KOSOVO: Road to the New Kosovo

MARIO HOLZNER

The Kosovo economy is growing fast, at least by current European standards. Due to a favourable outlook for Germany and Switzerland, the prime host countries of Kosovo migrant workers and remittances senders, as well as due to higher government spending in the wake of the upcoming parliamentary elections, we expect a GDP growth rate of 5% for 2014. A number of large infrastructure projects in the transport and energy sector are being planned for the years to come, hence growth is likely to remain firm, at around 4% in both 2015 and 2016.

Compared to other countries in the region, the economy of Kosovo is developing quite vibrantly, admittedly from a very low level of economic activity. In the first three quarters of 2013 the number of newly established businesses was growing by almost 7% on the year. This was especially due to a host of new firms in real estate and business services. Also the number of companies in health services and construction increased above average. It should be mentioned that there is still no public health insurance system existing in the country. Public health care institutions, which are free of charge to pregnant women, children, elderly, families that receive social assistance and persons with disabilities, are of poor quality and hence there is a strong demand for private health care providers of all sorts.

The many new firms active in the real estate and building sector are likely related to the ongoing construction boom. Another evidence for this is a 14% increase in new household mortgage loans in 2013, year-on-year. New investment loans to non-financial corporations increased by 10%. However, most of the financing stems from diaspora workers' remittances and foreign direct investment, rather than domestic credit. Both inflows increased strongly in the first three quarters of 2013 as compared to a year earlier. Remittances increased by 11% and will most likely reach a billion euro over the whole year (almost 20% of GDP). FDI increased by 15% and might make some 270 million euro for the year.

The largest part of the increases in FDI occurred in the transport sector. In October 2013, the new terminal and facilities of Prishtina's International Airport, built by the Turkish-French consortium Limak-Aéroports de Lyon, was inaugurated under the auspices of the Prime Ministers of Turkey, Kosovo and Albania. The investment was worth a 140 million euro, whereby the airport's annual passenger capacity was increased from 2 to 5 million. Further infrastructure investment was announced, such as in modern electric power grids and roads. In particular, the development of Kosovo's highway network is being pushed by the government.

In early 2014 the US-Turkish consortium Bechtel-Enka was contracted to build a 65 km motorway from Prishtina to the Macedonian border. The consortium, which has recently completed Kosovo's first highway, from Prishtina to the Albanian border in the west, offered to build the southern motorway to Macedonia for 600 million euro within 42 months. Macedonia is expected to issue soon a tender for the smaller 13 km stretch of the highway from the border to Skopje. Macedonia is one of Kosovo's most important trading partners, both in terms of imports and exports.

However, Kosovo's overall exports are still rather small. Exports of goods make up only some 300 million euro per year. Nevertheless, they are on the rise. In the first three quarters of 2013 they increased by more than 9% in euro terms on the year. At the same time imports of goods, which account for about 2.3 billion euro, decreased by 2.5%. Customs data for most of the year 2013 show that the largest part of the exports' increase stems from additional energy exports. This is also the most important sector responsible for the decrease in imports.

Data from the Kosovo Energy Corporation (KEK) for the first nine month of 2013 show an increase of coal production in tonnes by some 4% year on year and a subsequent increase of electricity production in MWh by more than 13%, together with substantial increases in exports and import substitution. The Kosovo basin holds the world's fifth-largest proven reserves of lignite. The main sources of electricity production are hence KEK's two old, inefficient and highly polluting coal-fired power plants Kosovo A (450 MW) and Kosovo B (580 MW). As the older plant, Kosovo A (built in the 1960s), has to be closed by 2017, the government plans to announce a tender for a new thermal power plant in March 2014, still before parliamentary elections. The project title for the power plant is 'Kosova e Re' – 'New Kosovo'.

Given the urgent need for investment in modern infrastructure as well as the approaching general elections, the government is slightly increasing the so far negligible budget deficit. Until November 2013, the cumulated government deficit was almost 2 percentage points in GDP higher as compared to a year earlier. Expenditures will likely further increase as a share in GDP in 2014 and reach a level of close to 40%, while only seven years earlier it was still below 30%. The average in the EU is at about 50%.

Apart from stronger than expected government demand it is especially due to the surprisingly high inflow of remittances that we had to raise our GDP growth projection for 2013 from 3% to 4%. Growth forecasts for the following years did not change substantially. Due to the improved outlook both for the German and the Swiss economy, where most of Kosovo's diaspora is residing, as well as higher public spending before the upcoming elections, we expect 5% growth for 2014. In the subsequent years of 2015 and 2016 growth is likely to oscillate around a robust 4%, given the strong demand for infrastructure investment.

Table 1 / Kosovo: Selected Economic Indicators

	2009	2010	2011	2012	2013 1)	2014	2015 Forecast	2016
Population, th pers., average	1748	1775	1800	1816	1829	1845	1861	1877
Gross domestic product, EUR mn, nom.	4008	4291	4770	4916	5200	5700	6200	6600
annual change in % (real)	3.5	3.2	4.5	2.5	4.0	5.0	4.0	4.0
GDP/capita (EUR at exchange rate)	2300	2400	2700	2700	2800	.	.	.
GDP/capita (EUR at PPP)	5000	5200	5400	5500	5600	.	.	.
Consumption of households, EUR mn, nom.	3605	3822	4220	5256	5500	.	.	.
annual change in % (real)	2.1	3.1	3.0	2.8	3.5	4.0	3.0	3.0
Gross fixed capital form., EUR mn, nom.	1027	1193	1387	1239	1300	.	.	.
annual change in % (real)	13.6	12.7	12.1	-12.4	6.0	10.0	9.0	8.0
Gross industrial production 2)								
annual change in % (real)	-1.5	-5.6	19.2	-10.0	5.0	7.0	10.0	5.0
Gross agricultural production 2)								
annual change in % (real)	19.3	0.5	26.3	0.0	3.0	4.0	3.0	4.0
Construction output 2)								
annual change in % (real)	32.8	-27.7	11.2	3.0	6.0	6.0	4.0	5.0
Unemployment rate, LFS, in %, average 3)	45.4	45.1	44.8	30.9	31.0	29.0	30.0	30.0
Reg. unemployed persons, th, end of period	339	335	325	260	268	.	.	.
Average monthly net wages, EUR	246	286	348	353	362	.	.	.
annual change in % (real, net)	22.8	12.7	14.4	-1.1	1.5	5.0	3.0	3.0
Consumer prices, % p.a.	-2.4	3.5	7.3	2.5	1.8	4.0	4.0	3.0
annual change in % (real, gross)	3.8	4.7	5.7	1.7	3.0	.	.	.
General governm.budget, nat.def., % of GDP 4)								
Revenues	36.7	33.8	35.3	36.3	35.0	36.0	38.0	37.0
Expenditures	32.6	35.1	35.6	36.7	37.0	38.0	38.0	38.0
Deficit (-) / surplus (+)	4.1	-1.3	-0.2	-0.5	-2.0	-2.0	0.0	-1.0
Public debt, nat.def., % of GDP 4)	6.2	6.1	5.3	5.6	6.3	7.7	7.1	7.7
Central bank policy rate, % p.a., end of period 5)	14.1	14.3	13.9	12.9	12.2	.	.	.
Current account, EUR mn	-374.2	-515.7	-658.4	-380.2	-350.0	-700	-800	-700
Current account, % of GDP	-9.3	-12.0	-13.8	-7.7	-6.7	-12.3	-12.9	-10.6
Exports of goods, BOP, EUR mn	160.6	288.2	304.1	269.6	310.0	350	400	450
annual change in %	-16.9	79.5	5.5	-11.3	15.0	12.9	14.3	12.5
Imports of goods, BOP, EUR mn	1811.8	2033.2	2354.8	2319.3	2300.0	2600	2650	2700
annual change in %	2.5	12.2	15.8	-1.5	-0.8	13.0	1.9	1.9
Exports of services, BOP, EUR mn	517.6	573.0	618.5	635.1	650.0	660	700	750
annual change in %	31.9	10.7	7.9	2.7	2.3	1.5	6.1	7.1
Imports of services, BOP, EUR mn	285.3	386.1	352.8	288.8	300.0	450	450	500
annual change in %	18.5	35.3	-8.6	-18.1	3.9	50.0	0.0	11.1
FDI inflow, EUR mn	287.4	365.8	393.9	229.1	270.0	500	600	500
FDI outflow, EUR mn	10.5	34.7	15.7	15.8	20.0	30	40	50
Gross reserves of NB excl. gold, EUR mn	576	634	575	840	900	.	.	.
Gross external debt, EUR mn	1146	1348	1427	1518	1600	.	.	.
Gross external debt, % of GDP	28.6	31.4	29.9	30.9	30.8	.	.	.
Purchasing power parity EUR/EUR	0.461	0.463	0.488	0.493	0.500	.	.	.

1) Preliminary and wiiw estimates. - 2) According to gross value added data. - 3) From 2012 new improved sample survey based on census 2011, not comparable with previous years. - 4) National definition based on ESA'95. - 5) Average weighted lending interest rate (Kosovo uses the euro as national currency).
Source: National statistics and IMF. Forecasts by wiiw.