the consolidated fiscal deficit to 2.4 percent of GDP. Public debt continues to decline gradually and reached 45 percent of GDP at the end of December.

Strong export performance helped contain the widening of the current account deficit, which increased only slightly in 2025, to 4.9 percent of GDP. Exports proved resilient, helping reduce the trade deficit by 4.2 percent (in euro terms). In contrast, the surplus in trade in services was significantly lower (down by 17.6 percent). Financing of the CAD deteriorated since net FDI inflows decreased by 50 percent. Foreign

currency reserves reached EUR 29 billion in December, covering 6.7 months of imports. Performance of the banking sector remains solid. Overall credit increased by 13.5 percent (year-over-year) through December. Loans to businesses increased by 10.6 percent, while loans to households increased by 19.5 percent and loans to the government increased by 6.4 percent. Gross nonperforming loans declined to 2.1 percent in December 2025.

Outlook

The Serbian economy is expected to grow at around 3-4 percent over the medium term, driven primarily by consumption and, to some extent, by investment. However, there are downside risks. These include continued problems in SOEs, the lack of progress in the next stage of structural reforms, global and domestic uncertainty, and the recent conflict in the Middle East. Inflation is expected to remain elevated in 2026 in part due to the expected impact of the Middle East conflict on energy prices, but is projected to stay within the target range. Fiscal performance in 2026 should remain broadly in check, provided that energy-crisis support measures prove temporary or are offset by measures on expenditure side.

Economic growth, if sustained, will continue to lift more Serbian citizens out of poverty. However, the remaining poor are concentrated among pensioners, the long-term unemployed, or those completely out of the labor force. Thus, targeted social assistance, care services for the disabled and elderly, job search support, and training programs will become essential to ensure further poverty reduction.

Serbia - Selected Economic Indicators	2023	2024	2025e	2026f	2027f	2028f
Real GDP growth (percent)	3.7	3.9	2.0	2.7	3.0	4.0
Composition (percentage points):						
Consumption	-0.1	3.9	2.5	2.3	2.7	3.5
Investment	1.3	2.1	1.5	0.7	1.1	0.9
Net exports	2.6	-2.1	-2.0	-0.4	-0.8	-0.4
Exports	1.6	3.1	3.4	3.3	3.5	3.4
Imports (-)	-1.0	5.2	5.4	3.8	4.4	3.9
Consumer price inflation (percent, period average)	12.1	4.6	3.8	4.2	3.9	3.0
Public revenues (percent of GDP)	39.4	40.5	40.9	40.3	40.2	40.0
Public expenditures (percent of GDP)	41.4	42.4	43.4	43.3	43.2	42.6
<i>Of which:</i>						
Wage bill (percent of GDP)	8.8	9.3	9.9	10.1	10.1	10.1
Social benefits (percent of GDP)	12.5	12.9	13.3	13.2	13.0	12.8
Capital expenditures (percent of GDP)	6.4	7.2	6.9	6.7	7.1	6.8
Fiscal balance (percent of GDP)	-2.0	-2.0	-2.4	-3.0	-3.0	-2.5
Primary fiscal balance (percent of GDP)	-0.4	-0.1	-0.6	-0.9	-1.0	-0.6
Public debt (percent of GDP)	46.2	45.3	42.9	41.7	40.9	40.5
Public and publicly guaranteed debt (percent of GDP)	48.4	47.3	45.0	44.9	44.7	44.7
<i>Of which:</i> External (percent of GDP)	33.7	33.4	31.1	31.0	31.0	30.0
Goods exports (percent of GDP)	37.1	35.9	36.6	34.3	34.9	33.5
Goods imports (percent of GDP)	46.0	44.0	43.9	43.8	43.7	42.4
Net services exports (percent of GDP)	4.1	3.4	2.6	3.5	3.8	4.2
Trade balance (percent of GDP)	-4.7	-4.7	-4.7	-6.0	-5.0	-4.7
Net remittance inflows (percent of GDP)	4.9	4.3	4.2	4.4	4.2	3.9
Current account balance (percent of GDP)	-2.4	-4.5	-4.9	-4.9	-4.5	-4.3
Net foreign direct investment inflows (percent of GDP)	5.7	5.5	2.6	4.0	4.5	4.2
External debt (percent of GDP)	58.7	58.6	58.6	57.9	57.5	57.0
Real private credit growth (percent, period average)	-9.2	0.9	7.9	-	-	-
Nonperforming loans (percent of gross loans, end of period)	3.2	2.5	2.1	-	-	-
Unemployment rate (percent, period average)	9.4	8.6	8.7	-	-	-
Youth unemployment rate (percent, period average)	25.0	23.0	23.4	-	-	-
Labor force participation rate (percent, period average)	55.4	56.2	56.0	-	-	-
GDP per capita, PPP (current international \$)	28,914	31,001	32,742	34,790	37,275	39,627
Upper middle-income poverty rate (\$8.30 in 2021 PPP)	9.0	8.2	7.8	7.3	6.8	6.3

Sources: Country authorities, World Bank estimates and projections.



Adjusting to Shocks, Mobilizing Untapped Potential

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