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# MACROECONOMIC PERFORMANCE OF WB COUNTRIES - EMPIRICAL INVESTIGATION

**Abstract:** The subject of this paper is a comparative analysis of key macroeconomic indicators (Real GDP, Inflation, Unemployment rate, and Government debt) of the Western Balkans in the period 2018 – 2021. The aim is to assess their relationship and position and accordingly draw adequate conclusions and recommendations for policymakers. The research is based on a descriptive analysis of secondary data from The Global Economy database.

A comparative analysis of the selected macroeconomic indicators indicates that the COVID-19 pandemic and the global slowdown have had the least severe impact on Serbia compared to other Western Balkan countries. This resulted from the Serbian economy's achieved macroeconomic and financial stability, previous growth dynamics, built fiscal position, timely implementation of the comprehensive package of measures, and its economic structure. In the forthcoming period, it can be expected that the Western Balkan region, with the implemented structural reforms, will ensure macroeconomic stability and the creation of a favorable foreign direct investment environment, which will undoubtedly impact their further economic growth and development.

**Keywords**: macroeconomic indicators, WB countries, economic growth

**JEL Classification:** O11

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## Introduction

The beginning of the 21st century was dominated by significant events that reshaped the Western Balkan region's political and social structure. The period was characterized by political stabilization and renewal of the transition process, which resulted in economic growth and development of the region. During this period, the Western Balkan countries based their economic growth on accelerating domestic consumption (as a part of aggregate demand) and, consequently, real wages.

Nevertheless, the global financial crisis dramatically affected the Western Balkan region. Even though the crisis began in 2007, the Western Balkan countries felt the crisis's adverse effects at the end of 2008, when institutional investors started to withdraw their funds, which profoundly impacted the level of foreign currency savings. Furthermore, the global financial crisis caused a decline in imports, a balance of payments deficit, and reduced FDI inflows, which further affected the macroeconomic stability of the region. The economic recovery began in 2010. The main result was moderate economic growth in almost all Western Balkan countries.

The positive economic trends were abruptly interrupted in early 2020 by the COVID-19 influenced health and economic crisis. The COVID-19 crisis resulted in a global trade and economic activity slowdown, with health and other pandemic costs rising sharply. The emerging crisis has negatively affected most Western Balkan countries' economic growth and development. In order to prevent the adverse economic effects of the crisis, the Western Balkan economies have introduced a set of fiscal and monetary policy measures (tax policy measures, measures of direct incentives from the budget, measures to preserve liquidity, etc.). These measures aim to help maintain companies' liquidity and preserve jobs, which can significantly induce a faster exit from the economic crisis after the end of the global pandemic. After the initial shock in the second quarter of 2020 and the subsequent recession, most Western Balkan countries' economic and social support programs contributed to their slight recovery in 2021. In other words, macroeconomic stability was preserved, and new production capacities were activated, which was followed by a slight recovery of foreign direct investments. Provided that the Western Balkan countries managed to achieve macroeconomic stability before the crisis, there was room for the economic policy response to be adequate in scope and structure.

## 1. LITERATURE REVIEW

The macroeconomic policy comprises the measures and activities by which the state influences economic flows in the national economy (Vasylieva et al., 2018; Marjanović & Domazet, 2021). Consequently, countries may have different goals they want to achieve through macroeconomic policy measures and instruments (Mitchell et al., 2019). Economic efficiency is measured by macroeconomic indicators' stability (e.g. GDP growth, inflation, unemployment rate, the balance of payments, etc.). One of the main goals for each national economy and therefore economic policymakers is to maintain a general macroeconomic balance. (Marjanović & Zubović, 2020). As a consequence of the globalization and regionalization of the global economy, macroeconomic stability is becoming increasingly important in national economies' growth and development (Marjanović et al., 2022). It is essential to ensure the sustainability of macroeconomic indicators in the long run (Mügge, 2016; Tas et al., 2013). Macroeconomic balance is the fundamental economic goal of every country, and it implies the simultaneous achievement of price stability, high levels of employment, and foreign economic balance (balance of payments), with constant economic growth (Marjanović & Zubović, 2020).

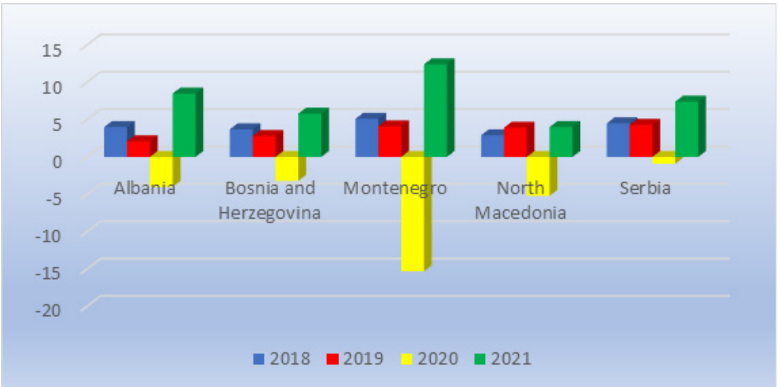
GDP represents the total market value of all goods and services that the economy produces in one year. The key figure to look at is the GDP growth rate (Feldstein, 2017). In general, deviations from normal levels should be alarming. An increase above this level is often considered unsustainable and is a generator of high inflation, while a growth rate below this level (especially negative growth) indicates slow economic growth, which can further lead to higher unemployment and reduced spending (Stock & Watson, 2016). Vladi & Hysa (2019) concluded that macroeconomic variables (inflation, interest rates, GDP, and FDI) significantly affect the unemployment rate in all Western Balkan countries. As employment has not consistently followed growth, the Western Balkans must address structural rigidities affecting the labor market and delay formalization. Over the last decade, the elasticity of employment growth relative to GDP growth has been minimal in several countries (Chakraborty et al., 2020). The decline of real GDP in the first half of 2020 resulted from the reductions in private consumption, investment and the negative contribution of net exports (Stanceva Gigov, 2020). Bodroža & Lazić (2021) concluded that the COVID-19 influenced crisis significantly slowed down the Western Balkan economies and that the intensity of this crisis was not the same in all observed countries.

## 2. RESEARCH METHODOLOGY AND RESULTS

Macroeconomic stability is a prerequisite for economic growth and integration, as it protects the economy from external shocks and helps reduce uncertainty for consumers and investors. In that way, trade, investments, and capital market development are promoted. Macroeconomic stability in the Western Balkans has been challenging to maintain, especially since 2008. After the global financial crisis, Western Balkan economies had a common need to ensure macroeconomic stability through consolidating public finances, reducing debt levels, and strengthening the quality of public spending. Accordingly, the main goal of this paper is to present the current state of the national economies of the Western Balkans in terms of key macroeconomic indicators. The paper presents a comparative analysis of the following macroeconomic indicators: Real GDP, Inflation, Unemployment rate, and Government debt. The period covered by this analysis is from 2018 to 2021. years, while the research itself is based on descriptive analysis of secondary data from databases World Bank, UNCTAD, and The Global Economy.

The outburst of the COVID-19 pandemic in 2020, accompanied by the introduction of the so-called lockdown economy, strongly affected Western Balkan economies. The region is facing a new range of economic challenges, despite a better-than-expected rebound from the recession caused by the COVID-19 pandemic. Nevertheless, GDP is expected to surpass pre-pandemic levels by the end of 2022.

**Graph 1. Real GDP (% change, y/y), 2018-2021**




*Source: Authors based on World Bank database*

Like other countries in the region, Albania's economy recovered faster than expected after the historic recession created by the COVID-19 pandemic. The strong recovery is supported by consumption, tourism, and construction. As growth rebounds, Albania has the opportunity to strengthen the sustainability of its economic model and implement reforms that further support sustainable and shared growth while preserving macroeconomic stability.

In 2021, Bosnia and Herzegovina achieved economic growth of 7.1%, primarily due to an increase in real private consumption (2.8% y/y) and real investment (2.5% y/y). Looking at the structure of economic trends in 2021, we can conclude that this GDP growth was a consequence of the simultaneous growth of both aggregate supply and aggregate demand due to improving epidemiological and economic conditions in the country and the external environment.

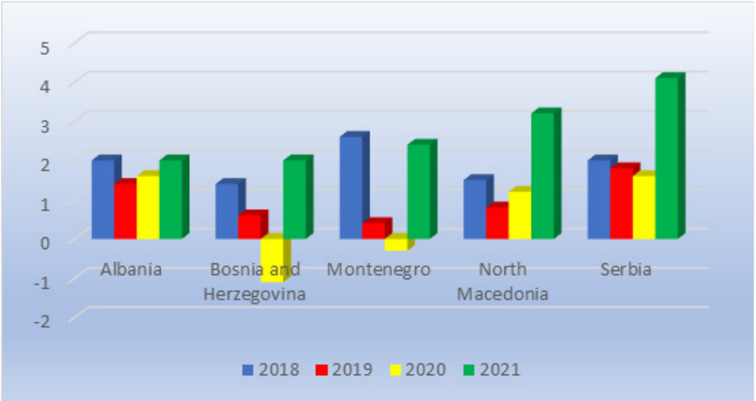
In 2021 the Montenegrin economy began to recover, where real GDP growth of 14% was achieved in the first three quarters. The GDP growth was led mainly by the growth of services exports generated through greater tourist activity, but the growth of household and government consumption.

Macedonian economy rebounded in 2021 following a 5.2 % contraction in 2020, with GDP rising by 4 % in 2021, driven by both domestic and external demand. The optimistic forecasts for an economic recovery in 2021 were replaced with a more pessimistic reality as the year unfolded. The year was marked by a slow rise in GDP, historically high public debt, and an accelerating energy crisis. Although the GDP started to recover, other economic indicators such as public debt and inflation left little room for optimism about the mid-to-long term condition of the Macedonian economy.

In 2020 economic activity in Serbia decreased by only 0.9%, which was one of Europe's best results. The worst-case scenario (5% drop in economic activity) of GDP contraction induced by the COVID-19 pandemic was avoided due to the comprehensive program of support measures for businesses and households, timely adopted and implemented by the Government of the Republic of  Serbia and the National Bank of Serbia.

In all Western Balkans countries, consumer prices have been rising gradually since 2021 on the back of higher food and energy prices. Fiscal policy has remained accommodative, and monetary policy rates are at historical lows to support the economy. However, the likelihood of tightening is increasing amid persistent inflationary pressures in the eurozone. Inflation is on the rise due to a combination of factors. More robust global growth since mid-2020 has placed upward pressure on commodity prices and shipping costs, feeding through higher imported inflation across the Western Balkans.

**Graph 2. Inflation (percent change in the CPI), 2018-2021**




*Source: Authors based on The Global Economy database*

Inflation in Albania was registered at 1.4% in 2019 and 1.6% in 2020. Strong food price increases in the first half of 2020 challenged an eight-year period of below-target (3%) inflation rates. The Bank of Albania's attempts to control inflation by continuously cutting the interest rate had little effect due to the euroization of the financial sector, low commodity prices, and below-potential economic output.

The inflation rate for consumer prices in Bosnia and Herzegovina moved over the past 15 years between -1.6% and 7.4%. In 2021, moderate inflation was recorded in Bosnia and Herzegovina. Political instability in northern Europe and the rise in energy prices through the spillover effect have caused a rise in prices in Bosnia and Herzegovina's market.

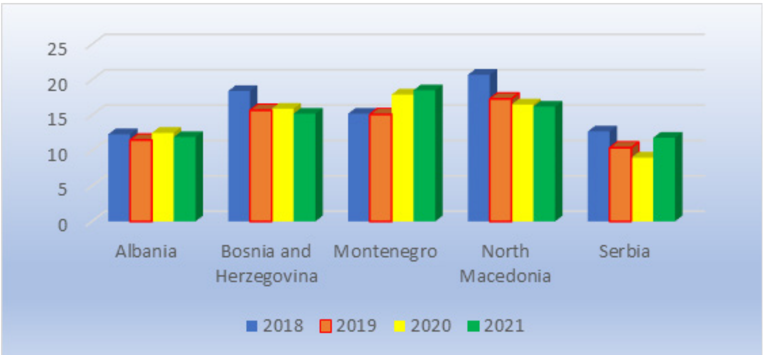
The consequences of the COVID pandemic in 2020 were considerable in Montenegro. The inflation rate has fallen from 0.4% to -0.3% by the end of 2020. The most significant price increase was recorded in the category of hotels and restaurants (4.1%). When the aspect of annual inflation in June 2021 is taken into account, we conclude that inflation measured by Consumer Prices Index amounted to 2.3%, while inflation measured by the Harmonized Index of Consumer Prices amounted to 2.8%.

The inflation rate for consumer prices in North Macedonia moved over the past 26 years between -1.3% and 126.6%. The inflation rate, measured by the CPI index, amounted to 1.2% in 2018, which is higher by 0.4 percentage points than the inflation in 2019 (0.8%). Meanwhile, inflation accelerated in 2021, reaching 3.2%, mainly due to increased energy, food, and transportation costs.

In 2021, intense inflationary pressures were recorded in the Republic of Serbia. The high inflation rate was influenced primarily by the global growth of prices of oil products, primary agricultural products, as well as disruptions in the global supply chain. In response to high inflationary pressures, the National Bank of Serbia decided to tighten monetary policy in the last quarter of 2021 by increasing the weighted average interest rate on reverse repo auctions. The most significant inflationary pressures are still on the supply side, which monetary policy cannot influence much, confirming the core inflation movement.

Prior to the COVID-19 crisis, the Western Balkans recorded record-high employment rates. However, the COVID-19 already annulled part of the previously achieved positive labor market trends: by April 2020, 40% of the increase in employment in 2019 had been lost. In this regard, all Western Balkan countries have taken action to support businesses to maintain jobs and protect employment. The region's unemployment rate fell to a historically low level of 13.4% in 2019, which is about 2.3% less than in 2018. The average unemployment rate of the younger population in Western Balkans is over 30%, which is significantly higher than the European Union average (16.9%). The loss of jobs due to the recession and its consequences has disproportionately affected women and young people, which could jeopardize efforts to increase the long-term low rates of their participation in the labor force.

**Graph 3. Unemployment, total (% of the total labor force), 2018-2021**




*Source: Authors based on World Bank database and The Global Economy database*

The economic impact of the COVID-19 led to a sharp drop in economic activity and a marked deterioration in the labor market.

Albania is one of the European countries with the highest informality of the labor market and high youth inactivity. Compared to 2020, the unemployment rate in 2021 was 11.9%, whereas 61.6% of the population was employed. The dip in employment and rise in unemployment is attributed to the COVID-19 pandemic that saw thousands of businesses go bankrupt and many employees laid off.

The unemployment rate in Bosnia and Herzegovina rose slightly in the first half of 2020 due to the COVID-19 outburst. In the third and fourth quarters of 2020, its value stabilized at around 16%. The most significant decline in employment in the second half of 2020 occurred in the processing industry, wholesale and retail trade, and transport and storage.

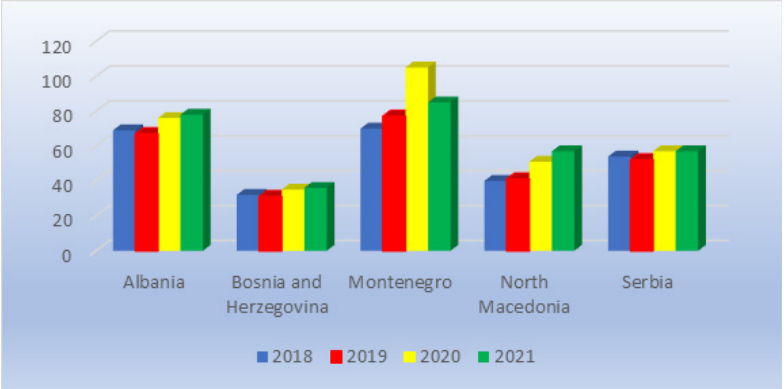
In 2021, the growth of economic activity in Montenegro had not been accompanied by favorable trends in the labor market, characterized by high unemployment rates at their highest level in the last fifteen years.

The Macedonian labor market suffers from low activity, low employment rates, high unemployment, and (vertical and horizontal) mismatch between supplied labor and demanded skills. North Macedonia's unemployment rate fell to 15.9% in the second quarter of 2021 from 16.7% in the same period a year earlier. The unemployment rate has constantly been falling in the last few years, but the pace slowed in 2020 due to the coronavirus pandemic.

Regarding the labor market's dynamics in 2021, insight into the Labor market survey in Serbia revealed an increase in the unemployment rate, which rose to 11.1%. This was expected since the health and resulting economic crisis led to a large wave of layoffs and negligible labor market pressures, which maintained instability. The situation can be expected to remain stable in the next period, primarily due to wage growth, consistent economic growth, and general economic stability.

The global financial crisis and the crisis caused by the COVID-19 pandemic led to the increase in indebtedness of almost all countries worldwide (including the Western Balkan countries). The increase in public debt in the analyzed countries was mainly due to the high costs intended for combating the pandemic and helping the economies and the population. The current European crisis caused by the Ukraine and Russia armed conflict will significantly change the structure and level of the public debt of many countries.

**Graph 4. Government debt (% of GDP), 2018-2021**




*Source: Authors based on official documents of the WB countries*

Following the 2019 earthquake, the COVID-19 pandemic, and historical spending levels, including dozens of public-private partnerships, Albanian public debt is estimated at somewhere between 78% and 86%. The government has increased the public debt by about 2 billion EUR in the last two years. Most of it was used to finance disaster-related projects.

Bosnia and Herzegovina is forced to borrow as a transition country facing a lack of domestic investment accumulation. It is essential to outline that the public debt of Bosnia and Herzegovina (debt-to-GDP ratio amounts to approximately 40%) is within the Maastricht criteria, meaning that it does not belong to a group of heavily indebted countries but a group of medium-indebted ones.

Montenegro's public debt at the end of 2020 amounted to as much as 105% of GDP. The current crisis caused by the coronavirus significantly contributed to this situation. However, due to China's participation in major energy and infrastructure projects, special attention needs to be paid to Montenegro's debt. At the end of 2021, compared to the same period previous year, Montenegrin public debt was significantly reduced, both in absolute terms and in the debt-to-GDP ratio.

The public debt of North Macedonia is growing gradually as the current spending increases due to rising wages, pensions, and subsidies in relation to moderate revenue growth. The public debt and the debt guaranteed by the state increased in 2020 because the government had to increase borrowing to finance the growing deficit and repay the due obligations.

The crisis also affected Serbian public debt, which was 26.7 billion EUR in 2020, and 30.1 billion EUR (57% of GDP) in 2021. Efficient public debt servicing is substantial for Serbia, as well as implementing methods that imply more efficient use of foreign funds, reduction of interest rates, or significant retained foreign earnings.

## Conclusion

All Western Balkan countries need to try to maintain general macroeconomic stability. Therefore, it is important to consider all trends and react to their movements according to the situation. Properly conducted macroeconomic policy significantly contributes to the growth and development of the region. That is why it is important to ensure economic stability in each of these countries and thus enable economic growth. GDP growth in the Western Balkans reached 7.4% in 2021, after falling by 3.2% in 2020. The main driver of growth was an extremely strong recovery in spending, fueled by fiscal stimulus, increased demand, and easing restrictions on movement and travel. However, the post-pandemic recovery was interrupted by the war in Ukraine, the consequences being felt throughout the region. According to current projections, in 2022, the growth rate in the Western Balkans will be around 3.1%. Despite a strong recovery from the pandemic, the Western Balkans are now facing new challenges further aggravated by the war in Ukraine, including rising energy and food prices, high inflation, and a slowdown in trade and investment. The Western Balkans countries will need strong support in the form of public policies that will enable them to find a way out of this crisis and protect the significant results achieved in 2021, including those in the field of poverty reduction.

Policy needs to focus on building resilience and undertaking structural reforms to support growth and steer through the crises. With limited fiscal space, countries will need to carefully weigh the costs and benefits of new spending commitments in response to higher energy and food prices, prioritizing vulnerable households. Structural measures to reduce business regulatory costs, increase market competition, support labor market participation, and strengthen public institutions' independence would all support growth in an uncertain environment.

Serious negative risks threaten the economic prospects of the region. The spread of the conflict or the protracted war in Ukraine could further complicate global trade and raise energy and food prices. Refinancing risks may arise if the trend of unfavourable conditions in foreign financial markets continues. The sustainability of public debt can be a cause for concern if the already limited fiscal space is further narrowed due to the response of public policies to higher energy and food prices with increased refinancing costs.

In the following years, it will be crucial to create conditions for macroeconomic stability and economic growth in the region through adequate economic policy and accelerated structural reforms. This would increase investment, exports, savings, and productivity and strengthen competitiveness while, on the other hand, reducing macroeconomic imbalances, especially the fiscal deficit, inflation, and the current account deficit. Effective fiscal policy should be aimed at implementing measures that will slow down debt growth and reduce the fiscal deficit. With a shared vision that will ensure macroeconomic stability, and provided they implement decisive reforms, the Western Balkans countries can ensure accelerated economic growth and an increase in the living standards of the population. That way, economic integrations would be accelerated, and the advantages of the new global economy would be used.

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