

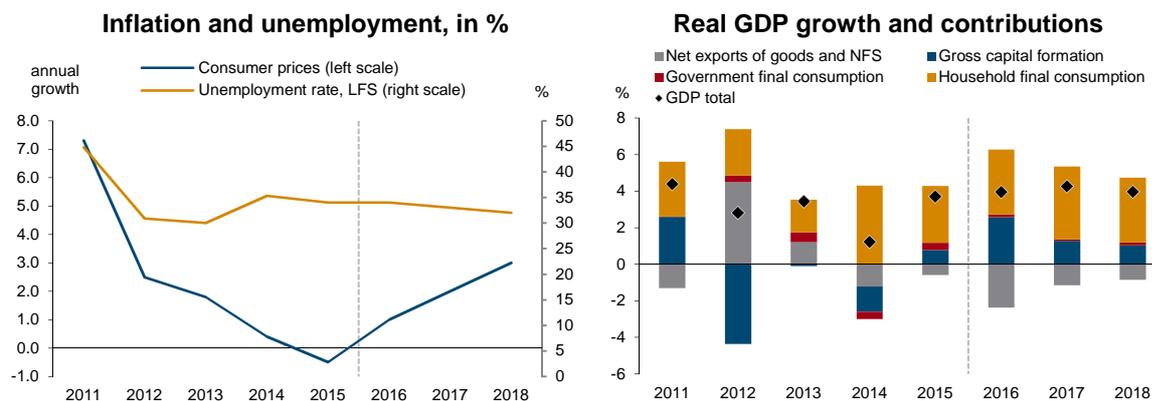


## KOSOVO: A long passage to prosperity

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Despite hefty political infighting, the economy of Kosovo is growing at a rate of almost 4% per annum. The dynamics might even accelerate in the years to come. The major growth drivers are remittances and foreign direct investment. However, still more growth will be needed if mass unemployment is to be reduced substantially as the population is young and ever-increasing.

**Figure 45 / Kosovo: main macroeconomic indicators**



Source: wiiw Annual Database incorporating national and Eurostat statistics, own calculation. Forecasts by wiiw.

The economy of Kosovo is performing surprisingly well despite considerable headwinds in the political and economic sphere. The opposition is organising anti-government protests on a regular basis. Moreover, the opposition's nationalist MP's have repeatedly violently interrupted parliament sessions, inter alia by releasing canisters of tear gas or by using pepper spray. They demand the abandonment of a deal signed in August 2015 which gives the Serb minority greater autonomy as well as of an agreement on the border demarcation between Kosovo and Montenegro. They also violently reject the parliament's planned election of Foreign Minister Hashim Thaci as new President of the Republic. It is feared that the political unrest in the country will hinder foreign direct investment. In particular, the implementation of the large Brezovica winter tourism FDI project (in the order of 3% of GDP split over the next years) might be at risk.

However, in the first eleven months of 2015 cumulated FDI inflows almost doubled as compared to the same period a year earlier. The main sectors targeted were finance, construction, real estate, renting and business activities. The investors seemingly have confidence in the country's successful

cooperation with the international community. In late January 2016, the European Parliament gave its consent to the EU-Kosovo Stabilisation and Association Agreement. This agreement constitutes an important first formal step in Kosovo's integration into Europe. The Parliament's decision paved the way for the European Council of Ministers to formally conclude the agreement and enable its entry into force in the next months. Earlier in January the IMF's Executive Board completed the first review of Kosovo's economic performance under the Stand-By Arrangement, which gave a green light to the disbursement of the second tranche of the funds agreed. The IMF mission's overall assessment was mostly positive.

Kosovo's goods export sector, which is dominated by mining and manufacturing of metals, has recently suffered from a strong decline in metals prices. According to the World Bank's aggregate commodity price indices, the year 2015 saw a drop in metals prices by more than 20%. However, apart from the fact that Kosovo's export sector is still tiny and of only limited importance for the overall economic development (according to the balance of payments, goods exports were less than 6% of GDP in 2015), it is remarkable to notice that the nominal values of total exports have not changed in 2015 as compared to 2014. Hence it is fair to assume that in real terms the country's export industry is expanding quite substantially, a trend that should continue over the next few years also given the expected stabilisation of commodity prices.

A strong economic boost to growth is the positive development of remittances. Inflows from January to November 2015 show a 9% increase as compared to a year earlier. Given the improving GDP growth for Germany and Switzerland (the main destination countries for Kosovo migrants) it can be expected that this trend will even intensify. Apart from consumption, remittances typically support also household investment, which is expected to pick up as well.

Another factor that is likely to boost investments (despite the government's rather modest investment plans which include a railway line to the Macedonian border and a large-scale irrigation project) is the strongly falling interest rates on new investment loans to the economy. These dropped from 9.3% in December 2014 to 7.2% in December 2015. Over the same period, total new loans for investment increased by more than 20% and new household mortgage loans soared by almost 28%. These encouraging developments occur against the backdrop of a stable banking sector. In November 2015 the share of nonperforming loans stood at 6.5% and the capital adequacy ratio at 18.9%. The loan loss provisions to nonperforming loans were at 116.7%.

Hence overall prospects for the economy of Kosovo are rather favourable. Based on a broad range of dynamic contributions of household consumption, investment and exports, the overall GDP growth is expected to accelerate to almost 4% in 2016. This rate might be even surpassed in the following years. However, it has to be noticed that this development started from a very low level and that growth is still not strong enough to substantially reduce the extremely high unemployment rate. This is also due to the fact that Kosovo's young population is still growing and new age cohorts pour each year into the tight labour market. Emigration is often seen as the sole option to improve life conditions. The growing anti-immigration mood throughout Europe is of little help in this respect and might hence have also repercussions on the already fragile political climate in this small Balkan country.

**Table 14 / Kosovo: selected economic indicators**

	2011	2012	2013	2014	2015 <sup>1)</sup>	2016	2017	2018
						Forecast		
Population, th pers., average	1,796	1,807	1,818	1,813	1,830	1,847	1,860	1,880
Gross domestic product, EUR mn, nom.	4,815	5,059	5,327	5,567	5,800	6,100	6,500	7,000
annual change in % (real)	4.4	2.8	3.4	1.2	3.7	3.9	4.3	4.0
GDP/capita (EUR at exchange rate)	2700	2800	2900	3100	3200	3,300	3,500	3,700
GDP/capita (EUR at PPP)	6200	6500	6700	7000	7500	.	.	.
Consumption of households, EUR mn, nom.	4,142	4,458	4,652	4,926	5,100	.	.	.
annual change in % (real)	3.5	2.9	2.0	4.9	3.5	4.0	4.5	4.0
Gross fixed capital form., EUR mn, nom.	1,476	1,317	1,323	1,294	1,330	.	.	.
annual change in % (real)	8.1	-13.6	-0.2	-3.3	3.0	10.0	5.0	4.0
Gross industrial production <sup>2)</sup>								
annual change in % (real)	-5.7	14.9	6.5	-1.3	5.0	6.0	5.0	4.0
Gross agricultural production <sup>2)</sup>								
annual change in % (real)	0.2	-8.5	1.4	0.8	-3.0	.	.	.
Construction output <sup>2)</sup>								
annual change in % (real)	18.0	-8.5	2.6	-6.1	4.0	.	.	.
Employed persons, LFS, th, average <sup>3)</sup>	280	303	338	324	333	340	350	360
annual change in %	.	.	11.7	-4.4	2.9	3.0	4.0	3.0
Unemployed persons, LFS, th, average <sup>3)</sup>	228	136	145	177	170	180	170	170
Unemployment rate, LFS, in %, average <sup>3)</sup>	44.8	30.9	30.0	35.3	34.0	34.0	33.0	32.0
Unemployment rate, reg., in %, end of period	.	.	.	.	.	.	.	.
Average monthly net wages, EUR <sup>4)</sup>	348	354	356	416	450	460	480	510
annual change in % (real, net)	13.4	-0.8	-1.2	16.4	9.0	2.0	3.0	4.0
Consumer prices, % p.a.	7.3	2.5	1.8	0.4	-0.5	1.0	2.0	3.0
Producer prices, % p.a.	4.5	1.9	2.5	1.7	4.0	2.0	3.0	3.0
General government budget, nat. def., % of GDP								
Revenues	27.2	27.3	25.5	24.2	26.0	27.0	28.0	29.0
Expenditures	28.3	28.6	28.0	27.2	28.0	28.0	30.0	30.0
Deficit (-) / surplus (+)	-1.1	-1.2	-2.5	-2.9	-2.0	-1.0	-2.0	-1.0
Public debt, nat. def., % of GDP	5.3	8.1	8.9	10.5	12.0	12.4	13.6	13.7
Central bank policy rate, % p.a., end of period <sup>5)</sup>	13.3	12.2	10.9	9.3	8.0	6.0	6.0	5.0
Current account, EUR mn	-658	-380	-339	-437	-475	-550	-560	-580
Current account, % of GDP	-13.7	-7.5	-6.4	-7.8	-8.2	-9.0	-8.6	-8.3
Exports of goods, BOP, EUR mn	317	282	292	324	330	360	390	420
annual change in %	5.8	-10.9	3.4	11.3	1.8	9.1	8.3	7.7
Imports of goods, BOP, EUR mn	2,364	2,332	2,287	2,383	2,390	2,600	2,780	2,950
annual change in %	15.8	-1.3	-1.9	4.2	0.3	8.8	6.9	6.1
Exports of services, BOP, EUR mn	625	641	633	767	790	850	1,050	1,130
annual change in %	8.9	2.6	-1.4	21.3	3.0	7.6	23.5	7.6
Imports of services, BOP, EUR mn	369	318	320	431	450	490	520	550
annual change in %	-7.4	-13.9	0.9	34.6	4.3	8.9	6.1	5.8
FDI liabilities (inflow), EUR mn	384	229	280	151	370	.	.	.
FDI assets (outflow), EUR mn	5	16	30	27	30	.	.	.
Gross reserves of NB excl. gold, EUR mn	573	840	800	747	900	.	.	.
Gross external debt, EUR mn	1,428	1,517	1,608	1,737	2,000	2,100	2,300	2,500
Gross external debt, % of GDP	29.7	30.0	30.2	31.2	34.5	35.0	35.0	36.0
Purchasing power parity EUR/EUR	0.433	0.431	0.436	0.437	0.424	.	.	.

1) Preliminary and wiiw estimates. - 2) According to gross value added (manufacturing industry for industrial production). -

3) Population 15-64. From 2012 new improved sample survey based on census 2011, not comparable with previous years. -

4) Net wages in state administration. - 5) Average weighted effective lending interest rate (Kosovo uses the euro as national currency).

Source: wiiw Databases incorporating national statistics. Forecasts by wiiw.