Assessing the Impact of the Ukraine Crisis on Kosovo

An Exercise in Strategic Foresight Including Scenario-Based Projections

December 2022

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EXECUTIVE SUMMARY

1. Kosovo[1] finds itself at several crossroads, all of which demand complex policy, institutional, and investment decision-making within a volatile regional and global economy. What makes the challenge of addressing both structural imbalances and exogenous shocks even more challenging, are the uncertainties related to the war in Ukraine, and future growth, revenue, and employment outcomes are already being revised down. In this context, this research presents a diagnostic analysis of the current impact of the Ukraine crisis on various factors, from GDP to remittances, energy to food inflation, to the changing composition of institutional spending, while also rolling out several scenarios for 2022 – 2026 period, to concentrate debate on critical issues.

2. This report looks at the impact of the war in Ukraine on current and future energy, food, and material prices as well as growth, and fiscal and institutional spending futures. These futures speak to the following major crossroads facing the central institutions in Kosovo, during the winter with significant energy challenges.

- **Energy and Green Transition Crossroad**: At a time when energy security is a primary agenda for Kosovo, with Kosovo remaining heavily dependent on elderly coal-based production systems, the EU is moving stridently forward with the EU Green Agenda and decarbonization. While the recent € 1 billion package from the EU to support the energy transition in the Western Balkans is helping the transition forward, the energy transition will shine a light on fiscal space limitations and lack of capital spending, at the same time as leading to higher energy prices, particularly affecting the poor.

- **Per Capital Income Crossroads**: Over the past 25 years, per capita income in Kosovo has increased more than 900 % - from about US$400 in 1995 to over US$4,000 in 2022. Despite this progress, however, per capita income is still only 12 % of the average EU member state or 20 % of aspirational peers. Raising incomes can only occur with greater productivity, increased innovation, improved competitiveness, improved market integration (for energy, but also trade) and a strong foundation of tax and non-tax incentives. Failure to elevate incomes will continue to be a push factor for youth to go abroad (principally Germany, Switzerland, and the US). Kosovo is caught in an upper-middle income trap where the opportunities it has used to get ahead now holds it back from bouncing forward.

- **Agenda 2030 and Poverty Crossroads**: While the average wage in Kosovo is around €500 per person per month, the minimum wage is half of that, with many living below the poverty line. Meeting Agenda 2030 goals and eliminating poverty through inclusive and equitable growth can only be met through adopting a progressive reform agenda with targeted social protection, creation of green jobs, etc., to leave no one behind. While growth outturns have historically been good, they are insufficient to overcome the upper-middle income trap, elevate people out of poverty, and address unemployment challenges, which have a strong gender bias.

[1] References to Kosovo shall be understood to be in the context of United Nations Security Council resolution 1244 (1999).

- **Fiscal Space Crossroads**: In ramping up social and energy subsidies, capital spending has been reduced, further impacting future growth outcomes (as noted by financial institutions adjusting down growth projections). While the 2023 Kosovo budget projects a reduced budget deficit by 2025, the current budget deficit does not detail how the energy and digital transitions, or Agenda 2030 are to be financed with costs beyond the current fiscal capacity of central institutions. At a time when global capital tightening to combat inflation is leading to higher borrowing costs, and with fully costed transitional plans that would likely cost tens of billions of €, the debt and equity mix of future investments become of great significance. Down one road lays a balanced budget with limited reform and low capital spending, and down the other path lays improved growth outcomes matched by continued deficits and growing debt.

3. Maintaining a virtuous inclusive growth and investment cycle – mitigating the risks of falling into a vicious cycle of under-investment leading to low growth, revenue, and social dividends – requires setting policy based on evidence. To this end, the research findings presented here, and the scenario-based projections are devised to stimulate debate and to encourage discussion on how best to navigate the various transitions/crossroads, strengthening the data foundation, particularly for impacts at the household level will be key to success. In this regard, the 2017 Household Budget Survey should be updated to provide a more robust picture, following the events of the COVID-19 pandemic and war in Ukraine.

4. Though research findings highlight that in general Kosovo has so far remained very resilient to the impact of the war in Ukraine, with remittances for example increasing to historical highs, as the data highlights, likely the biggest impacts of the war in Ukraine are yet to come. While energy prices have increased massively, recent supply-side restrictions (both in terms of domestic energy generation and the regional energy deals), as well as the long winter, bear the risk of further elevating prices with negative impacts on both productivity and human welfare. The impact of energy price inflation as a result of supply-side shocks is an economic pinch point that will lead to negative GDP outturns, unemployment and poverty, given Kosovo's limited ability to outcompete European economies in energy bidding. With Europe's commitment to decarbonization and moving towards an alternative energy mix, navigating the energy transition in the context of growing debt, capital tightening and a fiscal and budget deficit will require greater fiscal space than currently available as the fiscal rule sets the ceiling of deficit at 2% of GDP. The International Monetary Fund (IMF) agreed to an exception during the pandemic, but the return to rule will happen 2023.

5. As highlighted in the summary of key socio-economic impacts recorded so far (see below), the crisis has already negatively impacted energy and food prices and increased the budget deficit with expenditures growing faster than revenues, particularly due to energy subsidies and social contributions and benefits. Though GDP and remittance outturns have continued at a positive trend, the increase in household spending due to food and energy inflation is already estimated at 9-18 % for different income groups, and this is set to increase with winters, with pressure on energy prices combined with supply side (and shorter supply chains) constraints leading to possible load shedding. Increasing subsidies – as occurred during COVID-19 – appears to expose worrying trends where domestic amplifiers to external shocks are eroding growth, revenue, and expenditure outturns while putting increased pressure on domestic debt.

6. While the Concluding Statement of the 2022 Article IV Mission states that stronger fiscal revenues have allowed the central institutions to cushion the impact of the terms of trade shock on households and firms, while also replenishing its liquidity buffers, lower growth forecasts from the World Bank and OECD call for a high degree of caution going into 2023. The key socio-economic impacts reported in the table below based largely on Q3 outturns reported by the Kosovo Agency for Statistics provide evidence of the impact of the war in Ukraine on Kosovo.

Key Socio-Economic Variables	
Impact Variable	Year-On-Year Impact
Energy Inflation	The inflation rate for July 2021 - July 2022 of fuels and lubricants for transport equipment was 44.1% and solid fuels, firewood, and pellets 43.5% though these exclude electricity prices. For November 2021 – November 2022, solid fuels, firewood, and pellets had a rate of 43.7% whereas fuels and lubricants for transport equipment was lower at 21.3%.
Energy Inflation Gross Domestic Product	While GDP outturns for Q1-Q3 have shown resilience the international financial institutions (IMF, WB) have adjusted their GDP growth projections downwards as the year has gone by. Already in May 2022 the IMF estimated impacts of energy and food on Kosovo's imports could be as high as 5.5% of GDP.
Institutional Revenues	Total general revenues increased 3.5 % from €673.9 million in Q3 2021 to €697.5 million in Q3 2022, with the IMF reporting that stronger fiscal revenues have allowed the central institutions to cushion the impact of the terms of trade shock on households and firms, while also replenishing its liquidity buffers.
Institutional Expenditures	Total general institutional expenditures increased by 16.9% from €526.9 million in Q3 2021 to €615.9 million in Q3 2022.
Kosovo Subsidies	Total Kosovo subsidies increased by 233.9% from €42.2 million in Q3 2021 to €140.9 million in Q3 2022, largely resulting from increased electricity subsidies and increased social protection spending. The European Commission granted € 75 million to Kosovo to support vulnerable households and businesses during the energy crisis in the short term (1-3 years).
Social Protection Spendinga	Total social protection spending increased by 11.4% from €134.7 million in Q3 2021 to €150.1 million in Q3 2022.
Import Price Index	Compared to Q3 2021, import prices increased by an average of 17.5% in Q3 2022.
Remittance Flows	Compared to Q3 2021, import prices increased by an average of 17.5% in Q3 2022.
Household Cost of Living Changes	The combined effect of the rise of energy and food prices can be estimated between 9.5% and 18% of the household budget.
Trade Balance	The trade deficit increased from €361.1 million in November 2021 to €401.4 million in July 2022, an 11.2% increase. Moreover, the export of goods in November 2022 was valued at €73.9 million, while imports were valued at €475.4 million, which is an increase of 4.6% for exports and 10.1% for imports, compared to the same period of 2021. Both exports and imports with the EU increased by 32.3% and 7.8% respectively.
ODA Flows	Though no data on ODA flows is not yet available for 2022, given the re-purposing of ODA by development partners to deal with the Ukraine crisis dealing with the over 9 million refugees, ODA/OOF flows for critical reforms for 2023 are likely to come under increasing pressure, impacting reforms such as those outlined in the Economic Reform Programme (ERP).

7. Building from the vulnerability and resilience context outlined in section 2, section 3 provides a concise overview of the transmission challenges, key transmission factors such as price shocks or impact on exchange rates, as well as domestic amplifiers. External factors amplify existing domestic strengths, vulnerabilities and resilience to changes in the economy, leading to both episodes of growth accelerations and reversals. Domestic amplifiers are policies and existing structural attributes that amplify or mitigate the effect that shifts in external conditions may have on growth and accumulation patterns in the Kosovo socio-economic system. In many cases, these amplifiers act as accelerators of change (both positive and negative).

8. Section 4 provides a deep dive into the key data essential for mapping impact and informing the scenarios and projections made, for different variables. These cover – in relation to framing social impacts – quantification of household income baselines, sources of household income and what is known about household consumption by different income groups. While the data and analysis draw largely from the 2017 Household Budget Survey, the research notes that both COVID-19 and the current crisis make that baseline a poor reference point for extrapolating findings. While assumptions could be applied, the reality is that updating the Household Budget Survey in 2023 will be essential to fully understand the impact of the war in Ukraine and future energy transitions on vulnerable households.

9. The report also documents changes in energy and food prices, changes in remittances, impact on GDP and the trade balance, changes to revenues and expenditures and commodity and produce prices. The analysis provides the basis for developing several key strategic foresight narratives as outlined in section 5, as the basis for developing the five variable projections as outlined in section 6. These projections cover (i) food price inflation (ii) energy price inflation (iii) material price scenarios (iv) growth and fiscal scenarios and (v) institutional spending scenarios. Projections draw from historical trends and make explicit assumptions, as summarized below:

- **Scenario 1 (10-year average)**: Current trend continues (inflation), and institutions maintain stability (continues at the trend over the past 10 years). Projection uses average price change since 2011.

- **Scenario 2 (2021 price Change)**: Inflation continues to worsen, recession, collapse in institutional spending (accelerates at 2021 rate). Projection uses price change 2021.

- **Scenario 3 (Average 2014-2018)**: Return to pre-war in Ukraine trends post-COVID-19 pathway (resumes past 5-year trend before COVID). Projection uses the average of 5 years before COVID-19 (2014-2018)

10. The projections highlight several worrying trends that have been forming for some time but have been elevated and/or accelerate as a result of COVID-19 and the Ukraine crisis. In most cases, the 10-year trend confirms growth challenges, growing remittances, increasing domestic debt, increased cost of borrowing, imported food price inflation and other commodities due to lack of domestic productive capacities, a reduction in gross fixed capital formation and an increasing burden of Kosovo subsidies and social protection/welfare spending. Future revenue and expenditure management will benefit from increasing public investment and public finance efficiency (both operational and allocative) with a coherent development finance approach. Underinvestment in the emerging digital economy, in Agenda 2030 priorities, research, development, and innovation, as well as lack of deepening of both financial and capital market, are impeding both resilience and growth outturns. These trends, allow the following broad conclusions to be drawn:

- **Updated data on poverty rates and the impact of inflation on households should be central to future policy decisions**: Findings show that higher food and energy import prices have led to increased inflation, negatively impacting households' real disposable income, and impacting both consumption patterns and levels of saving. Given the risks of decarbonization-elevated energy costs when inflation is eroding savings and the values of incomes, balancing future transitions to protect those being left behind requires clarity on how to target these effectively.

- **Future Growth, Fiscal and Debt Projections Would Appear to be Unrealistic**: The IMF predicts that half of the Euro zone countries are heading for recession as a result of the energy crisis, and given the need to combat inflation, tightening financial conditions are set to continue into 2023 and beyond. Even if Kosovo follows a counter-cyclical investment cycle, given increased social and reduced capital spending, increased spending can only be maintained by increasing debt levels (even if they stay below the current legal ceiling of 30 % of GDP) and running bigger budget and fiscal deficits. Gains in formalization and increased tax collection will also create downward pressure on businesses, at a time of increased energy spending and commodity prices.

- **Capital Spending on Public Investment and Private Flows Must be Ramped Up**: To successfully negotiate the energy and other normative agenda transitions (digital economy, Agenda 2030, etc.) and to overcome the middle-income trap, capital spending is going to have to increase, as is the mobilization of private capital. Gaps in physical and social infrastructure remain significant, limiting foreign direct investment. With EU funding for the Green Agenda to form just part of a new mix of flows, new blended financing and sustainable financing instruments are going to be needed. Many of these will require the new EU Green Taxonomy to be adopted alongside standards for green and climate bonds. Accelerating financing for critical transitions will also require new financing instruments to be deployed. New debt instruments – such as "State Contingent Debt Instruments" (SCDIs) and GDP Linked Warrants should be explored.

- **Only A Virtuous Cycle Can Avoid Worsening Debt Futures**: Given worsening economic conditions in Europe, compounded by Kosovo being limited in managing key areas of its economy as a result of its status, rates of return on public investment must significantly improve, and new streams of investment will be required alongside accelerated reforms. To address energy insecurities, a more reliable and greener electricity supply has the potential to reduce fiscal and business costs while also enabling Kosovo's contribution to a decarbonized future now made essential for European integration. Not only does this mean that programs to mitigate the impact of rising energy costs need to be temporary and targeted, but it also means that central institutions need to balance addressing short-term issues while still investing in necessary longer-term transitions. While the new law regulating public wages (to begin its implementation in 2023) will only marginally increase wage costs, increasing social and energy subsidies, other contingent liabilities and lower growth outturns must be managed through a policy of increased investment, linked to better investment planning and increased absorption.

11. The impact of the Ukraine crisis merely exposes the vulnerability of Kosovo and Europe to both energy and food security shocks, though changes in trade composition are noted. While the impact on remittances and GDP has yet to be fully felt (Europe-wide economic downturn is expected), the impact on the poorest household's micro, small and medium enterprises has already been large, but can only increase. With the institutions having already allocated €100 million to offset the costs of energy increases to the poorest households, as shown with the increase of subsidies highlighted above, the cost of minimizing the human and business cost can only lead to greater indebtedness and an expenditure budget adjustment that institutions would rather not make, in the transition out of COVID-19.[2] In October 2022, the EU also committed to providing €75 million direct budget support to reduce the impact of elevated energy prices on Kosovo, focused on targeting vulnerable businesses and households.[3]

12. The impact of the war in Ukraine will not be fully known for some years, with the winter of 2022/2023 likely to be one of the most challenging on record. GDP losses (as already noted by several financial institutions adjusting down growth projections during the year), increased expenditure needs for energy and food subsidies, and social protection could easily be in a similar order of magnitude to the resources needed to combat the socioeconomic impact of COVID-19. International financing institutions, the EU and bilateral partners will need to continue to provide both fiscal support and incentives to secure the implementation of the Green Agenda, during a period where Kosovo must carefully transition down several crossroads, towards a more virtuous, inclusive, and decarbonized growth future.

[2] The Gap Institute reports that "Kosovo has allocated €100 million to support citizens mostly with one-off payments of €100 each for all employees, pensioners, and students. The central institutions have subsidized electricity with over €120 million, to provide relief to citizens, especially those most in need; allocated funds to increase public reserves; amplified subsidies for key agricultural crops and introduced oil excise subsidies for farmers". See https://www.institutigap.org/documents/20407_Impact%20of%20the%20war%20in%20Ukraine%20on%20Kosovos%20Economy.pdf
[3] https://ec.europa.eu/commission/presscorner/detail/en/STATEMENT_22_6422

1

INTRODUCTION

13. Following the socio-economic upheaval caused by the COVID-19 pandemic, in February 2022, war broke out in Ukraine, sending further shockwaves across the world, throughout Europe and the Western Balkans. While the early impact of the war was initially localized to Ukraine's immediate neighbours – with approximately 8 million refugees having left Ukraine for other European countries as of 10 January 2023 – the war has led to a major schism in international affairs, foreign, security and trade policy. The war has also had a profound impact on inflation, as well as military spending and public debt.

14. The war in Ukraine broke out at a time when global energy prices were already increasing and central banks were advancing capital market tightening to offset inflation caused by a surge in quantitative easing, to deal with the COVID-19 pandemic. For Kosovo, like the rest of the Western Balkans, direct, indirect and induced impacts spilt out beyond the economic domain, leading to an increase in tensions with Serbia.

15. On the socio-economic front, the impact of elevated oil and food prices, among other factors, has had a deleterious impact on the cost of living, hitting the poorest quintile of the population particularly hard. While the central institutions' fiscal position and remittances have remained buoyant, the war in Ukraine has led to a deep energy crisis in Europe at the beginning of what was to have been the EU Green Deal and a major new push to secure the Paris Climate Agreement. Though European countries are often energy exporters in summer, in winter when end usage increases substantially, marketable surpluses collapse and the cost to consumers elevates, in the case of 2022, substantially. While food prices have been elevated by various factors, the impact of rising costs of energy hits every industry and market hard, at a time when Kosovo has just bounced back from the pandemic with growth making up for more than the pandemic-related losses in 2020. The public response has been to increase targeted subsidies and to strike new energy and food deals, and while this research highlights the impacts of the Ukraine crisis on Kosovo, there is a long winter ahead.

RESEARCH RATIONALE AND APPROACH

16. Given that the research focuses on quantifying the various impacts of the war in Ukraine on the socio-economic well-being of people in Kosovo, the basic premise for the assessment method is that while the shocks are exogenous (albeit accentuated by pre-existing vulnerabilities) they also have significant domestic amplifiers; in that, they are aggravated by domestic factors, given lack of resilience to energy and food shocks in particular. In terms of setting baselines for the period before the war in Ukraine (31 December 2021) is selected as the basis for assessing departure from the trend.

17. A large number of potential transmission factors (See Table 1 below) – set against the probability of risks being actualized – underlines the importance of identifying which factors

– and the interplay between factors – are likely to impact Kosovo. For example, at a time when global official development assistance (ODA) and humanitarian aid are being re-purposed to respond to the impacts of the Ukraine crisis, the availability of financing for ongoing reforms such as those related to Agenda 2030 are likely to be negatively impacted. This leaves the Kosovo institutions more exposed than previously, as they navigate new and complex social and economic challenges, including new rounds of energy subsidies to substitute for an increased cost of living among the poorest members of society. Impact on militarization, polarization, and new strategic alignments in the Western Balkans, including between non-state actors, remittances and other factors must be carefully mapped into 2023 and beyond.

18. While the range of transmission factors, channels and domestic amplifiers outlined in Table 1 below demonstrate the complex interplay between factors (i.e., elevated energy prices can increase the cost of subsidies squeezing out other important social spending etc.), as the outcome of this support is to be translated into practicable and actionable recommendations, this assessment balances complexity with simplicity. If the analysis is too complex and academic, it will have limited application in the real world. However, if an overly generalized (simplified) approach is taken, research results will not be specific enough to suggest institutional policy responses. Given the lessons learned from the Kosovo institutions' management of COVID-19, preparing in advance by pre-positioning resources to protect the vulnerable with lower incomes and businesses from the harsh winter ahead is necessary.

RESEARCH OBJECTIVE AND SCOPE

19. The objective is to undertake an evidence-based assessment of the impact of the war in Ukraine in Kosovo, drawing from relevant data sources, to disentangle the policy support implications and options available to the authorities and development partners. This assessment focused on quantifying the impact of the crisis on **rising fuel, energy and food prices,** changes in **economic outturns and remittance flows, household consumption and vulnerability, trade balance and fiscal costs,** and to the extent possible on the impact on ODA flows.

METHODOLOGY AND LIMITATIONS

20. Ideally, macro-economic modelling could be undertaken based on a General Equilibrium (GE) model to capture the structure of the economy and behavioural response of agents (firms, households, institutions), from the application of a given policy (e.g., import tariffs or taxation). However, among other factors, data limitations present a problem in establishing a robust GE model from which to draw analysis.[4]

21. The approach adopted has therefore been to collect all data points for key variables from the Central Bank of Kosovo (CBK), Kosovo Agency of Statistics (KAS) and Ministry of Finance, Labour, and Transfers (MFLT) for the period pre-31 December 2021 up until the end of Quarter 2 (Q2) and where available Quarter 3 (Q3), as the basis for documenting trends

[4] The use of GE models is limited when data is unavailable or when the following assumptions do not apply: (i) there is perfect competition both in the commodity and factor markets (ii) consumer tastes and habits of consumers are given and constant (iii) incomes of consumers are given and constant and (v) when factors of production are perfectly mobile between different occupations and places (v) there are constant returns to scale (vi) all firms operate under identical cost conditions (vii) all units of a productive service are homogeneous (viii) there are no changes in the techniques of production and (ix) there is full employment of labour and other resources.

in performance of the variables. The data, alongside other diagnostic work, has allowed the primary transmission channels, factors, and domestic amplifiers to be documented, including an assessment of prior and proposed institutional policy responses.

22. Direct impacts as a result of the war in Ukraine (i.e., food price hikes, the risk and impacts of secondary sanctions etc.) are documented and quantified to the extent possible, using primary transmission factors and channels as the points of enquiry. Indirect impacts (i.e., trade restrictions, broader commodity price inflation and supply chain constraints etc.) including the impact of local industries buying goods and services are documented where data is available. Induced impacts are the response by the Kosovo institutions to an initial change (direct effect) that occurs through re-spending or re-allocation of the budget. For example, this can be changes to taxation, and subsidies as the crisis can have spill over impacts on ODA and public welfare programmes, impacting poverty rates, as well as having wider impacts (backward and forward linkages) with specific sectors and populations.

23. The research has also taken the 2017 data from the Living Standards Measurement Study (LSMS) and assessed the likely impact on households' incomes, among other factors. The outcome is a hybrid diagnostic approach that is not a GE/PE model per se, though impacts are modelled, and trends documented. The results are presented in sections 3, 4 and 5 below, with section 6 providing strategic foresight, horizon scan and scenarios, and section 7 providing recommendations to the Kosovo institutions on likely impacts and what will need to be done to manage and mitigate, in the worst-case scenario.

2

EXISTING VULNERABILITY AND RESILIENCE

The economic implications of the war in Ukraine risk to further undermining inclusive growth and social equality and place increase pressure on a social protection system that needs strengthening. Fostering social inclusion and combating poverty are also core values of the EU's multilateral agenda, and social market-based solutions, therefore, need to be identified for those being left behind. Despite the sizeable increase in social protection spending in 2022 (though social protection spending is still low by EU standards), the targeting of allocations to beneficiaries needs to be improved to reduce the risk of growing inequality.[5] While reforming the social protection system will take considerable effort, the increase in subsidies and spending as reported as a result of energy insecurity justifies a greater focus on more inclusive growth, and further developing employment and labour market policies, as well as unifying the pension system.

24. An important source of existing vulnerability is the high reliance on European economies, and the constraints on discretionary macroeconomic (particularly monetary/exchange rate) policies. The status of Kosovo, and the consequences thereof – not least the absence of a credit rating – are factors holding back the emergence of a strong economy. While improving connectivity within the Western Balkans, as well as between the Western Balkans and the EU, can assist in driving growth and employment, dealing with the impact of COVID-19, followed by a rebound and now dealing with food and energy inflation, undermine capital spending to support further integration. As a result, over the past 25 years, per capita income in Kosovo has increased more than 900 % from about US$ 400 in 1995 to over US$ 4,000 in 2022. Despite this progress, however, per capita income is still only 12 %of the average EU member state or 20 % of aspirational peers.[6]

25. With regards to the impact of transmission factors outlined in Table 1, including sanctions, inflation, depreciating € and changing trading context, there is a potential for challenges to social cohesion and counter claims on the social contract, as well as a risk of fragility and potential for violence. In 2019 the World Bank identified three main resilience-related risks, as follows:

- Economic and political disenfranchisement, especially among the youth.
- Unresolved issues with Serbia and interethnic relations, and,
- Motives and actions of various political actors capitalizing on structural drivers of fragility.

26. According to the World Bank, Kosovo's poverty rate (measured at US$ 5.5/day, 2011 PPP) decreased from 21.6 % in 2017 to an estimated 16.7 % in 2020, thanks to a sustained positive economic performance (growth averaged 3.4 % annually over the period 2012-2017).

[5] https://www.worldbank.org/en/news/press-release/2022/03/22/-a-better-social-protection-system-can-help-kosovo-promote-human-capital-foster-productivity-and-reduce-poverty

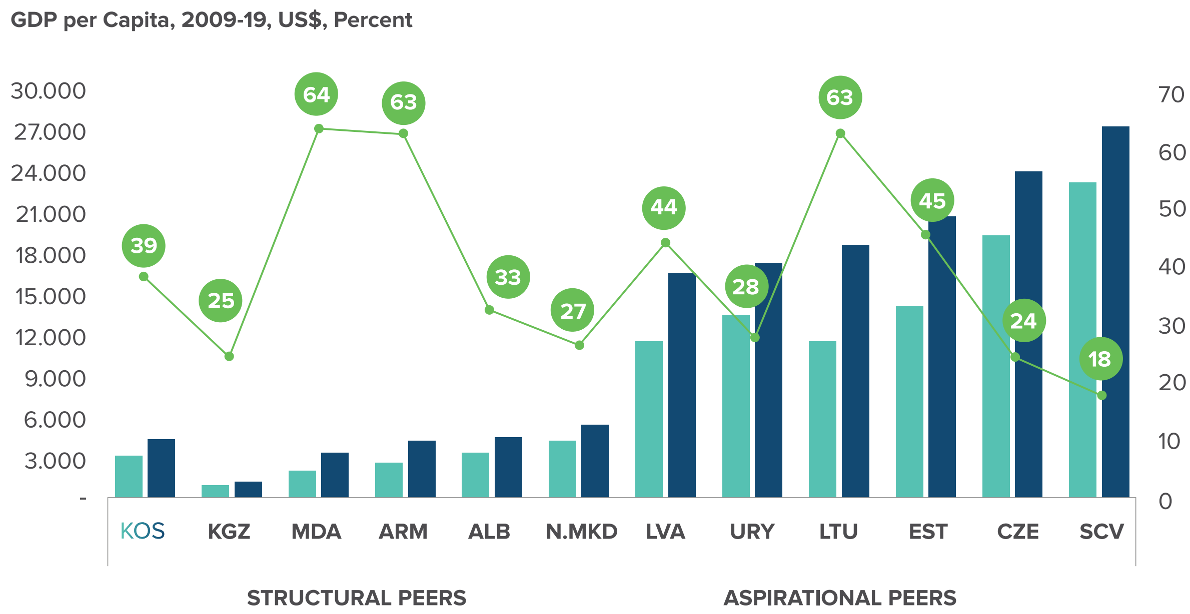
[6] https://www.worldbank.org/en/country/kosovo/publication/kosovo-cem

Analysis of poverty drivers between 2012-2017 suggests that an increase in earnings significantly contributed to a reduction of 6 percentage points during the period since labour is the primary source of income for people with a lower income. According to the “Strategy for the Prevention and Combating of Informal Economy, Money Laundering, Terrorist Financing and Financial Crimes 2019-2023”, the informal economy in Kosovo was estimated to be 31.7 % in 2017 (no later assessment has been done). With one of the highest informality rates in Europe, the size of the shadow and informal economy certainly impacts institutional revenues but also impacts social protection. Moreover, given that the labour force participation continues to be chronically low at 40.6 % of the working-age population in Q3 2021, and that poverty and unemployment increased as a result of COVID-19 and the economic lockdown, historically high inflationary pressures almost certainly increased poverty rates and reduced employment opportunities. These factors influence the policy implications of the findings presented in this report.

27. According to the World Bank, Kosovo’s income per capita is only 12 % of the average EU member or 20 % of aspirational peers (Latvia, Estonia, Lithuania, the Czech Republic, and Slovenia), the current crisis risks recent progress in lifting people out of poverty and increasing incomes towards so-called aspirational partners (see chart 1 below). Addressing growth, income and unemployment requires investment in firm and farm productivity, human capital, exports, competition and investment and macro-economic stability and sound governance. The impact of current crisis negatively impacts many of these areas.

Chart 1. INCOME GAP BETWEEN KOSOVO AND ASPIRATIONAL EU MEMBERS

Source: World Bank, “Kosovo Country Economic Memorandum, June 2022”



28. Drawing lessons from the institutions’ COVID-19 response plan are important, given that the energy crisis can only get worse (particularly given the aged power-generation infrastructure) and even if price inflation falls for food and other staples, the price of energy will impact the entire economy, and in particular the purchasing ability and habits of the poorer parts of society. The various transmission channels, factors and domestic amplifiers developed below, provides insight into how impacts are transmitted in practice.

[7] https://mf.rks-gov.net/desk/inc/media/0211B611-A5EB-45F5-BE19-45A408D1DFA8.pdf
[8]https://databankfiles.worldbank.org/data/download/poverty/95142451-550D-4C1B-A389-26FD74C6B018QA-2019/Global_POV-EQ_XKX.pdf

3

TRANSMISSION CHANNELS, FACTORS & AMPLIFIERS

29. While assessment results (i.e., impact on price inflation on incomes etc.) are provided in detail in Section 4, this section documents the primary transmission channels, factors and domestic amplifiers on Kosovo, resulting from the war in Ukraine. This analysis, therefore, identifies the primary factors impacting the socio-economy, the routes of how these factors impact the socio-economy, but also what impact they have on the domestic economy, and why the impact exposes Kosovo the way that it does. Given that this section includes an overview of institutional policy responses to addressing socio-economic threats and risks (i.e., increased spending on social protection and on subsidies), it also provides a greater sense of how these factors impact the most vulnerable elements of society.

FACTORS, CHANNELS AND AMPLIFIERS

30. Not only does this overall analysis intimate towards emerging threats and risks, but it also provides useful insights into programmatic responses and overall engagement recommendations, for each factor. While the Kosovo institutions can do very little to impact global energy and food prices, it can improve ex-ante analysis of mountings costs, including investing in mitigation measures to remove suffering from those exposed to a specific factor. Learning lessons from the COVID-19 response, where defining interventions that targeted those most at risk, lessons can be learned and applied to final recommendations. However, in terms of concept definitions, and how to interpret Table 1 below, the following should be noted:

- **Transmission Factors**: Transmission factors are clearly defined variables such as interest rates, global energy and food prices, the value of remittances, cost of credit and factors such as political alignment with trading partners, among other factors.

- **Transmission Channels**: Transmission channels are the process through which various factors affect an economy in general and the price or employment level in particular. The transmission mechanism can be characterised by long, variable and uncertain time lags and it is therefore often difficult to predict the precise effect of a particular factor on the socio-economy, food security or social cohesion for example, or to isolate a particular factor such as inflation, which can have a multiplicity of impacts, including on demographic and gender groups. A transmission channel describes how a factor is impacting the domestic environment.

- **Domestic Amplifiers**: External factors amplify existing domestic strengths, vulnerabilities, and resilience to changes in the economy, leading to both episodes of growth accelerations and reversals. Domestic amplifiers are policies and existing structural attributes (i.e., trade dependencies, geospatial, demographic and gender exclusion factors, etc.) that amplify or mitigate the effect that shifts in external conditions may have on growth and accumulation patterns in the Kosovo socio-economic system.

31. Table 1 below provides the results of an investigation into primary transmission factors, channels, and domestic amplifiers for Kosovo, as a result of the war in Ukraine. These factors represent the most visible and observable impacts, though other more intangible factors (i.e., shifts in foreign policy and foreign allegiance etc.) may also exist.

Table 1: THE WAR IN UKRAINE IMPACT ON KOSOVO

Factor and Description	Transmission Channels	Domestic Amplifiers
Sanctions: Import and export restrictions on Russia, adding to measures over Crimea since 2014.	Trade between Kosovo and Russia is limited and as a result, the direct impact of sanctions was minor. However, the EU embargo on Russian crude in February 2022 has impacted energy security alongside EU sanctions on technology, oil and energy, transportation, and aviation impact supplies.	A major impact of the Ukraine crisis and related sanctions has been a hardening of historical geopolitical positions. According to the IMF, while direct trade and financial channels with war-affected countries are negligible, the impact of the increase in the international prices of food and energy on Kosovo's imports could be as high as 5.5 % of GDP.
Energy Price Inflation: The impact of the crisis and sanctions has led to a huge spike in global energy prices.	Russia's export of crude and oil products to Europe, the US, Japan, and Korea fell by nearly 2.2 mb/d since the start of the war. Global overserved inventories have contracted, fuel switching has been applied in Europe and growing demand during winter will see European electricity prices reach new record highs. This has led to a larger electricity import bill.	Kosovo's power sector was developed to produce basic electricity from lignite, and in relying on 2 primary plants which are outdated and inflexible. In its ambition to diversify energy generation, Kosovo aims to have 32% of its energy consumption from renewable sources, but currently lacks the battery capacity for storing solar or wind-generated energy. While energy output is conventionally enough to cover demand, due to ageing plans and lack of storage, Kosovo cannot achieve maximum load coverage in winter months and is therefore reliant on imports to meet domestic demand. In February 2022, the Energy Regulatory Office (ERO) increased electricity prices for consumers with average electricity consumption above 800 kWh per month from € 2.89 to € 5.9 (over 100 % increase) and from € 6.75 to € 12.52 for the high daily tariff. On 29 August 2022, Kosovo Electricity Supply Company (KESCO) submitted a new request to the ERO asking to raise the prices that was denied. A second request was submitted on 5 December 2022, and the outcome is still uncertain. The inflation rate for July 2021 - July 2022 for fuels and lubricants for transport equipment was 44.1%. For November 2021 – November 2022, the inflation rate for fuels and lubricants for transport equipment was lower at 21.3%. As domestic consumers dominate demand, particularly in winter, the additional cost will impact

		lower-income groups. There may be a need to larger imports from the HUPX market, the prices of which will be reflected in the upcoming price review scheduled for February. The institutions allocated €100 million to soften the impact of higher energy prices for the people though this will likely need to be increased/ extended. In October 2022, the EU committed to providing a further €75 million budget support to reduce the impact of elevated energy prices on Kosovo, focused on targeting vulnerable businesses and households. The surge in energy prices in Kosovo as a result of the Ukraine war has increased the urgency to invest in sustainable domestic energy generation and reduce dependence on expensive imports.
Food Price Inflation: Disruption of Ukraine and Russian (major global market agricultural producers) barley, corn, wheat, and sunflower oil exports.	Price transmission through global food commodity markets. Export restrictions/protectionist measures other producer countries. Increased sourcing from countries outside Russia and Ukraine.	Kosovo authorities had already started tackling rising global food prices in late 2021. The inflation rate for July 2021 - July 2022 was 14.2%, though price hikes in certain products have exceeded this level substantially. Edible oils increased in price by 54.1 %, bread and cereals (32.1%), milk, cheese, and eggs (26.3%), sugar, chocolate, and sweets (19.1%) and coffee and tea (16.8%). For November 2021 – November 2022, the annual inflation rate was 11.6%, remarkable, but still lower than the summer peaks. This is mainly explained by edible oils and fats (34.4%); milk, cheese and eggs (24.7%); bread and cereals (21.9%); meat (21.2%); sugar, jam, honey, chocolate and sweets (18.3%); and sauces, spices, salt, baby food, etc. (17.2%). The institutions have responded with increased subsidies for agricultural inputs, wage bonuses and temporary increases in pension benefits and social transfers. Additionally, there is ongoing discussion into the possibility of allowing early withdrawals (of up to 30%) from the Kosovo Pension Savings Trust (KPST).
Currency / Exchange Rate Risks: The € has lost 20 % on the dollar since the beginning of 2022 and is trading close to parity.	Kosovo is vulnerable to importing inflation as a result of currency depreciation, one result of the euroization of the economy. Higher rates impact debt levels and the costs of credit. However, the Euroization of the financial system can also be seen as a general source of financial stability.	Currency depreciation will erode the income of middle- and lower-income groups, at the same time increasing costs of energy, food, commodities, and services, raising the cost of living and lowering savings. Among other factors, depreciation has led to a reduction in the real value of the minimum wage, leading to an institutional discussion on raising the minimum wage by close to 50%, but did not raise pensions in parallel.
European Capital Tightening: Tighter financial conditions in Europe could	As global capital markets tighten to address historically high-interest rates, the cost of borrowing will increase impacting many of Kosovo's growing industries	Raising EU interest rates could translate into higher domestic interest rates, creating vulnerabilities for sectors that have expanded strongly, including construction.

Credit Ratings: Due to the status of Kosovo, the ability to be afforded a credit rating has been impeded, undermining the development of financial markets.	Reduces market liquidity and negatively impacts the domestic debt market, and the ability for international borrowing from capital markets	A pre-existing constraint that is not impacted by the war in Ukraine, but this does impact the functioning of capital markets, portfolios, and other foreign investment inflows.
Official Development Assistance: Gross ODA was valued at US$556.7 million in 2020.	ODA supports policy reforms, and economic and social infrastructure, freeing up fiscal space and supporting poverty reduction and the SDGs. ODA repurposing to deal with Ukrainian refugees.	Though data on 2022 ODA commitments is not yet available, against a GDP of US$ 9 billion in 2021, Gross ODA constituted about 6.1 % of GDP. Re-purposing of EU assistance to respond to the energy crisis and redirecting overall ODA resources to respond to the needs of the people displaced by the war, alongside with increased defence spending, is likely to lead to a change in focus and allocations of ODA.
Remittances/migrant transfers: Remittances from the large Kosovo Diaspora have remained buoyant with August 2022 figures reaching an all-time high of €131.6 million, up from €110.2 million in August 2021 and €91.6 million in August 2020 whereas September 2022 was a bit lower again at €102.6 million.	Remittances from abroad impact Kosovo's foreign currency reserves and provide a direct financial flow to households to support the cost of living.	Most households remain dependent on remittance flows, though as most migrants are in EU countries, the immediate impact of the war in Ukraine will likely have a limited impact on the volume of remittance flows, which were already resilient through the COVID-19 crisis. 30% of the Kosovo diaspora live in Germany however, and should Germany have an economic downturn as a result of the energy price increase and supply side constraints, remittances could be impacted in 2023.
Debt (Cost of Borrowing): Global credit tightening by all major central banks to control inflation	Rising inflation raises borrowing costs, exacerbating debt affordability.	While public debt is anchored below the 40 % GDP fiscal rule, unless the tax base is expanded, fiscal transparency is strengthened and the investor base expanded, the public debt count increase along with the increased cost of borrowing.
Geopolitical Risks: Escalation in tensions.		Geopolitical risks have accelerated globally as a result of the war in Ukraine with wider implications for Europe and the Balkans.

4

IMPACT RESEARCH FINDINGS

32. Based on the impact factors cited in the previous section, drivers of the socio-economic crisis are high global food and energy prices, overall global inflationary pressures, and likely recession in European countries from which Kosovo draws its remittances, to which it exports, and from which it gets its bank financing from. As noted above, however, and as this report identifies, of particular concern are not just the causes of impact, but also their effects on the socio-economy. Domestic amplifiers such as dependency on remittances, uncertainty over Kosovo's international status, lack of a domestic credit rating, challenging road to EU accession, high levels of informality and still low per capita incomes, contribute towards a vicious cycle.

33. As of May 2022, the central institutions' response to the emerging economic situation included (i) €100 million committed for employees, students, pensioners, and 40 thousand food packages (ii) €120 million for electricity subsidies (iii) €10 million to increase Kosovo reserves (iv) €5 million or 36 cents per litre subsidy for oil in agriculture, as well as reduction of oil profit margin and (v) a doubling of subsidies for key agricultural crops.[9]

34. As noted in the scope and method section outlined above, this research looks at the impact of the Ukraine crisis on key variables, including the impact on commodities and producers. The results reported reflect the latest Q2 data where it is reported and draw from the 2017 Living Standards Measurement Study (LSMS), in the absence of an alternative. The following impact factors are reviewed, based on available data and multivariate analysis, within the framework of what is known about household income and consumption.

Energy Price Impact on Households	Food Price Impact on Households	Changes in Remittances	Impact on Household Consumption
Impact on Trade Balance	Impact on Revenues & Expenditures	Impact on Commodity Prices	Impact on Producer Prices

HOUSEHOLD INCOME BASELINES

35. According to a study conducted in 2018, titled "Kosovo Labour Force and Time Use Study Research Report", funded by Millennium Challenge Corporation,[10] the average annual household income in Kosovo was € 5,496, with urban households earning € 6,230 and rural households earning € 5,300, on average (See Table 2 below).

[9] In May 2022, the Gap Institute assessed the 'Impact of the War in Ukraine on Kosovo's Economy'. https://www.institutigap.org/documents/20407_Impact%20of%20the%20war%20in%20Ukraine%20on%20Kosovos%20Economy.pdf
[10] Available at: https://millenniumkosovo.org/wp-content/uploads/2018/11/MCC-Kosovo-Labor-Force-and-Time-Use-Study-Final-Research-Report-1.pdf

Table 2: KOSOVO ANNUAL HOUSEHOLD INCOME (%) PER REGION							
Region	**Average Hh Income (€)**	**<1000**	**1000-2000**	**2000-3000**	**3000-5000**	**5000-10,000**	**>10,000**
Ferizaj/ Uroševac	6,086	3.1%	12.0%	14.3%	25.8%	31.5%	13.3%
Gjakovë/ Djakovica	5,642	3.3%	11.2%	17.7%	23.7%	29.4%	14.7%
Gjilan/ Gnjilane	5,482	6.6%	8.3%	14.8%	28.1%	29.8%	12.4%
Mitrovicë/ Mitrovica	4,133	10.3%	20.5%	15.8%	21.7%	24.9%	6.8%
Pejë/Peć	5,480	4.7%	12.0%	13.6%	23.6%	37.1%	9.0%
Prishtinë/ Priština	6,487	6.0%	9.3%	13.6%	21.7%	30.2%	19.3%
Prizren	5,297	6.6%	10.2%	16.0%	27.7%	28.8%	10.7%
Average	5,497	6.0%	12.1%	15.2%	24.4%	29.9%	12.4%

Source: "Kosovo Labour Force and Time Use Study Research Report", MCS, (2018)

36. Though this data is from 2018, nearly 50 % of the total households included in the survey had a total annual household income in the range of €3,000 and €10,000. Some 24.4 % of households are earning in the range of € 3,000 and € 5,000 and 29.9 % of households earning in the range of € 5,000 and € 10,000, on average. While 6 % of households have an annual income of less than € 1,000, 12.4 % of households reported an annual income of € 10,000 and above. These figures are before the COVID-19 pandemic, which already undermined productivity and employment.

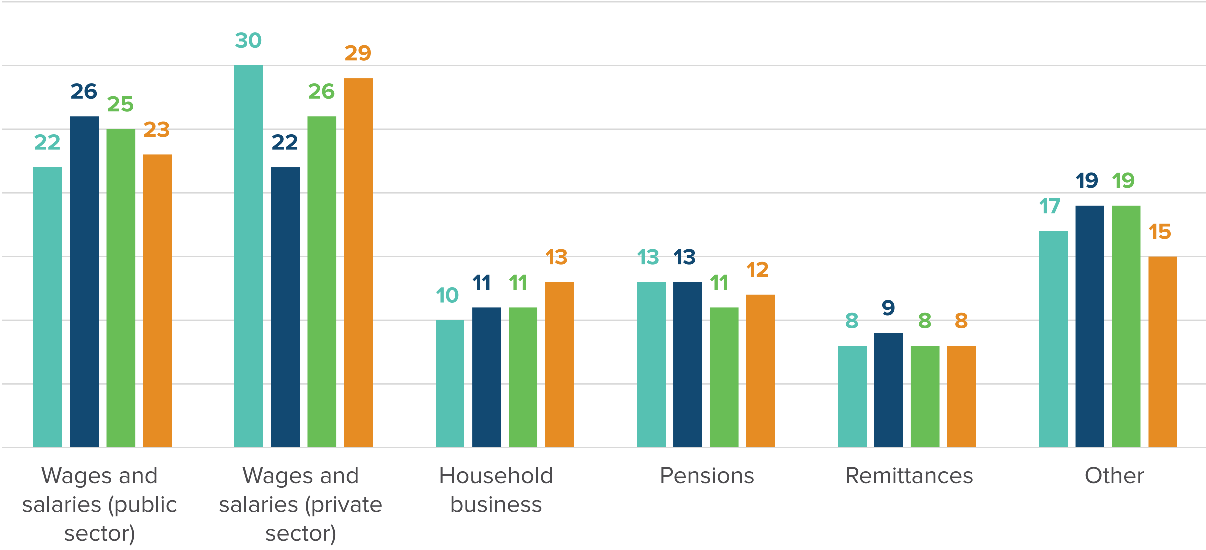
37. The average annual household income for the bottom 40 % was € 2,230, compared to € 8,859 for the top 60%. In addition, it was found that the annual household income of male-headed households, at € 5,196, was higher than female-headed households, at € 4,505 and the difference was statistically significant. Differences are also noted across regions, with Mitrovicë/a characterized by the lowest average income levels at € 4,133 and Prishtinë/Priština with the highest at € 6,487, on average. People in the poorest regions will be more significantly impacted by the rise in energy and food prices, as they spend a higher percentage of disposable incomes on utilities and essential commodities. The share of households with income of up to €1,000 is highest in Mitrovicë/a (10.3%) and lowest in Ferizaj/Uroševac (3.1%). On average, 33.4% of households in Kosovo have income levels up to €3,000, with 46.6% of households in Mitrovicë/a belonging to this category. With regards to the income group of €10,000 and above, Mitrovicë/a again stands worse off since only 6.8% of households reported falling into this category, with Prishtinë/Priština having the highest percentage of households, at 19.3%, belonging to this income level.

SOURCES OF HOUSEHOLD INCOME

38. In understanding the impact of the war in Ukraine on income, it is useful to identify the primary household income sources, as follows: wages and salaries (public and private), household businesses, pensions, remittances, and other incomes (loans, unspecified) (See Chart 2 below). In terms of breakdown, in 2017 the main source of income was wages and salaries at 51%, loans and unspecified at 15%, household businesses and pensions (at 13% and 12%), and lastly remittances at 8%. The decrease in incomes from 'other sources' is almost compensated by the increase under 'wages and salaries, private sector'. Otherwise, these shares appear to be quite steady over the 2014-2017 period, and as there is no data available for the period 2018 to 2022, these reference points are used as a basis for understanding sources of income.

Chart 2. **SOURCES OF HOUSEHOLD INCOME (IN %)**

Source: a) For 2014-2015, KAS -Annual Statistical Report (2016), Table 2, p. 7; b) For 2016-2017, KAS -Annual Statistical Report (2018), Table 5, p. 17. Further Annual Statistical Reports have no updates.
Note: Blue = 2014, Orange = 2015, Grey = 2016 and Yellow = 2017



39. The KAS report cited above finds that 20.2% of households received remittances from outside of Kosovo and that remittance flows are higher to rural areas, at 21.4% of households, compared to urban areas (16.1%). Across regions, the largest share of households receiving remittances is in Gjakovë/Djakovica (37.1%), while the smallest share is found in Prishtinë/Priština, with only 11.7% of households having received remittances. Among remittance recipients, on average, remittances accounted for 47.7% of total household income, of a larger share in rural areas of 48.4%, compared to urban areas (44.6%). The median remittance-receiving household received 40% of remittances as a share of their household income, with the median for urban households at 30% and rural households at 40%. By regions, the greatest contribution of remittances to household income was noted in Prizren, as remittances composed 57.6% of total household income as opposed to Prishtinë/Priština, where remittances contributed only 36.6% to household income.

40. Regarding wages and salaries, evidence shows that all categories of employment have increased wages from 2016 to 2021 except for private sector wages which were heavily impacted by the COVID-19 pandemic, though bouncing back in 2021 above pre-Covid levels. Table 3 below shows the average gross and net salary by year, categorized, though gender-disaggregated data is not available, these averages inevitably mask inequalities. As the cost of living has however increased substantially over this period, gross and net increases have barely kept pace with inflation.

Table 3: AVERAGE GROSS AND NET SALARY BY YEAR								
Year	**Total**		**Public sector**		**Public Owned sector**		**Private Sector**	
	Gross	Net	Gross	Net	Gross	Net	Gross	Net
2016	422	382	525	467	686	609	340	310
2017	431	390	532	474	699	620	356	324
2018	453	409	573	509	721	639	376	342
2019	477	430	584	519	766	677	411	372
2020	466	416	624	552	769	680	380	342
2021	484	432	612	542	768	680	419	376

Source: KAS

HOUSEHOLD CONSUMPTION

41. The 2017 household budget survey illustrates five main categories constituting some 83% of consumption (food, housing, transport, clothing, alcohol, and tobacco).[11] Food and beverages made up 45% of all consumption in 2013, and this fell slightly to 40% by 2017 (where meat accounts for 20% of its subtotal and bread accounts for 16%), to be followed by housing. These two alone accounted for 75% of total consumption by households in 2013, and in the last year of reporting (2017) around 60%. The trend in food consumption has been declining over the years, as people were lifted out of poverty and greater disposable incomes impacted consumption choices. However, as there are no data available beyond the year 2017, to estimate the impact of price increases on household income, it will be considered that the figure for 2017 (40%) is the current figure for the year 2022. The same will be assumed for housing.

Table 4: HOUSEHOLD ANNUAL CONSUMPTION IN KOSOVO BY ITEMS (%)				
Consumption item (as % of total)	**2014**	**2015**	**2016**	**2017**
Food	44	43	42	40
Alcohol and tobacco	4	4	4	4
Alcohol and tobacco	4	4	5	5
Housing	28	30	29	29
Furniture	4	3	4	4
Health	3	3	3	3
Transport	5	4	4	5
Communication	3	3	3	3
Recreation	0	1	1	1

[11] Housing includes construction or renovating a house, furniture, household appliances, renting and associated expenses such as electricity and water supply bills.

Education	1	1	0	0
Hotel and restaurants	2	2	2	3
Other	2	2	3	3
Total:	**100**	**100**	**100**	**100**

Source: KAS, Household Budget Survey, 2017

IMPACT OF ENERGY PRICES ON HOUSEHOLDS

42. Though Kosovo has no direct connection with Russian or Ukrainian energy markets as it does not have the gas infrastructure, the lack of reliable domestic generation capacity has impacted both supply and costs of energy provision. In February 2022, Kosovo Energy Regulatory Office (ERO) issued a normative act on energy tariffs. The prices in effect for the consumption of up to 800 kWh were 2.89 cents for the lower tariff, and 6.75 for the higher tariff. As of March 31, 2022, new tariffs entered into effect as follows: Tariffs for households for the consumption of up to 800 kWh per month will remain the same, while consumption over 800 kWh per month will be billed with 5.9 cents during the low overnight tariff and 12.52 cents during the rest of the day. Implying a doubling of tariffs. These measures are, to this date, valid until March 31, 2023, despite the risk that further price increases appear almost inevitable, and high tariffs may need to be introduced, or energy subsidies increased.

43. According to the Kosovo Electricity Supply Company (KESCO) and Kosovo institutions, 22-30 % of households consume more than 800 kWh per month (the lower estimate is by KESCO).[12] The impact on the budget for the 70-78 % of Households that consume less than 800kWh/month is that they would spend a maximum of €48 per month above the previous amount. Overall, the Kosovo institutions estimate that this measure would result in a price increase ranging from 5%-30% (assuming 60% of consumption occurs during the daytime). The impact on the household budget cannot be measured with accuracy (given data limitations and LSMS data from 2017), as the energy bill is under the "housing" consumption item, which represents on average 29% of consumption in a household in 2017. Despite 2017 providing a poor reference point, based on 2017 data, around 60% of Kosovo urban homes were paying between 10% and 30% of their family income on electricity consumption in 2013, and the cost to poorer households of a considerable hike in energy prices may lead to an increase of up to 40-50 % for certain households.[13] [14] The levels of energy usage beyond the 800kWh threshold can be assumed to be attributed to high-income households, which can better afford the increased price. Therefore, to flatten the demand curve and encourage energy efficiency, the institutions have created a new scheme that intends to reimburse a portion of the energy bill if consumption falls relative to previous year.

44. Two requests were made Q3-Q4 2022 by Kosovo Energy Distribution Company (KED) to ERO for a further doubling of household energy bills, on both the low and high ends of consumption. The first request on 29 August was denied, but simultaneously between 15 August and early September 2022, the Kosovo institutions introduced scheduled power cuts, reducing 25% of energy supply hours in 24hrs (i.e., to 18 hours of daily supply) and thus induced energy savings, beyond self-adjustment/demand reduction by households. While it remains to be seen whether the second request (5 December) will be considered by ERO, the coming generation and consumption mismatch will likely lead to power cuts (as was already the case in winter 2021/2022), potentially compounded by technical difficulties with ageing power plants.

[12] https://balkangreenenergynews.com/kosovo-doubles-electricity-prices-for-households/
[13] https://www.rit.edu/research/cenr/sites/rit.edu.research.cenr/files/2013_03_01_cenr_kosovo_household_energy_consumption.pdf
[14] "Housing" item as share of overall consumption has been rounded up here to 30%.

45. With the institutions already allocating €100 million to soften the impact of higher energy prices for the people, a G7 energy price cap on Russian energy followed by a Russian ban on selling to countries implementing the gap will lead to the biggest energy crisis faced by Europe since 1972. Given that Kosovo is in many ways a price taker and that the additional costs of energy further erode disposable incomes, additional energy subsidies will be likely. In October 2022, the EU committed to providing a further €75 million as budget support to reduce the impact of elevated energy prices on Kosovo, focused on targeting vulnerable businesses and households with a special focus in promoting energy efficiency. This support is in addition to the wider €500 million to the region to support the transition to energy independence and security of supply, focused on renewables and energy market connectivity.[15]

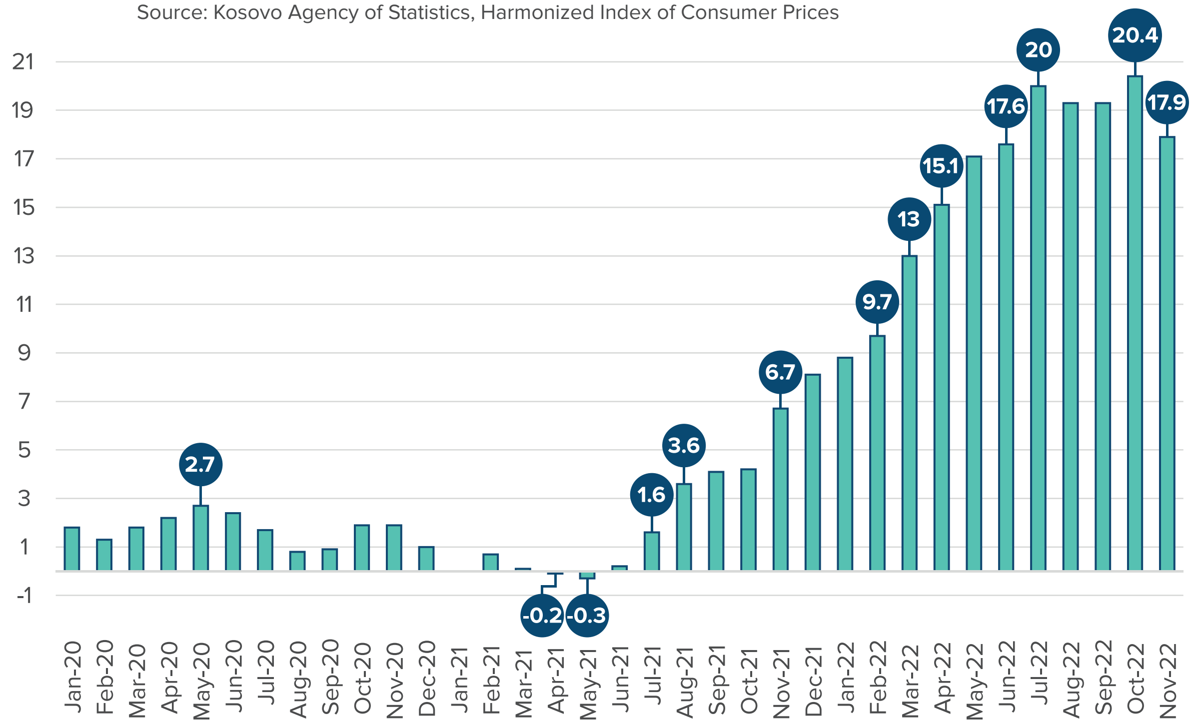
IMPACT OF FOOD PRICES ON HOUSEHOLDS

46. End user demand for energy is generally more elastic, whereas food consumption levels (including for cheaper and less nutritious substitutes) tend to be maintained. Substitution, although possible, is determined by a wide range of factors including cultural norms and gender, for example.

47. Food prices started to increase above historical levels from August 2021, continuing a steep upward trend from November 2021 (at 6.7%) until reaching 20% in July 2022. In the short run, rapid food price increases can be assumed to be directly transferred into a reduction of disposable income (little time and opportunity for substitution effects). Given its weight in the household consumption budget (at 40%), that would result in the increase of the consumption budget to 48% of the total (reducing by 8% the disposable budget). Chart 3 shows the steady increase in food price inflation starting in July 2021, almost straight lining to July 2022, with the beginning of the war appearing to have had only a modest impact on price increases.

Chart 3. **MONTHLY FOOD PRICE INFLATION (IN %) SINCE JANUARY 2020**

Source: Kosovo Agency of Statistics, Harmonized Index of Consumer Prices

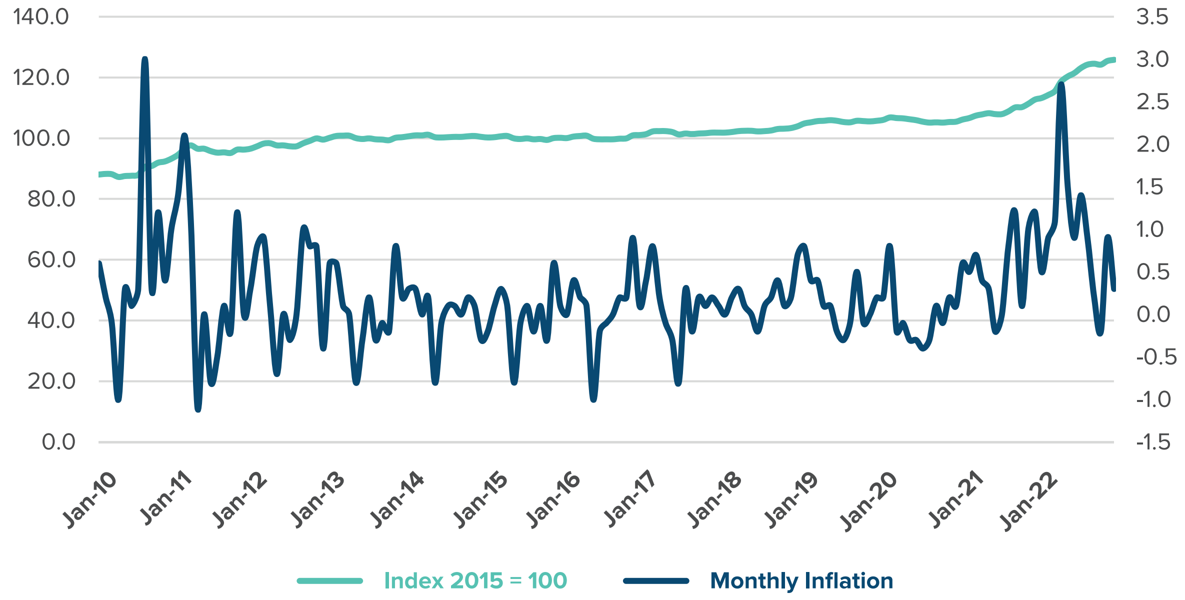


[15] https://ec.europa.eu/commission/presscorner/detail/en/statement_22_6422

48. The purchasing power of households is negatively impacted by the combined effect of fuel/energy and food prices, as outlined in Chart 4 below. The harmonized indices of consumer prices – with 2015 as the index baseline – running from 2010 to November 2022 shows the biggest uptick in prices for over a decade, with monthly inflation levels at 2022 levels last seen in August 2010.

Chart 4. **HARMONIZED INDICES OF CONSUMER PRICES (2010- 2022)**

Source: Kosovo Agency of Statistics, Harmonized Indices of Consumer Prices



49. The combined effect of the rise of energy and food prices on the Household budget can be estimated between 9.5% and 18% of spending. Energy poverty in Kosovo pre-exists the current crisis. A 2021 study by the EU's Energy Community (EnC) on Addressing Energy Poverty notes that electricity prices in Kosovo for household consumers inclusive of all taxes and levies are among the lowest in the Energy Communities, i.e., 21% lower than the average in the EnC contracting parties and that decarbonization policies will lead to upward pressure on energy prices. Among the nine Energy Community contracting parties, Kosovo has the largest share of households living in energy poverty, up to 40 %, and Montenegro the lowest, between 8 and 15 %, according to a study on addressing energy poverty in the members of the Energy Community.

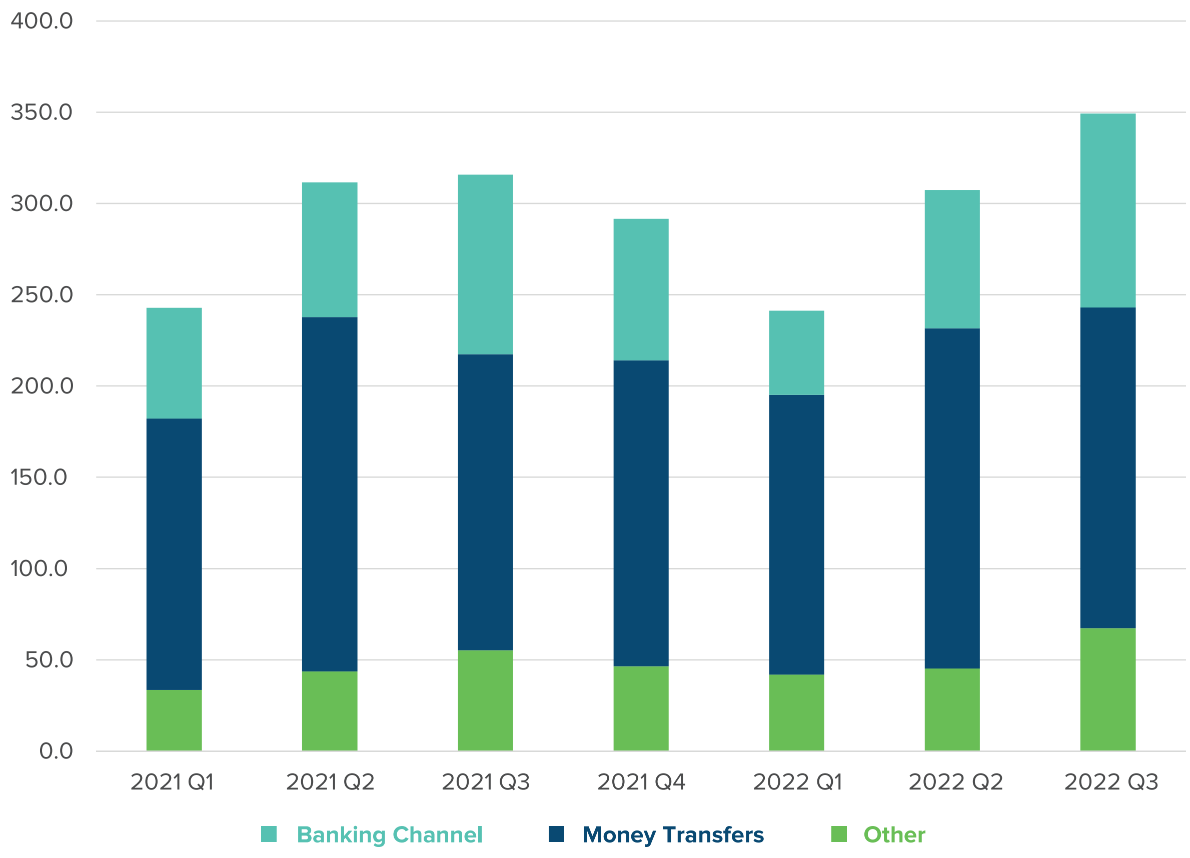
50. As a conclusion, while the impact of the recent crisis is felt far more by low-income groups, the majority of which will be experiencing considerable economic stress now and going into the winter, a successful energy transition to meet the EU Green Agenda and decarbonization goals risks increasing energy poverty even further. Though many families will be partly shielded by remittance flows, the upwards and resilient trend of remittances may not continue, certainly if further economic pain is experienced by Germany and other economies, which seems to be the case as the ECB continues capital tightening. A protracted worldwide crisis resulting in further increases in commodity prices will likely increase savings, reducing the use of remittance for more luxurious goods and services, and this will impact productivity. As a result, Kosovo policies will need to focus on increasing the resilience of low-income groups, perhaps through a basket of subsidies and tax breaks.

CHANGES IN REMITTANCES

51. Despite forecasts by the IMF and World Bank that the value of global remittances was threatened by COVID-19, the reality is that remittances remain highly buoyant, demonstrating the value added of having a strong diaspora community to shield households from domestic exogenous shocks. Available data show that income from remittances has increased steadily starting in May 2020, noting a decrease during Jan-March 2022, only to increase again as the impact of the food and energy price crisis mounted into October 2022. Chart 5 below shows the overall trend, which appears likely to be extended further into 2022, showing an increase between Q2 and Q3 2022.

Chart 5. **REMITTANCES BY CHANNEL (2021 (Q1) TO 2022 (Q3) (€ MILLION)**

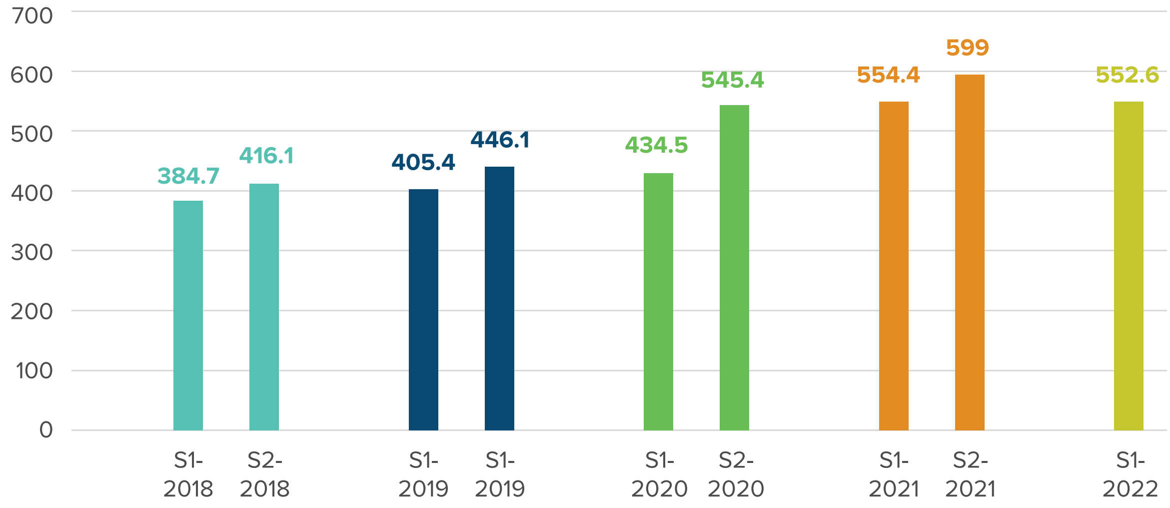
Source: Central Bank of Kosovo.



52. In financial terms, income from remittances in the first semester of 2022 was valued at €552.6 million, a mere €1.8 million lower than the same semester of 2021, and higher still than all preceding quarters from 2018 onwards. Remittances remain a major source of resilience for households, for GDP and for servicing the balance of trade. Given the increased pressure on foreign currency for energy exports, a collapse in remittances would have a devasting impact on households first, and macro-economic stability as well. Chart 6 below illustrates this finding and bodes well for medium-term flows to support low-income households to offset the impact of an elevated cost of living.

Chart 6. **TOTAL REMITTANCES BY SEMESTER (2018-S1 2022) (€ MILLION)**

Source: CBK, Table 32, and Geopolicity calculations.



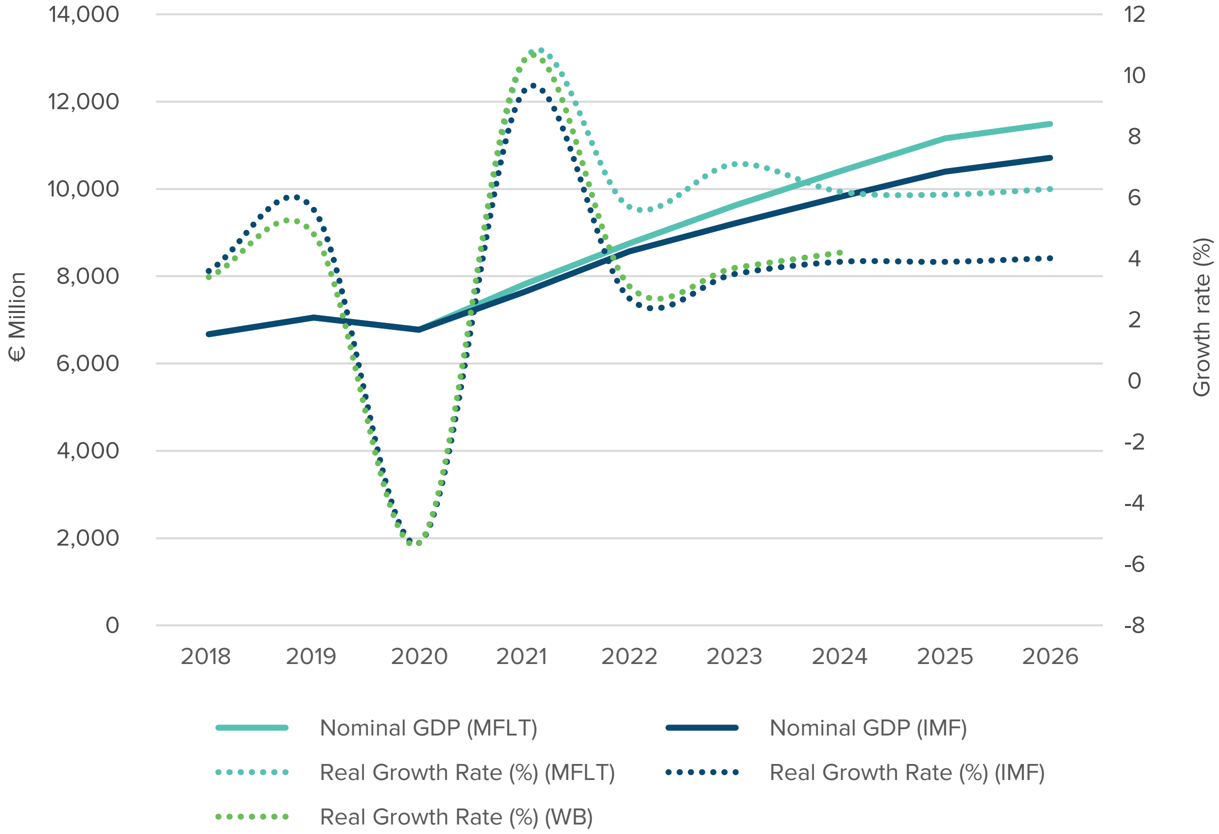
IMPACT ON GDP AND TRADE BALANCE

53. GDP in Q3 2022 marked a real increase by 2.07% compared to Q3 2021. According to the Kosovo Agency for Statistics (KAS), during the reporting period, Financial and insurance activities increased by 12.67%; Scientific, professional and technical activities; Administrative and support services activities (8.61%); Information and communication (8.28%); Arts, entertainment and recreation, household goods production activities for own use and other services (7.49%); Wholesale and retail trade, vehicle and motorcycle repair, Transport and storage, Accommodation and food service activities (4.31%); Mining and manufacturing industry, electricity, gas, steam and air conditioning supply, Water supply, waste treatment and management activities and rehabilitation (2.24%); Agriculture, forestry and fishing (2.18%); and Real estate activities (1.38%). The economic activities that marked a decline in Q3 were Construction (-7.78%); and Public administration, social security, education and health (-0.48%). Export of goods and services increase by 6.30%, import of goods and services by 3.87%, final consumption expenditures by 2.64%, and the gross capital formation decreased by 2.33%.[16] GDP in Q2 2022 marked a real increase of 2.14% compared to Q2 2021. Chart 7 below provides nominal GDP actuals for the period 2018 to 2021 with forecast growth for 2022-2026 based on the 2023-2025 MFLT Medium-Term Expenditure Framework (MTEF) and with the latest revisions from IMF and WB. Since the MTEF was released in April 2022, the forecasts have been adjusted down by the financial institutions, which shows the significant impact on the economy.

[16] https://ask.rks-gov.net/media/7214/gross-domestic-product-gdp-of-the-expenditure-and-production-approach-q3-2022.pdf

Chart 7. **NOMINAL GDP ACTUALS (2018-2021) AND FORECAST (2022-2026)**

Source: MFLT MTEF 2023-2025 (April 2022) including updated projections by the IMF/WB.

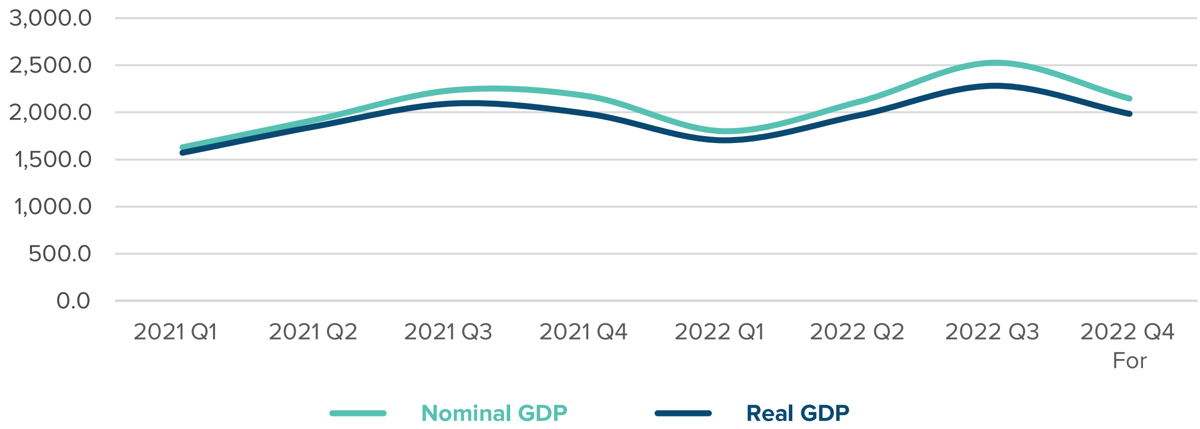


54. Kosovo has very limited exposure to direct trade with Ukraine and Russia. Data shows that the trade deficit increased from €361.1 million in November 2021 to €401.4 million in November 2022, showing a 11.2% increase. Moreover, the export of goods in November 2022 was valued at €73.9 million, while imports were valued at €475.4 million, which is an increase of 4.6% for exports and 10.1% for imports, compared to the same period of 2021. Both exports and imports with the EU increased by 32.3% and 7.8% respectively.

55. While the impact on GDP was not negatively affected based on Q3 outturns, it is too early to make any assumptions on impacts into Q1 2023 when energy shortages and costs will be at their peak. In May 2022 the IMF estimated the price impact of energy and food inflation on Kosovo's imports could be as high as 5.5% of GDP, or an impact of €550 million, which would also price in the expected GDP growth deceleration coming out of the pandemic. However, Chart 7 provides quarterly GDP (€ million at current prices) for the period Q1 2021 to Q3 outturns for 2022, with simple two-quarter moving averages applied for Q4 2022.

Chart 8. **QUARTERLY GDP (€ MILLION) CURRENT PRICES**

Source: Kosovo Agency of Statistics



CHANGES TO REVENUES AND EXPENDITURES

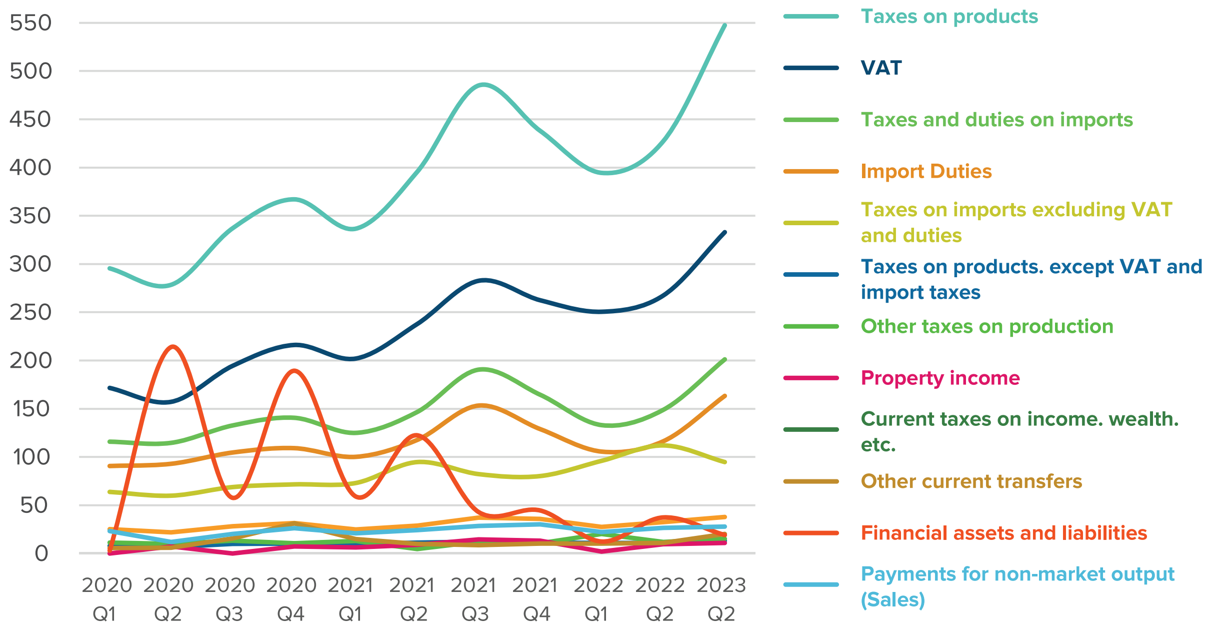
56. While stronger fiscal performance has allowed the central institutions to cushion the impact of the terms of trade shock on households and firms, while also replenishing its liquidity buffers[17], and though the 2023 Kosovo budget foresees a considerable increase in revenues[18], current fiscal space is insufficient to finance major new investments such as the Digital Economy transition, energy transition or Agenda 2030 Sustainable Development Goals (SDGs). To accommodate new spending priorities in 2022, capital spending has been reduced, likely impacting growth outturns and under-performance in expenditures has allowed the fiscal deficit to remain broadly within the fiscal rule. Central institutional financing needs as outlined in the 2023 budget do not include these large big-ticket items.

57. Year-on-year changes show that revenues expanded between Q3 2021 and Q3 2022, and institutional expenditures also increased considerably, as a result of increases to social protection and energy subsidies in particular. According to the Kosovo Agency of Statistics, General institutional revenues in Q3 2021 were €673.9 million, and year-on-year this increased to €697.5 million, 3.5% (or €23.6 million). The majority of revenues are comprised of taxes on products, which represent 78% of the total revenues, current taxes on income 14%, payments for non-commercial products 4%, and other currents transfers 3%, while the rest is distributed into other categories of revenues.[19] Chart 9 provides revenue by source for the period Q1 2020 to the end of Q3 2022, showing an increase in taxes on products (increases in VAT and taxes on duties of imports).

[17] https://www.imf.org/en/News/Articles/2022/11/04/Kosovo
[18] https://mf.rks-gov.net/desk/inc/media/FB8AED72-35CD-4636-BAB5-D675B2967296.pdf
[19] https://ask.rks-gov.net/media/7187/llogarit%C3%AB-qeveritare-t%C3%AB-kosov%C3%ABs-tm3_2022.pdf

Chart 9. **GENERAL INSTITUTIONAL REVENUES (ESA2010) (Q1 2020 TO Q3 2022)**

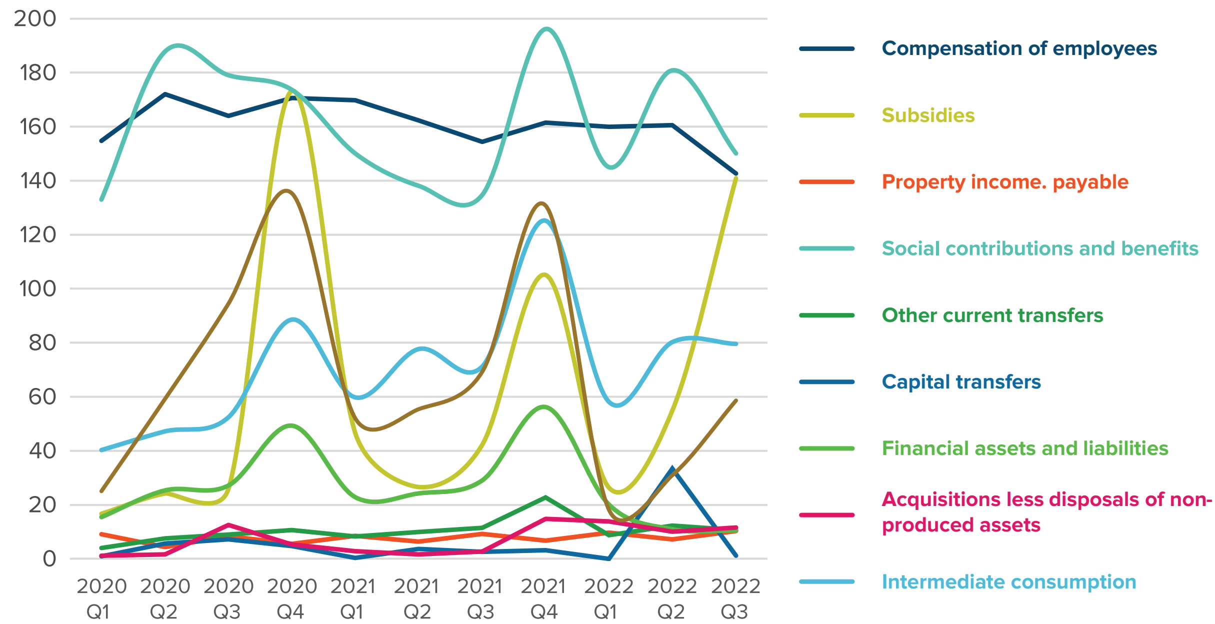
Source: Kosovo Agency of Statistics



58. Over the same period, general institutional expenditures increased from €526.9 million Q3 2021 to €615.9 million Q3 2022, an increase of 16.9% (€89 million) year-on-year. Most of the expenditures are comprised of social contributions and benefits, which represent 24%, subsidies 23%, compensation of employees which represents 23%, intermediate consumption 13%, while the rest is distributed into other categories of expenditures. The cost of general institutional services increased year-on-year from €82.0 million to €125.5 million and social protection spending increased from €133.0 million to €149.2 million. These expenditure categories are likely to increase further into Q4 2022 and Q1 2023. With revenues increasing much slower than the (potentially temporarily) expenditures, the fiscal and budget deficits may increase.

Chart 10. **GENERAL INSTITUTIONAL EXPENDITURES BASED ON ESA2010 (€ MILLION)**

Source: Kosovo Agency of Statistics

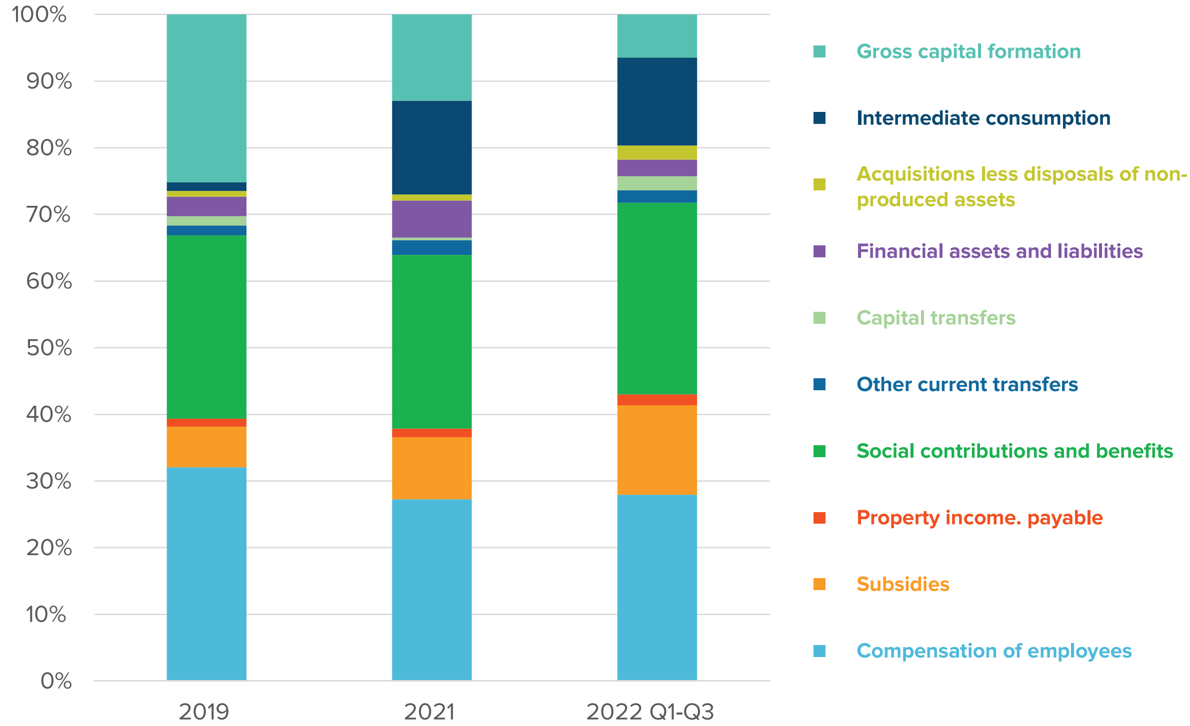


59. Chart 10 above provides a breakdown of general institutional expenditures from Q1 2020 to Q3 2022, showing a general uptick in expenditures for social contributions and benefits, intermediate consumption and subsidies in particular, though these items remain below peaks from both waves I and II of COVID-19. Additionally, financial assets and liabilities have been reduced.

60. Changes in the composition of expenditures for the period 2019-2022 Q1-Q3 are provided in Chart 11 below, showing a significant increase in social expenditures and subsidies alongside a massive downturn in gross capital formation. Such an outcome would lead to a forecast of increased macro-fiscal stress.

Chart 11. **CHANGE IN COMPOSITION OF EXPENDITURES 2019, 2021 AND 2022 Q1-Q3**

Source: Kosovo MFLT



61. The 2023 Budget provides a foundation for understanding Kosovo institutions working assumptions going forward. Nevertheless, as GDP growth outturns projected for 2022 have fallen short and given that a near cessation of the war in Ukraine appears unlikely, in a context where Kosovo is required to do more than balance the budget but also invest in expensive energy and digital transitions, existing fiscal space is insufficient. Despite considerable gains made by the Kosovo Tax Administration (TAK), as projected for the period 2023-2025, a combination of improved tax administration combined with higher energy costs is going to impact the private sector. Total debt is projected at 23.7 % of GDP by the end of 2025 with the budget deficit moving from -3.9 % in 2022 to 0.1 per cent in 2025. However, ramping up capital spending to meet both the energy and digital transition – not accounting for the SDGs – alongside higher costs of borrowing, higher energy prices and growing pressures on social protection and subsidies will challenge these projections.

Table 5: STATEMENT OF INSTITUTIONS REVENUE AND EXPENDITURES FOR THE 2023 KOSOVO BUDGET

Description	2020	2021	2022 Revision	2023 Proj.	2024 Proj.	2025 Proj.
In millions of Euros:						
1. Total Revenue [1]	**1,722.2**	**2,200.9**	**2,430.4**	**2,884.1**	**2,982.2**	**3,196.1**
1.1 Tax Revenue	**1,507.0**	**1,947.9**	**2,168.9**	**2,525.4**	**2,684.9**	**2,885.4**
Direct Taxes	**267.2**	**342.2**	**392.6**	**504.5**	**513.6**	**550.6**
Tax on Corporate	85.3	113.9	136.2	192.9	206.2	221.1
Tax on Personal Income	158.0	189.5	212.7	263.0	257.2	277.5
Tax on Immovable Property	22.7	36.3	41.0	44.6	45.9	47.4
Other	1.3	2.4	2.7	4.0	4.3	4.5
Indirect Taxes	**1,272.7**	**1,664.7**	**1,837.8**	**2,097.3**	**2,252.5**	**2,422.1**
Value Added Tax:	770.1	1,038.2	1,176.0	1,387.3	1,495.8	1,612.3
Domestic:	222.4	291.7	360.0	435.9	462.8	493.8
Border:	547.8	746.5	816.0	951.4	1,033.0	1,118.5
Customs Duty	101.6	124.6	134.3	138.9	150.8	163.3
Excise	398.1	501.3	524.9	570.6	605.4	645.8
Other indirect	2.9	0.6	2.6	0.5	0.6	0.6
Tax Refunds	-33.0	-58.9	-61.5	-76.4	-81.2	-87.3
1.2 Non-tax revenue	**181.2**	**236.1**	**239.1**	**261.2**	**274.7**	**288.2**
Fees, charges, and other	146.2	186.8	188.5	208.5	220.6	234.4
Fees, charges, and other - Central Level	103.5	129.6	142.1	154.6	164.0	175.0
Fees, charges, and other - Local Level	42.7	57.3	46.4	53.9	56.6	59.5
Concessionary fees	2.7	17.0	17.0	19.0	21.0	21.0
Royalties	29.4	19.2	30.2	30.2	30.1	30.1
Dividend	0.00	10.0	0.0	0.0	0.0	0.0
Interest income	3.0	3.1	3.4	3.5	3.0	2.7
1.3 Grants	**43.1**	**16.8**	**22.5**	**97.5**	**22.5**	**22.5**
From which: Grants from the EU for energy	0.0	0.0	0.0	75.0	0.0	0.0
2. Total Expenditure [1]	**2,234.9**	**2,299.3**	**2,898.2**	**3,211.7**	**3,219.6**	**3,323.8**
2.1 Recurrent Expenditure	**1,827.7**	**1,837.6**	**2,140.8**	**2,342.1**	**2,270.7**	**2,341.9**
Wages and Salaries	660.8	667.3	670.9	745.5	749.9	756.3
Goods and Services	299.2	327.7	403.8	493.1	494.8	508.3
Subsidies and Transfers	867.8	842.6	1,045.0	1,098.0	1,021.2	1,072.5
Recurrent reserves	0.0	0.0	21.0	5.4	4.8	4.8
2.2 Capital Expenditure	**379.7**	**419.8**	**704.4**	**810.7**	**885.7**	**913.0**
Regular budget financing	261.2	399.8	570.1	681.4	768.4	771.4
Debt financing through the investment clause	47.1	20.0	113.2	129.4	117.3	141.6
Liquidation proceeds (PAK)	71.5	0.0	21.0	0.0	0.0	0.0
2.3 Public Debt Interest	**27.5**	**32.186**	**41.1**	**46.9**	**51.2**	**56.9**
2.4 DDG- Donor-designated grants	**9.2**	**9.7**	**12.0**	**12.0**	**12.0**	**12.0**
3. Budget Balance (1-2)	**-512.7**	**-104.2**	**-466.5**	**-326.0**	**-236.0**	**-126.4**

4.Expenditure exempted from the fiscal rule:	**148.6**	**53.9**	**134.2**	**129.4**	**117.3**	**141.6**
Expenditure from dedicated revenue	0.0	0.0	0.0	0.0	0.0	0.0
Expenditure financed from municipal						
carried-over OSR	30.1	33.8	0.0	0.0	0.0	0.0
Capital spending from the liquidation p.	71.5	0.0	21.0	0.0	0.0	0.0
Capital spending from the investment clause	47.1	20.0	113.2	129.4	117.3	141.6
5. Budget Balance, as						
per fiscal rule definition (5+6)	**-364.1**	**-50.3**	**-332.3**	**-196.6**	**-118.7**	**15.3**
A.Financing Need:	**-512.7**	**-104.2**	**-466.5**	**-326.0**	**-236.0**	**-126.4**
B.External Financing(net)	139.5	53.4	359.9	367.7	123.6	163.4
C.Internal Financing(net)	240.8	122.0	52.5	56.3	95.6	83.7
D.Change in usable bank balance:	-132.5	71.2	-54.1	98.1	-16.8	120.8
E.The stock of Usable Bank Balance (Net)	235.5	312.7	258.7	293.8	277.0	397.8
F.Designated Funds, Saldo	94.5	130.1	129.5	129.5	129.5	129.5
G.END-YEAR GROSS BANK BALANCE	**330.0**	**442.8**	**388.1**	**423.3**	**406.5**	**527.2**
Revenues received from TAK	466.9	597.7	711.6	895.8	930.5	996.9
Revenues received from Customs	1,050.4	1,376.7	1,477.8	1,661.4	1,789.8	1,928.3
Tax Refunds	-33.0	-58.9	-61.5	-76.4	-81.2	-87.3
Inflows from DDG-s	9.0	16.8	12.0	12.0	12.0	12.0
Outflows from DDG-s	9.2	9.7	12.0	12.0	12.0	12.0
GDP	**6,771.6**	**7,957.9**	**8,593.9**	**9,842.9**	**10,605.2**	**11,400.6**
The budget deficit (fiscal rule def.)	-5.4%	-0.6%	-3.9%	-2.0%	-1.1%	0.1%
as % of GDP						
Available bank balance as % of GDP	3.5%	3.9%	3.0%	3.0%	2.6%	3.5%
Memo 2:						
The stock of Domestic Debt	961.9	1,106.1	1,226.1	1,232.1	1,352.1	1,472.1
Stock of Foreign Debt +guarantees) Kosovo	525.8	576.9	925.9	955.4	1,069.7	1,226.0
guarantees	31.7	30.6	29.6	28.6	3.6	2.6
Total debt as % of GDP	22.4%	21.5%	25.4%	22.5%	22.9%	23.7%

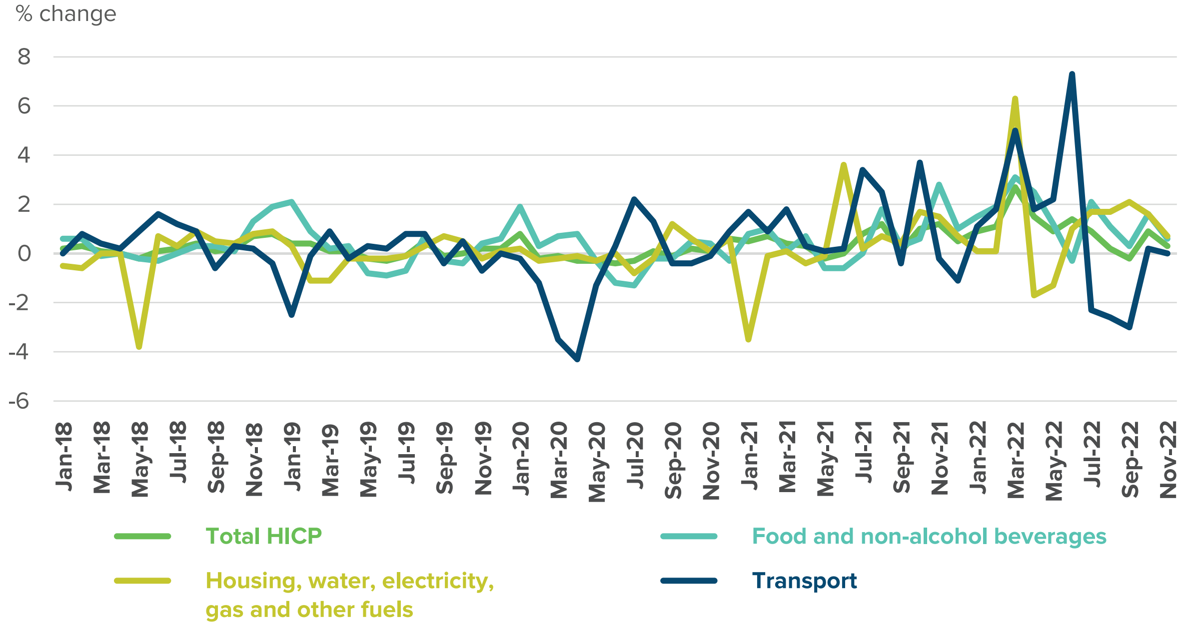
COMMODITY PRICE INDEX

62. Prices were already on the rise before the war, resulting from the COVID-19 crisis and the related fiscal interventions. In 2021, the war in Ukraine exacerbated the situation, with steep price increases in commodity markets, pushing food prices to a record and natural gas to historic highs. Prices for wheat, a staple in which Russia and Ukraine together account for about a quarter of global exports, were up 54% in March 2022 from a year earlier. It has since decreased but is still far above 2021 price levels.[20] With food and energy imports from these sources disrupted, and with other countries placing a ban on exports, countries face high costs and uncertainty about supplies. Kosovo is no exception. Chart 12 below provides monthly price changes for the Harmonized Index of Consumer Prices (HIPC) (total and selected items) in Kosovo, from 2018 to the November 2022. The price of food items, especially cereals, which increase started in the third quarter of 2021, has continued to grow substantially over the current year. The same is valid for the price of transport which is directly affected by the fuel prices increases (and saw a bump at the end of the summer), and housing.

[20] https://www.fao.org/worldfoodsituation/foodpricesindex/en/

Chart 12. **MONTHLY CHANGES OF HICP BY MAIN GROUPS JAN 2018-NOV 2022 (IN %)**

Source: Kosovo Agency of Statistics



CHANGES TO COMMODITY PRICES

63. The import price index in Kosovo increased by 1.7% in Q3 2022 compared to Q2 2022. Compared to Q3 2021, import prices increased by an average of 17.5%. Sorted by magnitude and sector mineral products increased by 52.8%; stone, mortar, ceramic and glass products (41.2%); edible oils (37.0%); wood and articles thereof (30.3%); plastic, rubber and articles thereof (18.9%); plant products (18.8%); live animals and animal outputs (15.3%); base metals and articles of base metals (11.5%); footwear (10.5%); prepared foodstuffs, beverages and tobacco (9.0%); means of transport (9.0%); papers and articles thereof (8.4%); textile and articles thereof (7.2%); machinery equipment and electrical equipment (6.6%); products of chemical industries (4.9%); various manufactured items (4.5%); and optical, photographic, measuring, medicinal and musical instruments and clock mechanisms (1.8%).[21]

CHANGES TO PRODUCER PRICES

64. The producer price index in Kosovo increased by 11.3% in Q3 2022 compared to Q2 2022. Compared to Q3 2021, producer prices increased by an average of 17.2%. The largest increase by branches of economic activity is observed in: electricity, gas, steam and air conditioning supply (49.7%); manufacture of paper and articles thereof (14.3%); manufacture of food products (14.2%); manufacture of electrical equipment (11.6%); manufacture of articles from straw and woven materials - knitting (9.4%); manufacture of machinery and equipment (8.2%); manufacture of fabricated metal products, except machinery and equipment (8.1%); manufacture of non-metallic mineral products (7.3%); manufacture of metal (6.1%); production of beverages (5.7%); manufacture of leather products and articles thereof (5.3%); manufacture of rubber and plastic products (4.7%); water collection, treatment and supply (3.8%); manufacture of chemical products (2.8%); other ores and quarries (1.5%); and manufacture of motor vehicles (transport), trailers and semi-trailers (0.1%). The increase was counteracted by the decrease in prices of metal ore extraction with -28.8% and manufacture of furniture (-7.3%).[22]

[21] https://ask.rks-gov.net/media/7182/import-price-index-ipi-q3-2022.pdf
[22] https://ask.rks-gov.net/media/7192/producer-price-index-ppi-q3-2022.pdf

5

STRATEGIC FORESIGHT

65. The impact analysis quantified above provides the characterization of an economy impacted by higher global oil and food prices and made worse by several domestic amplifiers: (i) weak domestic energy generation resilience (ii) import dependency and limited levels of private investment outside of construction, which limits growth multipliers as well as critical forwards and backwards linkages.

66. While consumption and diaspora-driven service exports remain key drivers of growth, poverty levels, a social protection system undergoing reforms, low labour force participation (particularly female workers), and dependence on the regional energy market substantially determine vulnerability and resilience to external shocks. On top of existing vulnerabilities, which were not emerging clearly due to the 3.2% GDP fiscal stimulus that elevated the economy during COVID-19[23], and based on the trajectory of global international affairs around the war in Ukraine, the following strategic foresight issues will need to be deliberated by the Kosovo institutions in terms of setting short- and medium-term policy, investment, expenditure, and mitigation priorities. Alongside a growing import bill which likely leads to a further deterioration in the current account deficit (CAD), growing fiscal and budget deficits and the reality that the impact of the war in Ukraine on the Western Balkans and Europe can only get worse, the issues outlined below will remain pertinent to policymakers for some time to come.

GLOBAL CAPITAL TIGHTENING INCREASES THE COST OF BORROWING

67. Though Kosovo's financial markets remain small and fairly shallow, the increased cost of credit as a result of capital tightening will likely impact borrowing rates and the profitability of the private sector. In July the European Central Bank (ECB) announced that the interest rate on the main refinancing operations and the interest rates on the marginal lending facility and the deposit facility will be increased to 0.50%, 0.75% and 1.00% respectively, with effect from 27 July 2022. By the 27th of October 2022, the ECB further announced that the interest rate on the main refinancing operations and the interest rates on the marginal lending facility and the deposit facility will be increased to 2.00%, 2.25% and 1.50% respectively, with effect from 2 November 2022.

68. While EU member state policymakers face the challenge of reining in inflation without compounding the economic slowdown and increasing debt default risks, higher interest rates will slow investment and reduce investment flows into key areas of the economy. With the € losing ground against the US$ in 2022 alone, the cost of imports across the Eurozone has spiked inflation for many critical commodities. In such a context, and where the central institutions' capital spending has been reduced, the risks of reduced fiscal space and the potential for greater

[23] https://www.worldbank.org/en/country/kosovo/overview#3

borrowing will need to be watched closely. While the energy transition and the costs of meeting Agenda 2030 SDGs have not been costed, in Bosnia and Herzegovina (for example), the price tag is forecasted at tens of billions of €.

69. The European Union has introduced the European Green Deal to improve life and move the economy away from fossil fuels and greenhouse gas-intensive industries, as well as to mitigate the socio-economic costs of transition. Agenda 2030 supports this agenda and the digital economy transition, which again comes at considerable expense. For both the energy and digital transitions, and given limited fiscal space and low capital spending, crowding in private capital will be essential if both transitions are to be given sufficient resources. This will require various forms of blended finance beyond Public Private Partnerships (PPPs) to include catalytic first loss finance, guarantees and risk transfer arrangements for example.

70. The key takeaway is that addressing inflation is a double-edged sword. Bringing inflation down means raising interest rates which impacts borrowing costs, debt servicing and levels of investment. At a time when decarbonization and the EU Green Deal have been launched, a combination of the energy crisis (pushing EU member states towards greater dependency on conventional generation) and increased costs of financing will impact the ability of low-income households in Kosovo to pay.

ENERGY COST FUTURES

71. The future price of energy and food is difficult to assess, partly because global supply and demand fluctuate, but also because climate change has uneven impacts. While the IMF predict that international energy prices are expected to remain above their pre-war levels for the foreseeable future and that surging energy costs and a weaker outlook will impact asset quality and firms' earnings, ongoing and upcoming support from the EU is planned to cushion rising energy costs and to protect businesses and consumers. Such transitional support measures are expected to continue.

72. What is clear for Kosovo is that replacing the two aged coal power plants (Kosova A and B) in the context of a transition to a clean energy future involves a challenging energy-mix transition at a time when supply-side shocks from Russia have disrupted critical imports. With regional and global demand for energy set to increase against an uncertain supply side future,[24] and with investments in solar power (KfW will provide a grant of 31.5 million euros, WBIF will provide a grant of 21.5 million euros, and the EBRD will loan 23.2 million euros to finance the 100-megawatt plant.) to take years to come to scale, the transition to independent domestic generation will not be a smooth ride, and energy rationing may become the new normal, impacting productivity and incomes. Possible load-shedding schemes will need to be adjusted to reflect changes to the power generation system as it too transitions. In the meantime, unless a peace is restored in Ukraine, securing Kosovo's energy futures will take five years or more, impacting medium-term growth and prosperity outcomes.

[23] After falling by about 1% in 2020 due to the impacts of the Covid-19 pandemic, global electricity demand is set to grow by close to 5% in 2021 and 4% in 2022 – driven by the global economic recovery – according to the latest edition of the IEA's semi-annual Electricity Market Report.

THE CRISIS MAY CHALLENGE THE SOCIAL CONTRACT AND COHESION

73. With high levels of unemployment and social exclusion among minorities and vulnerable groups, against a social protection system undergoing reforms, progress in reducing poverty rates could be reversed, undermining social cohesion. At the same time, social protection spending and energy subsidies to low-income groups will inevitably grow, reducing fiscal space, undermining critical investment in the Great Reset Agenda, Fourth Industrial Revolution (4IR), Industry 4.0 transition, and the Digital and Green economy transitions. Support for ethnic and social cohesion needs to be ramped up and reform of the social protection and pension system expedited.

IS THE CRISIS A SILVER LINING FOR THE GREEN AGENDA AND AGENDA 2030?

74. Though on the face of it the current crisis appears to distract from implementing the Green Agenda and Agenda 2030, the reality is that the issues raised by these agendas are thrust centre stage by the current crisis. The need for the Green Agenda to finance the energy transition has never been more pressing and the many targets set through the SDGs provide useful metrics for the central institutions to invest towards a less vulnerable and more resilient future.

6

SCENARIOS AND PROJECTIONS

75. Based on the diagnostic analysis conducted and partially presented above, five variables have been projected out as follows (i) food price inflation (ii) energy price inflation (iii) material price scenarios (iv) growth and fiscal scenarios and (v) institutional spending. The scenario assumptions are provided in Table 6 below, with a further description provided under the relevant scenario section below:

Table 6: SCENARIO ASSUMPTIONS

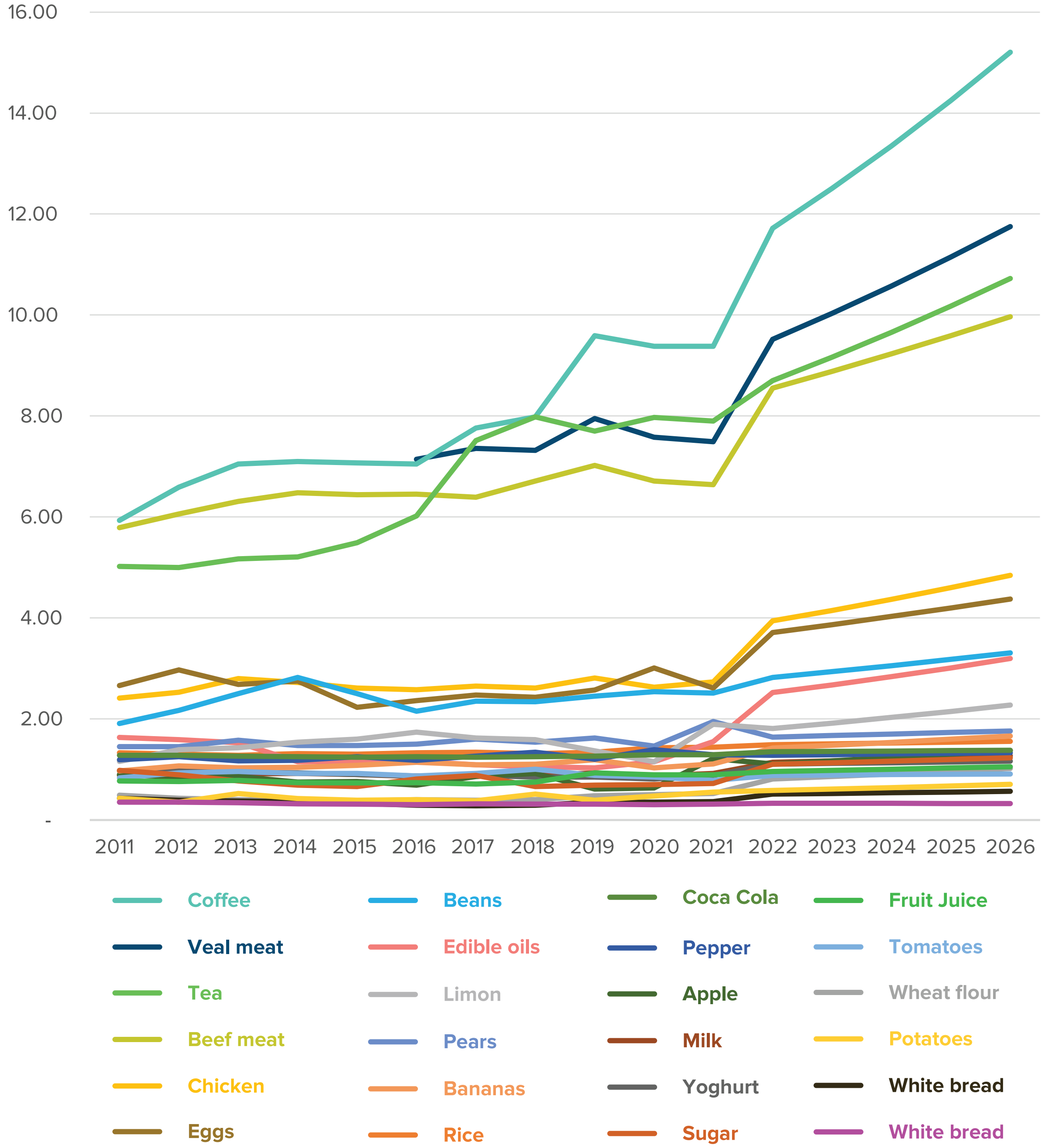
Scenario 1 (10-year average)	The current trend continues (inflation), and the central institutions maintain stability (continues the trend over the past 10 years). Projection uses average price change since 2011.
Scenario 2 (2021 Price Change)	Inflation continues to worsen, recession, and collapse in the central institutions spending (accelerates at 2021 rate). Projection uses price change 2021.
Scenario 3 (Average 2014-2018)	Return to pre-war trends post-COVID-19 pathway (resumes past 5-year trend before COVID). Projection uses an average of 5 years prior covid (2014-2018).

FOOD PRICE INFLATION FUTURE SCENARIO

76. Food price inflation is provided in Chart 13 below and is based upon the 10-year average price change projected out until 2026. Historical data is drawn from the harmonized commodity price index, with historical food prices from Q1 2011 to the end of Q2 2022. Long-term trend increases for edible oils, milk and beef would suggest growing import prices that cannot be immediately offset by import substitution. Increasing chicken and egg prices however could be offset by import substitution.

Chart 13. **FOOD PRICE (2011-2022 ACT.) - (2023-2026 FORECAST - 10-YEAR Average)**

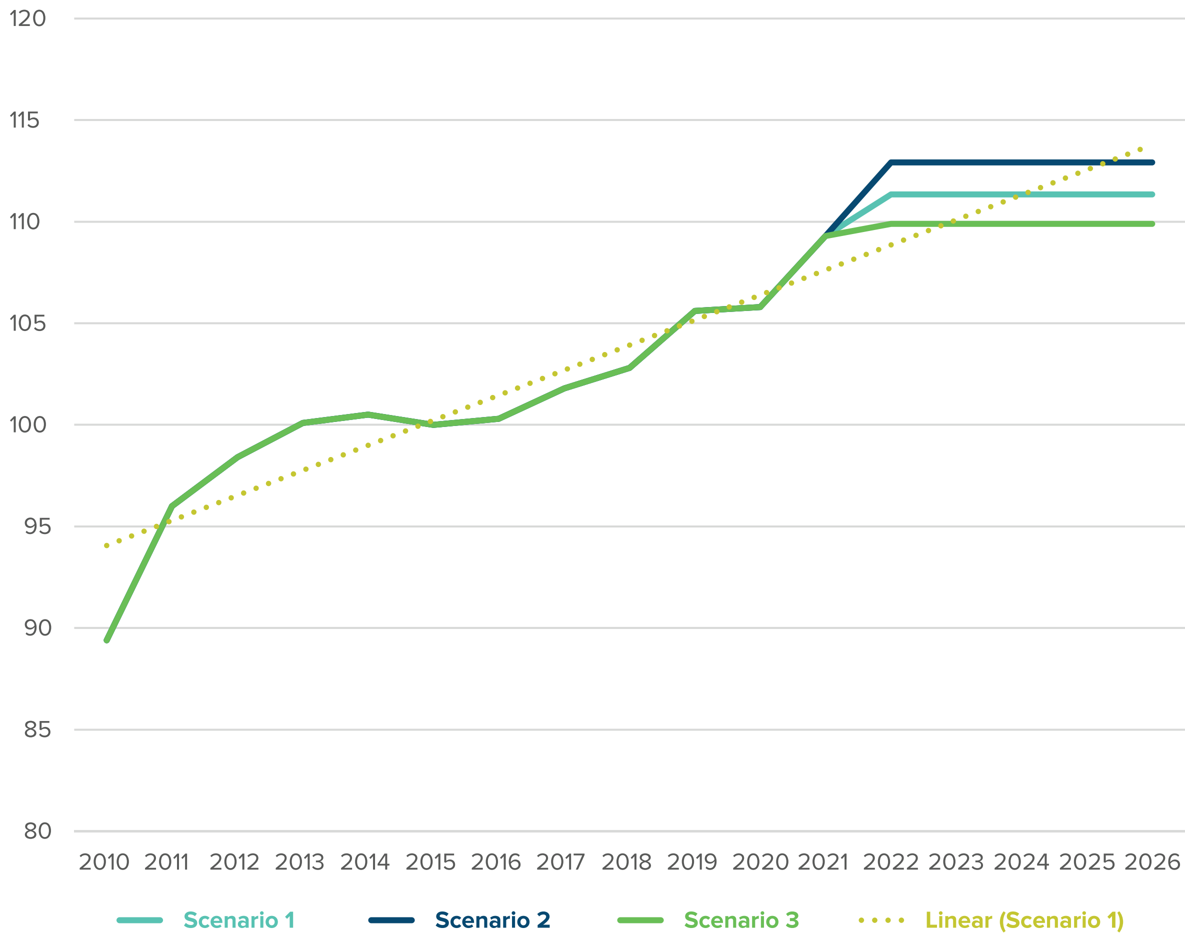
Source: Kosovo Agency of Statistics, Geopolicity Inc, Projections



77. As for the three scenarios applied to the overall harmonized commodity process, Chart 14 below provides the projections for the period 2022 -2026. While the assumptions cannot be future tested, as a combination they cover the most likely range of market eventualities, even assuming that peace is not restored in Ukraine any time soon. What is equally complex to project is the impact of global capital market tightening and the reduced value of the Euro against the US Dollar, for example, given that inflation will continue to be imported and shorter supply chains will likely continue to put pressure on prices.

Chart 14. **FOOD PRICE (2011-2022 ACT.) - (2023-2026 FORECAST - 10 YEAR AVG.)**

Source: Kosovo Agency of Statistics, Geopolicity Inc, Projections



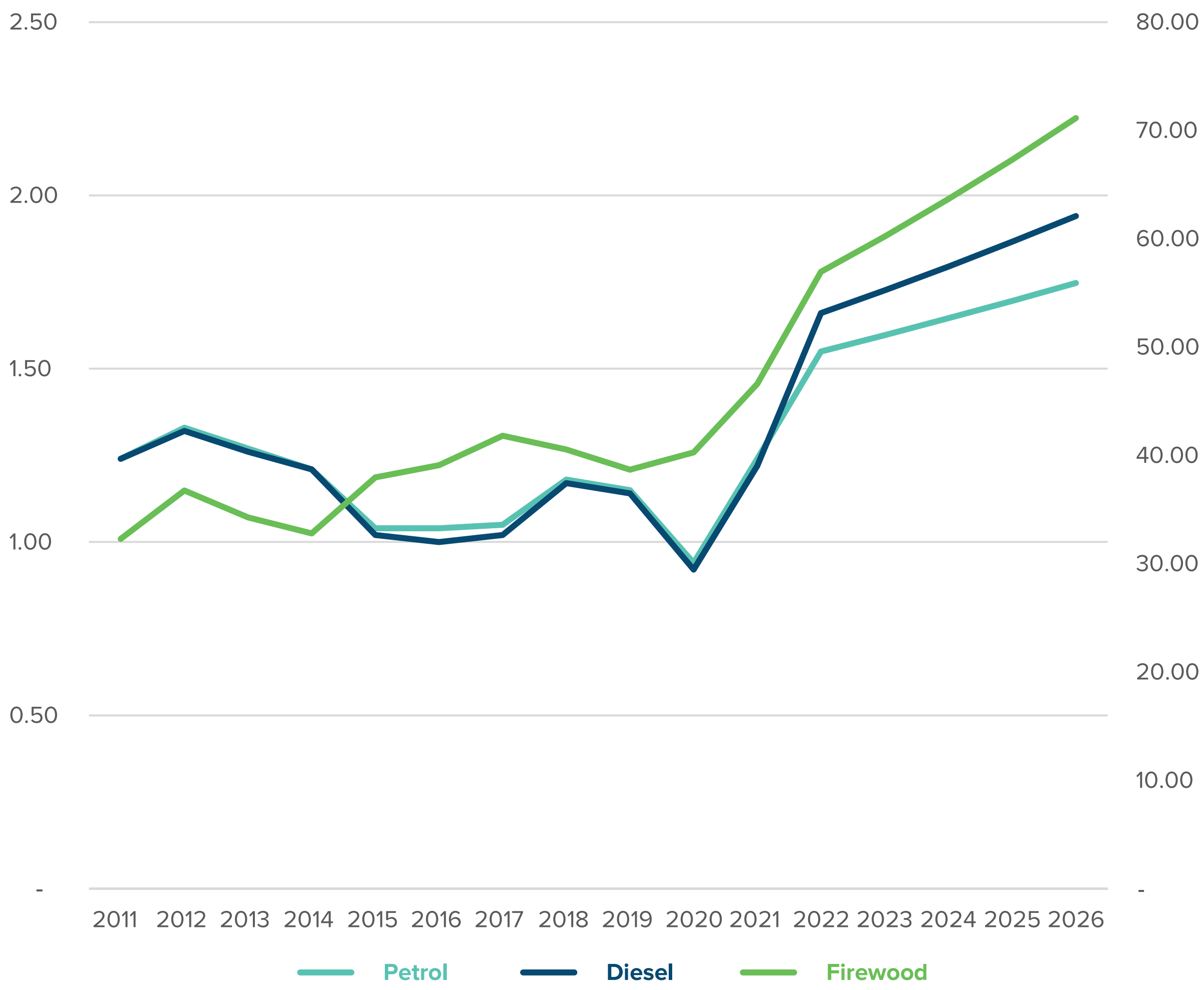
ENERGY PRICE FUTURE SCENARIOS

78. Energy price inflation is provided in Chart 15 below, based upon the 10-year average price change and projected out until 2026. Despite the considerable power generation by the two coal power plants (Kosovo A and B) to meet domestic needs, the increased electricity price trend from 2020 to 2021 would appear set to continue, given costly imports and the time and finance required to move towards a new energy mix. Feed-in tariffs for hydropower, wind, photovoltaic, and biomass, alongside an auction mechanism, will help. While the UK banned imports of Russian gas from the start of 2023, the EU on the other hand has not agreed on a ban on Russian gas. Instead, it has introduced policies to move away from dependence on it.[25] In November 2022 the EU announced a new €1 billion energy support package for the Western Balkans and welcomed new agreements to strengthen the Common Regional Market.[26] In a period of energy transition – to make the energy switch from conventional to alternative generation – external financing is going to be key to an orderly transition.

[25] https://commonslibrary.parliament.uk/research-briefings/cbp-9523/
[26] https://ec.europa.eu/commission/presscorner/detail/en/ip_22_6478

Chart 15. **ENERGY PRICE (2011-2022 ACT.) - (2023-2026 FORECAST - 10-YEAR TREND)**

Source: Kosovo Agency of Statistics, Geopolicity Inc, Projections

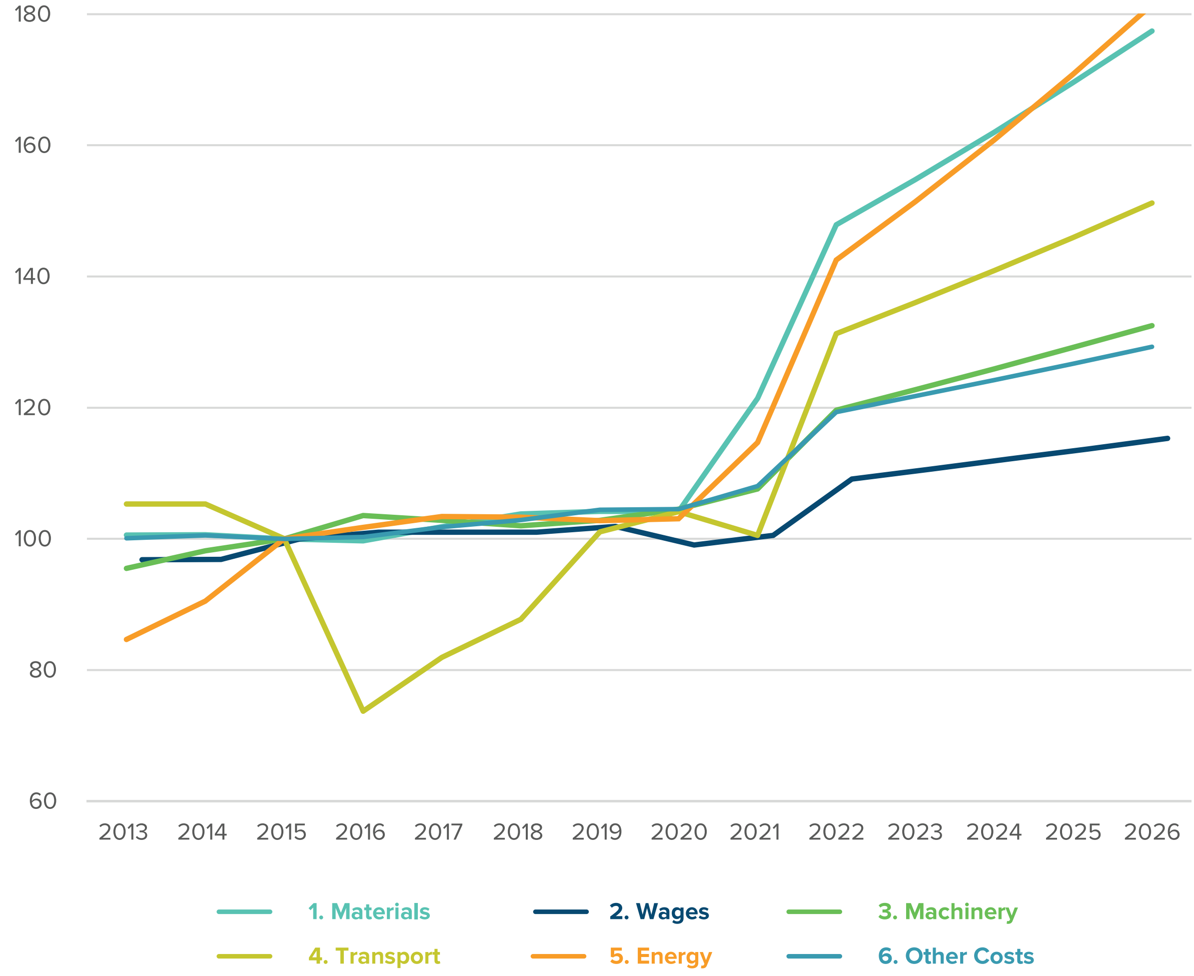


MATERIAL PRICE FUTURES SCENARIOS

79. Data from the Kosovo Harmonized Commodity Price Index tells the story of elevated prices corroborating with universal commodity price increases as shown in Chart 16 below. Problematically, building materials, energy prices and other costs have increased considerably, and yet labour prices are on a long-term slow rising trend, below the rate of inflation. Given Kosovo's import dependence on many materials, and in the light of a changing global trading regime and shorter supply chains, elevated costs are projected to increase for some time, into 2023 and beyond, as shown. Downward pressure on prices can only be met through a strong import substitution effect (which is complicated) or increased regional trade cooperation which would lower tariffs between Balkan economies.

Chart 16. **CONSTRUCTION MATERIALS PRICE INDEX (2013-2022 Q3 ACT., 2022 Q4 PROJ.) - (2023-2026 FORECAST - 10-YEAR TREND)**

Source: Kosovo Agency of Statistics, Geopolicity Inc, Projections

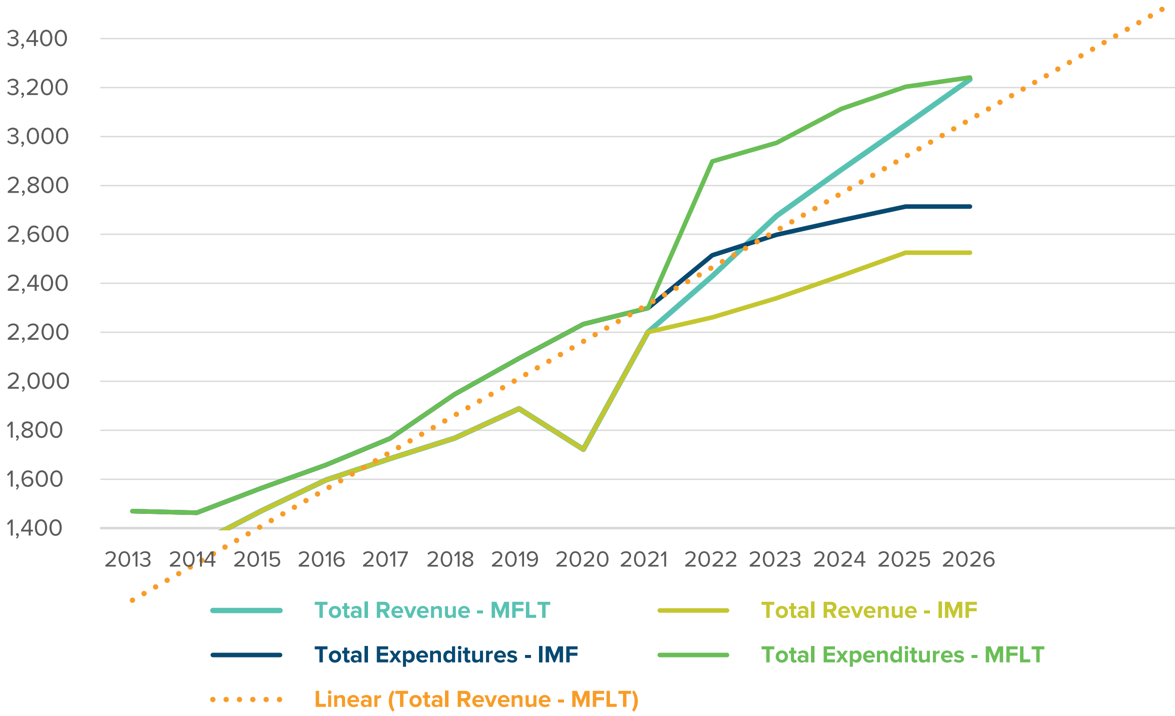


GROWTH AND FISCAL FUTURES SCENARIOS

80. GDP growth projections have been provided in the 2022-2025 MTEF, though with Kosovo institutions projecting higher growth outturns than the World Bank, European Bank for Reconstruction and Development (EBRD) or IMF, and with the IMF lowering global and regional growth forecasts, 2022 is forecast to underperform with elevated prices undermining real growth. Long-run projections provided by the MFLT MTEF, and IMF are provided in Chart 17 below, showing the significant difference between optimistic Kosovo institutions and more realistic IMF outturns.

Chart 17. MFLT MTEF AND IMF REVENUE AND EXPENDITURES 2012-2021 (ACTUAL) 2022-2026 (PROJECTED) (€ MILLION)

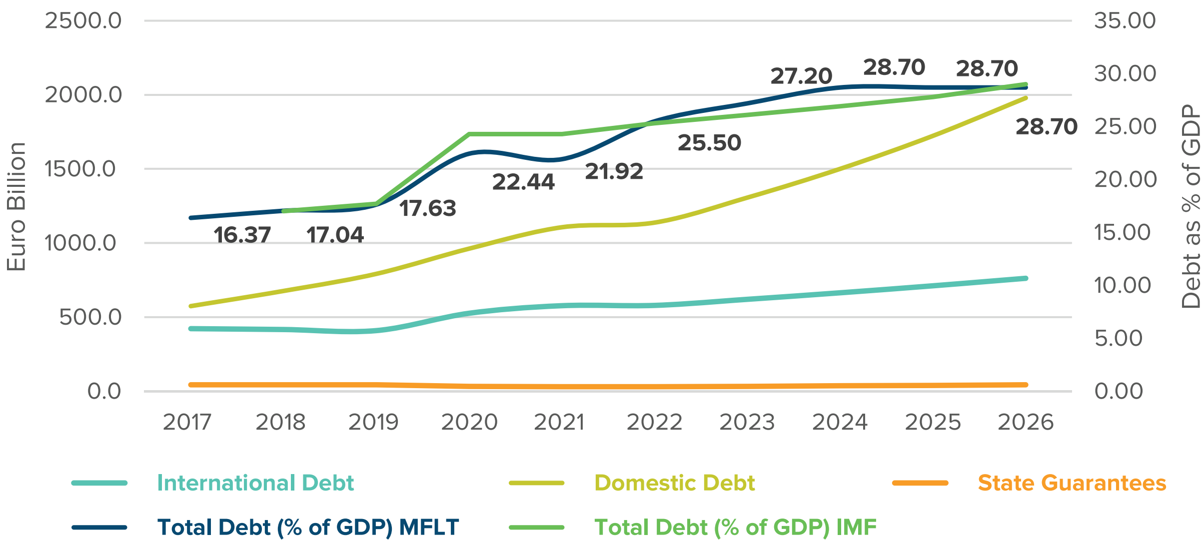
Source: Kosovo Agency of Statistics



81. As a result, the budget and fiscal deficits look to continue to grow over the medium term, with increasing dependence on domestic debt as shown in Chart 18 below. While the public debt ratio is projected to remain broadly unchanged at about 24 % of GDP in 2021 due to the strong rebound in fiscal revenues and lower-than-expected expenditure execution, and despite a fiscal rule anchoring debt to less than 40 % of GDP, the long-term costs of the energy transition, digital economy transition and meeting Agenda 2030 could see overall long-term debt increase.

Chart 18. PUBLIC DEBT COMPOSITION AND FORECASTS (2017-2026)

Source: MFLT MTEF (2023-2025), ERP (2022-2024), Geopolicity Inc, Projections

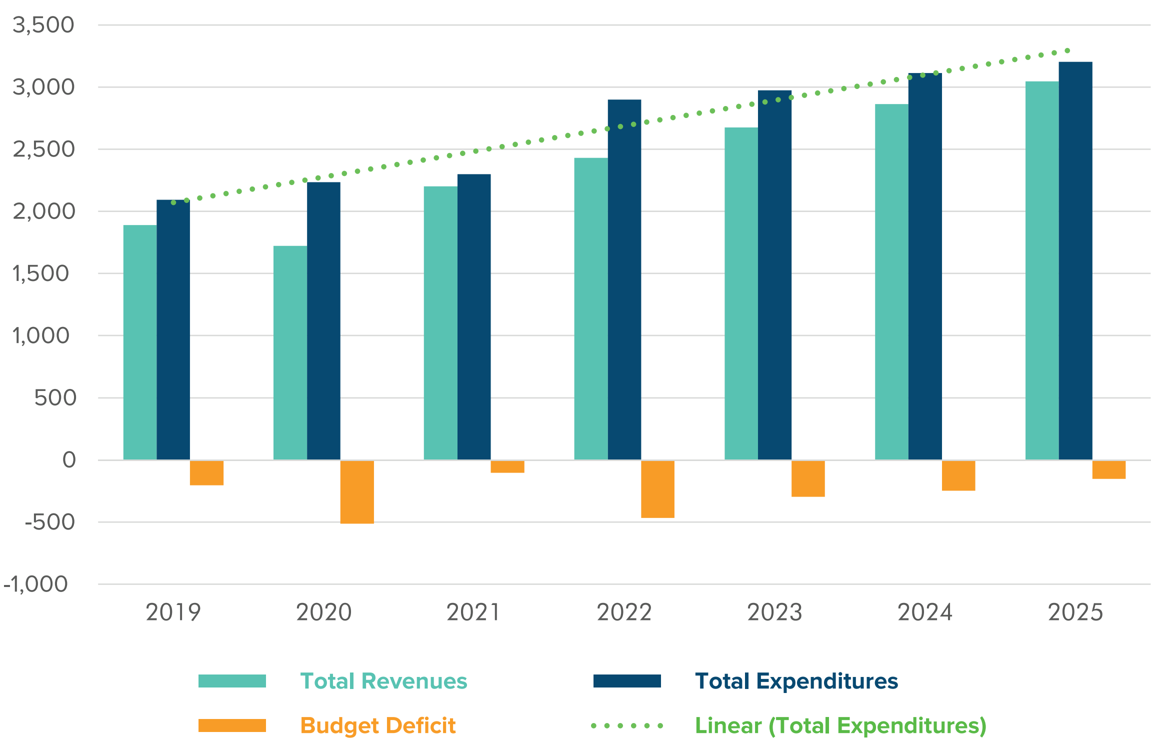


INSTITUTIONAL SPENDING FUTURE SCENARIOS

82. Institutional spending futures do not include a projection for operational and development spending by functional or economic classification, though these trends have been reported in previous sections. With inflation up and growth down, rates of fixed capital formation are likely to be negatively impacted and the increased cost of borrowing will likely slow investment, even if a counter-cyclical policy is maintained. Chart 19 below provides the budget deficit and financing need for the 2019-2025 period, showing an optimistic budget deficit, based on the MFLTs' strong revenue forecasts. However, if the trend established in 2020 and 2022 continues, either debt increases or investment spending towards growth will need to be reduced. With growing energy demand and the need to finance the energy transition, alongside increased costs of financing, new ways to finance sustainable development will need to emerge from e.g., the private sector.

Chart 19. **BUDGET DEFICIT AND FINANCING NEEDS (2019-2025) (€ MILLION)**

Sources: MFLT MTEF (2023-2025)



[27] "State Contingent Debt Instruments" for example link a public debt service payments to its capacity to pay, where the latter is linked to real world variables or events. Instruments can be linked to a country's GDP, to commodity prices, or to natural disasters such as hurricanes or earthquakes. when times are bad – such as during an economic downturn as a result of the war in Ukraine there is an automatic reduction in the public debt service burden. Similarly, GDP-linked bonds are a debt security or derivative security in which the authorized issuer (a country) promises to pay a return, in addition to amortization, that varies with the behaviour GDP. This type of security can be thought as a "stock on a country" in the sense that it has "equity-like" features. It pays more/less when the performance of the country is better/worse than expected. Other instruments cane be explored.

7

RISKS & MITIGATION MEASURES

83. This impact assessment shows how domestic amplifiers of vulnerability and resilience impede Kosovo's growth and prosperity future. Kosovo does not control its energy prices, remittances or regional security threats, and it remains heavily import-dependent due to a lack of product space development and investments towards diversification and frontier market development. As a result, the factors negatively impacting the economy cannot be controlled by the Kosovo central institutions, with energy and food prices, remittances and regional stabilization and security arrangements beyond its influence. However, the Kosovo institutions can influence the pace of the energy transition, the modernization of the social protection and welfare system, the composition of subsidies and incentives, and the investment framework to usher in a more resilient society, accepting complex regional dependencies.

PRIMARY RISKS

84. While other risks have been documented, the assessment highlights the following major risks to the socio-economy, people and institutions (see Table 7 below).

Table 7: PRIMARY RISKS FACING KOSOVO FROM THE UKRAINE CRISIS

Threats	Description
Energy Insecurity	The central institutions have limited to no ability to influence the costs of energy over the short term and the slow pace of the domestic energy transition secures that current energy vulnerabilities are here to stay over the medium term at best. In April 2022, the average price per megawatt-hour (MWh) on the HupX exceeded € 200 compared to € 55 in the same week 2021, highlighting the devasting impact that the slow pace of energy reform is now having on consumers. While investments to transition generation towards a new energy mix are underway, this transition would usefully have started many years ago, putting Kosovo in place to minimize external supply needs, and potentially to be a net exporter. The cost of energy provision is borne by households, and though energy subsidies will need to double or triple over the next 6-12 months, so will investments in new generation infrastructure to slowly reduce supply-side constraints.
Growth Challenges	While growth rebounded from the 2020 COVID-19 slowed down, growth was supported by fiscal subsidies, and the increased cost of energy and food has had a significant impact on growth futures over the short to medium term. Growth challenges have negative multipliers on employment, equality, social protection and social cohesion, and additional external fiscal support from the EU, IMF and World Bank may be required to balance the budget and meet growing social expenditure needs.

Rising Cost of Subsidies	Energy subsidies and increased welfare payments for those dealing with elevated costs of living more than doubled between Q3 2021 and Q3 2022, with probably the worst still to come. In addition to the €100 million energy subsidy bill (as the EU's €75 million budget support does not affect Kosovo's finances), the costs of subsidies will increase, at a time when overall institutional spending has increased. This would impact institutional debt, at a time of higher interest rates. However, there is a fiscal rule set with the IMF, and the institutions are returning to spending within the fiscal rule in 2023.
Social Cohesion	Economic pressures are often transmitted through challenges to the social contract and social cohesion. There are long-term risks for weakened social cohesion that should not be underestimated. The likelihood of demonstrations against the central institutions should not be ruled out, and investment in maintaining social stability through subsidies (for example) will remain of increased importance.

MITIGATION MEASURES

85. The immediate implications of the current situation for Kosovo institutions impact fiscal, expenditure, social policy, energy policy and development financing domains. As was the case during COVID-19, Kosovo institutions will need to be proactive in dealing with issues before they arrive, rather than reactive. Many of the strategic foresight issues are likely to manifest to differing degrees and given the current crisis in Europe and Eurozone-wide, external support is likely to be more stretched, implying the need for domestic players to drive policy, energy, and financial market reforms, to improve financing to secure the complex transition ahead; private capital will be key. Moreover, given the need for a revised social protection policy, putting measures in place before negative social impacts emerge will be important. As a result, the following mitigation measures (see Table 8) are proposed, as part of a proactive approach to minimizing future risks and contingent liabilities.

Table 8: PROPOSED MITIGATION MEASURES

Mitigation Measures	**Description**
Energy Insecurity	Current power generation is mainly from aged lignite power plants (Kosova A and Kosova B, but also from the Ujmani/Gazivode and other hydropower plants, all owned by the central institutions. Kosovo has installed generation capacities of 1,431 megawatts (MW), including renewable generation capacities. However, the operational capacity is considered to be 1,099 MW, of which lignite thermal power plants account for about 87.36%, and the rest consists of the Ujmani/Gazivode hydropower plant with 2.91%, the Kitka wind power plant with 2.95% and other renewables (hydropower plants, solar panels and wind power plants), which consisted 5.43 % of total generation during 2021 (Eurostat, 2021).[28] Ramping up investment to support energy security through the EU Green Agenda and other tax and non-tax incentives is vital, including clarity of how to transition the energy mix (from coal-based generation dependency) to a more resilient and self-sustained system, mobilizing public and private capital. Moreover, with a focus on the green transition, while recognizing the limitation faced by Kosovo in receiving an international credit rating, both Green and SDG bonds can be rapidly issued to finance the transition, with de-risking and catalytic first-loss capital

	deployed incentive private capital that will be required for on an off-grid generation and distribution. The Energy Strategy (2022-2031) addressing supply security needs to be effectively implemented. Increasing energy efficiency and promoting near-zero energy buildings links the energy strategy with the real economy.
Growth Challenges	Heavy dependence on remittances, consumption and diaspora-driven service exports needs to be reduced through encouraging private capital to drive the necessary diversification, intensification, and export-driven growth future. Increased private capital flows, improving labour market participation, continued strong credit growth, better use of remittances and attracting increased foreign direct investment and portfolio inflows must remain central to improving growth outcomes. To continue growth, Kosovo needs to unleash productivity gains and create more quality jobs, address infrastructure bottlenecks, prioritize human capital investment, and ensure increased competitiveness and development of high-potential sectors. Increasing firm productivity, raising farm productivity, boosting exports, and increasing competition and private investment are vital. As a net importer of food, agricultural inputs, and energy, improving market resilience in these areas should strengthen policy focus, even though agriculture will continue to become a declining function of growth.
Fiscal Challenges	Maintaining and increasing fiscal space has never been more critical, given an expected negative impact on future revenue and increased pressure on general institutional and energy-related subsidies and social spending. If fiscal space remains too tight, given the limited capacity for market borrowing, investments in energy and diversified (resilient) growth will be impacted. A focus on the efficiency of the public administration, institution-owned enterprises and social protection as well as ramping up capacities for public-private partnerships and blending will be necessary, given a limited tax base and potentially growing levels of informality. A medium-term revenue strategy must remain policy objective number one, to include a focus on formalization and fiscal savings across public spending and increasing the space for private sector investment.
Social Cohesion	Dialogue between stakeholders and communities will be increasingly necessary, implying a move to a new way of working best defined as a whole-of-society approach to building forward better. It is important to invest in social dialogue, social equity and social justice space, to minimize the risk that un-reconciled issues come to the fore.

[28] https://bankwatch.org/blog/narrow-road-ahead-the-energy-crisis-in-kosovo-in-the-context-of-russia-s-invasion-of-ukraine

8

RECOMMENDATIONS

86. The impacts, risks and proposed mitigation measures included here emerge from an assessment of quantifiable impacts resulting from the Ukraine crisis with a focus on factors outlined in the scope of work. While projections will need to be regularly updated, supported by both Q2 and Q3 data, the emerging trends resulting from the crisis have already been formed and are documented here. Remittances are rising, as is domestic debt, inflation and subsidies, and wages will remain stagnant until the enforcement of the new law regulating public wages is introduced.

87. In navigating the various crossroads and transitions, the central institutions need to crowd in private capital wherever possible and use EU funds through blended solutions that de-risk and accelerate the energy and other transitions. Currently, these transitions are not fully costed and while public debt is sustainable and the fiscal deficit remains within limits, going forward, a new Kosovo investment strategy and approach will be required. As the Green Deal and key elements of the Agenda 2030 remain central to EU integration, new ways of aligning Kosovo's public investment system with the EU taxonomy on sustainable activities are needed. Given UNDP's work with the EU on INFF (Integrated National Financing Frameworks) to promote this agenda, opportunities for deeper collaboration in the sustainable financing space seem both necessary and urgent.

88. Given the need for the Kosovo institutions and international partners to use this work to inform a proactive policy and investment agenda, it is clear that any reset would need to focus on energy transition and market development, growth diversification and intensification, social protection and investments to promote social cohesion the social contract, as well as a ramping up of institutional revenue generation and mobilization capacities. To offset long-term fiscal challenges, crowding in private capital and blended financing instruments will be needed to finance the energy transition, albeit supported by the EU Green Agenda. To navigate the complex transition ahead, new resource flows need to be integrated into the ERP – particularly private capital – and international partners will need to provide catalytic and de-risking support. If the transition is under-financed, vulnerabilities will remain, and resilience will be compromised.

89. The many issues and challenges evidenced here would be the natural target for a transition to more innovative and sustainable financing solutions, which are now necessary to secure the forthcoming transition. Ushering in a new generation of innovative and sustainable financing instruments must be policy central unless domestic debt piles are to mount up and institutional spending be caught in a vicious cycle.

ANNEX 1: DATA AND STATISTICAL ANNEX

Kosovo Public Debt Composition and Levels (2017-2022 (Projected)										
	2017	2018	2019	2020	2021	2022	2023	2024	2025	2026
International Debt	422.2	416.4	409.1	525.8	576.8	578.7	619.7	663.6	710.6	761.0
Domestic Debt	574.3	676.6	791.9	961.9	1106.1	1137.5	1306.2	1500.0	1722.5	1977.9
Kosovo Guarantees	44.0	43.7	42.7	31.7	30.6	30.1	33.1	36.3	39.8	43.7
Total Debt (% of GDP) MFLT	16.37	17.04	17.63	22.44	21.92	25.50	27.20	28.70	28.70	28.70
Total Debt (% of GDP) IMF		17.00	17.70	24.30	24.30	25.30	26.10	26.90	27.80	29.00
Total Debt	996.4	1093.1	1201.1	1487.7	1682.9	1716.2	1925.9	2163.6	2433.1	2738.9

SOURCE: Kosovo ERP 2022- 2024

General Institutional Revenues based on ESA2010											
ESA Description	**2020 Q1**	**2020 Q2**	**2020 Q3**	**2020 Q4**	**2021 Q1**	**2021 Q2**	**2021 Q3**	**2021 Q4**	**2022 Q1**	**2022 Q2**	**2022 Q3**
Taxes on products	295.5	278.5	337.1	367	336.6	395.5	485	437.9	394.4	427.2	547.3
VAT	171.5	157.1	194.4	216	201.9	237.7	282.5	262.3	250.4	267.2	332.8
Taxes and duties on imports	116	114.8	132.8	140.7	125.1	146.7	190.5	164.5	133.1	148.9	201.1
Import Duties	25.3	21.9	28.1	31.5	24.9	29	37.1	35.7	27.5	32.6	37.8
Taxes on imports excluding VAT and duties	90.7	93	104.7	109.2	100.2	117.7	153.3	128.9	105.6	116.3	163.3
Taxes on products except for VAT and import taxes	8	6.6	9.9	10.3	9.5	11.1	12.1	11.1	10.9	11	13.3
Other taxes on production	11.3	9.8	13.3	10.7	13	4.5	12.2	10.5	20.2	12	15.4
Property income	-	7.2	-	7.2	6.2	8.9	14.5	13.3	2.1	9.5	11
Current taxes on income. wealth. etc.	63.9	60	68.9	71.7	73.1	94.8	82.3	80.3	96.1	112	94.8
Other current transfers	5.7	6	15.5	31.2	14.9	9.9	8.6	10.4	10.4	10.8	20.2
Financial assets and liabilities	2.8	213.8	57.5	189.2	58.9	122.3	42.7	44.4	12.2	37.2	18.9
Payments for non-market output (Sales)	23.3	11.9	20.3	26.2	20.9	24.2	28.6	30.3	22.2	26.5	27.7
Totals	**402.4**	**587.2**	**512.6**	**703.2**	**523.6**	**660**	**673.9**	**627.1**	**557.6**	**635.2**	**697.5**

General Institutional Expenditures based on ESA2010											
ESA Description	**2020 Q1**	**2020 Q2**	**2020 Q3**	**2020 Q4**	**2021 Q1**	**2021 Q2**	**2021 Q3**	**2021 Q4**	**2022 Q1**	**2022 Q2**	**2022 Q3**
Compensation of employees	154.7	172.1	164	170.6	169.8	162.3	154.4	161.5	160	160.5	142.7
Subsidies	16.7	24.2	25.8	173.2	46.6	26.6	42.2	105.1	26.3	55.1	140.9
Property income. payable	9.1	4.4	8.4	5.6	8.5	6.4	9.2	6.7	9.7	7.2	10.3
Social contributions and benefits	133	187.8	179.1	173.7	150.1	138.1	134.7	196.2	145	180.9	150.1
Other current transfers	4	7.6	9	10.7	8.3	9.9	11.5	22.7	8.7	12.3	10.6
Capital transfers	0.9	5.7	7.2	4.7	0.3	3.6	2.6	3.2	0	33.4	1.2
Financial assets and liabilities	15.4	25.3	27.1	49.3	22.8	24.2	29	56.2	20	10.9	10.4
Acquisitions less disposals of non-produced assets	1.2	1.6	12.5	5.3	2.8	1.6	2.7	14.8	13.9	10.1	11.6
Intermediate consumption	40.3	47.2	52.4	88.6	59.8	77.7	71.2	125.2	58.1	80.3	79.6
Gross capital formation	25	59.1	94.4	135.4	52	55.4	69.2	130.8	18	31	58.6
Totals	**400.3**	**534.9**	**579.8**	**817.1**	**521**	**505.9**	**526.9**	**822.6**	**459.7**	**581.7**	**615.9**

Nominal GDP (€ Millions) 2018 – 2021 (Actuals) – 2022-2026 (Projected)									
	2018	2019	2020	2021	2022	2023	2024	2025	2026
Nominal GDP (MFLT)	6,672.0	7,056.0	6,772.0	7,817.0	8,754.0	9,621.3	10,407.8	11,156.4	11,491.1
Nominal GDP (IMF)	6,672	7,056	6,772	7,637	8,568	9,212	9,815	10,400	10,712.0
Real Growth Rate (%) (MFLT)	3.60	5.60	-5.30	10.50	5.70	7.10	6.20	6.10	6.3
Real Growth Rate (%) (IMF)	3.60	5.60	-5.30	-9.50	2.80	3.90	4.10	3.90	4.0

Source: MFLT METF 2023-2025 (April 2022)

Budget Deficit and Financing Needs (2019-2025)							
	2019	2020	2021	2022	2023	2024	2025
Total Revenues (1)	1,882	1,722	2,201	2,430	2,676	2,864	3,047
Total Expenditures (2)	2,093.00	2,234.00	2,299.00	2,898.00	2,974.00	3,113.00	3,203.00
Budget Deficit	-205.00	-512	-104	-466	-297	-248	-154

Source: MFLT METF 2023-2025 (April 2022)

Remittance inflows - by channels (In € million, flow statistics)				
Description	Total remittance inflow	Banking channel	Money transfer operators	Other channels
January	62.3	10.1	29.6	22.6
February	63.3	5.9	34.5	22.9
March	61.7	7.3	41.2	13.2
April	60.3	8.8	51.5	n.a.
May	104.0	15.4	88.6	n.a.
June	82.9	12.6	59.0	11.3
July	92.3	15.0	69.3	8.1
August	81.6	13.5	59.5	8.5
September	88.3	13.7	64.8	9.9
October	99.6	11.9	59.1	28.5
November	88.3	12.1	58.4	17.9
2020 December	95.3	15.0	56.6	23.7
January	69.3	10.3	41.2	17.7
February	76.8	9.6	46.8	20.4
March	96.8	13.5	60.8	22.6
April	90.5	13.5	64.8	12.1
May	113.3	14.1	69.0	30.2
June	107.7	16.0	60.2	31.5
July	102.5	20.1	49.6	32.7
August	110.2	20.1	45.6	44.5
September	94.7	15.1	58.5	21.1
October	94.8	14.5	58.0	22.2
November	89.5	15.2	56.5	17.8
2021 December	107.3	16.7	53.0	37.6
January	70.5	14.9	42.4	13.3
February	76.2	12.0	49.2	15.0
March	94.7	15.1	61.7	17.8
April	108.1	14.6	66.7	26.9
May	101.1	15.3	58.4	27.4
June	104.9	17.4	61.2	26.4
July	114.9	23.6	57.4	33.8
August	131.6	22.4	55.6	47.4
September	102.6	17.1	62.6	22.9
October (p)	104.4	15.5	64.6	24.3
2022 November (p)	93.7	15.0	62.4	16.3

Monthly changes of CPI-HICP by main groups of COICOP by main groups

	2021-01	2021-02	2021-03	2021-04	2021-05	2021-06	2021-07	2021-08	2021-09	2021-10	2021-11	2021-12	2022-01	2022-02	2022-03	2022-04	2022-05	2022-06	2022-07	2022-08	2022-09	2022-10	2022-11
Total HICP	0.5	0.7	0.4	0.3	-0.2	0.0	0.8	1.2	0.1	1.0	1.2	0.5	0.9	1.1	2.7	1.5	0.9	1.4	0.9	0.3	-0.2	0.9	0.3
Food and non-alcoholic beverages	0.8	1.0	0.1	0.7	-0.6	-0.6	0.0	1.8	0.3	0.6	2.8	1.0	1.5	1.9	3.1	2.5	1.2	-0.3	2.1	0.6	0.3	1.6	0.6
Alcoholic beverages, tobacco	1.2	0.7	0.8	0.6	-0.4	-0.9	1.1	0.4	0.2	0.1	-0.5	1.3	0.2	-0.5	0.2	2.1	0.3	0.6	1.0	-0.4	0.2	1.0	-0.4
03. Clothing and footwear	0.5	1.5	1.4	0.2	-0.2	-0.5	0.1	-0.4	-0.1	-0.5	-0.4	-0.9	-0.8	0.4	3.0	-0.8	0.6	0.2	-0.3	-2.6	0.4	1.6	-2.6
Housing, water, electricity, gas and other fuels	-3.5	-0.1	0.1	-0.4	-0.1	3.6	0.2	0.7	0.4	1.7	1.5	0.7	0.1	0.1	6.3	-1.7	-1.3	1.0	1.7	0.7	2.1	1.6	0.7
05. Furnishing, household equipment and routine maintenance of the house	-0.4	0.7	-0.2	-0.1	0.5	-0.1	0.4	0.5	0.4	0.1	0.6	0.6	0.3	0.5	0.6	1.4	0.7	0.6	0.8	0.5	1.5	0.4	0.5
06. Health	0.3	0.0	-0.2	0.1	0.0	0.0	0.0	0.1	-0.1	0.5	0.3	0.1	0.5	-0.1	0.6	0.1	0.1	0.5	0.0	0.2	-0.3	0.1	0.2
06. Health Transport	1.7	0.9	1.8	0.3	0.1	0.2	3.4	2.5	-0.4	3.7	-0.2	-1.1	1.1	1.8	5.0	1.8	2.2	7.3	-2.3	0.0	-3.0	0.2	0.0
08. Commu-nication	-0.2	0.0	0.1	0.1	0.0	-0.3	-0.1	0.4	-0.1	0.1	0.1	0.1	0.0	-0.1	-0.1	0.3	-0.1	0.2	-0.1	0.1	-0.2	0.2	0.1
09. Recreation and culture	0.5	0.2	0.0	0.2	-0.1	0.6	1.8	0.5	-1.3	-1.0	-0.3	0.5	0.5	0.2	0.4	0.2	0.4	0.2	3.9	0.3	-2.4	-1.0	0.3
10. Education	1.0	0.0	0.0	0.0	-0.1	0.0	0.0	0.0	0.7	0.0	0.0	0.1	0.7	0.0	0.0	0.0	0.0	0.0	-0.5	0.0	0.3	0.0	0.0
11. Restaurants and hotels	0.8	0.2	0.1	0.0	0.0	0.1	0.3	-0.1	0.7	0.4	1.9	1.4	1.2	0.6	0.9	1.3	0.5	2.1	1.9	0.1	0.1	0.2	0.1
12. Miscellan-eous goods and services	0.4	0.6	-0.1	0.1	0.1	0.0	-0.1	0.0	0.7	0.3	0.1	0.5	0.3	0.4	0.3	0.6	0.1	0.7	0.3	0.5	0.2	0.7	0.5

CPI-HICP by COICOP for Food and non-alcoholic beverages	2021-01	2021-02	2021-03	2021-04	2021-05	2021-06	2021-07	2021-08	2021-09	2021-10	2021-11	2021-12	2022-01	2022-02	2022-03	2022-04	2022-05	2022-06	2022-07	2022-08	2022-09	2022-10	2022-11
CPI-HICP	110.2	111.3	111.4	112.1	111.5	110.8	110.8	112.8	113.1	113.8	117.0	118.1	119.9	122.1	125.9	129.0	130.6	130.2	133.0	134.5	134.9	137.0	137.9
Monthly Change	0.8	1.0	0.1	0.7	-0.6	-0.6	0.0	1.8	0.3	0.6	2.8	1.0	1.5	1.9	3.1	2.5	1.2	-0.3	2.1	0.6	0.3	1.6	0.6

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