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Western Balkans Regular Economic Report
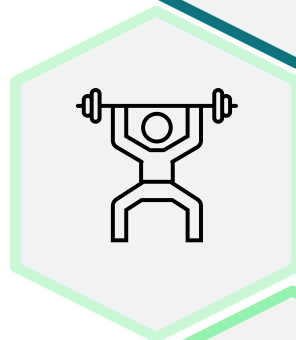
No. 25 | Spring 2024

Invigorating Growth

Western Balkans RER | Main messages for the Spring 2024 edition

01 | Growth has returned to pre-pandemic rates. The post-pandemic recovery displayed strong duality across the WB6 countries, which partially reconciled during 2023

02 | Both employment growth and the pace of poverty reduction have slowed. The employment rate reached a historic high at 48.1 percent. Over 1/3 of adults live in households not able to cope with a sudden loss of their main income
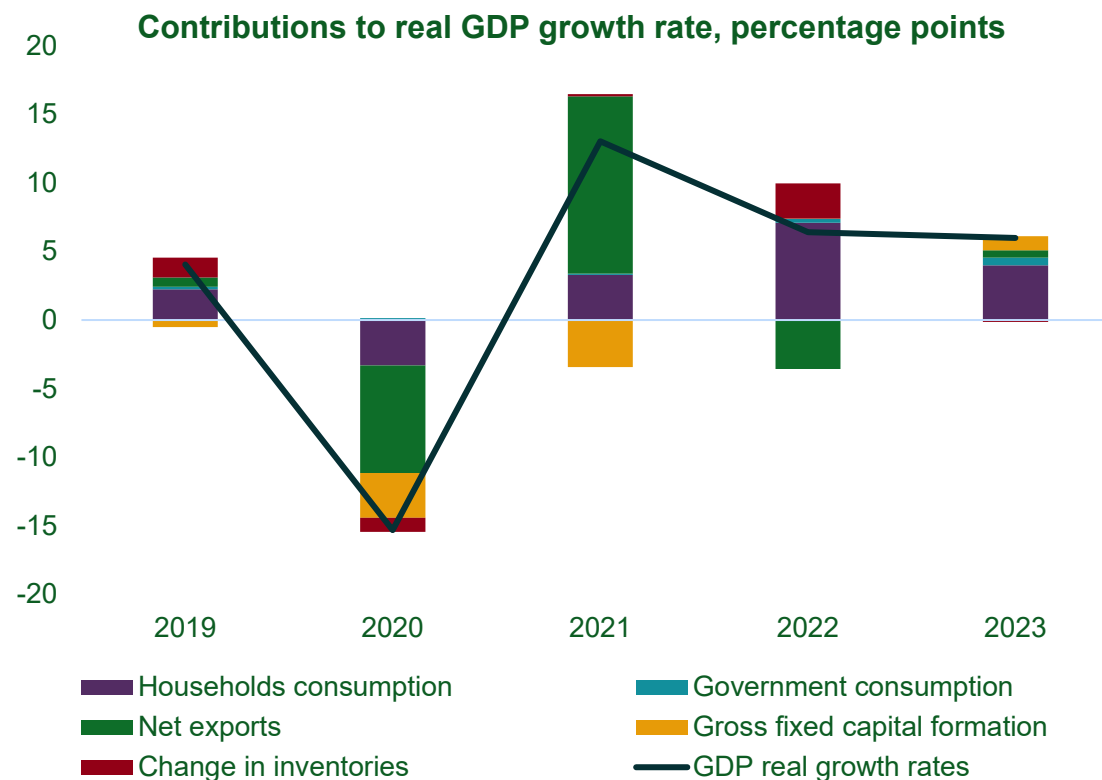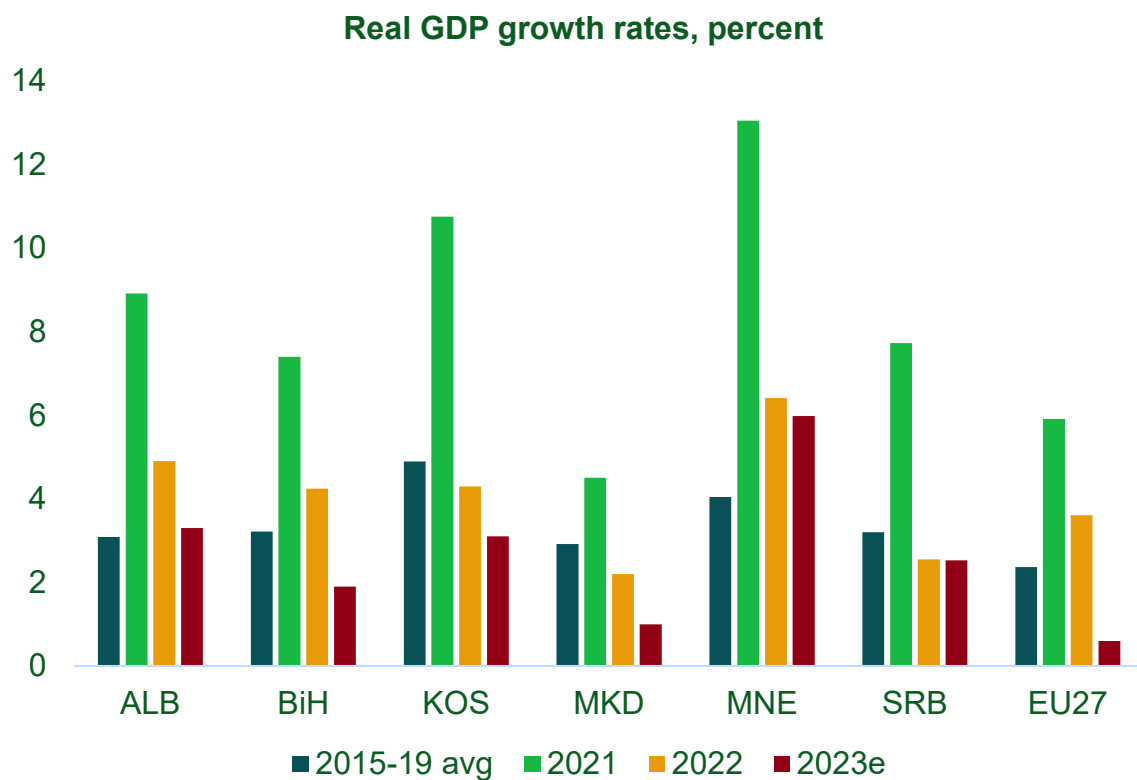
06 I The outlook has improved, but *invigorating growth* is necessary. The EU new Growth Plan and regional integration initiatives provide a potential boost to the reform agenda

03 I Inflation has eased substantially but pressures remain elevated. Domestic pressures come from wages and production costs, and translate into persistently high core inflation

05 I Current account deficits improved, and the financial sector proved resilient, despite heightened risks. In the financial sector, credit growth was weak throughout 2023, but experienced an uptick at the end

04 | Fiscal deficits contracted faster than previously expected, helped by strong revenue performance. Public debt declined to its lowest in a decade, but the cost of financing remains elevated

Growth | Montenegro's economic performance is the strongest in the region

**Montenegro's annual post-pandemic growth averaged 8.5 percent during 2021-23...**

Real GDP growth rates, percent

Legend: 2015-19 avg | 2021 | 2022 | 2023e

Categories: ALB, BiH, KOS, MKD, MNE, SRB, EU27

...driven by booming tourism and private consumption, further supported by an influx of foreigners

Contributions to real GDP growth rate, percentage points

Legend: Households consumption | Government consumption | Net exports | Gross fixed capital formation | Change in inventories | GDP real growth rates
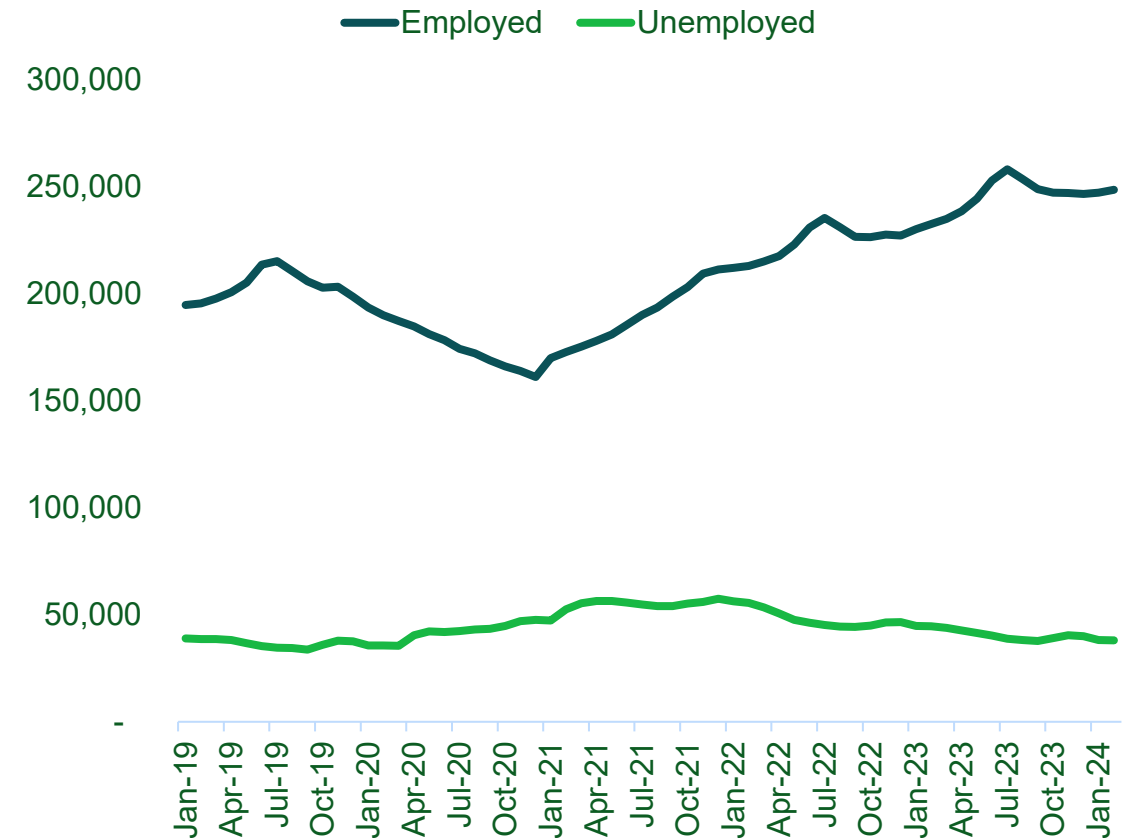
Years: 2019, 2020, 2021, 2022, 2023

Source: World Bank staff calculations based on data from national statistical offices

Labor market | Employment levels reached a new historical high

The employment and activity rates reached a new high, and unemployment rate a historic low in 2023.
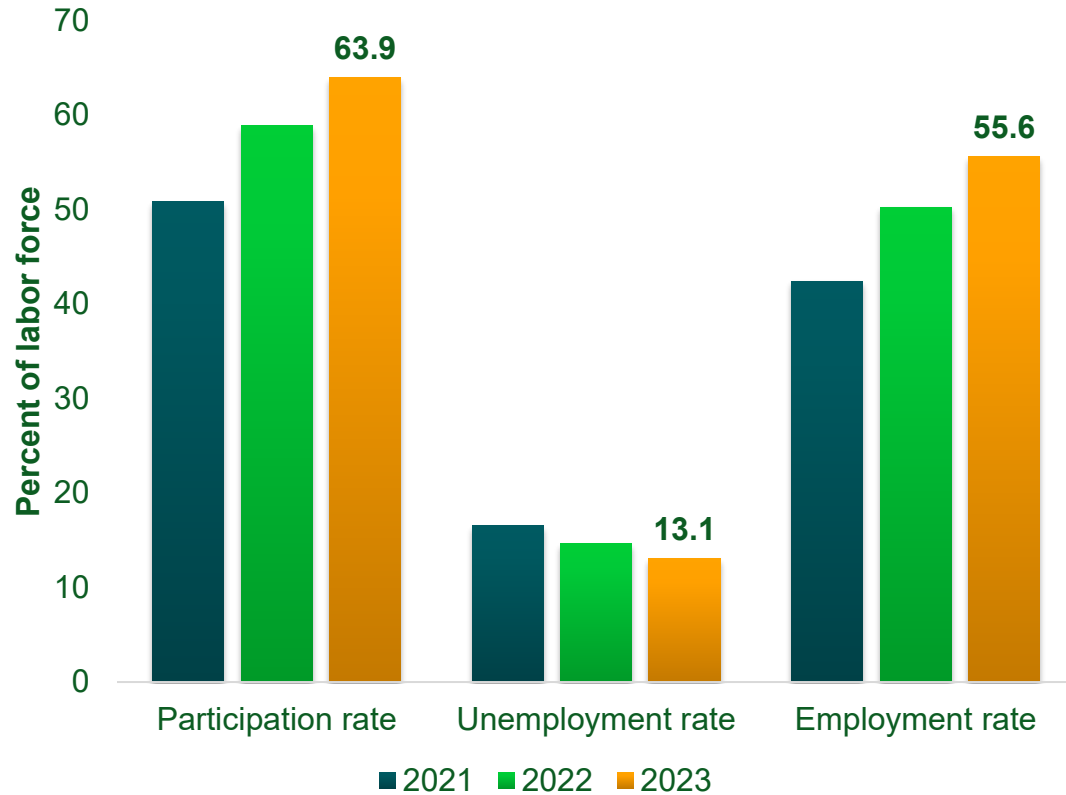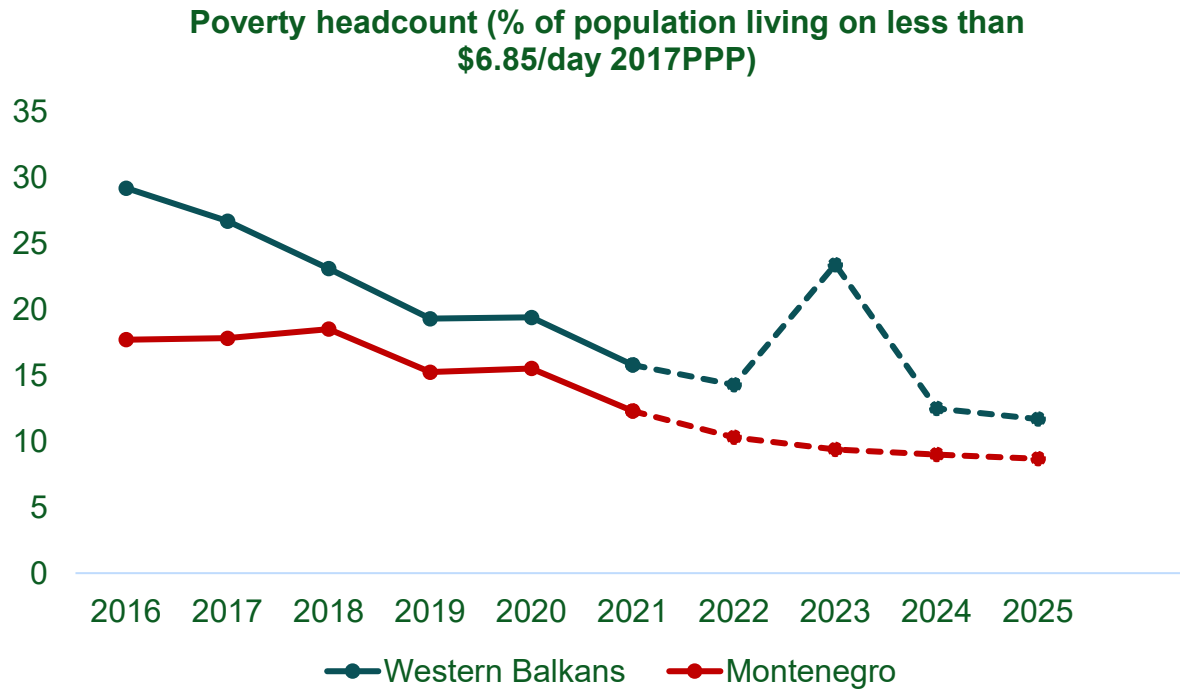

Administrative data indicate the trend in job creation continued into Q1 2024.
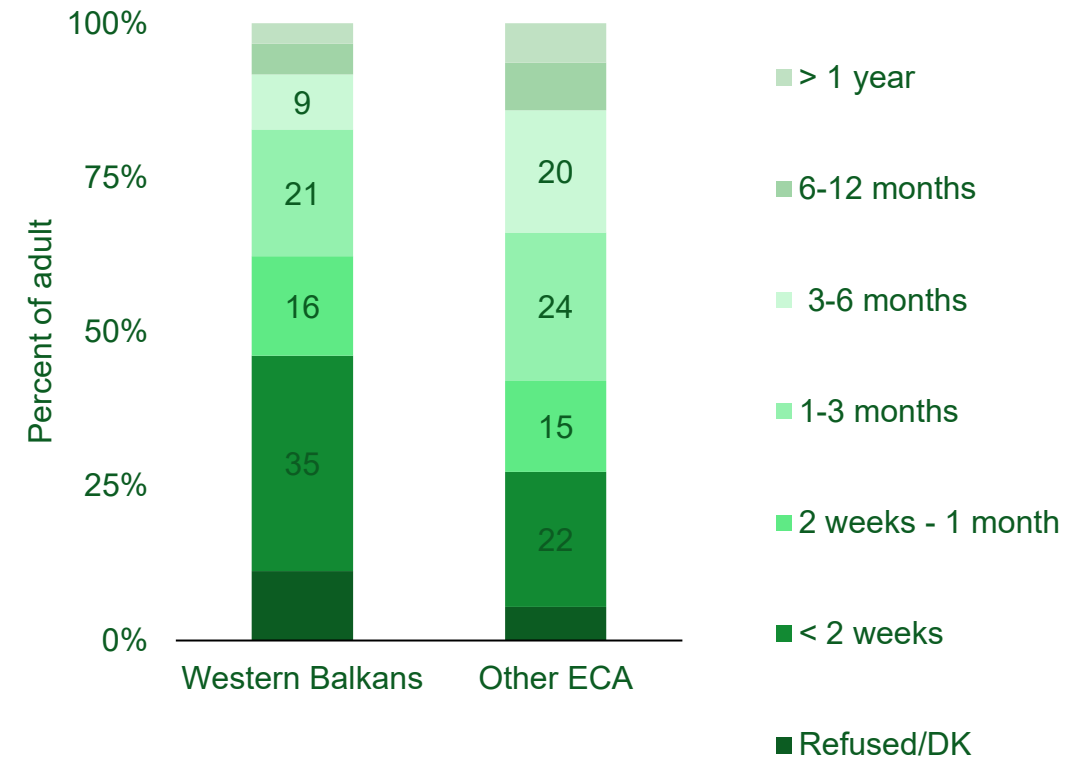
Poverty | Despite continued poverty reduction, the pace of progress has slowed, and vulnerability levels remain significantly elevated

The pace of poverty reduction is declining compared with the pre-pandemic years

Poverty headcount (% of population living on less than $6.85/day 2017PPP)

Legend: Western Balkans, Montenegro

Over 1/3 of adults live in households not able to cope with a sudden loss of their main income

Percent of adult

| Category	Western Balkans	Other ECA
> 1 year		
6-12 months		20
3-6 months	9	
1-3 months	21	24
2 weeks - 1 month	16	15
< 2 weeks	35	22
Refused/DK		

Source: World Bank estimates and projections based on 2021 income data from the Survey of Income and Living Conditions (SILC) for Montenegro; 2019 for Albania and North Macedonia, 2021 for Serbia; and 2017 Household Budget Survey (HBS) for Kosovo. Note: Income and consumption measures from the SILC and the HBS, respectively, are not strictly comparable. Welfare is estimated in U.S. dollars using 2017 PPPs. Due to a lack of comparable data, the regional estimate excludes Bosnia and Herzegovina (BiH). Forecasts are based on GDP per capita in constant LCU, e = estimate, f = forecast.
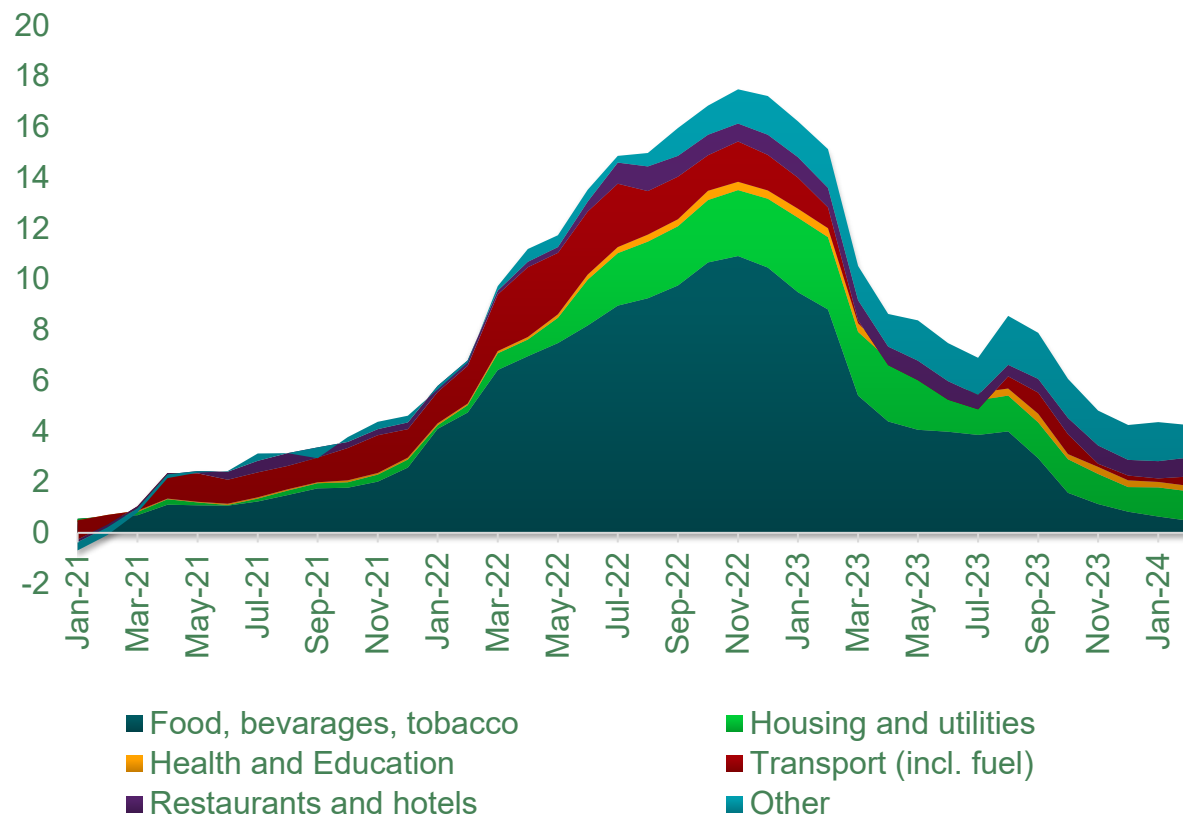
Source: Life in Transition IV data, 2023

Inflation | Inflation has eased substantially, but price pressures remain persistent
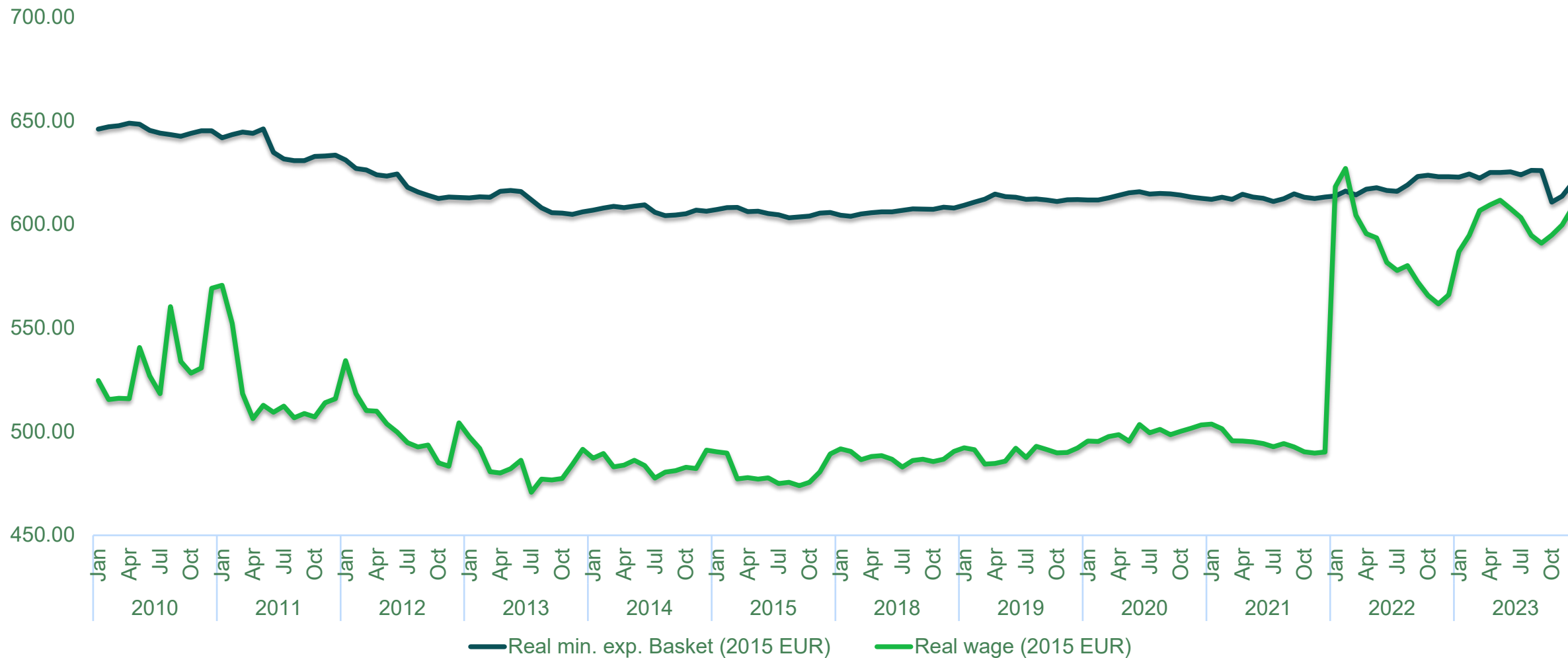
After increasing to levels not seen in multiple decades, inflation decreased substantially during 2023…

Legend: WB6, ALB, BIH, KOS, MKD, MNE, SRB
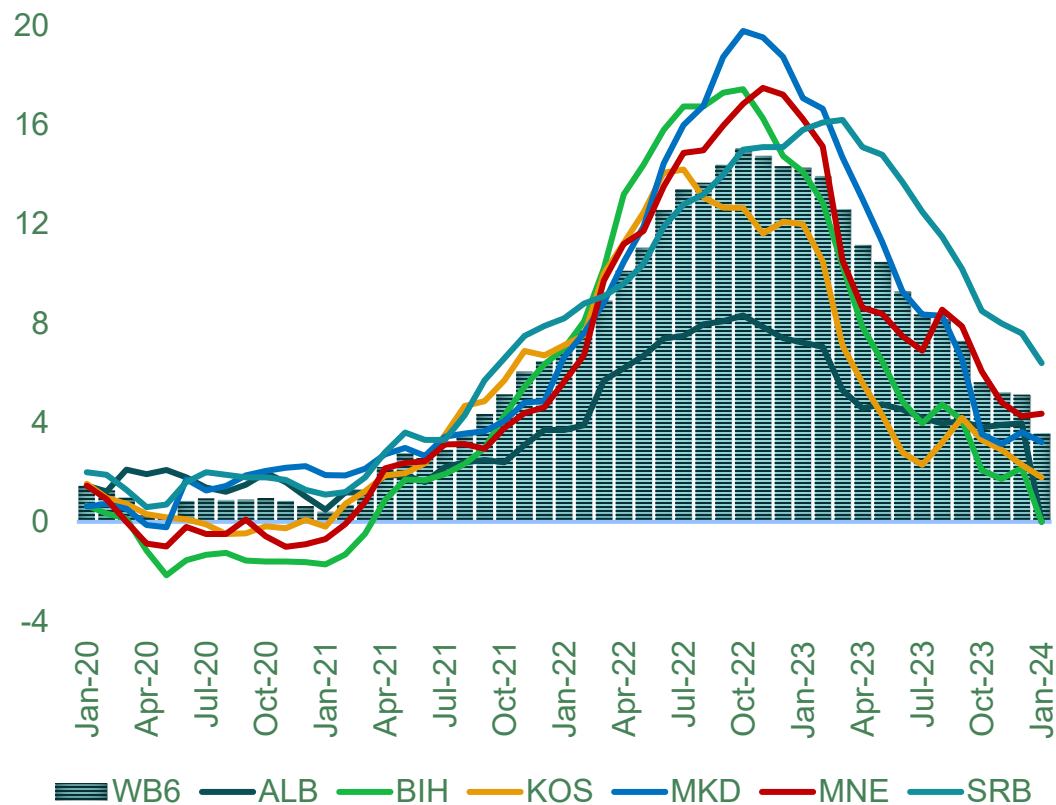
…but monthly inflation remains elevated, now led by clothing and footwear, housing, and other services.

Legend: Food, bevarages, tobacco; Housing and utilities; Health and Education; Transport (incl. fuel); Restaurants and hotels; Other

Source: World Bank staff calculations based on data from national statistical offices

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Inflation | Largely led by public sector wage increases, real wages edged by 2.3 percent

Real min. exp. Basket (2015 EUR)   Real wage (2015 EUR)

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The current account deficit improved thanks to strong service exports and reduced import prices, but net FDI declined, financing just over a half of the current account deficit in 2023.

Source: World Bank staff calculations based on data from central banks.

Legend: Trade deficit · Net remittances · Current account deficit · Net FDI

2017: 3.9, -16.1, 11.3, -23.5
2018: 4.0, -17.0, 6.9, -23.9
2019: 4.0, -14.3, 6.2, -21.2
2020: 5.3, -26.1, 11.2, -35.0
2021: 6.1, -9.2, 11.7, -19.4
2022: 6.5, -12.9, 13.2, -22.8
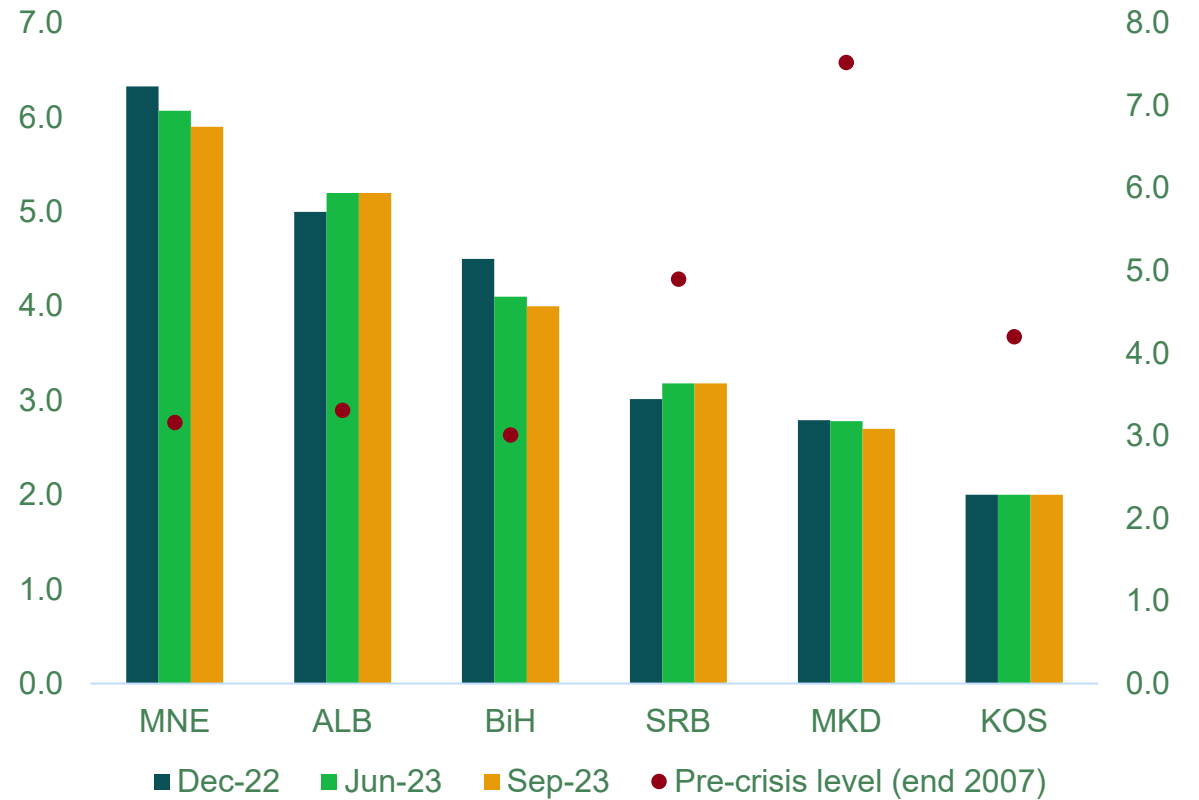2023: 4.9, -11.4, 6.3, -18.8
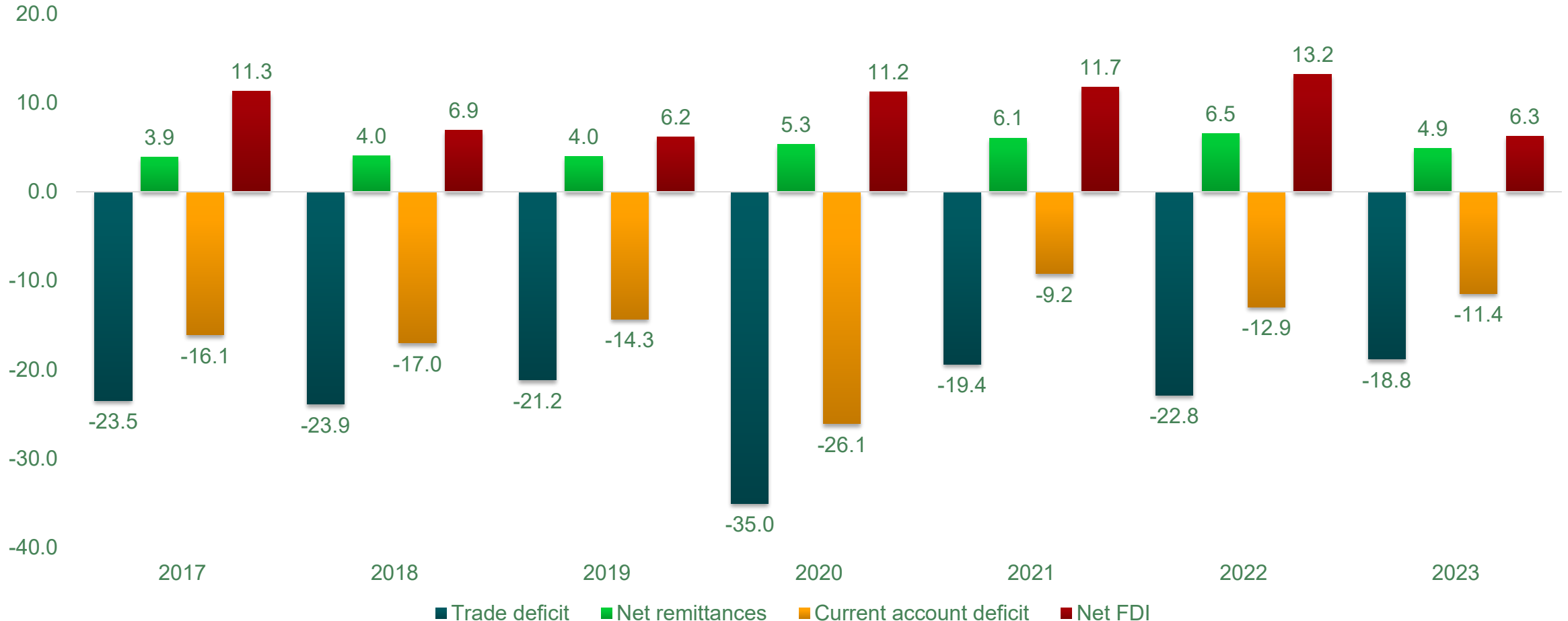
Financial | The financial sector maintains strong capital and liquidity buffers

Credit growth remains positive, supported both by residents and non-residents' borrowing.

Legend: Residents | Non-residents | Total
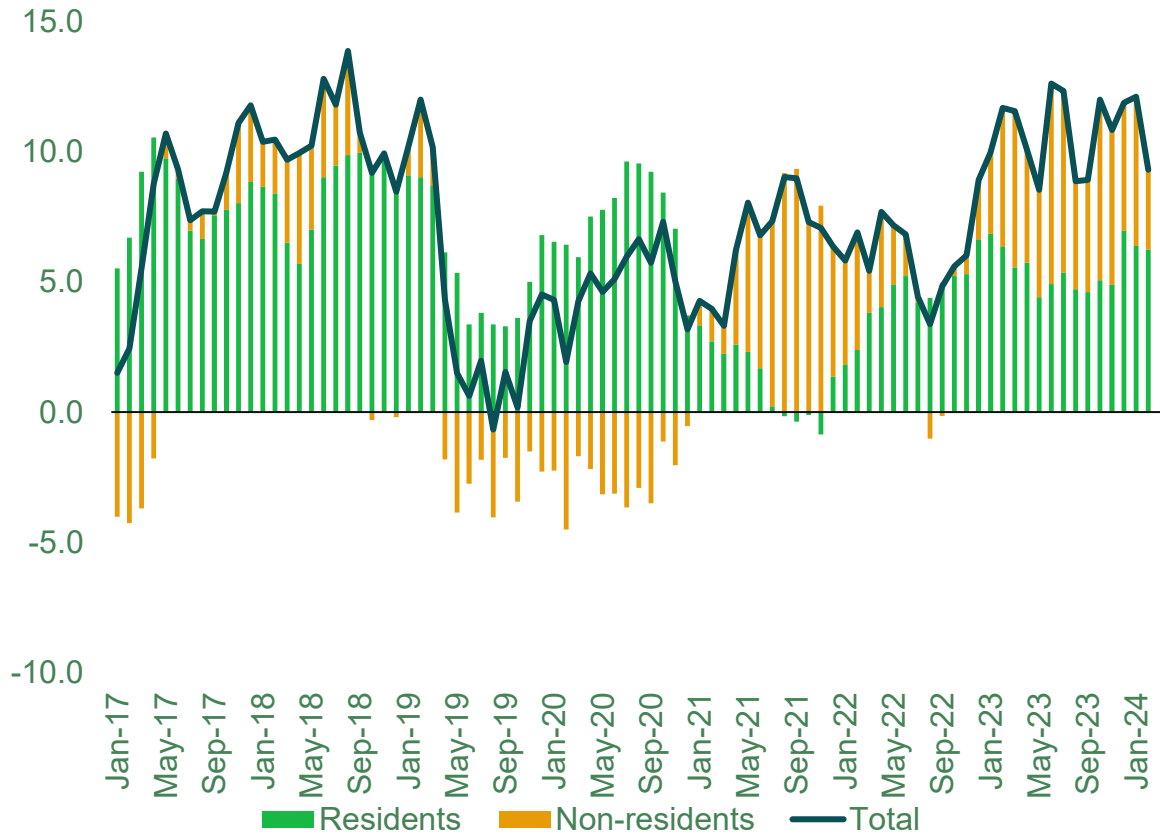
NPLs continued declining, but remain the highest among the Western Balkan countries.

Legend: Dec-22 | Jun-23 | Sep-23 | Pre-crisis level (end 2007)

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Fiscal | The fiscal performance was better than planned, resulting in a fiscal surplus
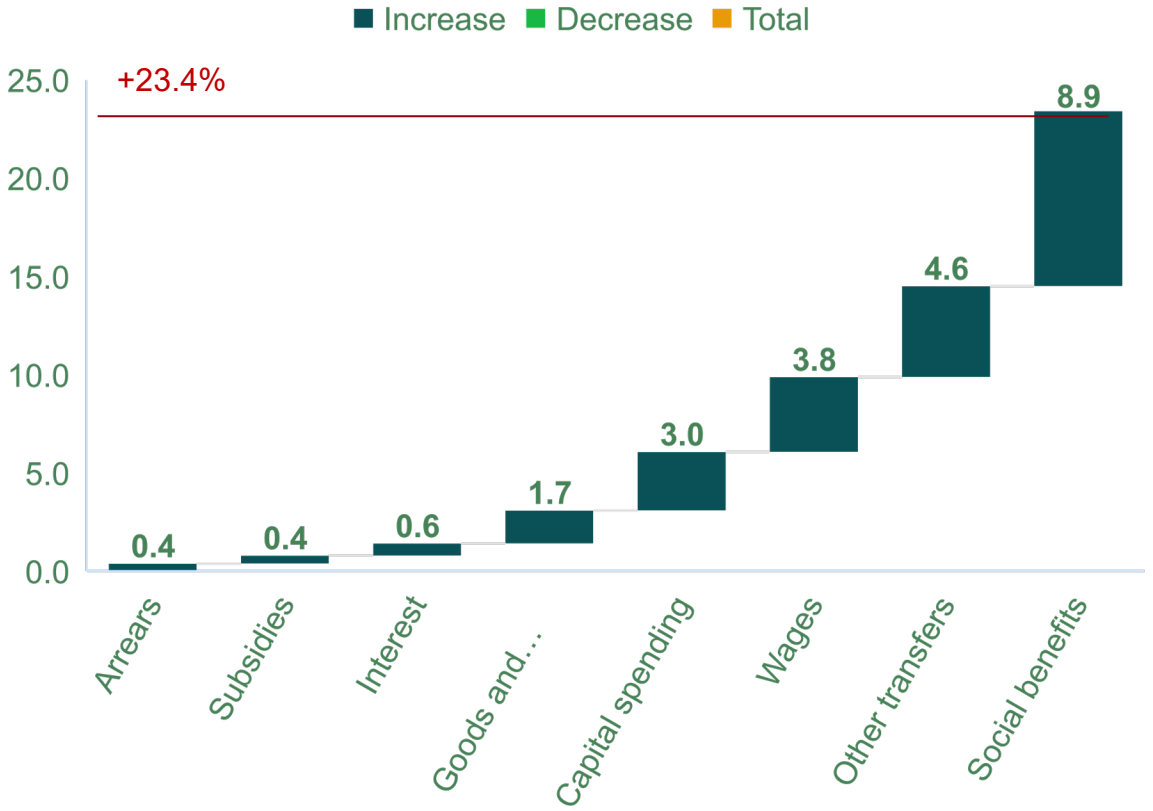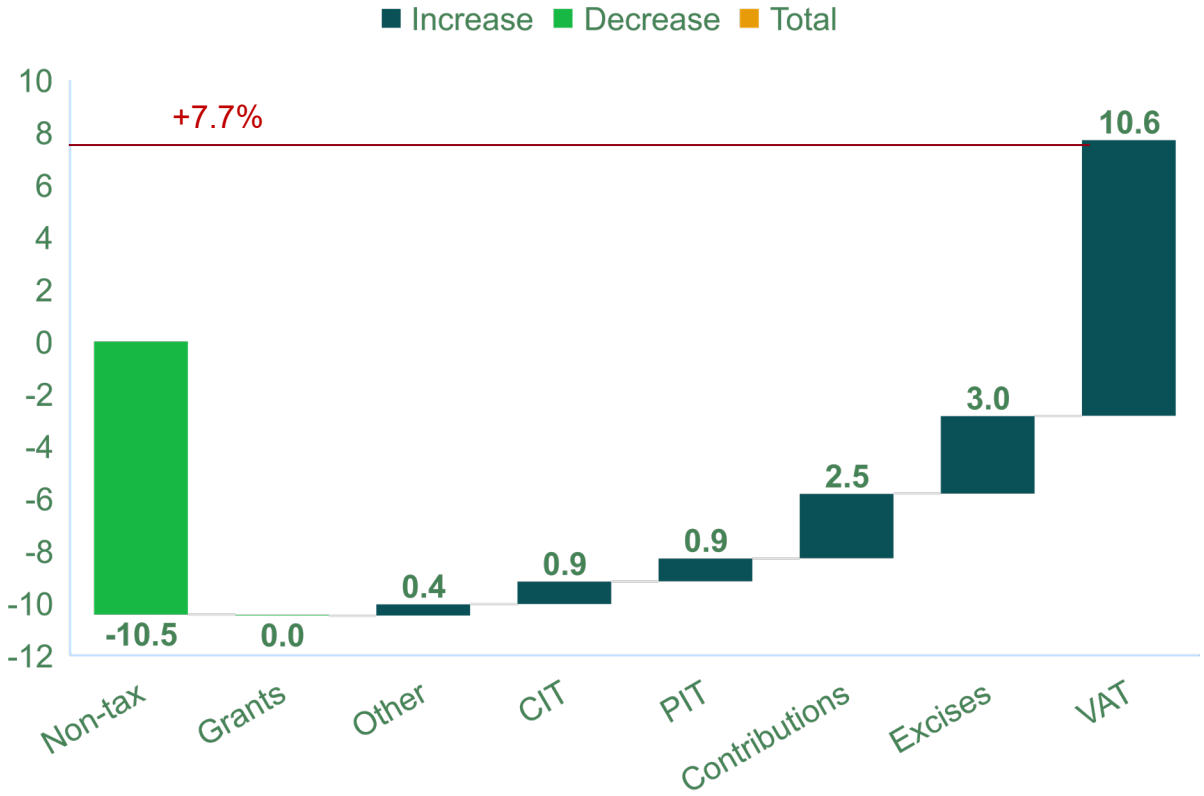
The government achieved a fiscal surplus, owing to a great extent to one-off revenues of 2.3 percent of GDP...

... but also lower capital spending, despite an increase in public sector wages and social spending.

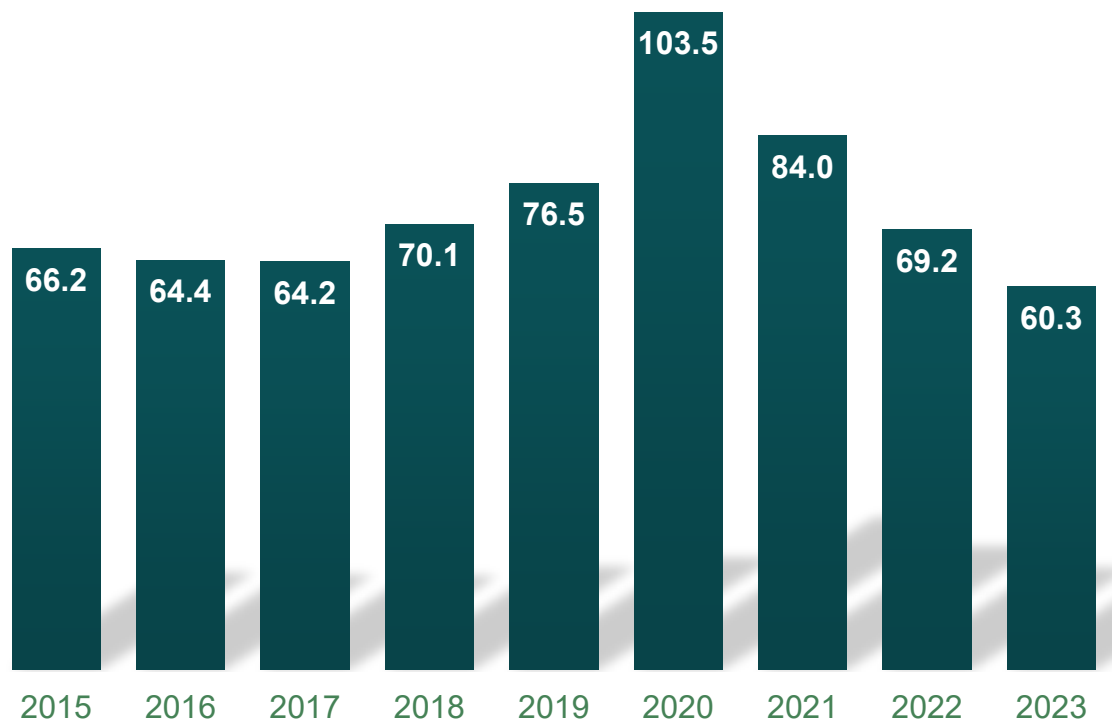*Source:* World Bank staff calculations based on data from the MOF.
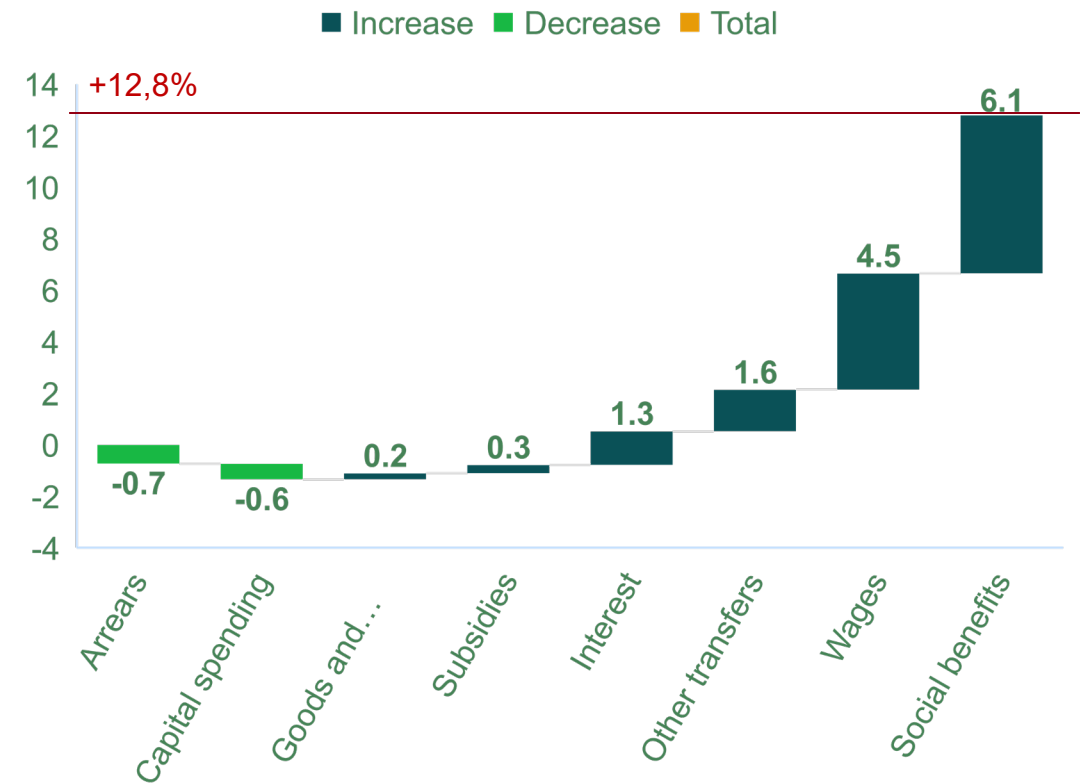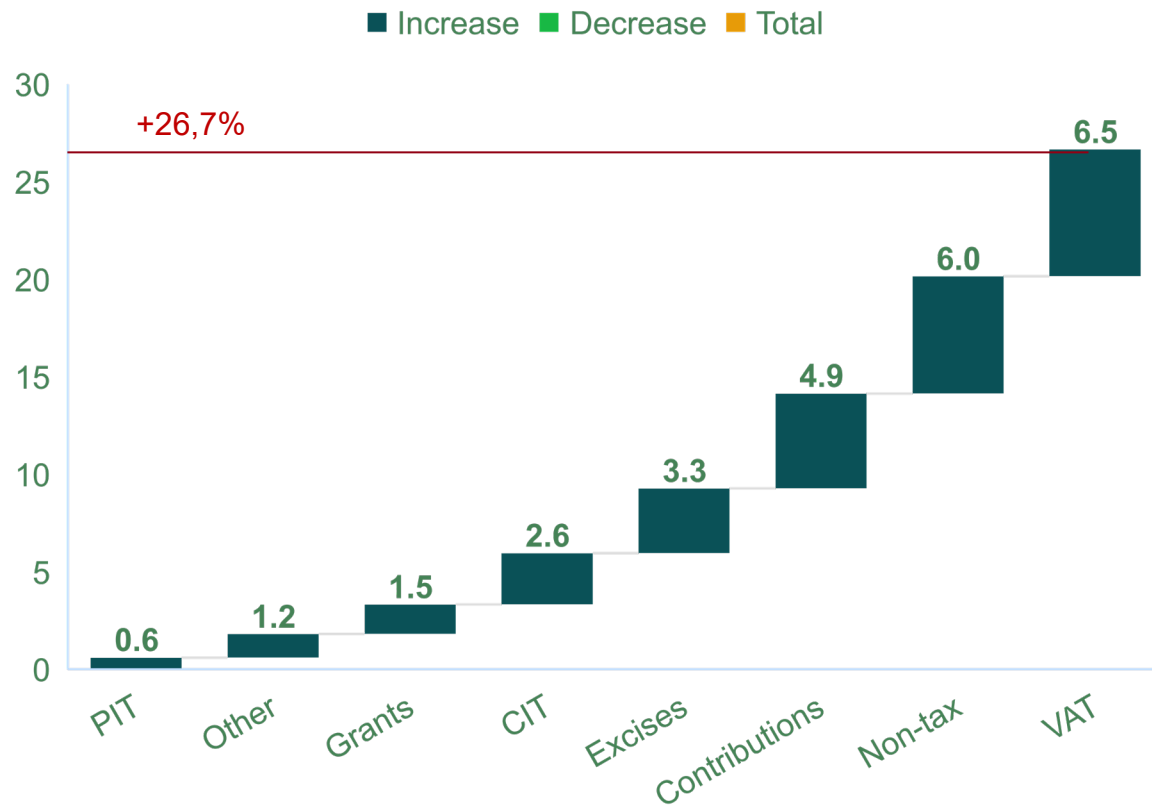
Fiscal | Good trend continued into 2024, though spending growth outpaced revenue growth

The fiscal position returned to deficit, as an increase in revenues was more than offset by higher pension spending.

Source: World Bank staff calculations based on data from the MOF.

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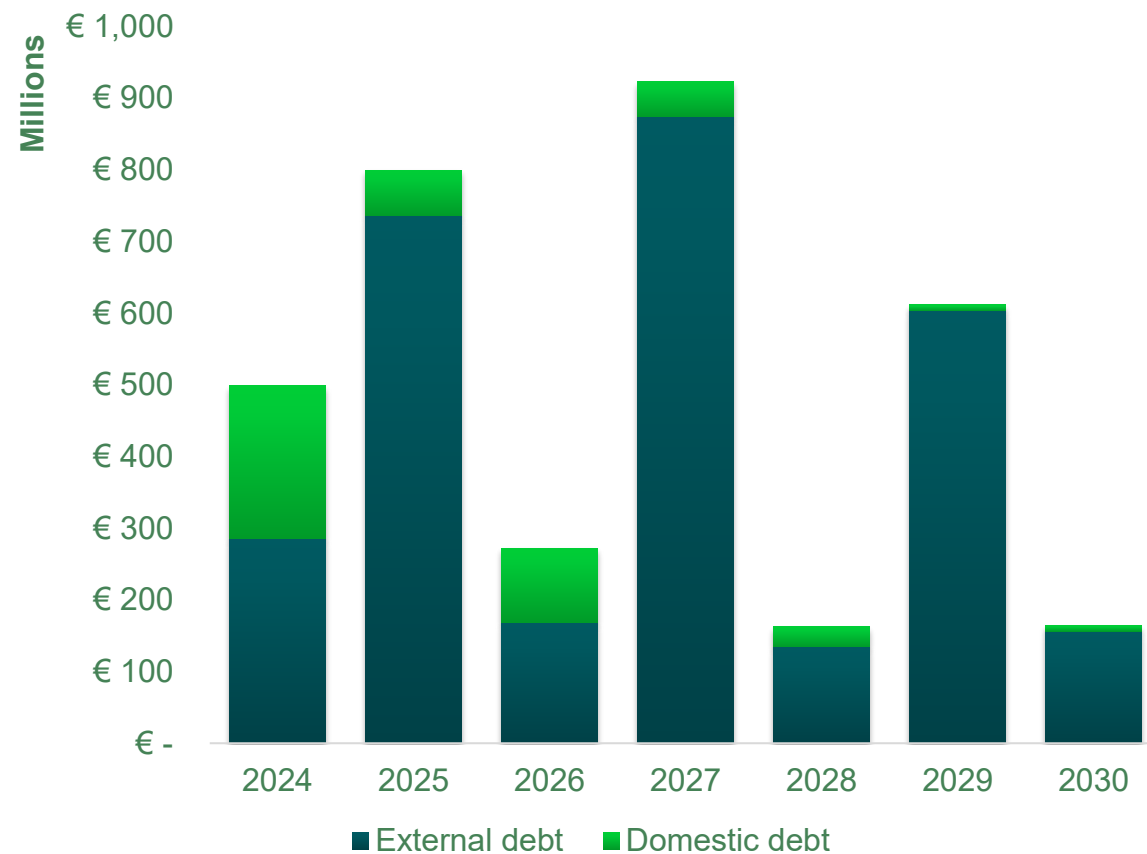# Fiscal | Public debt declined, but remains a vulnerability given debt repayments in 2025

Public debt as percent of GDP declined to its lowest since 2014, due to good fiscal performance and high inflation...

... But large repayments are approaching in 2025-27, requiring careful fiscal and debt management.

Source: World Bank staff calculations based on data from the MOF

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Fiscal | After a Eurobond placement in March, there was a slight increase in the price of the outstanding Eurobonds

— 2018 Eurobond, 3.375%, maturing in 2025
— 2019 Eurobond, 2.55%, maturing in 2029
— 2020 Eurobond, 2.875%, maturing in 2027
— 2024 Eurobond, 7.25%, maturing in 2031
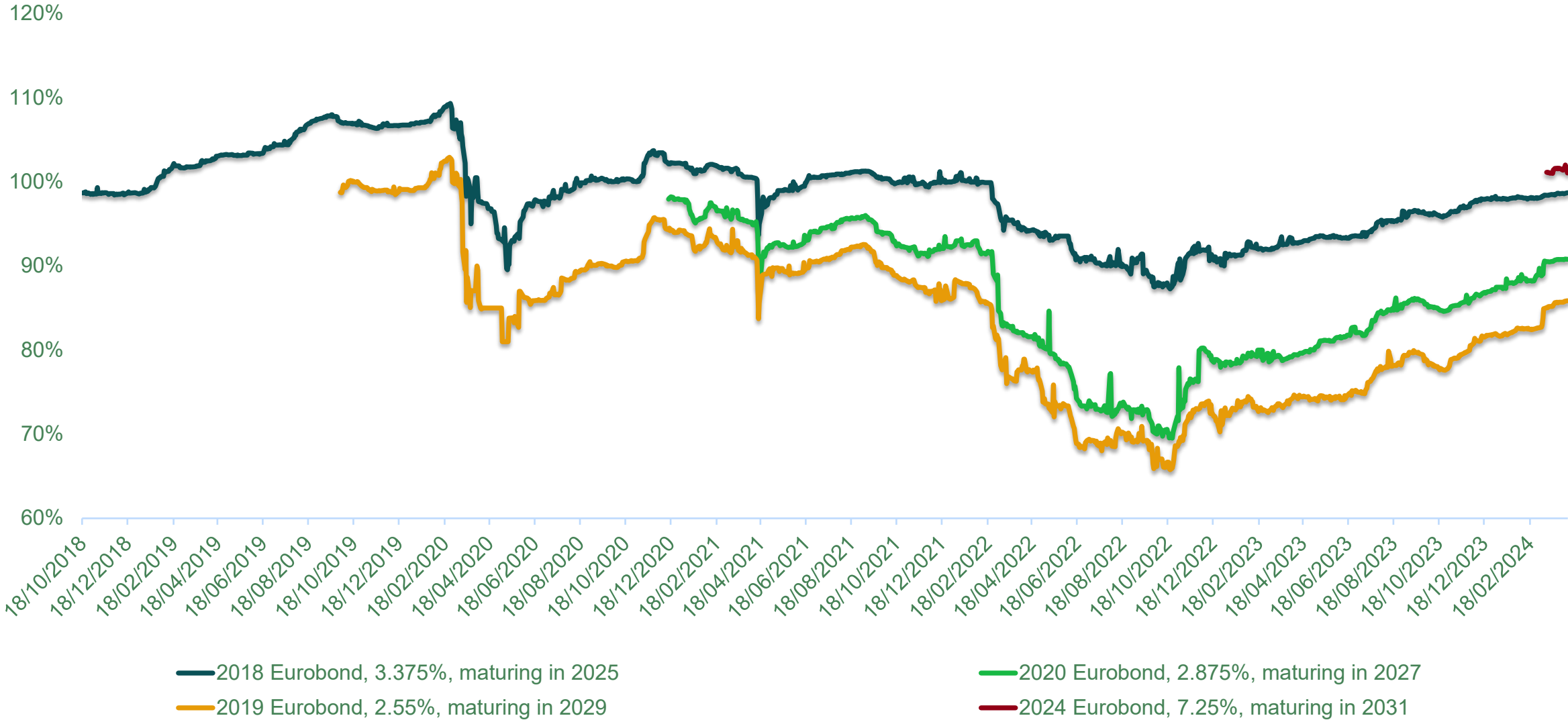
Source: World Bank staff calculations based on data from the Frankfurt Stock Exchange

Fiscal | Yields on outstanding bonds have decreased, but remain elevated amid high financing costs environment

	Coupon	Maturity	Yield in % (28 Mar 2023)	Yield in % (26 Sep 2023)	Yield in % (10 April 2024)	Spreads (basis points)
Albania	3.5	16/06/2027	6.5	5.5	4.6	213.6
	3.5	09/10/2025	6.1	5.5	4.5	112.38
Montenegro	2.785	16/12/2027	8.4	6.8	5.6	317.29
	3.375	21/04/2025	7.3	5.9	4.7	132.72
North Macedonia	6.96	13/03/2027	-	6	5.1	267.36
	2.75	18/01/2025	6.4	6	5.8	243.72
Serbia	3.125	15/05/2027	5.8	6.2	4.5	206.31
	6.25	26/05/2028	-	6.8	5.8	347.02
Bosnia & Herzegovina, Republic of Srpska	4.75	01/01/2026	7	7.1	7.4	459.02

Outlook | The outlook has improved, but *invigorating growth* is necessary to achieve faster convergence with the EU

Real GDP growth, percent				
	2022	**2023e**	**2024f**	**2025f**
ALB	4.9	🔽 3.3	🔼 3.3	🔼 3.4
BIH	4.2	🔽 1.9	🔽 2.6	🔽 3.3
KOS	4.3	🔽 3.1	🔽 3.7	🔽 3.9
MKD	2.2	🔽 1.0	⏸ 2.5	⏸ 2.9
MNE	6.4	🔼 6.0	🔼 3.4	🔽 2.8
SRB	2.5	🔼 2.5	🔼 3.5	⏸ 3.8
WB6	***3.4***	🔼 ***2.6***	🔼 ***3.2***	⏸ ***3.5***

Note: Upgrade / Downgrade / No change compared with Fall 2023

Domestic risks for Western Balkans
o Rising political uncertainty and election cycle, affecting several countries
o Further fiscal needs to mitigate cost-of-living crisis
o Increased frequency of climate-change related shocks

External risks for Western Balkans
o Further geopolitical tensions
o Further slowdown in global growth
o Further rise in financing costs
o Disruption of regional trade

➤ Acceleration of the EU accession process would provide a boost to reforms, with potential gains associated with the EU new Growth Plan and regional integration initiatives

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NEW | The RER heatmap tracks selected socio-economic indicators for the WB6 countries

Macro-financial management

		ALB	BIH	KOS	MKD	MNE	SRB
Real GDP growth	Q3 23	3.5	1.9	3.0	1.2	6.6	3.6
Inflation*	Dec 23	4.0	2.2	2.3	3.6	4.3	7.6
Employment rate	2023	57.2	41.5	35.4	45.4	55.6	50.3
Credit growth	Dec 23	5.0	7.2	12.7	5.3	6.9	1.8
NPLs*	Q3 23	5.2	4.0	2.0	2.7	5.9	3.2

Inclusive growth

		ALB	BIH	KOS	MKD	MNE	SRB
Poverty rate*	2022	23.5	-	23.4	18.3	10.3	8.5
GINI index*	latest	29.4	33.0	29.0	33.5	36.8	35.0
LFP gender gap*	2023	15.2	23.4	34.0	19.2	12.7	14.1
Unemployment rate*	2023	10.7	13.2	8.8	13.1	13.1	9.4
Youth unemployment rate*	2023	25.7	29.9	16.9	29.4	23.7	25.1

International economic integration

		ALB	BIH	KOS	MKD	MNE	SRB
Exports	2022	37.4	48.1	38.6	74.0	51.5	62.9
Imports*	2022	47.8	61.9	71.4	94.9	74.4	74.5
CAB	2022	-6.0	-4.3	-10.3	-6.1	-12.9	-6.9
FDI	2022	6.7	3.0	6.3	5.0	13.2	7.2
Remittances	2022	5.5	7.9	13.4	2.7	6.5	6.2

Sustainable growth

		ALB	BIH	KOS	MKD	MNE	SRB
Fiscal balance	2022	-3.7	0.5	-0.6	-4.4	-4.9	-3.0
Expenditures*	2022	30.5	39.7	28.4	36.5	43.4	46.4
Revenues	2022	26.8	40.2	27.9	32.1	38.6	43.4
PPG debt*	2022	65.4	31.5	20.0	59.0	70.9	55.6
Emissions*	2022	1.7	6.1	4.8	3.6	3.7	6.0

Note: Color shading: lighter - lower values, darker - higher values. For the indicators marked with *, higher values are associated with worse outcomes.

Spotlight | Cities, Growth, and Green Growth: what do we know?

What is a city? *A city is defined as a spatially contiguous, dense cluster of population grid cells in a global 1 square kilometer population grid. Each cell has a population density of at least 1,500 people per square kilometer and the aggregate population of the set is at least 50,000.*

What do we mean by "green" cities? *CO_2 emissions, $PM_{2.5}$ emissions, methane emissions, urban heat, and green cover*

What is the link between cities and growth and greening?

- *Cities are engines of growth*
- *Cities are also hotspots of a climate change*
- *Greening cities is good for climate and good for inclusive & resilient growth*

Cities in the region are small, sparse and shrinking

.....BUT capital cities continue to account for a large share of national GDP, population, labor force, jobs, and active enterprises

Climate change has increased vulnerabilities in cities

......BUT greening provides opportunities to mitigate the effects of a changing climate + it is good for growth, and for inclusion

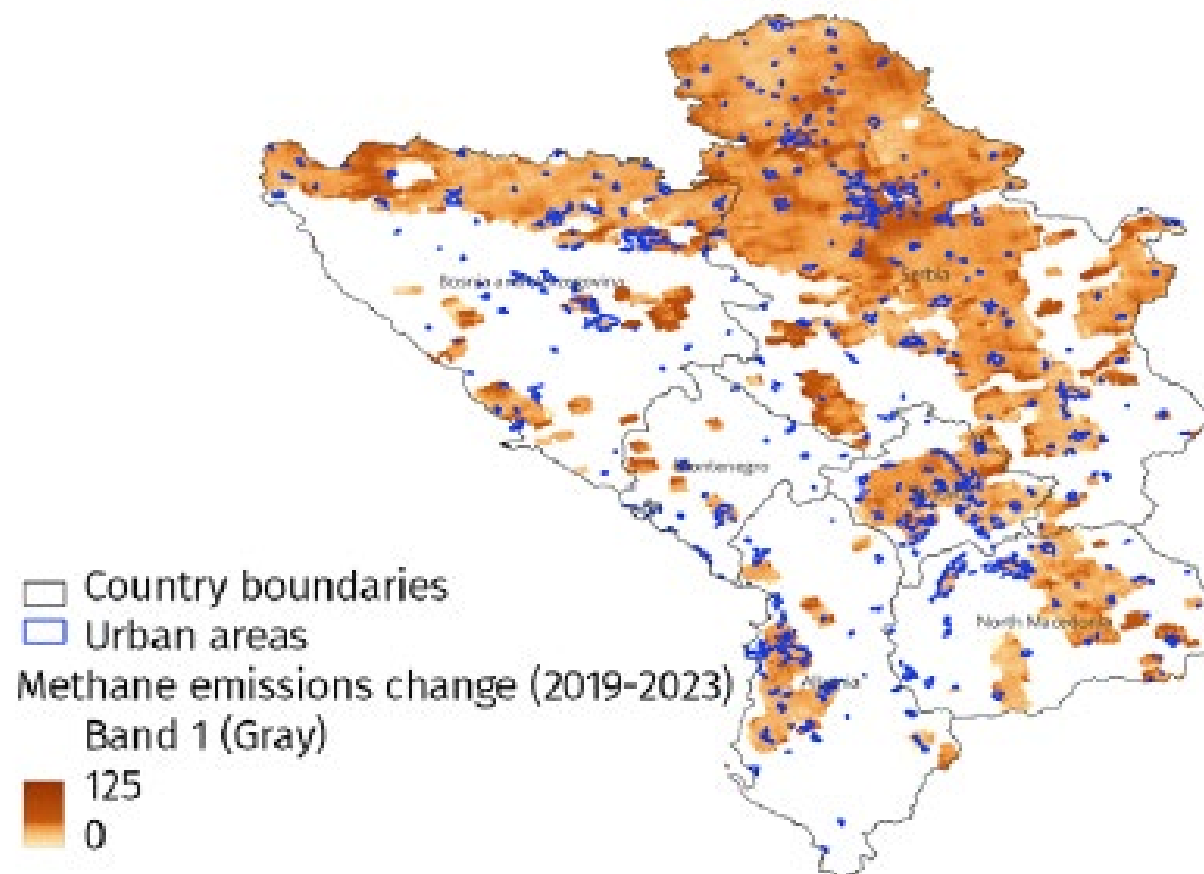# Spotlight | Cities in the Western Balkans: how green are they? (1/2)

Emissions

PM$_{2.5}$: Many cities in the region exceed safe PM2.5 levels and are amongst the most polluted in Europe

**CO$_2$:** Residential & transport sectors are important sources of CO2 emissions

Methane: Unregulated and poorly-managed landfills have resulted in fires, aggravating methane (CH4) emissions.

Methane Growth Rate (pbb/year) from 2019 to 2023

Country boundaries
Urban areas
Methane emissions change (2019-2023)
Band 1 (Gray)
125
0

Methane emissions measured as Column-averaged dry air mixing ratio of methane, as parts-per-billion from Sentinel-5 Precursor Tropospheric Monitoring Instrument (TROPOMI).
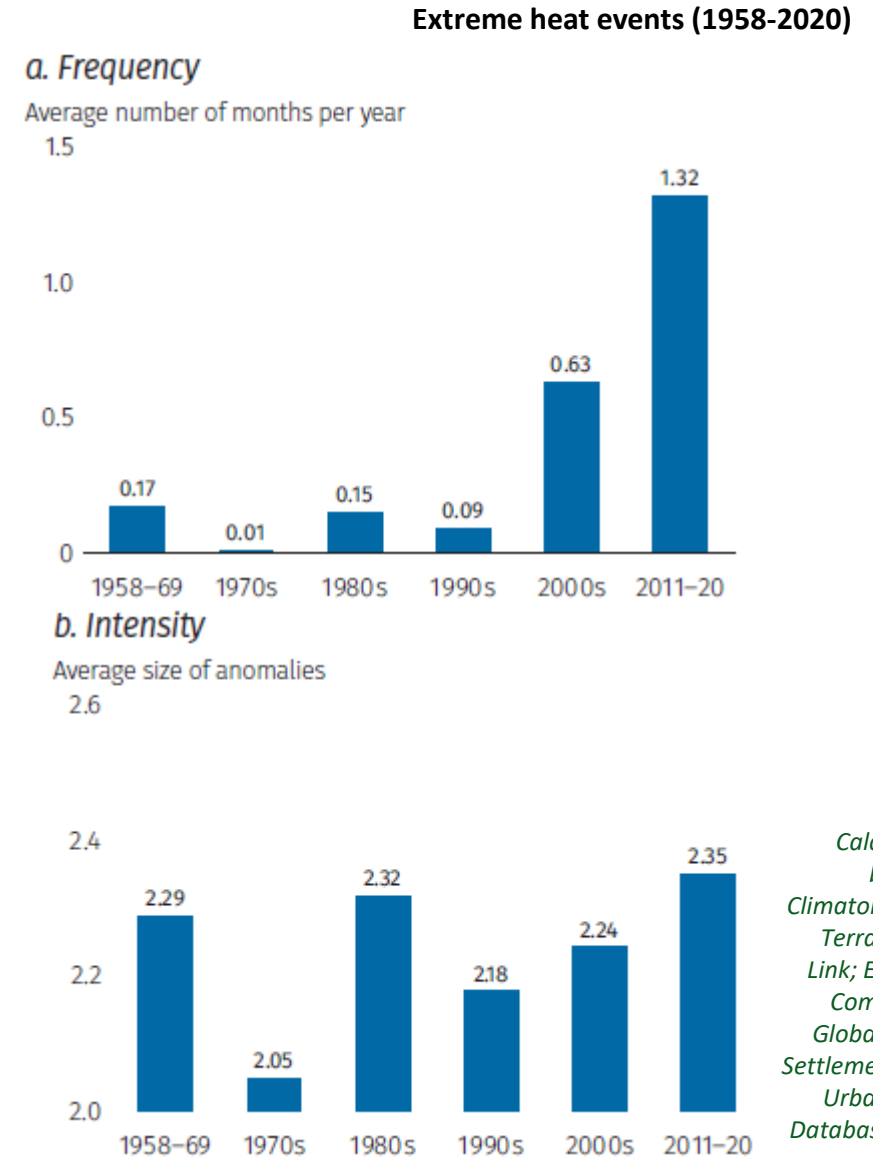
Spotlight | Cities in the Western Balkans: how green are they? (2/2)
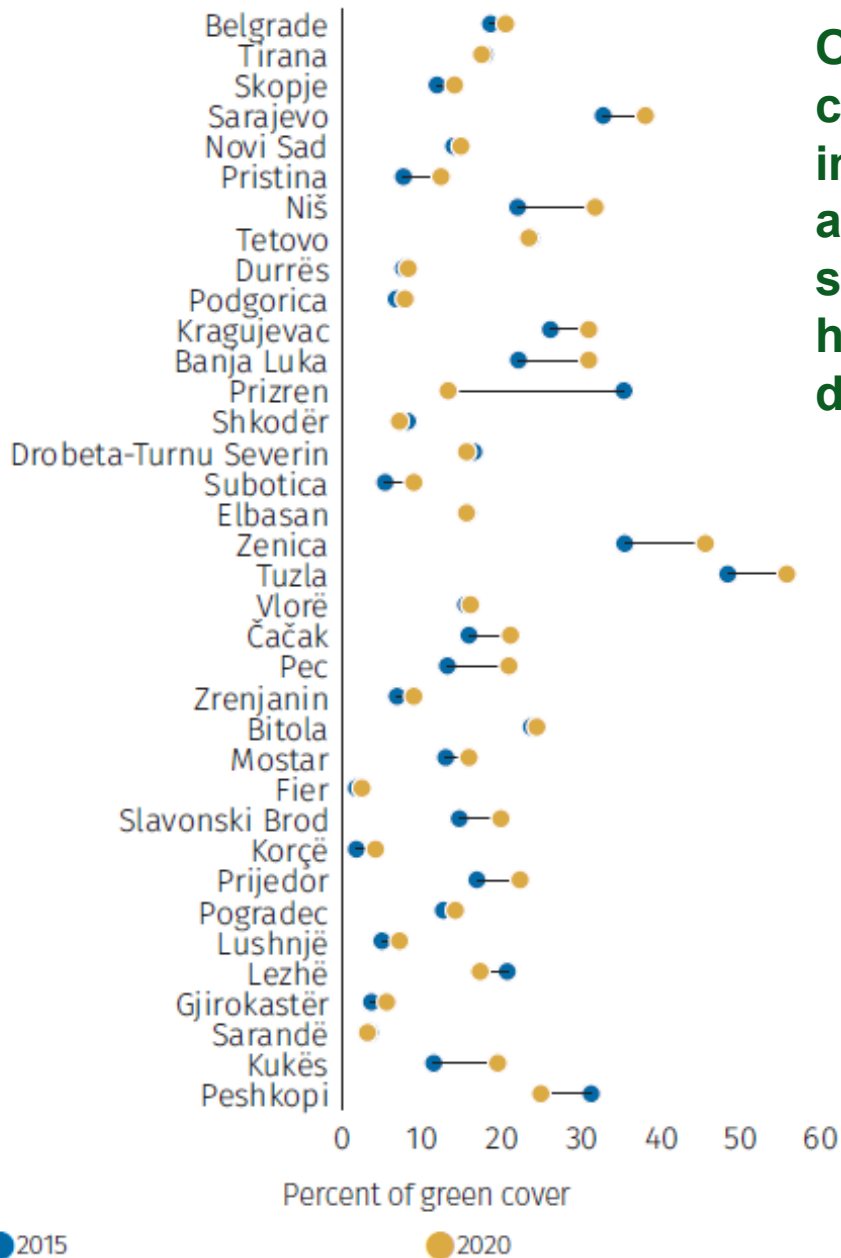
Overall, green cover has improved, although some cities have seen a decline

But cities are getting hotter, much hotter, lowering productivity, worsening health

Percent of green cover

● 2015   ● 2020

Source: World Bank analysis based on data for 36 urban clusters defined in GHS-POP R2023A - GHS population grid. European Commission, Joint Research Centre (JRC). Data on green cover obtained from Dynamic World 10m resolution land cover dataset.

Extreme heat events (1958-2020)

a. Frequency

Average number of months per year


b. Intensity

Average size of anomalies

Source: Calculations based on Climatology Lab, TerraClimate. Link; European Commission, Global Human Settlement (GHS) Urban Centre Database R2019

Spotlight | Cities in the Western Balkans: how to make them greener? (1/2)

1. Make cities more compact

Relationship between city compactness and CO2 emissions across cities in WB6, transport sectors
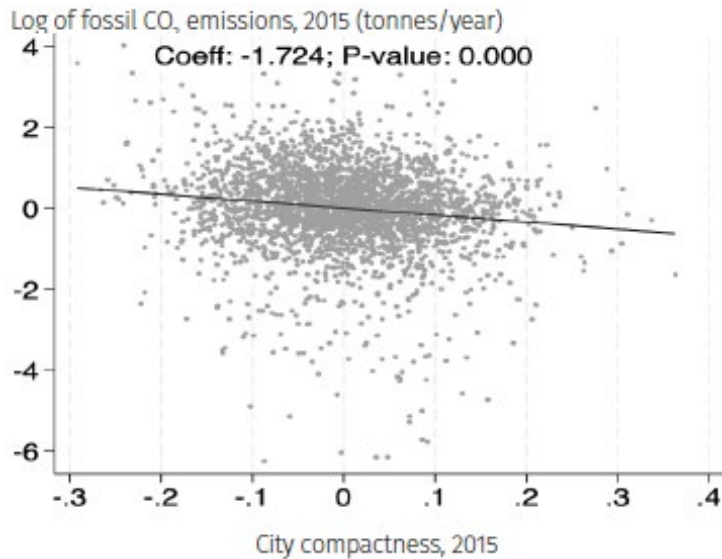

Source: World Bank analysis based on data for 39 cities from the European Commission's Global Human Settlement (GHS) Urban Centre Database R2019

Determinants of air pollution (PM2.5) for cities in the region, residential and transport sectors
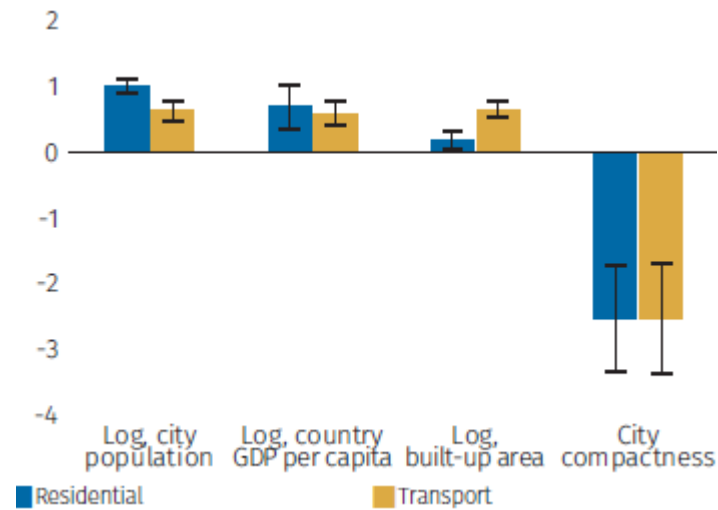
Source: World Bank analysis based on data for 39 cities from the European Commission's Global Human Settlement (GHS) Urban Centre Database R2019

Impact of a doubling of a city's total sum of tall building heights on population, land area, & NTL intensity
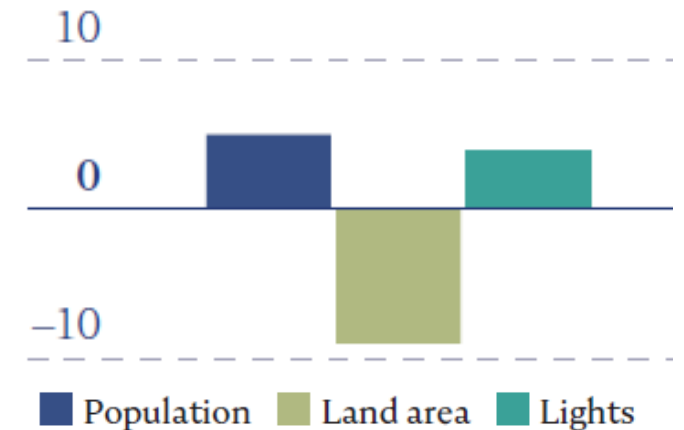
Source: World Bank based on results from Ahlfeldt and Jedwab (2022), whose data on tall buildings are based on data from Emporis.

2. Cut emissions in transport, buildings, and waste

- *through integrated smart transportation systems*
- *through standards (and retrofits) for energy-efficient and resilient buildings*
- *through regulation and improvement of urban waste management systems*

3. Tackle extreme heat in cities

- *expand urban green infrastructures (such as green roofs, green parking, and rain gardens) and green spaces (such as urban parks and gardens)*
- *implement adaptation measures to reduce the health impact, especially for those especially vulnerable*
- *information, incentives and regulation can equip cities for future heat waves*

Thank you!

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