

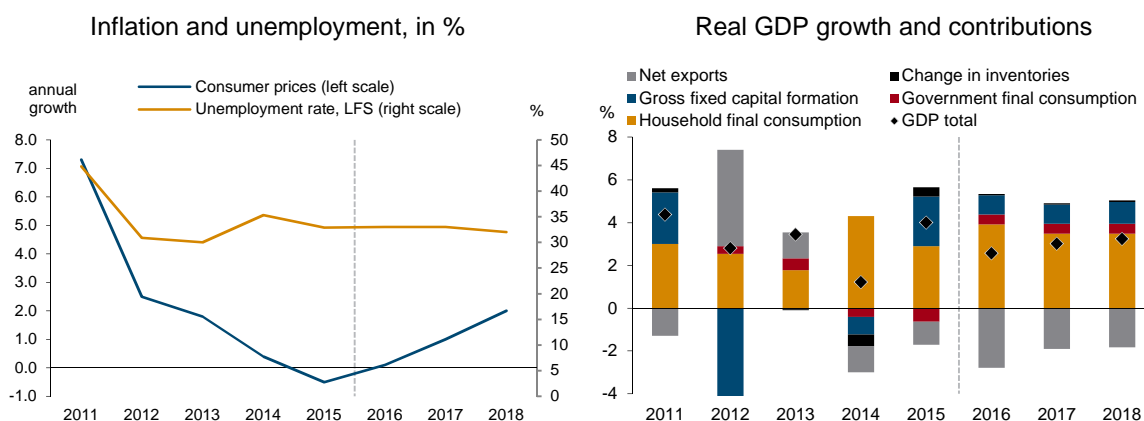


KOSOVO: Investment failure dragging down growth

MARIO HOLZNER

The main reason for revising Kosovo's GDP growth prospects downwards for the years ahead lies in the failure of a major foreign investment project in the winter tourism industry that accounted for some 7% of the country's GDP. Growth of less than 3% is expected for 2016, largely driven by household consumption.

Figure 32 / Kosovo: Main macroeconomic indicators



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

This summer it became clear that the envisaged sale of Kosovo's only ski resort to a French consortium had failed as the potential investor of the planned EUR 400 million (approximately 7% of 2016 GDP) project was unable to secure the contractually pledged funding. This is a severe setback for a small and poor country desperately in need of productive investments in the tiny export sector. In this respect it is only a small crumb of comfort that other potential investment projects are being discussed. Apparently several foreign investors have shown interest in taking part in the EUR 60 million worth construction of a second ski resort in Kosovo. And in other news, the Belgian bus manufacturer Van Hool is negotiating possible investments in the country with Kosovo's government.

Nevertheless, gross capital formation in the first half of 2016 increased by almost 15% in real terms as compared to the same period of 2015. This is also reflected in a fairly strong increase in construction activities of more than 5% in the first half. However, new investment loans decreased in the first seven months of 2016 by almost 19% as compared to the corresponding period a year earlier – despite new

loans' (effective) interest rates further declining year on year by 1.1 percentage points to a level of about 7% in July 2016. Another concern is the massive drop in FDI inflows: by more than 40% in the first half of 2016 compared to the first half of the previous year. Hence the surprisingly high growth of capital formation in the first half is unlikely to continue throughout the whole year.

Also government activity is supporting growth only marginally, if at all. In the first six months of 2016, public expenditures increased by 10% while revenues rose by 17% year on year. Still, on 8 July 2016, Kosovo's parliament approved a budget revision, raising the projected deficit slightly to EUR 122 million (from the previously expected 107 million, around 2% of GDP). In particular, planned capital expenditures were increased by almost 8%.

As it appears, household consumption will provide the biggest contribution to GDP growth in this and the following years. In the first half of 2016, real growth of household consumption of almost 6% was recorded year on year. This is also reflected in new consumer loans up by almost 19% over the period from January to July 2016 as compared to the same period of 2015. Moreover, customs data for the first half of the year indicate strong growth of imports by more than 8% year on year, which is another indicator of dynamic household consumption activity. (Nominal exports in the same period were declining by almost 6%, partly related to declining prices for metals.)

It is interesting to note that both household consumption and construction activities are doing well against the backdrop of a slight fall in remittances (-2.7%) in the first half of this year against the same period a year earlier. This is despite a stable outlook for the German economy in 2016 and the Swiss economy being able to regain momentum in recent quarters – the two countries being the main host countries for Kosovo migrant workers. (The Swiss growth outlook for 2017 is stable and that of Germany was revised slightly downwards due to assumed negative Brexit effects, but both are expected to grow at a relatively robust rate of around 1.7%.)

Overall, we have to substantially reduce our GDP growth forecast for Kosovo, mostly due to the failed ski resort investment. The new forecast is now 2.6% for 2016, 3.0% for 2017 and 3.2% for 2018 (down from 3.3%, 4.2% and 4.0%, respectively, in our summer 2016 forecast update). If, however, household consumption keeps on growing and investment does not plummet in the second half of the current year, GDP growth in 2016 could be above 3%. Nevertheless, without major foreign investment and an increase in export capacities, in the years to come the country will grow slightly below its trend growth rate of 3.3% observed since the outbreak of the global financial crisis.

Table 15 / Kosovo: Selected economic indicators

	2012	2013	2014	2015 ¹⁾	2015 January-June	2016	2016 Forecast	2017 Forecast	2018
Population, th pers., average	1,807	1,818	1,813	1,788	.	.	1,780	1,780	1,790
Gross domestic product, EUR mn, nom.	5,059	5,327	5,567	5,772	2,645	2,729	5,900	6,100	6,400
annual change in % (real)	2.8	3.4	1.2	4.0	3.3	3.5	2.6	3.0	3.2
GDP/capita (EUR at exchange rate)	2800	2900	3100	3200	.	.	3,300	3,400	3,600
GDP/capita (EUR at PPP)	6500	6700	7000	7600	.	.	.	.	.
Consumption of households, EUR mn, nom.	4,458	4,652	4,926	5,024	.	.	.	.	.
annual change in % (real)	2.9	2.0	4.9	3.3	.	.	4.5	4.0	4.0
Gross fixed capital form., EUR mn, nom.	1,317	1,323	1,294	1,480	.	.	.	.	.
annual change in % (real)	-13.6	-0.2	-3.3	10.0	.	.	3.5	3.5	4.0
Gross industrial production ²⁾									
annual change in % (real)	14.9	6.5	-1.3	5.0	.	.	3.5	4.0	5.0
Gross agricultural production ²⁾									
annual change in % (real)	-8.5	1.4	0.8	-3.0	.	.	.	.	.
Construction output ²⁾									
annual change in % (real)	-8.5	2.6	-6.1	4.0	.	.	.	.	.
Employed persons, LFS, th, average ³⁾	303	338	324	297	.	.	300	310	320
annual change in %	.	11.7	-4.4	-8.2	.	.	1.0	2.0	2.0
Unemployed persons, LFS, th, average ³⁾	136	145	177	146	.	.	150	150	150
Unemployment rate, LFS, in %, average ³⁾	30.9	30.0	35.3	32.9	.	.	33.0	33.0	32.0
Unemployment rate, reg., in %, end of period	.	.	.	.	.	.	.	.	.
Average monthly net wages, EUR ⁴⁾	354	356	416	446	.	.	460	480	500
annual change in % (real, net)	-0.8	-1.2	16.4	9.0	.	.	2.0	3.0	3.0
Consumer prices, % p.a.	2.5	1.8	0.4	-0.5	-0.4	0.0	0.1	1.0	2.0
Producer prices, % p.a.	1.9	2.5	1.7	2.7	3.9	-3.0	-2.0	2.0	4.0
General government budget, nat. def., % of GDP									
Revenues	27.3	25.5	24.2	29.6	.	.	31.0	30.0	31.0
Expenditures	28.6	28.0	27.2	27.9	.	.	30.5	31.0	32.0
Deficit (-) / surplus (+)	-1.2	-2.5	-2.9	1.6	.	.	0.5	-1.0	-1.0
Public debt, nat. def., % of GDP	8.1	8.9	10.5	13.0	11.2	13.8	12.2	12.8	13.2
Central bank policy rate, % p.a., end of period ⁵⁾	12.24	10.90	9.29	7.69	7.63	7.21	6.00	5.50	5.00
Current account, EUR mn	-380	-339	-437	-528	-208	-321	-760	-780	-810
Current account, % of GDP	-7.5	-6.4	-7.8	-9.1	-7.9	-11.8	-12.9	-12.8	-12.7
Exports of goods, BOP, EUR mn	282	291	324	322	158	150	320	340	370
annual change in %	-10.9	3.4	11.3	-0.6	11.9	-5.5	-0.8	6.3	8.8
Imports of goods, BOP, EUR mn	2,332	2,287	2,383	2,432	1,099	1,210	2,550	2,700	2,900
annual change in %	-1.3	-1.9	4.2	2.1	2.5	10.1	4.9	5.9	7.4
Exports of services, BOP, EUR mn	641	633	767	796	322	330	820	880	950
annual change in %	2.6	-1.4	21.3	3.8	10.9	2.6	3.0	7.3	8.0
Imports of services, BOP, EUR mn	318	320	431	442	189	157	350	370	400
annual change in %	-13.9	0.9	34.6	2.5	24.8	-16.9	-20.8	5.7	8.1
FDI liabilities (inflow), EUR mn	229	280	151	324	162	85	180	.	.
FDI assets (outflow), EUR mn	16	30	27	37	13	1	10	.	.
Gross reserves of NB excl. gold, EUR mn	840	800	747	862	750	919	.	.	.
Gross external debt, EUR mn	1,517	1,608	1,737	1,932	1,831	2,003	2,100	2,300	2,400
Gross external debt, % of GDP	30.0	30.2	31.2	33.5	31.7	34.0	36.0	37.0	38.0
Purchasing power parity EUR/EUR	0.431	0.436	0.437	0.424	.	.	.	.	.

1) Preliminary - 2) According to gross value added (manufacturing industry for industrial production). - 3) Population 15-64. - 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.