

Kosovo Economy in 2002

The budget in Kosovo is affected by many macroeconomic factors. First, the demographics of the country determine some aspects of revenue and expenditure – whenever the per capita calculations are made. Second, the structure and performance of the economy determines one of the important tax bases for government revenues. Third, household consumption and investment is another way of looking at the taxable base. Fourth, the trade balance and the balance of payments are determinants of changes in the money supply (when an external currency such as the euro is used) and the tax base for a tariff system. Fifth, money and prices are related to the stability of the economy. And sixth, the financial system and the investment process are determinants of future output and employment growth. In this chapter, each of these factors will be considered for the Kosovo economy in 2002. The final section of the paper presents information on the budget and the entire public sector in light of these macroeconomic factors.

An important element of any discussion of the Kosovo economy is the shortage of available data. During the last year, a significant progress has been made in economic data collection, processing and publication, in particular in the budget sector, banking, NGOs, and foreign trade. However, there still exist large data gaps in many areas, such as population and demography, donor activities, household income and spending, agricultural farms, and non-farm private and public enterprises. There is an urgent need for a national census and appropriate legislation and regulatory measures in the area of economic statistics.

Given the paucity of reliable data, the numbers presented here are a mixture of relatively “hard” data compiled from official reports as well as “soft” estimates, derived from pieces of information scattered throughout Kosovo governmental agencies and other institutions. Currently a joint team of MFE and IMF is working on producing a fresh batch of macroeconomic national account statistics. The final results of this work are expected to become available in July 2003. Initial results of this research are used in this chapter. Though these estimates in some cases differ significantly from estimates made by other institutions, they seem to provide a reasonably consistent picture of the Kosovo economy and the impact that macroeconomic development has had on the budget.

A. Population

Key Aspects

- *The population resident in Kosovo fluctuates between about 1.70 million (winter) and 1.76 million (summer) over the course of the year.*
- *The population of Kosovo is young relative to the rest of Europe. This reflects higher birth rates, in the past, than in other European countries.*

Because there has not been a census since the conflict, there are no precise figures for the population of Kosovo. But based on available data from many sources (household surveys, Kosovo Civil Register, school data, and other) the Kosovo population is estimated at 1,860,000, including about 190,000 who move back and forth between Kosovo and abroad. In addition, the Kosovo diaspora (Kosovars who emigrated during the last two decades and became permanent residents or citizens of other countries) counts about 550,000 people. Almost three-quarters of them live in three countries: Germany, Switzerland, and Serbia.

There are more people in Kosovo during summer (1.76 million) and less during winter (1.70 million). The largest number of arrivals (according to border crossing statistics) occurs in June while the largest number of departures occurs in September. The number of Kosovo residents is augmented by about 50,000 foreigners, including ex-patriot internationals (temporarily residing in Kosovo while working for diverse donor organizations), KFOR troops, short-term visitors and tourists.

Within Kosovo about 60% of residents live in the rural areas. And the population of the largest urban area, Prishtina, is about 170,000 -- higher estimates are not consistent with the distribution of household structures in the country.

From the perspective of budget planning, it is important to note that Kosovo has the youngest population in Europe. The age distribution reported in the four household surveys that have been conducted since 1999 is shown in Table 1. All have similar results -- half of its population is 22.5 years old and younger, one-third is 15 years and younger; 6% are 65 years and older.

Table 1. Kosovo resident population, by age groups, 1999-2002

Age	UNFPA [18] 1999	LSMS [16] 2000	SOK [5] 2001	Riinvest [19] 2002
Median	23	22	22	22
	Years			
	%			
0-4	9.97	10.68	9.98	8.76
5-9	10.61	10.88	10.27	10.22
10-14	10.71	11.05	11.44	11.90
15-19	10.92	11.05	10.43	11.58
20-24	9.41	9.74	10.02	10.22
25-29	7.51	8.24	8.45	8.30
30-34	6.52	6.53	6.87	6.96
35-39	6.01	5.78	5.79	5.95
40-44	5.67	4.89	5.09	5.87
45-49	5.47	4.58	5.01	4.62
50-54	4.57	3.73	3.90	4.21

55-59	3.87	3.68	3.48	3.17
60-64	3.18	2.93	2.81	3.17
65-69	2.38	2.30	2.90	2.09
70-74	1.49	1.98	1.98	1.45
75+	1.70	1.96	1.58	1.53
Total	100.00	100.00	100.00	100.00
0-15	33.53	34.75	33.81	33.16
16-64	60.90	59.00	59.73	61.77
65+	5.57	6.24	6.46	5.08
	100.00	100.00	100.00	100.00

Sources: [5], [16], [18], and [19]

Kosovo is one of the few countries in Europe in which the overall population is growing. The fertility rates, crude birthrates and death rates are the lowest in Europe. Even so, the 2002 birthrate (21 per one thousand of population) is significantly lower than the birthrate twenty years ago (around 32 per thousand) and the birthrate should continue to decline in the near future. As a result, the natural increase of population will also continue to decline. With the likelihood of some emigration, the increase in population during the current decade should be only slight or none.

This understanding of population dynamics affects budget considerations in several ways. First, the smaller size of the resident population than has been previously estimated leads estimates of per capita values to be larger than they would be with a higher estimate. Second, the large emigrant and transitory migrant population is associated with an increase in money earned outside of Kosovo, but spent inside the country (see below). Third, the youthfulness of the population affects the provision of services, education in particular. And fourth, the youthfulness of the population means that the large numbers of young persons will soon be included in the pool of persons of working age (16-64 years old), which will create a strong pressure on the labor market. On the one hand, this may worsen the situation of the government through additional anti-poverty type programs. On the other, a worsened labor market may stimulate additional emigration and remittances.

B. Labor and Domestic Product

Key Aspects

- *The main increase in employment of non-Serbs since 1999 has come in the public sector.*
- *Private medium and large-scale firms outside of trade and finance are almost non-existent.*
- *Agriculture remains the largest sector of employment, but has low productivity. The manufacturing sector is small.*

The labor data has been obtained from individual employment information through household surveys, from employer information through firm surveys, and from tax records. Based on these

sources, the MFE has produced a balance of labor force for 2002 that is shown in Table 2. Overall, of the approximately one million Kosovo residents belonging to the labor-force-age group, and one-third – or 341,400 -- are employed.

In Table 2, employment and wage information is shown separately for several institutional sub-sectors of the economy that belong to either the “official” sector – which pays taxes – or the “unofficial” sector – which does not pay taxes.

The first column shows the numbers of establishments with the status of “official” tax paying enterprises (as of June 2002) and the number of agricultural farms, each rural household being treated as a farm, since almost all of them are involved in some food production activities. The second column presents average number of persons employed per firm (according to the reports provided to Tax Administration by all tax paying enterprises); in agriculture an average of one worker per farm (rural household) is assumed. Columns 3-5 show total employment (thousands of persons), average monthly wage (euro) and aggregate annual labor income (millions of euro), respectively. Column 6 shows the structure of the economy, derived from labor income figures.

Table 2. Labor employment and income, by institutional sectors, 2002

Enterprises and other institutional entities	Firms	Average employment per firm	Total employment	Average monthly wage	Annual labor earnings	
	Number	Persons	Thous.. persons	Euro	Million euro	%
	1	2	3	4	5	6
TOTAL			341.4		636.6	100.0
Agriculture*			144.8		105.5	16.6
Non-farm sector			196.6	225	531.1	83.4
Non-farm, public sector			111.6	255	341.5	53.6
Non-farm, private sector			85.0	186	189.7	29.8
Total, official			140.6	221	373.5	58.7
Farms	388	4.6	1.8	194	4.2	0.7
Non-farms			138.8	222	369.3	58.0
Non-farm small businesses	21,149	1.2	25.4	171	52.1	8.2
Non-farm enterprises	2,070	22.3	46.2	303	167.8	26.4
Private (medium and large firms)	1,873	6.9	13	344	53.7	8.4
Socially-Owned	99	179.3	17.7	180	38.2	6.0
Public/State	99	157.2	15.5	408	75.9	11.9
Budget organizations			63.9	171	131.4	20.6
NGOs	500	6.6	3.3	454	18.0	2.8

Total, unofficial			197.8		262.6	41.3
Agriculture*	140,000	1.0	143.0	88	100.8	15.8
Non-farm, private sector			46.6	150	83.9	13.2
Donors			11.2	580	78.0	12.2

* An 8-month work year is assumed

Sources: [1], [5], [11], [16], and [19]

The largest employer in Kosovo is agriculture (145,000), followed by the non-farm public sector (112,000) and non-farm private sector (85,000). None of these sectors are likely to provide much source for increases in the tax base in the near future.

Agriculture includes a small number of co-operatives and commercial firms (both private and public) – about 1,800 entities – and 143,000 rural household units, 70% of which are defined as farms – they have an area larger than one hectare. Agriculture has the lowest labor productivity and the lowest monthly wage – 88 euro (labor activity is assumed to be confined to 8 months a year). In fact, only a small fraction of this remuneration is monetized. About 85% of food produced in Kosovo is consumed in-house and only a small amount is delivered to the market and sold for cash. In addition to the persons defined as “workers”, there is another large group of people, assumed to be equal to an equivalent of 143,000 of family members (one person per household) who help with the production of food, but are classified as “out-of-labor-market” persons – children, the elderly, house wives, students, etc.

The non-farm public sector includes socially-owned enterprises, public enterprises, state-owned enterprises, budget-financed organizations, UNMIK, KFOR, non-profit NGOs, and other donor-financed entities. The public sector is the largest in terms of its contribution to total labor income (342 million euro). It pays the highest wages (255 euro per month).

The historical heritage, including the most recent -- from the 1990s and that since 1999 -- has resulted in a private sector confined to predominantly family-run small businesses. There are few large-scale private firms. The non-farm private sector comes second high in terms of its share in labor incomes (30%). This income is composed of three parts, almost equal in size, generated by: (1) family businesses, including small firms, with 1-4 workers, (2) medium and large private enterprises with 5+ workers, and (3) the businesses and individuals operating outside of the tax system.

There is still a sizeable amount of income that is not included in Table 2, in particular the undeclared income of workers employed in the officially operating enterprises and income from self-employment. This income is accounted for in the national account system as business income (profit from business activities).

A second way to look at the employment data is to disaggregate by industry. Table 3 provides data on labor employment and income in Kosovo, by economic sectors, according to different data sources. The first column provides the employment data according to the official Business Register (SOK). The register’s figures reflect the numbers provided by the enterprises at the

moment of their registration, not the current employment. Because firms are not required to deregister or make regular updates, these figures also include firms that registered in the past but since have gone out of business or those whose output and employment status has changed. The second column shows the numbers of workers that are reported as employed in enterprises that pay either profit tax or presumptive tax (the firms that are officially registered as tax paying legal persons). The third column shows the data on the number of persons paying wage taxes. Columns 4-7 provide MFE estimates (based on the 2001-2002 labor surveys) for the actual (official plus unofficial) labor employment, thousands of persons, average monthly wage, euro, total annual labor income for the whole Kosovo, millions of euro, and the total income, percent.

Table 3. Labor employment and income, by economic sectors, 2002

	Busi- ness Regis- ter	Ente- rprise tax data	Wage tax data	MFE estimates					
				Employment			Avg wage	Total labor income	
				Thousands of persons			Euro	Mln euro	%
	1	2	3	4	5	6	7		
Total				341.4		636.6	100.0		
Agriculture*	7.4	1.8	2.0	144.8		105.5	19.5		
Total non-farm				196.6	225	531.1	80.5		
Manufacturing	54.1	24.2	27.6	33.0	189	74.8	13.8		
Construction	22.5	5.4	5.0	17.7	211	44.9	8.3		
Transportation and communications	15.7	4.4	4.7	10.4	208	26.0	4.8		
Finance	6.2	2.7	3.2	4.0	277	13.3	2.5		
Trade, hotels and restaurants	72.8	34.6	21.4	45.7	238	130.5	24.2		
Personal services and other	13.5	4.0	4.7	7.3	159	13.9	2.6		
Health			13.0	13.0	143	22.3	4.1		
Education			28.9	28.9	159	55.2	10.2		
Public administration and other			23.5	22.0	204	53.9	10.0		
Donors/NGOs				14.5	551	95.9			

* In the calculation of percentage values the donor/NGOs income was not included.

Sources: [1], [5], [11], [16], and [19]

The last column can be viewed as a rough approximation of the structure of GDP (on its income side). The income generated from the employment in the donors/NGOs sector was excluded from the calculation of percentages, since almost entire income generated in this sector is not classified as “domestic”, but rather as “foreign factor income” and as such is not treated as a GDP contribution but instead as a GNP contribution. Trade and agriculture maintain the largest shares of the Kosovo GDP, about 20-24% each. Manufacturing (14%), education (10%), public administration (10%), and construction (8%) come next. This structure provides a partial answer to the question concerning a relatively low share of domestically collected taxes in the Kosovo General Budget. Trade, agriculture, and construction are, to a significant extent, the “subsistence” branches of the economy. Self-produced food and self-constructed houses account

for most output in agriculture and construction. Many individuals operating in street peddling and small-scale trading activities remain outside of any official registration system.

The share of manufacturing in non-farm activities is relatively low, perhaps the lowest in Europe: one-sixth in employment and one-seventh in labor income.

A related topic to employment is unemployment. Recent estimates of the unemployment rate (those unemployed as a fraction of those who are employed and those who are unemployed) range to as high as 60 percent. These estimates are too high and more reasonable estimates would place the unemployment rate as high as 30-40 percent during the winter months, but less than half of that in the summer months. The reasons for the difference in the estimates are: the surveys upon which the previous estimates were made were conducted during the winter and these estimates included many persons who were not actively looking for a job as unemployed.

The disparity between productivity and wages demanded is also an issue in Kosovo. Recent labor market research has found a large gap between: (1) a relatively low labor productivity (reflected by wages in the private sector), at the level of 50 euro a month or less in the case of unskilled labor, on one side and (2) remuneration expectations of persons remaining out-of-labor-market who were not interested in the jobs that pay less than 150-200 euro per month, on the other side. As a result, labor demand at a wage that equals productivity in the private sector in most cases could not be met. This mismatch provides a partial explanation for the low labor market participation rate (high reservation wage) and low investment (high labor costs).

C. Household Income and Expenditure

Key Aspects

- *Only one half of households' cash income comes from labor and business activities.*
- *Food is the major component of households' budget.*
- *There are some housing investment and commercial investment.*
- *Saturation of consumer durables is high.*

Several surveys, case studies and anecdotal evidence suggest that during the last three years the incomes and consumption patterns of households have not changed much, except: (1) a major upgrade in the quality of residential housing, and (2) increase in the stock of passenger cars and consumer durables, many of them brought to Kosovo as property of returning repatriates or offered by family members as in-kind remittances.

There are about 290,000 dwelling units (houses and flats) in Kosovo and 85-90% of them are occupied. This brings the value of the residential housing stock to about 2.9 billion euro. House construction/reconstruction efforts during the last three years resulted in an augmentation of housing stock by 6-10% a year.

In 2002, total before-tax net cash income of households, private farms and non-farm private enterprises, was estimated at 1,570 million euro: 540 million income from labor, 260 million of other cash income (vaguely classified as "business net income"), 50 million from social transfers

from KGB and 720 million of cash remittances, which included foreign social transfers (especially pensions and other social benefits paid to the former workers by governments of Serbia, Germany, Switzerland, and other countries), labor income of Kosovars currently working abroad (including Serbia), cash gifts provided by foreign residents to Kosovo families, and cash brought to Kosovo by repatriates and visitors. The non-cash, incomes amounted to about 310 million, of which 90 million was estimated as “imputed rent” from residential housing (owner occupied dwelling units). This brings total disposable income (adjusted for in-kind income) to 1,880 million euro, or about 1,100 euro per Kosovo resident (daily income of 3 euro per capita).

A feature of the Kosovar economy is the high saturation with consumer durables, a pattern usually associated with higher levels of development. Table 4 shows the ownership of consumer durables in Kosovo households.

Table 4. Consumer durable saturation, per 100 households, survey data (600 households), June-August, 2002

	Urban	Rural	Total
TV	105	91	95
Video player	54	43	47
Satellite dish	74	65	67
Car	49	54	52
Cellular phone	54	50	51
Water heater	97	58	71
Refrigerator	95	80	85

Source: [5]

Despite the relatively low labor incomes, the available data shows that households in Kosovo acquire quite a large quantity of non-subsistence (“luxury”) goods. Since nearly all of these goods are imported, the tariff is an easily administered way to tax this consumption.

D. Foreign Trade

Key Aspects

- *Trade deficit is very large.*
- *There is little prospect for a significant increase in exports in the near future.*
- *The high level of imports is the main source of government revenue through tariffs.*

Kosovo suffers from a very high foreign trade balance deficit. While exports remain at a low level, imports are very high. As a result, Kosovo may face a serious balance of payments problem already in 2003 as well as during the next several years. The official figures for exports and imports (the components of the merchandise trade balance) are shown in Table 5.

Table 5. Export and import of goods, 2002, million euro*

	Export	Import
TOTAL	27.3	952.6
Consumer goods		522.1
Food	3.8	217.8
Of which: Meat and fish		22.4
Dairy		24.2
Fruits and vegetables		30.4
Non-alcoholic beverages		45.0
Coffee and tea		7.6
Alcohol	1.0	13.6
Tobacco		61.3
Non-food		243.0
Of which: Clothing and footwear		24.4
Furniture		39.6
Appliances (consumer durables)		48.2
Petroleum products (gasoline)		98.2
Intermediate producer goods		64.8
Of which: Fertilizers		15.6
Seeds		15.0
Office supplies (paper)		9.8
Livestock		4.3
Construction materials		151.4
Of which: Cement		25.0
Sand		8.4
Timber		14.5
Ceramic tiles		14.1
Metals	12.4	58.7
Electric and electronic equipment	4.7	27.8
Of which: Computers		7.6
Generators		4.9
Vehicles and spare parts		60.9
Miscellaneous	6.4	55.0

*Commercial imports only, electric power not included, tax-exempt donor import not included

Sources: [1] and [10]

The numbers presented in Table 5 show that Kosovo imports are dominated by consumer goods and intermediate producer goods. Roughly 200-250 million of imported goods can be classified as investment of goods, used by private and public investors. It is estimated that total investments financed by the Budget and donors in 2002 amounted to 270 million euro, most of it spent on imported building materials and equipment. Private sector investments in Kosovo were limited to house construction (225 million euro) and some equipment investment (70 million euro).

In fact, total exports are at least ten times larger than official exports of goods, since they include internal exports (sales of goods and services to foreigners in Kosovo) and unregistered exports, especially re-exports of cigarettes estimated at 50-80 million euro. Even so, the excess imports are being financed by sources of euros that cannot be expected to persist indefinitely into the future.

This pattern is among the most important for tax policy. Because of the heavy reliance of the budget sector on tariff revenues, this sector is dependent on maintaining the current high level of imports until other sources of revenue can be developed.

E. Money and Prices

Key Aspects

- *Inflation is low.*
- *Changes in money supply come from balance of payments.*

The official Kosovo currency is euro. Because the government of Kosovo does not directly control the supply of euros, the introduction of the euro has enabled rapid macroeconomic stabilization after many years of struggle with very high inflation in former Yugoslavia. For example (Table 6), the initial significant increase in prices at a two-digit annual rate (2000) was followed, in 2001-2002, by gradual price stabilization. And in December 2002, the prices were slightly lower than in December 2001. This price stabilization is an important factor for attracting investment.

Table 6. Price inflation: the cost of households' average consumer basket

	2000	2001	2002	2000	2001	2002
BASKET, monthly		Euro			%	
Total consumption	334.44	373.90	387.78	100.0	100.0	100.0
Of which: purchased	249.11	288.73	307.61	74.5	77.2	79.3
Total food	177.75	200.31	209.35	53.2	53.6	54.0
Of which: purchased	123.76	149.86	164.87	37.0	40.1	42.5
Total non-food	156.68	173.59	178.43	46.8	46.4	46.0
Of which: purchased	125.35	138.87	142.74	37.5	37.1	36.8
	2001/00	2002/01	2002/00			
CPI, annual		%				
Total	11.6	3.6	15.6			
Food	12.7	4.5	17.8			
Non-food	10.8	2.8	13.9			

Sources: [1], [5], [7], and [16]

The cost of standard monthly basket of goods and services consumed by a Kosovar family, composed of 6.3 persons, was 334 euro in 2000. This cost was 374 euro in 2001 and 388 euro in

2002. The share of purchased food in total consumption increased from 37% in 2000 to 42.5% in 2002. This increase was a result of two factors: (1) faster increase of food prices – by 17.8% between 2000 and 2002 (the prices of non-food items increased by 13.9%); and (2) decline in aid and gifts. During this period of time the share of self-produced food remained at about 20% of total food consumed.

F. Financial Intermediation, Savings, and Non-Residential Investment

Key Aspects

- *Banking system is undergoing rapid development*
- *Even so, financial system is not likely to help finance much domestic investment in near future.*

The last three years witnessed rapid development of the financial intermediation in Kosovo, especially in the banking sector. The rapid expansion of banking activities is illustrated by the increase in the number of banking units (commercial banks and their branches) -- by almost five times between December 2000 and December 2001 -- and again, at the same rate between the latter and December 2002 (Table 7). The annual amount of inter-bank operations increased almost ten times between 2001 and 2002. During this time, the ratio of bank operations to assets increased six times, from 0.33 to 1.91.

Table 7. Financial intermediation

	2000	2001	2002
Commercial banks, end of year, number of branches	5	24	112
Assets of commercial banks, end of year, million euro	103	518	471
Of which: Commercial credits	6	47	120
Liabilities of commercial banks, end of year, million euro	103	519	471
Of which: Deposits	93	492	427
Of which: Legal entities		169	192
Natural persons		313	228
Demand deposits		344	282
Long-term deposits		138	138
Inter-bank operations, number of transactions		5,124	75,763
Inter-bank operations, total amount, million euro		86	841
Annual average amount of assets, million euro		260	439
Turnover ratio: operations to assets		0.33	1.91
Wire transfers, million euro			
Turnover	468	1,141	1,591
Incoming - gross	293	630	854
Outgoing - gross	175	511	737

Incoming - net	117	119	118
Commercial imports of goods, million euro			
Gross	372	660	953
Net	353	637	925
Ratio: gross outgoing transfers to gross imports, %	47.1	77.4	78.9

Sources: [1], [10], and [13]

The data also suggests that banks processed the payments for an increasing share of imports. A growing number of individuals and businesses have been using banks for diverse financial operations, purchases and sales, cash transfers, etc.

Yet, both the banking system and the non-financial enterprises are still not ready to finance large investment projects in the private sector. During the last three years, there has been little private investment in Kosovo, outside of house (re)construction. About 80% of bank credits are short-term credits, which do not support long-term investments. Most of deposits are demand (“a vista”) deposits.

Rapid increase in bank deposits during 2000 and 2001 reflected, among other things, an increase in the savings of the population. In 2002, a noticeable “U-turn” occurred. While government account balance at BPK (budget cash surplus) increased by 120 million euro, the sum of population saving account balances in commercial banks declined by 85 million euro. It shrunk from 313 million euro at the end of 2001 to 242 million euro at the end of March 2002, and stabilized around 225 million euro since. Obviously, there are several factors that affect population’s bank deposits and withdrawals in Kosovo (including the DM-euro conversion at the beginning of 2002), yet gradual dissaving during 2002 – unlike savings accumulation during the two previous years -- is confirmed by other macroeconomic calculations (such as balance of payments accounts) and household case study research. Anticipated declines in donor activities, in repatriations and in the inflow of diaspora remittances are predicted to trigger further dissavings in 2003-04.

G. The Budget Sector

Key Aspects

- *In 1999-2002 Kosovo General Budget revenues exceeded its expenditures. The situation is likely to change during 2003.*
- *Revenues are highly dependent on imports (border tax collections).*
- *Expenditures of government may increase when additional functions are assumed by Kosovar government.*
- *At present, main potential for increases in other sources of revenues is growth of the domestic economy.*

All of the preceding sheds light on the current situation of the budget sector in Kosovo and the likely changes in its components in the near future. The public sector in Kosovo, in relative terms, is the largest in Europe. It encompasses activities financed from the Kosovo General

Budget, UNMIK budget, donor contributions recorded in the PIP data base, including the activities of NGOs (which are financed in 95% by the donors), KFOR budgets, public and socially owned enterprises. Table 8 presents some rough summary figures.

Table 8. Public sector: total annual expenditures

	2000	2001	2002	2003
	Million euro			
Total	6,262	5,251	4,066	3,086
KGB (Kosovo General Budget)*	204	251	376	438
Of which: Own revenue	43	167	337	413
Donor grants	161	84	39	25
UNMIK**	413	449	388	368
PIP/NGOs***	635	541	292	270
KFOR****	5,000	4,000	3,000	2,000
Public enterprises and SOEs*****	10	10	10	10
	Percent			
KGB own revenue share in total	0.7	3.2	8.3	13.4

* Social assistance transfers not included

** Wages paid to foreigners included only when covered by UNMIK budgets

*** Subsidies to Kosovo General Budget and social assistance transfers not included (rough estimates)

**** Total KFOR budgets (rough estimates)

***** Fixed capital formation financed from enterprises' own sources (rough estimates)

Sources: [1] and [14]

The data for KGB, UNMIK, and PIP/NGOs is based on reports provided by Kosovo Treasury and donor organizations. The total amounts calculated in Table 8 are at the same time both underestimates and overestimates of the true figures. In accounting terms they should be augmented by several hundred million euro, since they do not cover: (1) some activities of foreign organizations which are not registered in PIP; and (2) the costs of aid that are covered directly from the budgets of foreign governments and international organizations, especially remuneration and travel costs of international aid providers and the costs related to Kosovo aid activities incurred in other countries (administration, coordination, etc.). On the other hand, the public sector figures are suspected to over-estimate true expenditures. No thorough macroeconomic research has been undertaken to assess the effectiveness of these spendings (the value of public sector deliveries), which cost in per-capita terms are unusually high (between 2,000 and 4,000 euro per capita).

The data presented in Table 8 shows rapid shrinkage of the public sector. In 2002, its size, measured by its total expenditures, was 4.1 billion euro, as compared to total household consumption of 1.2 billion euro and total private investment, including residential housing, of 0.3 billion. In 2003, the public sector will diminish by almost a quarter.

The Kosovo General Budget includes expenditure of both the Central Budget and the municipal budgets. Its share in the public sector expenditure has been increasing at a high rate. The government consumption and investment (total budget expenditure, excluding social transfers but including subsidies to public enterprises and SOEs) financed from domestic sources was less than 1% in 2000, 3.2% in 2001, 8.2% in 2002 and is expected to exceed 13% in 2003. The expenditure on capital investment has remained at a very level – in 2000-02 it amounted to 0, 7, and 16 million euro, respectively (excluding subsidies to enterprises). A continued gradual reduction in donor subsidies and activities will force KGB's share in financing public sector needs to increase over time.

Given the projected shrinkage of several important sources of euros – donors, cash and goods brought in by repatriates, and remittances -- no increase in cash saving of the population and private direct investment is expected in the near future. Balance-of-payment pressures (due to a diminishing net income stream from abroad) may result in a decline in imports and reduce tax collections. Prudent fiscal policy is needed. The key for establishing long-run sustainability of the budget revenues is the promotion of the development of competitive market economy and private sector activities. This is a large task. More legislative and policy efforts will be necessary to improve the “investment climate” in Kosovo in order to increase commercial construction, investment into machinery and equipment, creation of jobs and income for Kosovars.

Data sources

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- [5] Statistical Office of Kosovo (SOK)
- [6] Ministry of Labor and Social Welfare, Labor and Employment Department
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- [11] Tax Administration
- [12] Ministry of Labor and Social Welfare, Social Welfare Department
- [13] Banking and Payments Authority of Kosovo
- [14] Ministry of Finance and Economy, Donor Coordination Unit
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- [18] United Nations Population Fund (UNFPA)
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- [20] Ministry of Finance and Economy, Property Tax Unit