



# Kosovo Monthly Economic Briefing

May/June 2006

## The Budget Process 2007 - full speed ahead

- The Kosovo authorities are already busy with the preparation of the 2007 Kosovo Consolidated Budget. After the heated debates on the 2006 budget, the Ministry of Economy and Finance has already issued two budget circulars to the ministries in preparation of the 2007 budget. As was the case in 2006, the overall expenditure ceiling is set out in the Letter of Intent that the authorities signed last year. This ceiling presupposes tough policy measures to deal with the hard budget constraints that Kosovo will face in 2007. The 2006 budget featured an agreed €44 million deficit, with slightly optimistic revenue projections of €656 million and expenditures capped at €700 million. One of the main policy decisions in the Letter of Intent was the commitment not to increase expenditures over the medium term (MTEF 2006 – 2008) by more than 0.5% annually in real terms. Taking into consideration declining prices, the authorities are therefore aiming at an expenditure ceiling of €685 million in 2007. The first budget circular was issued in March, and following a government meeting on priorities, the MEF issued another budget circular in June with budget ceilings for budget organizations for recurrent spending. For the first time this year, capital expenditure funds will be “up for grabs” for all budget organizations: in previous years, all budgetary organisations had individual ceilings for capital expenditures as well. Capital submissions, which will have to go through the previously established PIP process, will be evaluated based on the quality of the submission and their coherence with government priorities. The government is also preparing the Kosovo Development Strategy and Plan for the period 2007 – 2013 which should guide the Medium Term Expenditure Framework and the annual budget process, in terms of policy direction and priorities. The budget hearings are scheduled for September, appeals for October, and the final budget proposal, according to the Law on Public Financial Management should go to the parliament on October 30<sup>th</sup>, 2006.

- The Macro Unit at the Ministry of Economy and Finance publishes its first Quarterly Bulletin** - The re-established macroeconomic unit at the Ministry of Economy and Finance resumed its activities at the beginning of this year and immediately started publishing its first Quarterly Macroeconomic Bulletin. This kind of reporting, although in different format, was done by the ministry in 2003 and 2004. The report, covering the first quarter of the year 2006, presents the macroeconomic situation in Kosovo. The report aims to inform the public about the main economic developments in Kosovo. The report looks at the real, fiscal, financial and external sectors. According to the report, economic activity in the first quarter of 2006 has been fairly stable. As such, conditions are in place for the IMF projected growth of 3 percent. The Ministry also states that the fiscal situation, in both revenues and expenditures is in line with the budget projections, although revenues have been slightly less than in the same period last year, while expenditures have increased moderately. In the financial sector, one of the important conclusions is that the assets of the banking sector have increased by 4.5 percent compared to the end of 2005, while loans have increased by 8.1 percent. The external sector still represents one of the biggest challenges in the economy of Kosovo. While exports have increased, and there is a moderate decrease in imports, export coverage of imports is still only 6 percent. The MEF macro unit is expected to continue this kind of reporting on quarterly basis throughout the year. The Banking and Payments Authority of Kosovo (BPK) also produces a monthly bulletin of statistical information focusing on the financial sector.

### Key Statistics - at a glance

	2006						
	2002	2003	2004	2005	Feb	Mar	Apr
GDP (% change)	-2.4	-0.1	4.0	-0.2	..	..	..
Reg. unemployment	282.3	282.3	302.0	319.7	321	323.4	324.1
CPI (SOK)	..	1.6	-2.5	2.6	3.2	1.8	2.5
Fiscal balance (€mn)	106.4	62.6	-134.3	-67.8	-5.6	1.9	..
Exports (€mn)	27.6	35.6	56.5	48.9	3.9	7.2	8.0
Imports (€mn)	854.8	973.1	1,063.20	1,180.0	73.6	99.3	109.7

Note: Monthly fiscal balance, export and import figures are non-cumulative.

SOK (CPI) is % change year-on-year (e.g. Oct 2004 is change from Oct 2003 to Oct 2004). Registered unemployment in thousands.

Source: BPK, SoK, MFE, Kosovo Employment Office and IMF staff estimates

### Main KCB numbers since 2002

	2002	2003	2004	2005	2006 (b)
Revenues	535.7	630.7	635	628.3	656
Expenditures	428.6	567.7	769.9	696.1	700
Surplus/Deficit	107.1	63.0	-134.9	-67.8	-44.0

Note: b stands for budget regulation as approved by the parliament

2007 expenditures represent the ceiling based on the letter of intent

Source: Ministry of Economy and Finance



## Kosovo Development Strategy and Plan

The governing authorities of Kosovo are currently working on the preparation of the Kosovo Development Strategy & Plan (KDSP) with the active participation and support of civil society, international organizations, and the donor community. The KDSP represents a vision of Kosovo's development for the period 2007 – 2013. Having in mind the objective of sustainable development and EU integration, and taking into consideration the limited fiscal envelope, the preparation of such a planning mechanism is very timely. The KDSP will include a vision statement built on civil society discussions, a development strategy including sectoral strategies and cross-cutting issues, and a macro-economic framework based on these.

KDSP Technical Working Groups	
Agriculture and Rural Development	Private Sector Development
Housing and Construction	Tourism
Telecommunications and ICT	Poverty and Social Policy
Water Supply and Sanitation	Labor Market and Unemployment
Regional Development	Local and Central Administration
Environment	Justice and Police
Spatial Planning	European integration
Energy	Health
Mines	Culture, Youth and Sports
High Value added sector	Minorities
Transport	Gender Issues
Education, Science and Technology	

### Twenty Three Technical Working Groups

The KDSP aims to be the first post-conflict document to take a realistic and coherent approach to Kosovo's overall development by mobilizing all of the professional capacities, institutional resources, civil society, and interest groups in Kosovo for an overarching vision for future economic and social development while ensuring domestic ownership. Objectives, identified in the KDSP Terms of Reference and approved by the government in July 2005, include sustainable economic growth, increasing employment, reducing poverty, increasing competitiveness, building strategic planning capacity, adopting of EU standards, and the clear identification of goals and objectives, as well as policies needed to reach them for the period 2007-13. The KDSP should be used as a guide in the development of the Medium Term Expenditure Framework including a detailed Public Investment Programme for the years, 2007-09. The KDSP is assumed to be living document that stimulates policy debate within the government, civil society, and amongst key stakeholders, in order to serve as a consensus-building mechanism on Kosovo's development.

The KDSP process is led by the Prime Minister and an Inter-Ministerial Group, and is assisted by international organizations and the donor community. A KDSP Secretariat was established in January 2006 to coordinate and manage its preparation. In collaboration with international experts and funded by the PISG, DFID, SIDA and other donors the work has been grouped into three areas: (i) a process of consultation with civil society, ii) a macro-economic framework, and (iii) 23 Technical Working Groups covering individual sectors and cross-sectoral issues. The consultation process involving all sectors of civil society at the local, regional and Kosovo-wide level will result in the definition of a vision for Kosovo development. After the draft of the document is prepared there also needs to be a mechanism to discuss the findings once more with the wider public. A first draft of a macro-economic framework, representing one of the main pillars of the KDSP, was issued at the end of June for discussion and comments. Technical Working Groups are producing strategy papers and sectoral policy statements in collaboration with civil society, which product will be integrated in the vision and the macro-economic framework. After the preparation of the outputs of the TWG's, the process of prioritization will take place. Taking into consideration the fiscal and macro challenges for Kosovo in the coming few years, prioritization is of crucial importance. While the first draft is expected sometime in October, the final draft of the KDSP is expected to be launched by the Secretariat in November/December 2006.

One of the main challenges facing Kosovo is establishing sustainable growth and stabilizing the fiscal situation in the face of declining donor assistance, stabilizing remittances, slow private sector development, and limited access to external borrowing. A likely resolution of the political status could potentially subject Kosovo to increased fiscal costs as a consequence of inherited obligations to service foreign debt. This, combined with the additional takeover of responsibilities previously in the hands of UNMIK, could result in a severe post-status fiscal shock. Thus, in order to address these issues, the KDSP must be linked to the budget process, including the Public Investment Program and the Medium Term Expenditure Framework (MTEF). The KDSP must also facilitate a comprehensive process that puts together all sectoral strategies, prioritizing them and then adhering to the priorities. In order to get donors' support in the near future, Kosovo must present a clear set of reforms that puts it into a path of sustainable growth and EU integration. KDSP provides an excellent opportunity to do so.