Developments in Kosovo’s economy analysed on a macroeconomic point of view

Myrvete Badivuku-Pantina, Skender Ahmeti, Arbër Reçi

Abstract

Despite that in the last years, Kosovo has experienced economic growth, it still remains the least developed country in Europe. Kosovo’s economy is still fragile. During 2009 Kosovo’s economy peaked at 4.0% while during 2010, economic growth achieved 4.6%, while the GDP was estimated to be 4.2 Billion Euros. During 2009, Kosovo’s economy was characterised by deflation (-2.4%), during 2010 it saw a raise in inflation, while consumer price index was rated at 3.5%. There is still a high rate of unemployment in the labour market, about 45%, and it remains a challenge for the country’s economy. During 2009, money deposited from Kosovars living abroad experienced a decline of 5.6%, where during 2010 these deposits marked a slight improvement. Trading imbalances since the post-war period have continued in 2010, which has created a high level of dependence of commercial deficit (deficit constitutes about 45% of the GDP). The purpose of this study is to give a clear view of the macroeconomic situation of Kosovo through a comprehensive analysis and critical approach towards developments so far, in order to improve the economic state in the future.

Key terms: Economy, Kosovo, indicators, macroeconomic.
Introduction

Kosovo is relatively endowed in natural resources like: lignite, nickel and other metals. However, for their long-term and efficient exploitation, we need to resolve the issue of privatization and property, finance, technical and technological issues in order to attract the needed investments. Stabilization and development of the energy sector is of critical importance for attracting foreign investors, to support the new industry of Kosovo, in a time where global economy is facing serious problems. The huge number of unemployed and the rate of poverty are the more serious problems in Kosovo. Even though incomes per capita have improved, the material standing of Kosovo residents remains low. Official estimation of unemployment range around 45% and hundreds and thousand youngsters (included those with university degrees) enter the labour market. Poverty, especially extreme poverty, has marked an increase in the last years, which is very disturbing. This is a serious problem, that should be addressed by the Government of Kosovo, who should seek an urgent solution, within development policies.

Informal economy is a serious issue in Kosovo and measuring its extent is a real challenge. The informal sector in Kosovo (similar to countries in the region) is estimated around 30-40% of the country’s GDP and is present everywhere: agriculture, construction, small businesses, commerce, production, services etc. informal economy is an occurrence that has penetrated considerably in the labour market. A large portion of the employment is done through informal agreements, work legislation is overlooked and social security obligations are not met. It is estimated that around ¼ of the population and 30% of the active work force have emigrated out of Kosovo. For many years money sent from emigration has been an important source of budget for many Kosovo families. This kind of money had an important impact in the economic life of the country. For many years investments from abroad where key to the recovery from destruction brought by war, in the repairment and construction of new houses, supplying of furniture etc. Some researches that have been done after the war, show that on average, every third family has a member who has emigrated abroad. Mor than 70% of these families receive shipments from the emigrated members of the families. During 1999-2008, these shipments constituted aorun 17% of the country’s GDP.
2. Gross domestic product

Due to lack of complete statistic data, it is not easy to make a comprehensive assessment of the overall economic condition in Kosovo. The economic activity which is totally dependent on the private sector is insufficient to the growing needs of the public sector and domestic consumption. According to IMF, GDP per capita during 2007 was 1,600 € which is around 5.5% of the average of EU-27. The unstable power supply, with frequent interruption, remains the most limiting factor to economic growth in Kosovo. Despite the global financial crisis, Kosovo’s economy during 2008 marked a real growth of the GDP of 5.4% and during 2009 an increase of 3.9% (IMF assessment), which represents a deceleration of economic activity compared to 2008. Kosovo’s financial sector showed a satisfactory stability, which is something we can not say about the commercial developments in Kosovo. The negative trends of the post-war period have continued in 2008, 2009, 2010, which has created a high level of dependence in the economy of Kosovo. Commercial deficit in imports is accompanied with a high lever of commercial deficit (around 45% of the GDP).

The situation in the labour market is still difficult, where a high rate of unemployment is prevailing with over 40%, which is a challenge to the economy. In the following chart are given the main macroeconomic indicators in Kosovo for the years 2006-2010.

**Chart 1: Main macroeconomic indicators in Kosovo 2006-2010 (million €)**

<table>
<thead>
<tr>
<th>Description</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gross Domestic Product (GDP) – Millions euro(^1)</td>
<td>3,120</td>
<td>3,400</td>
<td>3,757</td>
<td>3,917</td>
<td>4,119</td>
</tr>
<tr>
<td>GDP %</td>
<td>4.0%</td>
<td>5.0%</td>
<td>5.4%</td>
<td>4.0%</td>
<td>4.6%</td>
</tr>
<tr>
<td>Inflation (IÇK)</td>
<td>0.6%</td>
<td>4.5%</td>
<td>9.2%</td>
<td>-2.4%</td>
<td>3.5%</td>
</tr>
<tr>
<td>Unemployment</td>
<td>44.9%</td>
<td>43.6%</td>
<td>47.5%</td>
<td>45.4%</td>
<td>45.0%</td>
</tr>
<tr>
<td>Remittances (in millions euro)</td>
<td>-</td>
<td>515.6</td>
<td>535.4</td>
<td>505.6</td>
<td>511.6</td>
</tr>
<tr>
<td>Gross Domestic Product per capita (euro)(^2)</td>
<td>1,486</td>
<td>1,593</td>
<td>1,789</td>
<td>1,795</td>
<td>-</td>
</tr>
</tbody>
</table>

Source: CBK, Annual Report 2010

\(^1\) Departament of Macroeconomy – MEF
\(^2\) Enti i Statistikes se Kosoves (Statistical Office of Kosovo), Bruto prodhimi vendor ne Kosove 2004-2009
Financial crisis in Kosovo is reflected more through the decrease of shipments from emigrants and direct foreign investments. Also, loans are harder to get from the commercial banks in Kosovo. Kosovo’s economy during 2008-2009 continued to be dominated largely by consumption and private sector investment, that constitute around 80% of the overall consumption and investments. Annual rate of private consumption growth in 2008 was 15.1% in comparison to 11.4% in the prior year, while private sector investments increased only by 3.6% in comparison to the 21.7% of 2007. This came from the decrease of foreign investments and the stagnation of the privatization process.

During 2009 Kosovo’s economy marked a real growth of GDP of 4%, while during 2010 the marked growth was 4.6%, while the GDP reached 4.2 billion euro. Economic growth during these years was largely generated by the growth of private consumption and public investments, which were largely financed with loans for the banking sector, emigrant shipments, considerable increase of public expenditure and external assistance. It is noteworthy that the economic growth of 2010 was a result of the private sector contribution, respectively the consumption and investment of this sector, in contrast to 2009 where the slow contributor of economic growth was the public sector. The year 2010 is characterized with the increase of general consumption of 3.3% (0.9% in 2009), while being influenced by the increase of the private and public sector. Investments also marked an increase during 2010, which was 7.8%, but this increase was lower than 2009 (9.8%). From 2006 to 2010 the GDP values has increased about 1 billion euro, where the average increase of GDP during these years has been 4-5%.

While during 2009 Kosovo’s economy was characterized by deflation (-2.4%), during 2010 it marked an increase of inflation, where consumer price index achieved 3.5%. The high level of dependence to imports influences the shifting of prices in Kosovo, therefore the global inflationary pressures have affected Kosovo so there was an increase of inflation (increase of grocery and oil derivative prices).

3. Unemployment in Kosovo

Unemployment in Kosovo presents the greatest challenge for the Government in Kosovo. The problem of unemployment is not only a social problem, but also an economic, psychologic and a problem of survival of a large number of Kosovar families. With the actual rate of growth, Kosovo’s economy cannot absorb the actual and potential army of unemployed, that every year reach labour age (around 29,000), thus the growing working force.
Anyway, partially due to the large size of informal economy, changes in the charted unemployment may not express correctly the factual dynamic of economy. In general, the registered unemployment is still very high, the high rate of 45% keeps dominating. Based on the data from the Ministry of Labour and Social Welfare, from 2004-2010, an average of 30,000 persons a year have been registered as new job-seekers, while the number of new job positions per year is approximately 7,500. It is estimated that approx. 80% of the employed in Kosovo are employed in the private sector, while in the public sector, which is considered an important employer, there are 20% of the general number of employed in the country (MPMS).

With the growing number of job-seekers, the largest portion of the unemployed in Kosovo are categorized as long-term unemployed, which testifies for a limited capacity and dynamic of Kosovo’s economy for generating new job positions. The general number of job-seekers registered in December 2008 was 335,942, which marks an increase of 0.4% in comparison to the same period a year ago. Unqualified unemployed compose the largest part of the new records. In terms of age groups, youngsters of 15-24 years are the largest part of the unemployed. In terms of gender, women compose around 47% of the general number of job-seekers.

Categorization of unemployment according to economy sectors shows that around 23.4 percent of the job-seekers were previously employed in industry, followed by commerce with 16.8% and construction with 11%. As for employment, the main employer remains the private sector who in 2008 absorbed around 59% of the new employments. The service sector opened around 64% of the new job positions offered by the private sector, while the production sector offered only 19%. Regarding wages in the labour market of Kosovo, according to ESK, the average monthly wage in 2008 was around 248 euro, which is an increase of 2.5% in comparison to the prior year. Higher wages are still offered by the private sector (258 euro) in comparison with the public sector (237), despite the increase of wages for 10% for public administration and 35% for education sector in the end of 2008.

4. Commerce development in Kosovo

Ratio between imports and exports are distinctly inconsistent, which more than proves, how low the production and competing capacity of the country’s economy is. A small increase of the covering of imports by exports of 8.5% in 2006 and 10.9% in July 2008 is a positive indicator, but in these reports it is not of significance, since the commercial deficit was further extended to 41% of the GDP in 2007, in comparison to the 37% in 2006, only to continue with this unwanted trend through 2008 and 2009.
In 2008, merchandise export was increased for about 60% and imports for 25% in comparison with 2007, bringing commercial deficit (merchandise only) to about 42% of the GDP. The negative trends in commercial trade from the post-war period have continued in 2010 as well, which is accountable for Kosovo’s high dependency to imports, which has resulted in a high level of commercial deficit (deficit composes about 45% of the GDP), while exports remain too low and cover only a small part of imports (about 13.7% in 2010 in comparison to 8.5 in 2009).

Even though in 2010 Kosovo’s economy marked an increase of exports, imports increased as well for 10.8% in comparison to 2009 and have reached the amount of 2.1 billion euros, which accounted for the increase of commercial deficit for 9.4% (CBK). Ratios between exports and imports, which are distinctly inconsistent show best how low the production and competing capacity of the economy is. It should be mentioned that in 2010, the rise of import amount was affected by the increase of oil products prices in the global market, while it should be taken to account that mineral products are one of the main categories of imports in the country. Kosovo’s exports in 2009 were characterized by a notable decrease, which may be partly due to the global crisis, while in 2010, after the recovery of the global economy, it came to an increase of demand in the global market. Since about 90% of metals exported from Kosovo are nickel ore, this resulted in an increase of Kosovo’s exports for 77.8%, achieving the amount of 294 million euros.

<table>
<thead>
<tr>
<th>Description</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
</tr>
</thead>
<tbody>
<tr>
<td>Exports</td>
<td>165.1</td>
<td>198.5</td>
<td>165.3</td>
<td>294.0</td>
</tr>
<tr>
<td>Imports</td>
<td>1,576.2</td>
<td>1,928.2</td>
<td>1,935.5</td>
<td>2,144.9</td>
</tr>
<tr>
<td>Commercial balance</td>
<td>-1,411.0</td>
<td>-1,927.7</td>
<td>-1,770.2</td>
<td>-1,850.9</td>
</tr>
<tr>
<td>Export/import ratio (%)</td>
<td>10.5</td>
<td>1.03</td>
<td>8.5</td>
<td>13.7</td>
</tr>
<tr>
<td>Commercial opening (% of the GDP)</td>
<td>51.0</td>
<td>55.3</td>
<td>54.3</td>
<td>59.3</td>
</tr>
</tbody>
</table>

Source: CBK (2011)

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Central Bank of Kosovo, Annual Report 2010, Prishtinë
Kosovo’s economy remains open to the outside world in regards to commercial trade, resulting that the level of commercial opening achieved 59.3% of the GDP, in comparison with 54.3% of 2009. Unfortunately this opening of kosovar economy is only unilateral, which means it is based on imports.

The structure of imports in 2010 remains similar to previous years, where the highest participation remain mineral products that mainly include fuels (19.6% of the total imports), grocery products, machinery, basic metals, means of transport etc.

The structure of exports in 2010 was dominated by basic metals and mineral products which compose 63% and 13.2% of the total exports. The third category of importance in total exports is grocery products.

The structure of Kosovo’s commercial partners remain unchanged. In regards to imports, in 2010, the EU and CEFTA countries remain the main commercial partners for Kosovo. In 2010, 38% of the imported merchandise came from the EU (Germany 12.8%, Greece 4.7%), while 37% came from CEFTA (Macedonia 14.7% and Serbia 12.1%). (CBK, 2011).

In 2009 commercial exchange with regional countries (members of CEFTA) had the value of over 745 million euros. From this amount, the import value was 692 million euros or 35.7 of the general import amount. This indicator shows a decrease of imports in these countries for 3.5% in comparison to 2008. Exports designated towards CEFTA member countries reached the amount of 53 million euros or 32.3% of the total exports amount, which shows negative performance since it is 13% lower than 2008. As main exporting destination was Albania, covering 49% of exports in comparison to other countries, members of CEFTA, and 16% participation general exports. Imports from Albania were lower in comparison to some countries in the region, from where 8% of the general CEFTA imports were covered and 3% participation in total imports.

In terms of the structure of commercial trade, it remains the same as in previous years. In 2009, Albania exported products like: scrap iron, cement, agricultural/grocery products, beverages and other products. While it has imported products such as iron and steel products, oil derivatives, furniture and it has exchanged electric power.

Macedonia in 2009 remains an important partner of Kosovo in regards of import and export, a country which has covered 42% of the general imports and 32% of the general exports in the level of CEFTA member countries (11% in covering of export, 15% in covering the general import of Kosovo). Oil and oil derivatives were the main products imported from Macedonia. Furthermore, from Macedonia were imported products of metal basis, grocery products, beverages, electronic devices and other products.
Kosovo’s trade with Serbia during 2009 was characterized by an increase of imports and a decrease of exports in comparison to 2008. Exports of Kosovo to Serbia marked a decrease of 64% in comparison to 2008, composing 2% of the general exports of Kosovo. This decrease of exports was a result of Kosovo products from Serbia, since December 2008. On the other hand, Serb imports covered 11% of the general imports of Kosovo. Main products imported from Serbia were construction materials, cereals, beverages and other grocery products.\(^4\)

During 2010 exports of Kosovo to EU countries marked a higher increase in comparison to the region. This came as a result of the non-implementation of the CEFTA agreement, on political grounds, by Serbia and Bosnia and Herzegovina. Thus the amount of exports of Kosovo to the EU during 2010 increased for 84.4%, or 44.7% of the amount of total exports of Kosovo, while the main partner for exports was Italy (27.3%), then Germany, Austria and Slovenia. The participation of Kosovo exports in the CEFTA countries was decreased for 32.4% (2009) and 24% (2010). Most of the exports are realized by Albania (11%) and Macedonia (9%). Despite the obstacles put by Serbia and Bosnia Herzegovina, exports in these two countries have marked a slight increase during 2010, where exports in Bosnia reached the amount of 1.9 million euros (1.2 million euros, 2009) and Serbia the amount of 3.8 million euros (3.5 million euros, 2009).\(^5\) (CBK, 2011)

From the balance sheet of Kosovo it was seen that Kosovo deals with a continuous problem, which is the deficit balance sheet. This implies that Kosovo is dependant of imports, while its possibilities to place local products in the global market are very low. Kosovo joined Cefta in a time where it dealt with a high commercial deficit and an undeveloped economy, so the membership was seen as a way out of this crisis, expecting that integration in a free market, the investors would invest in Kosovo and local manufacturer would export more easily. But during these years that Kosovo was a member of CEFTA, the expectations did not come true. Kosovo was even disadvantaged by CEFTA due to the low level of economic development. And if we base ourselves in the principle that if the countries that engage in an agreement such as CEFTA, should have a similar economic development to the other countries in this agreement, then Kosovo’s involvement in this integration will be a contradiction on this theory.

In order for Kosovo to have good relations with the CEFTA countries, besides the effect of the political factor, and to have the needed effect of economic

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\(^4\) MTI, Shkëmbimet Tregtare të Kosovës, 2009

\(^5\) Banka Qendrore e Kosovës, Raporti Vjetor 2010, Prishtinë
processes, we need schooling and education of younger generations and in the same time professional training through permanent trainings for those that are involved in these processes.

On the other hand, it is a duty of the businesses to strive the modernization and betterment of their activities, by opening to new technologies, improving management systems, by expanding their vision towards the regional and European market, and by focusing more on the quality of their products.

5. Direct Foreign Investments (DFI)

In terms of direct foreign investments (DFI) during the last years Kosovo reached the highest level of DFI in 2007 with 440 million euros, while experiencing a slight decrease in 2008 and 2009, as a result of other internal factors, and as a result of the global financial crisis. During 2009 a decrease of DFI of 20% was marked, but in the year 2010 Kosovo experienced an increase of DFI, achieving 311.2 million euros. But in the first trimester of 2011, the DFI decreased again in comparison to the same period in 2010, and if we base ourselves in the data of the World Bank from the report “Doing Business 2011” according to which in the research were included 183 countries of the world, and in ten included fields for research for evaluation of the business environment in these countries, Kosovo marked a deterioration in matters of building the business environment, since it fell from the 118\textsuperscript{th} place it held in 2010 to the 119\textsuperscript{th}, and in some fields it did even worse, in regards to ensuring construction permits and protection of investors in ranked 173, while in matters of contract implementation it ranked 130\textsuperscript{th}.

Figure 1: Direct foreign investments in Kosovo 2005-2010 (mil. EURO)

Source: IMF (2011) and CBK (2011)
From the following table we can see that most of the regional countries during 2010 have marked a decrease of foreign investments (B.and H., Croatia, Montenegro, Serbia), while Albania and Macedonia have marked an increase of the DFI, so if we wish the investors to not overlook Kosovo or relocate to the neighbour countries (Macedonia, Albania), the needed changes in legislation should be done, especially some of the laws that have direct impact on the establishment of business environment, such as economic laws, the law on cadastre or property registration, to ensure facilitation of procedures and lowering the cost for business registration.

Chart 3 : Foreign investments in regional countries 2005-2010, (mil. dollars)

<table>
<thead>
<tr>
<th>Countries</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
</tr>
</thead>
<tbody>
<tr>
<td>Albania</td>
<td>264</td>
<td>325</td>
<td>656</td>
<td>988</td>
<td>979</td>
<td>1 097</td>
</tr>
<tr>
<td>Bosnia and Herzegovina</td>
<td>613</td>
<td>766</td>
<td>2 080</td>
<td>932</td>
<td>246</td>
<td>63</td>
</tr>
<tr>
<td>Croatia</td>
<td>1 825</td>
<td>3 473</td>
<td>5 035</td>
<td>6 179</td>
<td>2 911</td>
<td>583</td>
</tr>
<tr>
<td>Macedonia</td>
<td>96</td>
<td>433</td>
<td>693</td>
<td>586</td>
<td>201</td>
<td>293</td>
</tr>
<tr>
<td>Montenegro</td>
<td>501</td>
<td>622</td>
<td>934</td>
<td>960</td>
<td>1 527</td>
<td>760</td>
</tr>
<tr>
<td>Serbia</td>
<td>1 577</td>
<td>4 256</td>
<td>3 439</td>
<td>2 955</td>
<td>1 959</td>
<td>1 329</td>
</tr>
</tbody>
</table>


Conclusion and recommendation

From this research we can come to some important conclusions:
• The economic growth of the last years was supported by the work of the emigrants, from trade and light industry, which exploits cheap labour in Kosovo. These factors are likely to be not so productive as they have been the last years. There are a lot of foreign and local experts that have begun to think about the long-term consequences of the crisis, which will bring more supervision of the financial systems of the developed countries and as a result, less investments in the developing countries such as Kosovo.
Kosovo’s economy continues to face a huge commercial deficit in merchandise and services, and remains open to the outside world in terms of commercial trade, but, this opening of Kosovar economy to the outside world is almost unilateral, which means it is bases on import.

The large number of unemployed and poverty are serious problems in Kosovo. Despite the improvement of the wages per capita, the material standing of Kosovar citizens remains fragile.

The level of taxation on consumption, that weigh on the more poorer layers, are not differentiated and a revision for decrease or two-level VAT tax would be desirable.

In order to improve the economic situation in the country in the future, it is recommended:

- The following of such fiscal policies that ensure on one hand macroeconomic stability, and on the other hand a stimulation of business development or at least no restriction of it.
- Approval of respective legislation, that presents the short-term and long-term interests of the country and the fair and correct implementation of the legislation.
- General revision of tax legislation in order to harmonize and adapt it with European legislation by ensuring conditions that:
  a) efficiently fight fiscal evasion and more security for foreign investors 
  b) establishment of differentiated tax policies for branches and activities that require more labour force and creation of new job positions.
- If we wish the investors to not overlook Kosovo or to relocate in the neighbour countries, the needed changes should be done in legislation, especially some of the laws that have a direct impact on business environment creation, such as economic laws, the law on cadastre or property registration.
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