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ANNUAL ECONOMIC FORUM

Overcoming the trap of insufficient growth and enhancing the efficiency of investments

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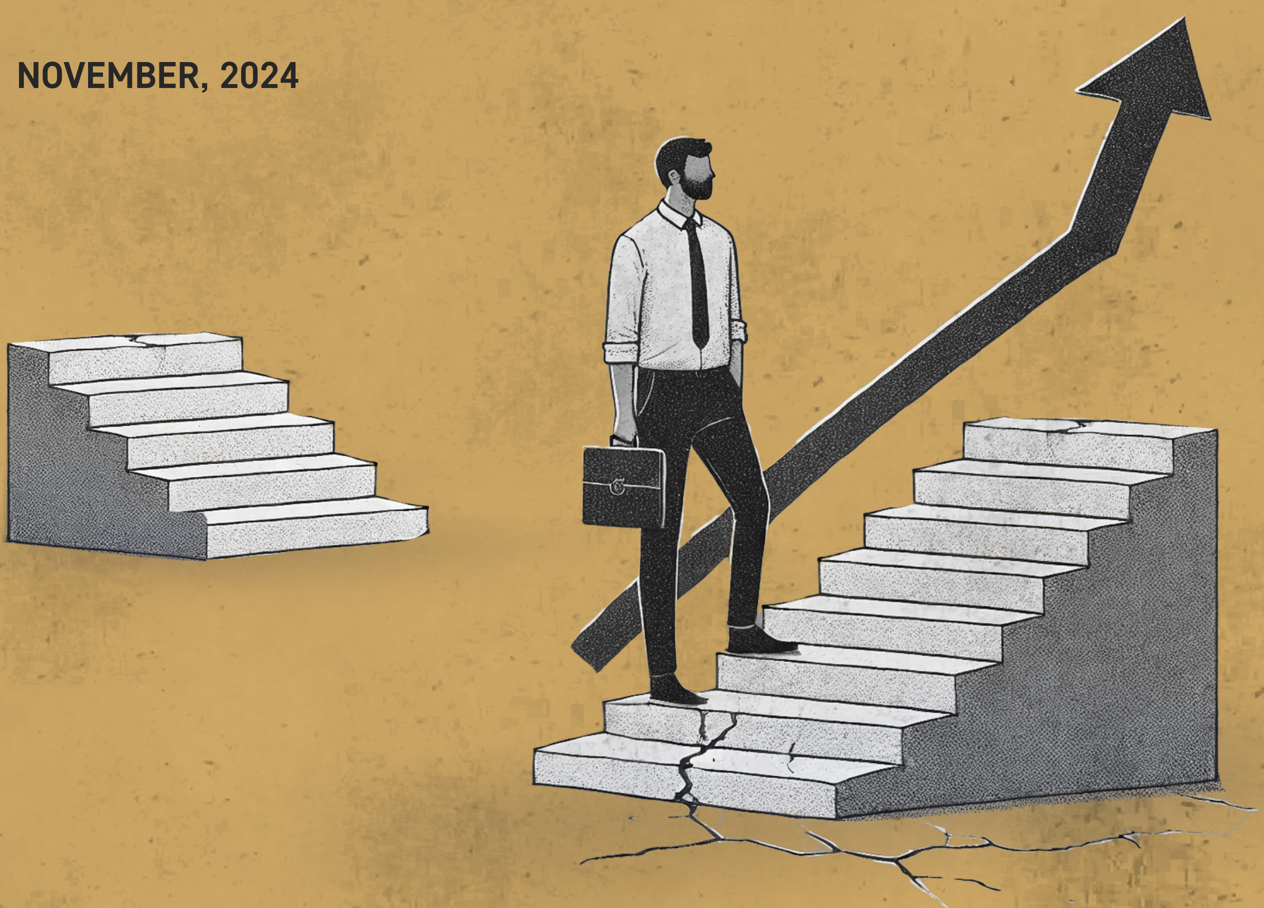

ANNUAL ECONOMIC FORUM

OVERCOMING THE TRAP OF INSUFFICIENT GROWTH AND ENHANCING THE EFFICIENCY OF INVESTMENTS

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Contents

ABBREVIATIONS

TAK	Tax Administration of Kosovo
WB	World Bank
EU	European Union
EBRD	European Bank for Reconstruction and Development
BP	Western Balkans
CBK	Central Bank of the Republic of Kosovo
CEFTA	Central European Free Trade Agreement
ERA	European Research Area
FEV	Annual Economic Forum
FKGK	Kosovo Credit Guarantee Fund
IMF	International Monetary Fund
GFCF	Gross Fixed Capital
HMIC	Higher-Middle-Income Countries
ICOR	Incremental Capital Output Ratio
FDI	Foreign Direct Investment
KEK	Kosovo Energy Corporation
KFOS	Kosovo Foundation for Open Society
MINT	Ministry of Industry, Entrepreneurship and Trade
NPQ	Central Public Enterprises
SME	Small and Medium Enterprises
OECD	Organisation for Economic Co-operation and Development
PRB	Board of Review Body Procurement
GDP	Gross Domestic Product
ICT	Information and Communication Technology
VAT	Value Added Tax
WEF	World Economic Forum
wiiw	Vienna Institute for International Economic Studies

EXECUTIVE SUMMARY AND RECOMMENDATIONS

This research report has been prepared to contribute to the debate at this year's session of the Riinvest Annual Economic Forum 2024 (AEF '24), a new product of the Institute that started with AEF '23 and aims to continuously assess economic developments over the years.

Although there is a lag compared to the Government's plans regarding the GDP growth rate; the International Monetary Fund (IMF) and the World Bank (WB) view Kosovo's economic trends in a more positive light than last year, especially in terms of macroeconomic stability and budget performance. In fact, economic growth has returned to pre-COVID-19 pandemic trends, oscillating around 4%. The Government's predictions, which accompany the 2025 budget, expect a GDP growth of 5.6%, a projection significantly higher than that of the IMF, WB, and wiiw (around 4%). This prediction could be challenged by difficulties in achieving the expected growth in real terms for exports (7%), and this also applies to expectations for investment growth, particularly public investments.

There is also concern over the deterioration of the external sector, where we have seen a decline in import coverage by the export of goods and an increase in the trade deficit, the current account deficit, and generally a deficit in the balance of payments. The level of remittances remains almost the same as last year, while foreign investments have shown an upward trend this year (7%) in a situation where the inflow of investments in the manufacturing sector and products with high-added value is still very low. The financial sector continues to perform well, with credit growth (12%) and a low level of non-performing loans, but it is still not sufficiently adapted to support development projects with more favourable conditions.

The projected budget for 2025 continues the growth trend of recent years, but it inherits significant issues related to the structure of capital investment execution, as well as the low financing of education, scientific research, innovation and healthcare. In all of these sensitive and essential sectors for improving the quality of development, Kosovo remains far behind the countries in the region and the requirements of the EU.

According to assessments from business leaders as part of a survey conducted with nearly 500 private SMEs (September-October 2024), the five main barriers to their business operations are informality and tax evasion, and workers' migration, both with almost equal intensity, followed by workers' skills and education, corruption, and financing costs, with an intensity ranging from 60 to 64 points out of a maximum of 100.

Special attention in this report is given to the volume, structure, and efficiency of investments expressed in GDP growth. While Kosovo has been investing 31-34% of its GDP in recent years, which is a higher investment intensity compared to the region, this does not adequately translate into economic growth due to lower efficiency, measured by the Incremental Capital Output Ratio (ICOR) indicator, which shows how much capital invested impacts GDP growth. Kosovo stands out with a high ICOR of 4.62, in contrast to other countries in the region, where this indicator ranges from 2.21 (Serbia) to 3.91 (North Macedonia). This means that Kosovo needs to use more capital to achieve a similar growth rate compared to other countries. This is consequence of low productivity, the capacity utilization level of about 60%, the unfavourable sectoral structure of investments, and the similarly unfavourable technical structure, where investments in buildings and land dominate over investments in equipment, research and development, and innovation.

The existing economic growth model in Kosovo is mainly based on increased consumption which leads to higher imports of consumer goods, and this in turn reduces the economic growth rate. This creates an unsuitable economic cycle that does not effectively support growth dynamics. Following the emphasis on the need for a new growth model in the report for the AEF 2023 session, it is essential to reiterate that this stage of the country's development requires serious commitment and an improvement in the quality of macroeconomic governance to overcome so-called "Middle Income Trap". The World Bank's report this year, addressing this issue—which also characterizes the situation in several other countries—suggests a synthesis of recommendations for a focused path for these countries, based on the so-called "3Is": Investments, Infusion, and Innovation.

One of the key problems Kosovo faces in overcoming this situation is an almost chronic shortcoming: the governing structures in Kosovo have lacked the ambition for qualitative changes in the country's economic reality. Therefore, a development ambition is needed that is free from the inertia and routine of previous policies, along with a national consensus focused on development that will steer the country towards advanced economies. Kosovo cannot escape this trap without first increasing investments in export-oriented sectors and, secondly, investing much more in knowledge and new technologies, research, development, and innovation. These are the essential elements for a new economic growth model. This would result in increased exports and a rise in the competitive domestic supply of products and services.

Based on the findings of this report, the Riinvest institute recommends:

1. The Government of Kosovo should establish a competent body composed of local and international experts to develop a long-term document with vision, ambition, and policy choices and measures that effectively overcome the existing economic growth model. This would also address the issues and barriers characteristic of the "middle-income trap" that prevent Kosovo from entering the group of high-income countries within a reasonable timeframe.

2. A restructuring of Kosovo's budget expenditures is needed to significantly increase spending and investments in education, healthcare, and research and innovation. Within a period of 2-3 years, the goal should be to reach the average level of spending and investments in these sectors found in the region, and gradually bring them in line with the EU average of government investments and expenditures as a percentage of GDP.

3. The Government should conduct a thorough analysis of the chronic weaknesses in capital investment execution, especially in projects funded by external loans, and increase accountability and leadership responsibility in ministries, agencies, and other budgetary organizations to address and overcome the current highlighted issues.

4. The entire external sector should also undergo a detailed, critical review to reduce deficits, particularly in the trade of goods, by promoting an integrated system of measures to stimulate and facilitate exports.

5. Business associations should engage with their membership to raise awareness that private investments, particularly from businesses themselves, in research, development, and innovation should be part of their daily agenda.

6. Business associations should also collaborate with research organizations and relevant institutions to advance the investment process in Kosovo, focusing on more efficient investments in equipment, knowledge, and new technologies, rather than oversized investments in construction, land, and other infrastructure. Some of these should be covered by capital investments from the public budget.

7. Research and academic institutions should establish systematic cooperation with the private sector; this requires improvement of the legislation and other regulations, especially in public universities.

8. It is recommended to improve the system for collecting and analysing statistical information, with a particular focus on private sector investments, to ensure more accurate and detailed data that can support strategic decision-making and effective economic policy planning.

INTRODUCTION

This research report has been prepared to contribute to the debate at this year's session of the Annual Economic Forum 2024 (AEF 24), following last year's inaugural session of the Forum, which is intended to continue as a traditional event.

The Economic Forum was initiated to ensure an engaged and productive debate on economic developments, the challenges faced during the calendar year, and the expectations for the coming year. Providing an audience consisting of the most responsible and interested actors in economic developments—including participants from public institutions, business associations, business executives, experts from financial institutions, and research and academic circles—the Annual Economic Forum (AEF) of the Riinvest Institute aims to be recognized as a significant event with high visibility regarding economic developments in the country.

In preparation for AEF '24, the Riinvest Institute has produced a research report that covers:

a) Current issues related to the dynamics and quality of economic growth, future expectations, especially for the coming year, and economic policies. The report answers why economic growth in Kosovo is in a sort of "trap" and how this situation can be overcome according to theoretical and empirical studies, as well as the experiences of other countries.

b) The evolution of the business environment and the intensity of certain barriers within the business environment.

c) A detailed analysis of investments in Kosovo, as a special topic for AEF '24, including their volume, structure, and efficiency, while offering recommendations and suggestions for economic policies aimed at promoting investment and improving their efficiency.

This report has been compiled based on research conducted by the Riinvest Institute, the Government Program and its reflections in the budget for 2024, its implementation, and the draft budget for 2025, budget consumption reports, press releases from the Kosovo Agency of Statistics (KAS) regarding developments in various sectors during 2023, monthly and annual reports from the Central Bank of Kosovo (CBK), and recent reports from the IMF, WB, EBRD, EU, as well as predictions from the Vienna Institute for International Economic Studies (wiiw). In addition, a survey was conducted with nearly 500 businesses (September–October 2024), focusing on investment activities in the private sector. This study was developed based on a standard random sample derived from the tax registry of the Tax Administration of Kosovo (TAK). For the section of the report on investments, we also relied on financial statements submitted by businesses to the TAK and consulted publications from the CBK regarding Foreign Direct Investments and remittances.

The report is supported by a grant from the Kosovo Foundation for an Open Society (KFOS) and is also related to the activities of the "Forum 2015," which, since last year, has been developing activities as a program and platform for debates on Kosovo's Euro-Atlantic integration within the Riinvest Institute. We would like to thank KFOS for supporting this important project. The findings presented represent the views of the research team, specifically the Riinvest Institute, and not necessarily those of other actors involved in the implementation of this project.

ECONOMIC GROWTH AND THE MACROECONOMIC CONFIGURATION

1

1.1 Global and regional context

The latest IMF projections on global economic growth in 2024 and 2025 remain more or less aligned with the growth achieved in 2023 (3.3 percent), with projected rates of 3.2 percent for 2024 and 3.3 percent for 2025. However, a narrowing trend in GDP level divergences globally is observed, driven by more dynamic growth in emerging economies (e.g., China, India). Nonetheless, the risk of inflation remains significant, particularly in countries where service prices are slowing the trend of disinflation, thereby sustaining high interest rates. This occurs even though declining energy and food prices have brought inflation rates nearly back to pre-pandemic levels. This situation is compounded by political and trade tensions arising from ongoing geopolitical uncertainties. The IMF's projections indicate weaker growth in major European economies during 2024 and 2025, with Germany expected to grow by 0.2 percent and 1.3 percent, France by 0.9 percent and 1.3 percent, and Italy by 0.7 percent and 0.9 percent, respectively. Overall, the European region is projected to grow at rates of 0.9 percent in 2024 and 1.5 percent in 2025. While China's economic growth fluctuates between 3 percent and 5 percent, India is emerging as a leader among the emerging economies with growth rates of 6 to 7 percent.

To complete this perspective, we can refer to the somewhat similar assessment of top executives from the world's most renowned companies, expressed in the "McKinsey Global Survey", regarding the current and expected conditions that may influence the trajectory of their businesses. Firstly, they assess the current conditions with heightened caution compared to previous months. They characterize the changes more as stabilizing rather than improving. They consider the primary risk to stem from geopolitical instability, as well as the fact that this year and the next, more than half of the global population will vote in local elections. Immediately following these concerns is the fear of a resurgence in inflation for these reasons (McKinsey & Company, 2024).

In the World Bank's report on trends and forecasts for Central Eurasia (World Bank, 2024), the economic growth projections for the Western Balkans for 2024 and 2025 are estimated at 3.3 percent and 3.5 percent, respectively. Similar projections are made for Turkey, an important economic partner for the region. Although inflation levels have declined, prices remain 20 percent higher compared to the pre-COVID-19 period, with food prices being particularly affected, showing an increase of 50 percent. Alongside these expectations, the World Bank warns of "headaches" stemming from various factors such as lower growth among key European trading partners, restrictive monetary policies, rising debt burdens, and the escalation of regional and global geopolitical tensions. All these factors could slow economic growth and erode investor and consumer confidence.

Nevertheless, the projections reflect expectations for a more vibrant economic growth trend in the region, driven by labour market improvements, wage increases, and EU fund-induced investments. According to the World Bank, there is still significant room for improvement across the region, particularly in enhancing business dynamism (entry and exit of businesses), as the competitive environment does not sufficiently encourage innovation, nor the creation and absorption of new knowledge and technologies. These challenges are compounded by excessive state involvement in the economy and significant weaknesses in education and training, which collectively hinder improvements in labour productivity levels.

One of the World Bank's major concerns is related to the consequences of continued emigration of educated young populations, a common characteristic across all countries in the region. The solution lies in leveraging networks with the diaspora, maximizing the benefits of remittances, and expanding opportunities in the local labour market. The new economic growth plan for the Western Balkans is expected to stimulate regional economic growth further, combined with deeper structural and democratic reforms.

Table 1. Economic Growth Projections in the Western Balkans (World Bank and wiiw)

	WB		wiiw	
	2024	2025	2024	2025
Albania	3.3	3.4	4.0	3.8
Bosnia and Herzegovina	2.8	3.2	2.6	2.9
Kosovo	3.8	3.9	4.1	3.8
Montenegro	3.4	3.5	3.5	3.7
North Macedonia	2.5	2.9	1.8	2.3
Serbia	3.8	4.2	3.7	3.7
Western Balkans	3.2	3.5	3.4	3.4

Source: World Bank: Retaining Growth Momentum, October 2024;
The Institute for International Economic Studies (wiiw): External-weakness-dampening-robust-consumer-driven-growth, October 2024)

1.2 Return to pre-COVID-19 growth trends

After a slower growth in 2023, Kosovo's economy is expected to return to pre-COVID-19 growth rates this year and next, with a projected rate of around 4 percent. Although falling short of government plans,[1] the IMF and World Bank view Kosovo's economic growth trends more positively than last year, particularly in terms of macroeconomic stability and fiscal performance. Kosovo ranks among the countries with economic growth rates close to 4 percent for these two years, followed closely by Albania and Serbia. While praising progress in tax collection and financial risk management, the IMF emphasizes the importance of creating mechanisms to ensure an adequate level of budget reserves and, notably, strengthening public investment management. This improvement compared to 2023 is also reflected in a 12 percent increase in budget revenues and preliminary estimates of GDP growth of 5.4 percent in the first quarter and 4.3 percent in the second quarter. Inflationary pressures have eased, with prices continuing to rise at a slower pace, leading to an inflation rate of 2.2 percent compared to August of last year.

However, the widening trade balance deficit remains a serious issue. Import growth, largely driven by increased consumption, is more dynamic than export growth. This has been influenced by rising incomes, credit growth (12 percent), and improved public spending compared to the previous year.

Judging by the perceptions of private company leaders in Kosovo regarding their business activities, 2023 was better than 2024, as 28 percent of companies reported increased sales (55 percent reported no change, and 13 percent reported a decline). In 2024, only about one-third of companies experienced growth, while this percentage rises to 54 percent when it comes to expectations for 2025.

From this perspective, the projected GDP growth rate of 5.6 percent in the 2025 budget documents may be challenged by difficulties in achieving real growth in exports (7 percent) and private investments (6.1 percent). Additionally, considering recent trends, the execution of approximately 800 million euros in planned capital investments appears overestimated.

It is also important to consider potential difficulties in consolidating government institutions following the national elections on February 9, which could influence business and household expectations, as well as the business cycle, further challenging the projected economic growth rate.

1 With budget projections for 2024, it was expected growth rate of 4.6 percent.

Table 2. Real GDP Growth of Kosovo in % and projections for 2024 and 2025

	2019	2020	2021	2022	2023	2024f	2025f
EBRD			10.7	4.3	3.3	4.0	4.0
IMF	4.8	-5.3	10.7	4.3	3.3	3.8	4.0
World Bank	4.8	-5.3	10.7	4.3	3.3	3.8	3.9
wiiw		-5.3	10.7	4.3	4.1	4.1	3.8
Government of Kosovo (Draft Law on the Budget of the Republic of Kosovo 2025)	4.8	-5.3	10.7	4.3	4.1	4.5	5.6

Source: Authors based on data from EBRD; IMF; WB; wiiw; Government of Kosovo

To complete this overview, two chronic issues need to be added: particularly the deterioration of the trade balance (the coverage of imports with exports of goods decreased from around 17.9 percent in 2022 to approximately 15 percent in 2023 and 2024) and the serious problem related to the low level of labor market participation (World Bank, 2024). According to World Bank estimates, only 37 percent of the working-age population is employed. This means that out of every 100 working-age individuals (15-64 years old), only 37 are employed. This fact undermines the positive changes reflected in official statistics showing a drop in unemployment to around 10 percent.

It seems that many working-age individuals are discouraged from entering the labor market through registration at employment offices due to the lack of active labor market instruments and policies (such as financial assistance for the unemployed) and the minor role of employment offices in mediating job placements. All of this is reflected in a reduction in the statistical unemployment rate.

When adding the concerning trend of migration, particularly among unemployed youth, it becomes clear that this has complicated statistical measurements and assessments of labor market dynamics.

1.3 "Trapped" economic growth in Kosovo

As we emphasized in the study report *"A New Model for Sustainable Economic Growth"* prepared for the Annual Economic Forum 2023, (Riinvest Institute, 2023) economic growth in Kosovo has hovered around 3-4 percent for nearly two decades. Considering the historical context characterized by a long, difficult, and specific transition with severe consequences of war, brutal deindustrialization, and a colonial position during the 1990s, this level of economic growth is insufficient.

This specific historical reality created a significant gap in terms of lagging behind other countries in the region and beyond, especially compared to the EU. Consequently, economic growth over these two and a half decades has been built on a critical and emergency-driven situation, which failed to establish the prerequisites for overcoming macroeconomic imbalances, particularly unemployment and the trade deficit.

This model, based on external factors—remittances, foreign technical and financial assistance, and credit—has nearly lost its transformative power and potential to generate the growth Kosovo needs. It has fallen short of enhancing its convergence with EU-27 countries and addressing macroeconomic imbalances in the overall economic configuration.

Kosovo's existing economic growth model has been primarily consumption-driven for nearly 25 years. This trend is evident in recent years, where consumption remains the main contributor to economic growth. Over the past two years, with economic growth rates of 3.3 percent and 3.8 percent, the contribution of consumption has been 3.9 and 4.6 percentage points, respectively, while investments contributed 1 and 1.7 percentage points (Table 3).

Assuming that imports and exports in Kosovo were balanced (i.e., net exports equaled zero), economic growth would have reached 4.9 percent (3.9 + 1) in 2023 and approximately 6.3 percent (4.6 + 1.7) in 2024. However, the negative trade balance reduces the growth rate. This means that to sustain this consumption, a significant portion of goods and services has been imported—produced outside the country—causing economic growth to decrease from 4.9 percent to 3.3 percent (4.9 - 1.7) in 2023 and to 3.8 percent in 2024 (6.3 - 2.5).

This demonstrates that Kosovo has insufficient contributions from investments and exports to generate higher economic growth. In this model, increased consumption drives higher imports of consumer goods, thereby lowering the economic growth rate and creating an unsustainable cycle in the economy. The import component in consumption reduces the multiplier effect's impact on accelerating economic growth, figuratively slowing the "speed" of growth from "5th gear" to "2nd" or "3rd" for the imported portion of consumption.

This simplified analysis illustrates the urgent need for fundamental changes in government development policies to address the stagnation and trap created by policies that have favoured an outdated growth model.

Table 3. Contributors to economic growth in Kosovo in 2023 and 2024

Description	2023	2024
Real Economic Growth (%)	3.3	3.8
Contribution to Growth		
Consumption	3.9	4.6
Investment	1.0	1.7
Net export (export-import)	-1.6	-2.5

Presented according to the data in: World Bank (2024)

The present challenges related to this in Kosovo are not so unique, as there are approximately 108 countries with a middle-income level (according to the World Bank classification)[2] struggling with unfavorable economic growth trends and, being "trapped," unable to transition into the club of developed economies. This phenomenon, known as the **"Middle-Income Countries Trap,"** has become a pressing and problematic issue because it can prolong a state of unsatisfactory development for an extended period.

For this reason, our main message at the Annual Economic Forum (AEF23) last year, directed at policymakers and economic actors, including businesses, was to promote and implement a new economic growth model. This model focuses on effective policies to increase the competitive supply of domestic products and services for export and the local market.

This can be achieved through investments in new technologies, new knowledge, research and development, innovation, education, and healthcare. All these factors are key determinants for enhancing the absorptive capacity of the economy and society, enabling more meaningful and qualitative economic growth.

2 According to the World Bank: **World Development Report Concept Note (2024)**, based on the World Bank classification and calculations under the **"World Bank Atlas Method,"** there are currently 26 low-income countries (LIC) globally, with Gross National Income (GNI) per capita up to $1,135. Following this, there are 64 countries classified as lower-middle-income countries (LMIC), with GNI per capita between $1,136 and $4,465. Next, 54 countries fall under the category of upper-middle-income countries (UMIC), with GNI per capita between $4,466 and $13,845. Kosovo, with a GNI per capita of $5,590 (2022), is part of this category. It is accompanied by the other five Western Balkan countries in this group. Finally, there are 83 high-income countries (HIC), where GNI per capita exceeds $13,846.

In September of this year, the World Bank published a special report titled *"Middle Income Trap"* addressing the challenges of economic growth in these countries from various perspectives. As a synthesis of recommendations, the report suggests a pathway for these countries based on the so-called "3Is": Investment, Infusion, Innovation.

The first "I" focuses on increasing investments in physical capital (machinery, equipment, and infrastructure) and expanding investments in improving human capital—quality education, training, and healthcare. Economic and investment policies should create and implement strategies that encourage the attraction of private and public investments, particularly foreign investments, which bring an "infusion" of ideas, models, and new technologies into the domestic economy. This report, especially in Chapter 3, delves into this issue in detail.

The second "I" relates to infusion, where countries focus on imitating, adopting, and disseminating new technologies and business models characteristic of developed economies. This entails equipping domestic industries to become suppliers of products and services on a global scale. Successful structural reforms that support the sustainability of achievements and positive changes in the external competitive environment are crucial for this phase. In this regard, Kosovo remains at an early stage.

The third "I" relates to innovation, where local capacities are developed to add value even to global technologies, becoming "creators of global knowledge." This is characteristic of upper-middle-income countries and represents a significant challenge in supporting the sustainability of existing firms in the global market. This phase requires advanced institutional maturity and capacity to reduce risks for successful and innovative businesses through incentive schemes, as well as to promote investments in research and development (R&D).

Experiences show that moving to this phase requires commitment to higher developmental ambitions and effective reforms. This demands serious efforts from policymakers to successfully link the macroeconomic growth structure with its determinants at the microeconomic level, such as incentives, policies, organizations, and enablers of the economic growth process. In this context, Kosovo must begin to address these issues much more seriously.

Given that Kosovo has now entered the group of "Higher r-middle-income countries" (HMIC), it must simultaneously address all three "I's." This naturally poses very serious tasks for macroeconomic governance at the national level and for local businesses to enhance their competitive capabilities.

Investments, as an essential factor in the dynamics, structure, and quality of economic growth and overall economic development, are analysed in detail in Chapter 3 of this report, based on field research with the private sector and an analysis of public and foreign investments using official published data. Kosovo's approach to this challenge can benefit from the EU's *"Economic Growth Plan for the Western Balkans,"* which could support the first "I" (investment) and the second "I" (infusion) by boosting investments. Structural reform remains critical for this, particularly in the development of the energy sector, ensuring water supply, advancing human capital, and the connectivity agenda with regional and pan-European physical and digital traffic corridors.

This must be achieved in parallel with commitments and obligations related to the Green Agenda, including its goal of "Net Zero CO2 Emissions" and decarbonization.

It is well known that European integration is one of the successful models that has helped countries effectively address the "middle-income trap," a model commonly referred to as the "European convergence machine" (World Bank, 2024). Recent research suggests that regional cooperation plays only a facilitative and supportive role but lacks transformative power for the Western Balkan economies without EU integration (Mustafa and Hashani, 2024). Since 1990, only 34 middle-income countries have transitioned into the group of high-income countries. Of these, more than one-third achieved this milestone through the process of EU integration. The others include Southeast Asian countries such as Taiwan and South Korea, which have focused their development policies on high value-added products and services for export while significantly increasing investments in education, new technologies, and innovations to bridge the gap with advanced global technologies.[3]

3 According to the World Bank: *World Development Report Concept Note*

In general, governments in Kosovo have paid little attention to these vital developmental issues. Chronically, they have lacked the ambition to make qualitative changes to Kosovo's economic reality. Kosovo, as a whole, requires a new developmental vision. A development ambition is needed, free from the inertia and routine of current policies, which have been primarily characterized by antagonistic confrontations among political actors on almost every issue. It is essential to concentrate energies on development that moves the country towards advanced economies.

Kosovo cannot escape this trap without, first, increasing investments in sectors with export potential and, second, investing in knowledge, new technologies, research, development, and innovation. This would result in increased exports and a rise in the competitive domestic supply of products and services.

In recent years, there has been an increase in exports, particularly in the export of services. However, the contribution of this to the quality of economic growth remains limited, especially given that the added value of the exported products and services does not appear to be significant.

Another issue with the existing model is that the composition of GDP, in terms of sectors and activities, has not undergone the necessary qualitative changes. From Table 4, we can observe that the contribution weight of manufacturing, mining, agriculture, professional activities, scientific research, and education in value creation has declined in 2023 compared to 2010. This has occurred at the expense of the increased weight of trade, transportation, hospitality, and construction.

Such a development does not favour export growth or facilitate the transition from the first "I" to the second and third "I" on the pathway that middle-income countries must follow toward becoming developed economies. Therefore, alongside changes related to the volume and technical structure of investments (real estate, facilities, equipment), changes in sectoral investment policies are necessary.

Tabela 4. Struktura e PVB sipas veprimtarive

Participation of Economic Activities in GDP as a Percentage from 2010 to 2023

Description of Economic Activities	2010	2015	2019	2023
Agriculture, Forestry, and Fishing	9.5	7.7	7.2	7.8
Mining and Quarrying	2.5	2	2	1.7
Manufacturing	13.8	13.3	12.9	12.8
(Electricity and Gas Supply) + Water Supply	**3.1**	**4.1**	**4**	**3.7**
Electricity and Gas Supply	2.5	3.4	3.4	3.1
Water Supply	0.7	0.7	0.7	0.6
Construction	7.7	7.6	8.2	8.2
Wholesale and Retail Trade; Vehicle and Motorcycle Repair	13	12.3	12.8	14.2
Transportation and Storage	4	4.6	4.4	4.5
Hotels and Restaurants	1.1	1.6	2.1	2.1
(Information and Communication) + (Financial and Insurance Activities)	**5.4**	**5.6**	**5.7**	**6.3**
Information and Communication	1.5	1.8	1.9	2
Financial and Insurance Activities	3.8	3.8	3.9	4.3
(Real Estate Activities) + (Professional, Scientific, and Technical Activities) + (Administrative and Support Activities) + (Public Administration and Defence; Social Security)	**16.1**	**15.6**	**15**	**13**
Real Estate Activities	8.8	7.5	7	5.9
Professional, Scientific, and Technical Activities	1.5	1.6	1.4	1.4
Administrative and Support Activities	0.7	0.7	0.7	0.7
Public Administration and Defence; Social Security	5.1	5.9	5.9	5
Education	3.6	4.1	3.7	3.2
Healthcare and Social Work Activities	1.8	2.1	2.2	2.2
(Arts, Entertainment, and Recreation) + Other Services	**0.9**	**0.8**	**0.6**	**0.5**
Arts, Entertainment, and Recreation	0.4	0.4	0.2	0.2
Other Services	0.5	0.4	0.4	0.3
Gross Value Added, Total	82.4	81.3	80.8	80.1
Net Taxes on Products	17.6	18.7	19.2	19.9
TOTAL GDP (at current prices)	100	100	100	100

Source: ASK, 2024

What is particularly concerning relates to investments in the fields of scientific research and development, education, innovation, and healthcare. The research and innovation sector still faces a poorly developed and insufficiently operationalized legal framework for implementation. The institutional structure is still incomplete to effectively implement research and innovation policies and programs. The National Research Program 2023-2028 has remained unimplemented and non-operational over the past two years. Within the Ministry of Education, Science, Technology, and Innovation (MASHTI), institutions such as the Agency/Fund for Research, which should implement this program, have not yet been established.

A positive development is the draft Law on Innovation and Entrepreneurship, which foresees the creation of the Innovation Fund. However, this document remains in draft form, pending approval since December 2023.[4] Kosovo still has modest participation in the European Research Area (ERA), including Horizon Europe, the EU's largest research program. Additionally, Kosovo has not yet become part of the EU Innovation Scoreboard, which leaves it without a statistical information system for tracking innovation development and other important components of scientific and research production.

Table 5 illustrates extremely low funding (as a percentage of GDP) for research, innovation, education, and healthcare—key components for building human capital that would enhance absorptive capacities, drive development dynamics, and promote the implementation of a new economic growth model in Kosovo.

Table 5. Investments in R&I, Education, and Healthcare in 2023 as a % of GDP

Description	Kosovo	Western Balkans	EU
Research and innovation	0.1 - 0,2[13]	0.50	1.7
Education	3.5	4.6	4.7
Health	5.8	8.5	10.2

1.4 External sector

The performance of Kosovo's foreign trade in recent years shows a continuous trend towards dependence on imports, which creates difficulties in improving the trade balance. The balance of service exchanges has had a positive impact, but that of goods, which is essential for trade dynamics, has contributed to the increase in the trade deficit. Data for the period January-September 2024 indicate a worsening of the trade deficit compared to the same period in 2023 (table 6). During this period, exports increased from 2.2 to 2.5 billion euros. On the other hand, this improvement remains insufficient to offset the larger increase in imports, which reached nearly 5.4 billion euros. Currently, exports of goods and services together cover 46 percent of imports, showing a slight improvement from the same period a year ago. However, this percentage remains far from what would be necessary for a more balanced trade balance.

4 According to Kosovo's Reform Agenda within the EU Instrument for Reforms and Economic Growth in the Western Balkans, the adoption of the Law on Innovation and Entrepreneurship is expected to take place in December 2024. (https://kryeministri.rks-gov.net/wp-content/uploads/2024/10/IRRrE-Agjenda-e-Reformave-te-Kosoves.pdf)

Table 6. Exports and Imports of Goods and Services (in millions of euros)

Year	Export	Import	Trade balance	Export coverage by imports (%)
2019	2,068	3,982	-1,914	52
2020	1,470	3,651	-2,181	40
2021	2,659	5,191	-2,532	51
2022	3,435	6,346	-2,911	54
2023	3,837	6,806	-2,969	56
January - September 2023	2,222	4,943	-2,723	45
January - September 2024	2,471	5,418	-2,947	46

Source: KAS

Excluding 2023, when there was a decrease of about seven percent compared to 2022; Kosovo's goods exports followed an upward trend (figure 1). However, this was also accompanied by an increase in imports, which caused the trade balance deficit to continue deepening, reaching a record value of about 4.6 billion euros in 2023. In other words, for every one euro exported in 2023, Kosovo imported about 6.3 euros or 0.7 euros more than in the previous year. Meanwhile, by September of this year, exports and imports of goods had increased by 8% and 9%, respectively, compared to the same period in 2023. During this period, the value of goods exports reached 690 million euros, while imports totalled 4.6 billion euros.

Table 7. Exports and Imports of Goods (in millions of euros)

Year	Export	Import	Trade balance	Export coverage by imports (%)
2019	393	3233	-2840	12.2
2020	475	3048	-2573	15.6
2021	753	4320	-3567	17.4
2022	932	5219	-4287	17.9
2023	871	5469	-4598	15.9
January - September 2023	643	4249	-3606	15.1
January – September 2024	690	4554	-3864	15.2

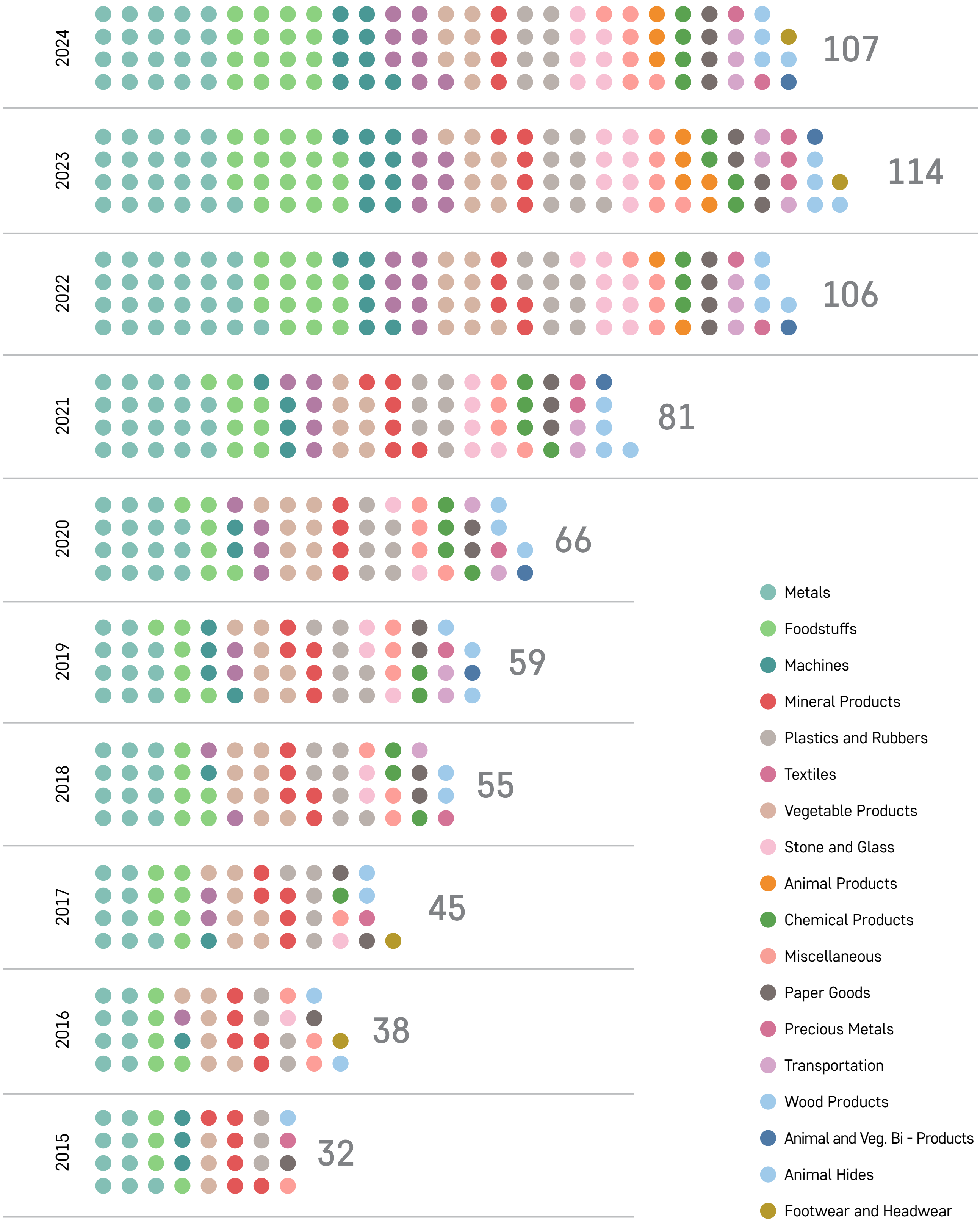
Source: KAS and CBK

According to the sectoral structure, we observe that the goods Kosovo exports the most in 2024 are still base metals and products made from them, accounting for around 25 percent of the total export value. However, after a 20-month closure due to high electricity prices, nickel production resumed in June 2023, but the producer refrained from immediate exports due to unfavourable export prices (IMF, 2024). The next category is plastics, rubber, and products made from them, while the third place is held by various manufactured goods (furniture, beds, mattresses, mattress holders, pillows, and similar filled layers), with 7 percentage points less than the same period last year.

It is worth mentioning that mattress exports halved in 2023, mainly because the Mattress Factory in Gjakova ceased production and relocated to North Macedonia, a move that may have been influenced by the new anti-dumping measures imposed on the U.S. market. These measures, which claim that Kosovo benefited from government subsidies, have led to tariffs that made exports less competitive. A positive circumstance is also the increase in the diversification of products and goods exported, from 32 products in 2015 to over 110 products in 2023 and 2024 (figure 1)[5].

5 Chart by Endrit Pllashniku, Kosovo Data. Source: Kosovo Customs

Figure 1. Number of products exceeding one million euros in annual export value (2015-2023, January – September 2024)



Furthermore, if we analyse the data for the first nine months of 2024, we notice that the United States, which in 2023 was one of the main countries to which Kosovo exported the most, has dropped in ranking, now positioning itself in sixth place. As for exports to EU countries, they have so far reached a value of 199.8 million euros, or about 32 percent of total exports. Around half of Kosovo's total goods exports are directed to CEFTA countries.

Similar to last year, the goods imported in the highest value up until August 2024 continue to be mineral products (mineral fuels, mineral oils, and their distillation products; bituminous substances) with 14 percent, followed by foodstuffs, beverages, alcoholic drinks, and tobacco with 13 percent, and machinery, mechanical and electrical equipment with about 12 percent of the total import value. Consistent with the previous year, the countries from which these products are mainly imported are Turkey, Germany, and China. Kosovo's imports from EU countries have reached 1.9 billion euros so far, or 46 percent of total imports. However, when analysing imports from CEFTA countries, a significant decline is observed in imports from Serbia, with imports showing a decrease of 71.9% from the January-August 2022 period. This decline occurred following the terrorist attack in Banjska in September of the previous year, after which the Kosovo Government decided to ban the import of goods originating from Serbia for security reasons, with the exception of construction materials. This decision raised concerns, particularly in the context of promoting the European common market within the framework of the Berlin Process and Kosovo's role in CEFTA. As a result, the import restriction from Serbia was lifted in exchange for the scanning of imported goods using advanced equipment and the establishment of Kosovo's proper position within CEFTA.

According to projections from the Vienna Institute for International Economic Studies (Wiiw, 2024), from 2024 to 2026, a gradual increase in both exports and imports is expected. Despite the slight annual growth in exports, the trade deficit is projected to widen during these years, reaching -4.95 billion euros by 2026. Additionally, the International Monetary Fund's projections for Kosovo's economy suggest that exports are expected to grow, contributing positively to GDP growth by 2.0% in 2024, 1.3% in 2025, and 2.3% in 2026. However, this will be weighed by a higher level of imports.

The seriousness of this topic is also reflected in the presentation of the Industrial Policy at the beginning of last year. Among the objectives in this document, the second one specifically aims to reduce the trade deficit through two main routes: increasing exports of goods produced in Kosovo and replacing imports with local products. To achieve this, the need to improve financing for export-oriented producers, expand access to new markets through product diversification, and improve export strategies is emphasized. Additionally, substituting imported products with local ones requires stimulating production and promoting them through public procurement and policies that support fair competition for domestic products.

Regarding services, every year we see a significant increase in exports (Table 8). In fact, services trade in 2023 was characterized by a growth in the positive balance, reaching a value of 1.6 billion euros, or 16.9 percent of GDP (CBK, 2024). Total service exports up to July 2024 have reached around 1.8 billion euros, marking a 13 percent increase compared to the same period last year, and by the end of the year, it is predicted to reach close to the value of three billion euros.

Table 8. Export and import of services over the years (in millions of euros)

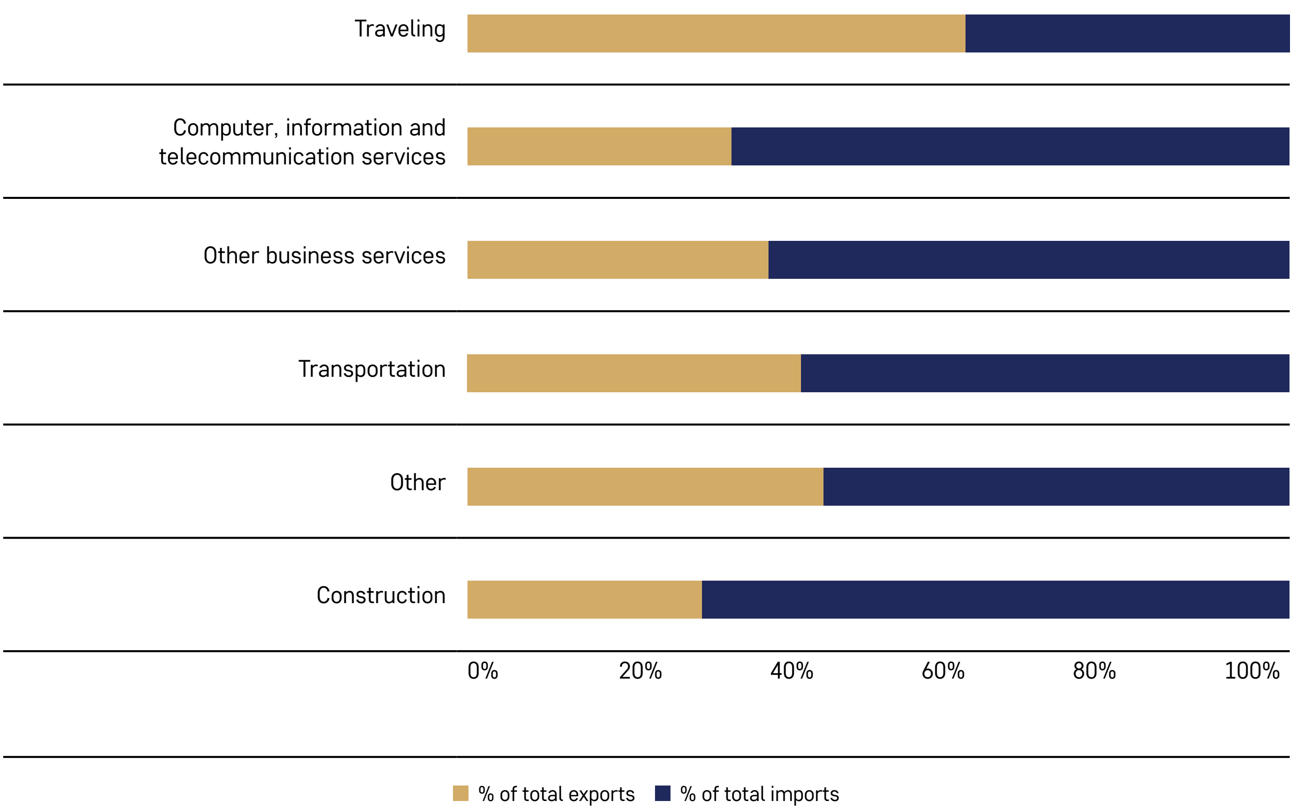
Year	Export of services	Import of services
2019	1,675	749
2020	995	603
2021	1,906	871
2022	2,503	1,127
2023	2,966	1,337
2023 January - September	1,579	694
2024 January - September	1,781	864

Source: CBK

As the main contributor to this value, the category of travel services accounts for three-quarters of total service exports. Expenditures from the diaspora in Kosovo are the primary driver of this dynamic. However, there has also been a 14 percent increase in the number of passengers and a 7 percent increase in the number of flights during the past year (Civil Aviation Authority, 2023). Furthermore, in 2023, the number of visitors to Kosovo increased by 35% compared to 2022, while the number of overnight stays by both domestic and foreign visitors grew by 86% compared to 2022 (KAS, 2023).

As a result of these developments, the Government of the Republic of Kosovo, in cooperation with other stakeholders, has committed to developing a national tourism strategy for the period 2024-2030, aimed at enabling the development of tourism on a competitive basis, fostering economic development, increasing employment, and broader growth.

● **Figure 2.** Share of services in exports and imports (January - September 2024)



Source: CBK

After travel services, the second largest category is computer, information, and telecommunications services, highlighting the significant growth of the ICT sector and digital services. Within this, telecommunications services account for about half of the total value, with 45 percent attributed to computer services and only three percent contributed by information services. According to the latest ICT barometer, 39 percent of these companies focus exclusively on international markets (Stikk, 2022). Meanwhile, data from the Kosovo Tax Administration shows that Kosovo exported around 60 million euros worth of ICT services to the United States, 44.4 million euros to Switzerland, and 38.4 million euros to Germany last year.

Regarding imported services, the leading category continues to be travel services, which have seen a 25 percent increase through the first seven months of 2024 compared to 2023. This increase is mainly due to the visa liberalization that took place in January 2024, and it is expected that the import of travel services will continue to rise, potentially affecting the services balance and, consequently, increasing the negative balance of the current account.

In recent years, Kosovo has consistently seen growth in remittances from the diaspora, reflecting on-going support from Kosovars abroad. However, the data show that while remittances continue to grow each year, the rate of this growth has begun to slow down. Comparing remittances for the period January-August of this year (2024) with the same period last year, there has been a modest increase of less than one percent.

Table 9. Foreign trade statistics over the years

	Migrant remittances		Foreign direct investments		Current account		Financial account balance		Balance of payments	
	In millions of euros	As part of GDP (in %)	In millions of euros	As part of GDP (in %)	In millions of euros	As part of GDP (in %)	In millions of euros	As part of GDP (in %)	In millions of euros	As part of GDP (in %)
2019	851.5	12.1	254.6	3.6	-408.3	-5.8	-161.1	-2.3	-399.5	-5.7
2020	980	14.5	345.7	5.1	-454.7	-6.7	-562.1	-8.3	-472.2	-7.0
2021	1153.4	14.5	420.7	5.3	-632.5	-7.9	-365.0	-4.6	-694.7	-8.7
2022	1222.8	13.7	732.0	8.2	-878.7	-9.9	-661.6	-7.4	-917.1	-10.3
2023	1335.8	13.8	840.1	8.7	-729.4	-7.5	-415.5	-4.3	-666.5	-6.9
2023 (January - June)	627.4	14.9	371.1	8.8	-538	-12.7	-255.7	-6.1	-491.6	-11.6
2024 (January - June)	630.1	13.9	419.1	9.3	-691.8	-15.3	-496.6	-11.0	-667.9	-14.8

Source: CBK and KAS

This year, remittances continue to be dominated primarily by German-speaking countries (Germany, Switzerland), followed by the United States. Remittances continue to have a significant impact on the income structure of household economies in Kosovo, especially during the summer months when local consumption increases, generating more revenue for businesses. However, the use of remittances mainly for consumption does not improve Kosovo's long-term economic competitiveness. A more sustainable approach would be channelling these funds into more productive investments, which could create new job opportunities and enhance the productive capacity of the industry. Additionally, initiatives could be developed to encourage the diaspora to invest directly in local development projects, turning remittances into a more powerful driver of sustainable economic growth.

Foreign direct investments (FDI) in 2024 recorded a 7 percent increase. However, their structure continues to be dominated by the real estate sector. This increase, which represents a 12 percentage point rise in investments in this sector in the first half of 2024 compared to 2023, is concerning because real estate investments often do not significantly contribute to long-term economic development and lack a noticeable multiplier effect. Other sectors with a significant share include financial and insurance activities (16%) and the energy sector (8%). While Switzerland leads with 21 percent of total investments, followed by Germany and Albania with 19 and 12 percent respectively, these investments are mainly in passive activities. Attracting investments in the manufacturing sector, as the key sector for developing export potential, still remains a challenge.

The current account deficit, as one of the two main components of the balance of payments, reached 738.4 million euros in 2023, representing 7.5 percent of GDP, a decrease of 19.5 percent compared to 2022. However, when comparing the first half of 2023 and 2024, we observe a significant deterioration, with the deficit increasing from 538 million euros (12.7% of GDP) in 2023 to 692 million euros (15.3% of GDP) in 2024. The rise in the deficit is primarily driven by the worsening trade balance, a key component that determines the dynamics of the current account. This deterioration reflects challenges in achieving economic sustainability and suggests the need for measures to boost exports and reduce reliance on imports. On the other hand, the financial account in the first half of 2023 showed a deficit of -255.7 million euros, representing -6.1 percent of GDP. In the same period in 2024, this balance worsened to -496.6 million euros, or -11.0 percent of GDP. Despite the increase in foreign direct investments in Kosovo in 2024, the deterioration of the financial account balance may be linked to the impact of portfolio investments and other investments, which have contributed to the net outflow of capital.

1.5 Financial Sector

The financial sector in Kosovo has continued its positive development trends this year in terms of stability, resilience, and growth. Structurally, banks dominate the sector and play a key role in financial intermediation. In the past year, 11 banks continued to operate in the banking sector, of which 8 were foreign-owned, accounting for 83% of the sector's assets. The number of branches and employees in the sector has continued to rise, despite advances in digitalization. Since the pandemic, payments through e-banking and point-of-sale terminals have doubled, both in terms of the number of transactions and the amounts. For example, payments through these channels have seen an annual growth of around 25%, indicating positive trends in digitalization.

Moreover, Kosovo leads compared to other countries in the region in terms of the number of e-banking accounts (per one million inhabitants), and is on par with the regional average for the number of debit cards (per one million inhabitants), outpacing Bosnia and Herzegovina, Albania, and Montenegro. Alongside advancements in digitalization, the banking sector, with the support of the Central Bank of Kosovo (CBK), has made progress on the green agenda, financial inclusion, and sustainable finance—known as ESG (Environmental, Social, and Governance). Banks have also started publishing annual reports on their ESG activities in this regard.

The financial sector remains well capitalized, profitable, and liquid. Key return indicators such as ROA (Return on Assets) and ROE (Return on Equity) in the banking sector, which stand at 2.6% and 19.2% respectively, reflect solid and sustainable returns over the years. Liquidity stands at around 31% (liquid assets to short-term liabilities), while the loan-to-deposit ratio is 84.7%, non-performing loans are only 2%, and capitalization is around 15.5%, indicating a strong performance within the banking sector.

Other financial sectors have also demonstrated good performance. For instance, insurance companies have improved their annual performance, particularly in terms of capitalization, asset growth, and profitability. Microfinance institutions have continued to expand lending, mainly to household economies, surpassing €500 million in loans, and accounting for nearly 10% of the total loans in the financial sector.

Credit growth in the economy continues its upward trend, with loans increasing by 15% annually. Household loans have seen a more significant rise compared to corporate loans, with growth rates of 20% and 11%, respectively. Deposits also grew by 11%, though this is slower than the previous year. In terms of structure, household loans now account for 40% of the total, reflecting a two-percentage-point increase. Corporate loans, however, maintain a similar structure, mirroring the composition of the economy. For example, loans in agriculture make up 2%, while industry, energy, and construction account for 34%, and services dominate with 64%, maintaining a consistent trend.

In terms of maturity, the loan structure has remained unchanged in recent years: loans with a maturity of up to one year account for 10%, loans with a maturity of 1-5 years make up 35%, and loans with a maturity of over 5 years account for 55%. Private sector credit as a percentage of GDP, at nearly 50%, is above the average for the Western Balkans, with Kosovo performing better compared to most countries in the region.

After a period of rising interest rates globally, driven by inflation and tightening monetary conditions, these trends do not appear to have fully reflected in the banking sector in Kosovo. Interest rates on loans have seen a slight decrease, while deposit rates have increased, narrowing the interest margin from 4.1 percentage points to 3.2 percentage points this year. The rise in prices and the need for liquidity may have increased the demand for credit. As a result, pressure for higher deposit rates may emerge. In the future, the on-going rise in prices could dampen demand, thereby increasing financing needs. This could lead to a tightening of credit conditions, with global monetary (and fiscal) outlooks indicating such a possibility.

The financial sector's exposure to the external sector remains high. Net foreign assets have reached €4.6 billion, nearly half of GDP, with the Pension Savings Fund (the Trust) accounting for half of this amount, followed by the Central Bank of Kosovo (CBK) and commercial banks. In the annual growth of net foreign assets of 11.5% (around €500 million), the Trust has been the main contributor, followed by commercial banks and the CBK. On the other hand, the financial sector's claims (mainly the Trust and commercial banks) on the central government have remained nearly unchanged. Positive performance in international securities markets has contributed to strong returns on the Trust's investments.

The high exposure of the financial sector to international markets, which are reflecting risks in many dimensions, implies a necessity to strengthen the principle of security, which is established in the investment policies of financial institutions (e.g., the Central Bank of Kosovo and the Pension Trust). Thus, by subordinating the principle of return on assets to a significant extent, at least in the short term—for example, an increase in the exposure of the Pension Trust's assets in the form of government securities and deposits in the financial market in Kosovo—may be desirable. However, this position of net foreign assets, in general, could be indicative of the absorptive capacity of Kosovo's economy.

1.6 Government expenditure – Budget

1.6.1 Revenues and budget expenses

Fiscal and budgetary policy is the main instrument of the government for its economic policies to maintain fiscal stability and encourage economic growth. Analysis of revenues and expenditures for 2024 and projections for 2025, shows that this budget is essentially a continuation of the instruments and policies from previous years. These policies have resulted in macro-fiscal stability, but they have also been accompanied by an unfavourable structure in terms of expenditures on infrastructure and mechanisms that accelerate economic growth, with insufficient financing in education, healthcare, scientific research, innovation, and a critical inefficiency in the realization of capital investments.

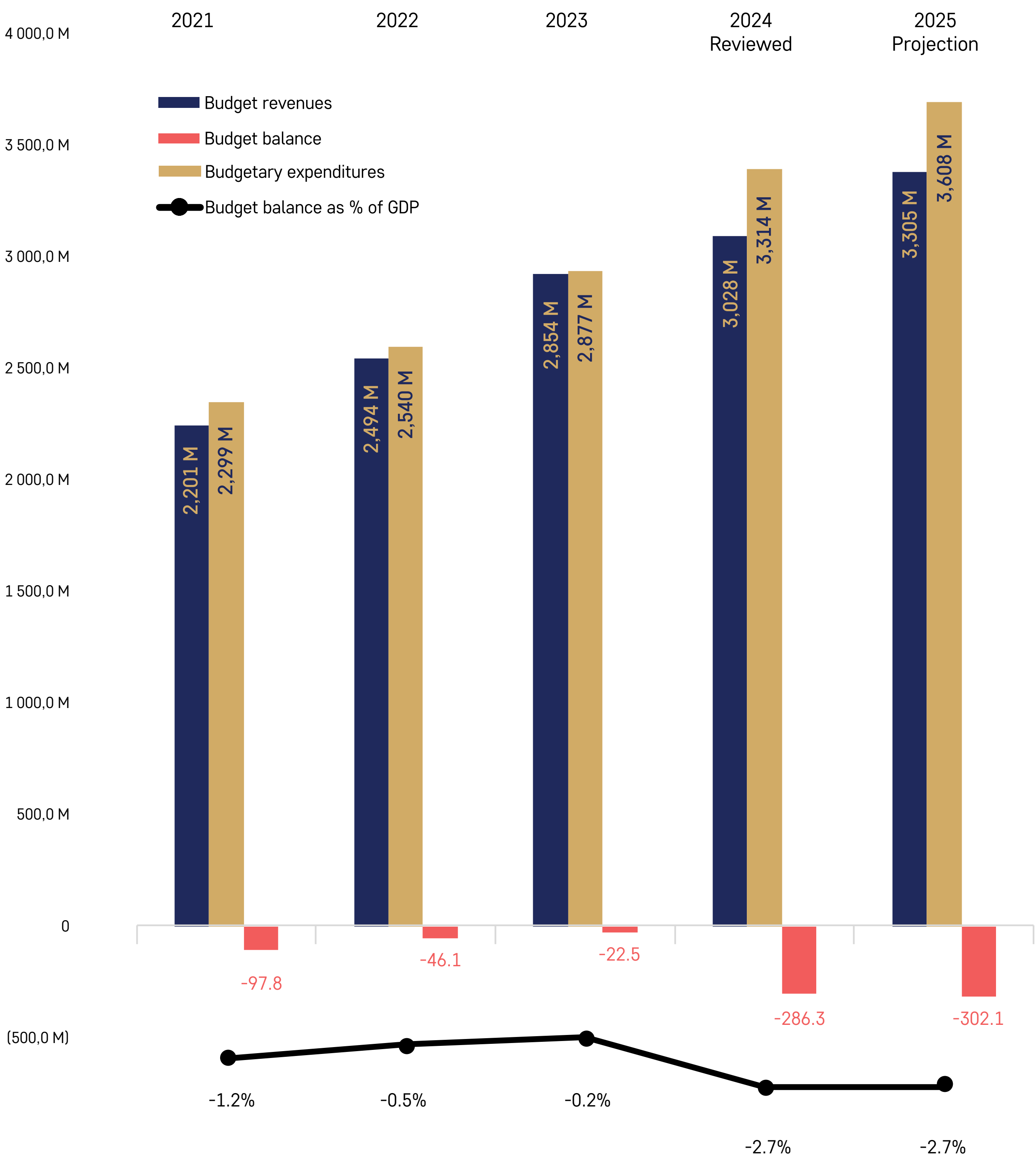
For 2024, annual revenues are estimated to reach 3.02 billion euros, of which approximately 2.6 billion euros or 86% have been collected from January to October (MFLT, 2024). Meanwhile, expenditures are projected to be around 3.3 billion euros, and by October 2024, 2.3 billion euros or 70% have been spent. With this pace of expenditures and revenues, it seems that by the end of the year, the government will collect the planned revenues, but it will not be able to spend the planned budget. For 2025(MFLT, 2024), budget expenditures are expected to increase by 8.8% compared to the previous year, representing 33% of GDP[6], while revenues are projected to rise by 9.2%, amounting to approximately 30% of GDP. These projected revenues will cover about 92% of the planned expenditures, leaving a need for financing from external sources, which will come from international credits from the IMF, World Bank, and EU, as well as domestic resources from bond issuances. This budget deficit[7] of -2.7% is almost identical to those of neighbouring countries[8]: Serbia is expected to have a budget deficit of -2.2%, Albania -2.6%, Montenegro -3.5%, and North Macedonia -4%.

6 The estimate for Gross Domestic Product (GDP) is taken from the 2025 Budget Law projected by the Government of Kosovo.

7 The data on the budget deficit are taken from the draft budgets of the respective countries.

8

Figure 3. Budget revenues and expenditures (billion euros)



Source: Law on Budget Allocations for the Republic of Kosovo's Budget for 2025

1.6.2 Budget revenues

Budget revenues primarily come from three main sources: indirect taxes, direct taxes, and non-tax revenues. Approximately 74% of total revenues are collected from indirect taxes (VAT, excise duty, and customs). VAT is the main source of revenue, accounting for about 57% of the total. Of the total VAT revenues in 2024, two-thirds (€1 billion[9]) are collected at the border, reflecting not only Kosovo's high trade deficit but also placing a heavy burden on local businesses, which must pay the tax even before production or sales begin, except in cases of equipment purchases. On the other hand, the collection of VAT within the country, although increasing from €478 million[10] to €534 million in 2025, constitutes about 14% of total revenues and remains insufficient. Excise duties (€593 million in 2024[11]) remain the second-largest source of revenue, accounting for about 20% of the budget. These revenues come from the import of fuels, cigarettes, and alcoholic beverages.

Direct Taxes, which include personal income tax, corporate tax, and property tax, are expected to increase by 10% in 2025 compared to 2024[12], and will account for about 17% of the total. This indicates that while tax rates are relatively low, there is also an insufficient domestic tax collection base. Furthermore, Kosovo is the only country in the region where dividends are not taxed at all, and capital gains, especially from real estate transactions, are almost untaxed due to administrative limitations (World Bank, 2023). For 2025, *non-tax revenues* are expected to reach €356 million, up from €292 million in 2024, with the largest increase coming from concessionary fees due to the growing number of passengers at the Pristina International Airport. This revenue structure shows that Kosovo's budget largely depends on border taxes, reflecting a high level of consumption and a structural issue in the economy.

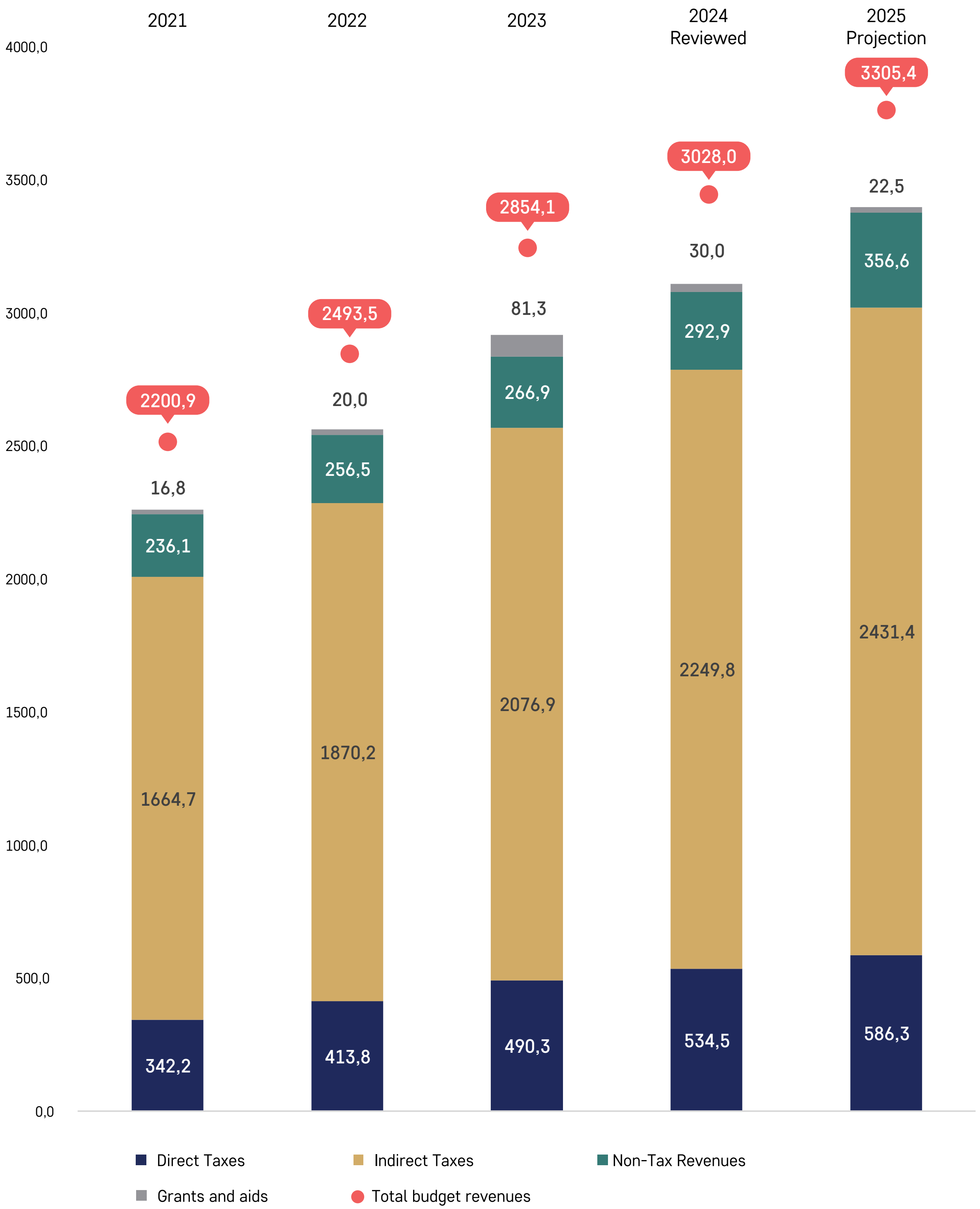
9 For the period January–October 2024, approximately 839 million euros were collected, or 83 percent of the planned revenues. MFLT (2024). Monthly Fiscal Series: https://mfpt.rks-gov.net/Thesari/Page/973

10 For the period January–October 2024, approximately 382 million euros were collected, or 80 percent of the planned revenues. MFLT (2024). Monthly Fiscal Series:: https://mfpt.rks-gov.net/Thesari/Page/973

11 For the period January–October 2024, approximately 539 million euros were collected, or 85 percent of the planned revenues. MFLT (2024). Monthly Fiscal Series: https://mfpt.rks-gov.net/Thesari/Page/973

12 For the period January–October 2024, approximately 464 million euros were collected, or 87 percent of the planned revenues. MFLT (2024). Monthly Fiscal Series: https://mfpt.rks-gov.net/Thesari/Page/973

Figure 4. Budget revenue structure



Source: Draft Law on Budget Allocations for the Republic of Kosovo's Budget for 2025; author's calculations

1.6.3 Structure of budget expenditures

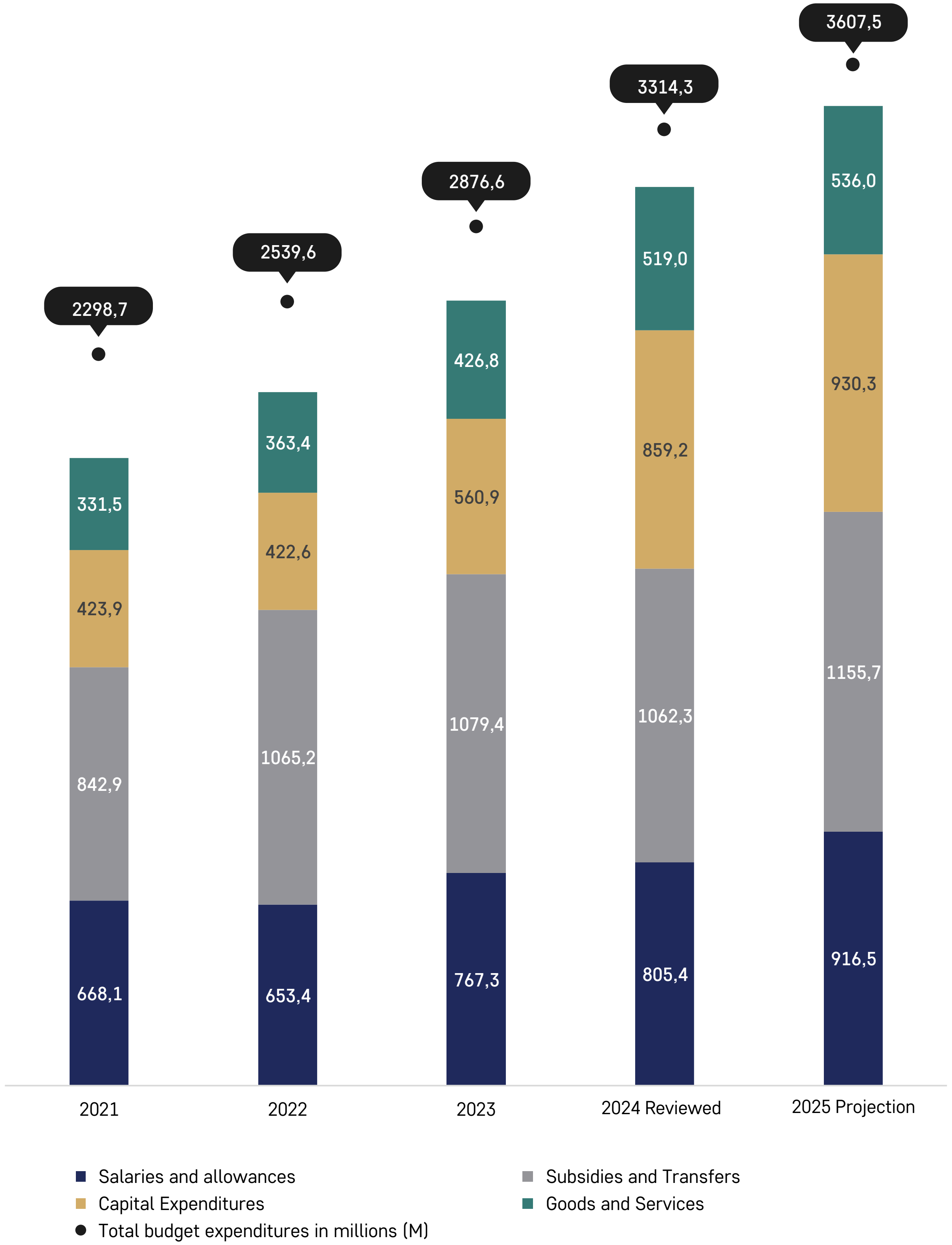
Total expenditures for 2025 are projected to be 3.6 billion euros, an increase of 8.8% compared to 2024. Current expenditures for salaries, subsidies, and goods are expected to be 2.6 billion euros, or 72% of total expenditures, representing 24% of GDP. Of this, salaries and allowances will increase by 14% compared to 2024, making up about 25% of the expenditures. This increase is due to the rise in the salary coefficient in the public sector and the implementation of regulations stemming from the Public Law on Salaries. Subsidies and transfers are projected at 1.15 billion euros in 2025[13], representing around 32% of total expenditures or 9% more compared to 2024[14], which is primarily related to pension increases.

Expenditures for goods and services will be 536 million euros, while the remaining expenditures include interest payments on public debt (50 million euros) and the state reserve (10 million euros). Capital investments for 2025 will increase by 8% compared to the previous year and will account for about 26% of total expenditures. A detailed analysis of these investments can be found in table 10. This atypical structure of budget expenditures, which is more oriented towards current expenditures than investments, slows down job creation, reduces productivity, and limits the potential for sustainable economic growth. The structure of the budget is clearly skewed towards transfers and subsidies at the expense of capital investments. Although this category still holds an insufficient share in Kosovo's budget, there are serious problems with the implementation of planned investments.

13 For the period January–October 2024, approximately 706 million euros were spent, or 88 percent of the planned revenues. MFLT (2024). Monthly Fiscal Series: https://mfpt.rks-gov.net/Thesari/Page/973

14 For the period January–October 2024, approximately 808 million euros were spent, or 76 percent of the planned revenues. MFLT (2024). Monthly Fiscal Series: https://mfpt.rks-gov.net/Thesari/Page/973

Figure 5. The structure of budget expenditures



Source: MFLT (2024). Draft Law on Budget Allocations for the Republic of Kosovo's Budget for 2025

Over a four-year period, or a government mandate, nearly 3 billion euros in capital investments were planned, of which around 1.78 billion euros or 60% of the planned expenditures were executed[15]. This underspending in capital investments has slowed the potential for economic growth by 1-2%, limited business activity, and negatively impacted the improvement of services for citizens. Additionally, considering the average inflation rate of around 20% over these years, the depreciation of unused funds represents another problem.

Although these investments have increased cumulatively over the years, in 2025 they will account for about 25% of total expenditures or 8% of GDP. In 2024, similar to previous years, the trend continues, with only 387 million euros spent by October out of the 859 million euros allocated, representing 45% of the total. At this rate, it is expected that no more than 60% of these expenditures will be realized by the end of the year[16]. Meanwhile, while the government argues that the underspending of capital projects was hindered by the lack of operationalization of the Procurement Review Body (PRB), the relevant audit reports highlight that the main issues are the delayed start of projects by budgetary organizations, contract terminations due to non-performance by economic operators, poor contract management, and unresolved land expropriation issues. The low level of capital project realization at the central level has also been caused by delays in completing works and services according to their dynamic plans (ZKA, 2023).

Table 10. Budgeting and implementation of capital investments (million euros)

	2021	2022	2023	2024 (January - October)
Capital investment budgeting	626	704	820	859
Implementation of capital investments	420	419	554	387
Unrealized Investments	206	285	266	472
Percentage of Implementation	67%	60%	68%	45%

Source: Draft Laws on Budget Allocations: Fiscal Series 2021 – 2024; author's calculations

15 Capital expenditures for 2024 have been calculated up to October.
16 Calculations are based on the trends of capital expenditures over the past three years.

Public expenditures at the sectoral level are essential for promoting economic stability, improving public services, and ensuring balanced development in various fields such as education, healthcare, infrastructure, social protection, and security. The allocation of funds is typically based on national priorities, economic demands, and social needs. Compared to previous years, the structure of sectoral expenditures in this year's budget has changed; from 10 priority sectors until 2024, there are now 16 such sectors. This change may have provided a better breakdown of budget allocations, but it has also caused a loss of connection with line ministries in terms of transparency and data presentation.

Similar to previous years, social care remains one of the government's priorities, with 770 million euros allocated to this category, or 7% of GDP, an amount that is nearly three times larger than expenditures for healthcare. This year, total expenditures for healthcare, including the healthcare grant (83 million euros) and funding for residential healthcare (8 million euros), amount to 370 million euros, or 3.4% of GDP.

This level of healthcare funding is noticeably lower not only compared to European Union (EU) and OECD countries but also when compared to regional countries, except for Albania (around 3% of GDP). Government expenditures on healthcare in Bosnia and Herzegovina reaches 6.5% of GDP, in Montenegro 6.5%, in Serbia 6.3%, and in North Macedonia 4.7% (Riinvest Institute, 2024).

Expenditures for education and science in 2025, including the education grant (249 million euros), are expected to be 388 million euros, or 3.5% of GDP (2025), which is below the EU average of 4.7%. Meanwhile, sectors related to the economy do not seem to be a priority for the government in 2025. Funds for the labour market (33 million euros) and support for businesses and industries (39 million euros) are insufficient to address urgent needs and do not align with Kosovo's strategies. Although Kosovo has committed to a green energy transition under the Sofia Agreement, financing for the environment (60 million euros) and energy (59 million euros) constitutes only around 4% of the sectoral budget.

Table 11. Framework of sectoral expenditures at the central level (million euros)

Sectors	2023 (Implemented)	2024 (Budgeted)	2025 (Budgeted)	Percentage of increase or decrease (2025/2024)
Public Administration, Finance, and Foreign Policy	234.3	371.1	350.0	-5.7%
Defence and Security	177.9	153.0	158.7	3.7%
Public Safety	190.5	185.1	204.2	10.3%
Justice	81.0	101.4	111.8	10.2%
Environment	53.9	72.9	60.7	-16.7%
Transport and Communication	113.1	205.0	272.8	33.1%
Energy	58.3	59.5	59.6	0.2%
Support for Businesses and Industry	39.9	31.3	39.7	26.8%
Agriculture	91.1	89.8	90.3	0.5%
Culture, Recreation, and Sports	56.1	99.2	107.0	7.9%
Labour Market and Employment	21.1	33.5	33.8	0.8%
Social Care	679.8	713.2	770.7	8.1%
Health	222.3	263.7	275.0	4.3%
Education and Science	99.0	134.4	139.3	3.7%

Source: MFLT (2024). Medium-Term Expenditure Framework 2025 -2027

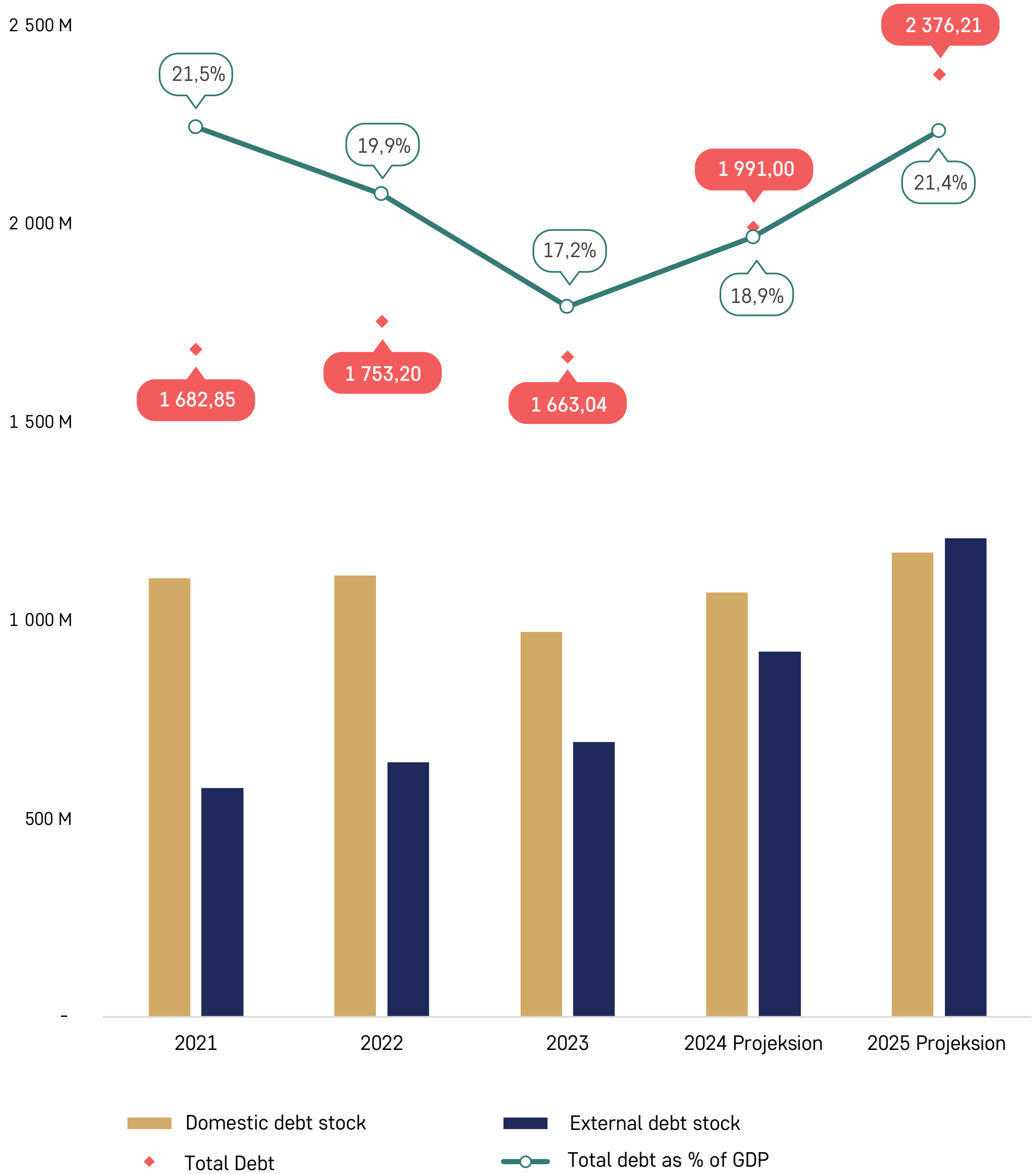
1.6.4 Analysis of Public Debt

The overall portfolio of Kosovo's public debt remains at sustainable levels and within the fiscal rules and the Law on Public Debt and State Guarantees, which stipulates that public debt should not exceed 40% of GDP.

Domestic debt mainly consists of treasury bond issuances, government bonds, and bonds. According to government projections, by the end of 2024, this component of public debt is expected to reach 1.07 billion euros, or 53.7% of the total debt. While it is positive that more than half of the total debt is domestic, it is concerning that this debt is being used to cover the budget deficit related to the purchase of goods and services, as well as transfers (ZKA , 2023), rather than financing capital investments.

External debt at the end of 2024 is expected to be around 921 million euros, showing a 33% increase compared to the previous year. This external debt is owed to international financial organizations, primarily the International Development Agency (World Bank) 36%, the European Bank for Reconstruction and Development (EBRD) 13%, the European Union (EU) 14%, and the International Monetary Fund (IMF) 11%. External debt has been borrowed to finance projects in sectors such as education, agriculture, land registry, energy, healthcare, wastewater treatment, central heating, road and railway rehabilitation (MFLT, 2023). In 2023, the Assembly ratified eight (8) loan/financial agreements to finance projects in the sectors of environment, energy, transport, digitalization of public administration, as well as public finance reforms and economic growth. However, the situation regarding the dynamics of implementing projects linked to contracted debts is concerning. According to the ZKA (2013), the delay in credit agreements and the slow withdrawal of available funds is a result of poor planning, the expropriation process, and the lack of governmental capacity to effectively and timely utilize borrowed funds. As a result of these shortcomings, the government continues to pay commitment fees for these unused loans.

Figure 6. Structure of Kosovo's Public Debt



Source: Public Debt Program 2024 – 2026, GDP = GNP

Business environment

2

This chapter provides a summary of the challenges in the business environment over the past three years. The critical role of the business environment in the development of the private sector in Kosovo is particularly related to barriers linked to the legal and fiscal aspects, access to finance, informality and corruption, the labour market, administrative and infrastructural barriers, and barriers directly related to business operations.

Barriers resulting from institutional factors are especially important to analyse in order to offer recommendations and implications for the policies that institutions should follow. In terms of the trend of businesses opening and closing, there have been few changes. Compared to the first three quarters of the previous year, on average, there has been a 5 percent increase in newly registered businesses, particularly in the sectors of trade, information and communication, construction, and transport. However, with the exception of the second quarter, in the other two quarters, there was a decrease in closed businesses.

During the first three quarters of 2023, there were 8,588 new businesses, compared to 1,206 closed businesses. In the same period in 2024, the number of new businesses was 9,017, while the number of closed businesses was 1,208. The proportion of closed businesses for the first three quarters of 2023 was 7.5, while in 2024 it was 7.1, meaning that for every closed business in 2024, 7.1 new businesses were opened (KAS, 2024).

2.1 Main barriers in the business environment 2024

The following part summarizes the results from the regular surveys conducted by the Riinvest Institute since 2017, covering a range of indicators and obstacles faced by businesses in Kosovo. Table 12 reflects the perceptions of businesses regarding 30 different indicators and their intensity over the years. The colours in the table represent the impact on doing business from the perspective of businesses for each barrier, where green indicates a low-intensity barrier, yellow and orange indicate medium intensity, and red indicates a high-intensity barrier[17]. It is clear that this year, according to the assessments of business leaders in the survey conducted during the period of September-October 2024, the five main barriers are informality and fiscal evasion, and the migration of workers, both with nearly the same intensity, followed by the skills and education of workers, corruption, and the cost of financing, with an intensity ranging from approximately 60 to 64 points out of a maximum of 100 points.

Barriers in the business environment have a significant impact on determining the sustainability and growth of businesses, directly influencing their competitiveness both at the national and international levels. Barriers such as access to finance, high informality, and administrative obstacles expose businesses to economic uncertainty and the risk of bankruptcy, which in turn affects their competitive ability. Moreover, the labour market faces challenges due to the lack of skilled workforce and continuous migration, which directly impacts the development of the private sector. Therefore, these barriers also affect the attractiveness of the business environment for foreign investors and domestic investments, limiting economic development and progress in the global market.

17 The intensity of each indicator (barrier) has been measured on an intensity scale from 0 to 100, where 0 indicates that the specific issue or indicator is not considered a barrier, while a value of 100 points represents a very significant barrier to doing business.

Table 12. Barriers in the business environment

Year	2017	2023	2024
Tax Rates	57.3	63.7	51.7
Administrative Burdens	54.3	63.5	-
Laws and the judicial system	52.8	55.4	47.3
Access to Credit	50.7	58	51.4
Cost of financing	56.5	63.5	56.8
Limited Business Potential	45.9	57.5	-
Managerial Skills	36.9	53.7	-
Supply of Raw Materials and Equipment	41.8	59.2	-
Small market (low demand)	61.3	65.7	-
Access to enterprise information	37.1	55.3	39.7
Debt collection	47.9	59.7	48.0
Corruption	58.9	59.8	59.4
Electricity supply	51.2	57.2	39.3
Transportation	35.7	51.2	35.8
Telecommunications	32	47.6	31.0
Security and political stability	52.2	57.6	44.1
Inefficient tax administration	53.8	62.8	52.4
Customs	47	60.6	47.4
Licensing procedures	43.8	-	39.9
Crime and stealing	57.3	61	-
Extortion	47.3	-	-
Skills and education of workers	38.7	55.1	60.4
Migration of workers	-	75.2	64.0
Fiscal evasion and informality	57	63.5	64.7
Breach of contracts by consumers and suppliers	-	-	48.0
Access to land	-	-	44.4
Non-tariff barriers	-	-	43.6
Production standards	-	-	42.6
Rapid technological changes	-	-	42.1
Labour laws and regulations	-	-	38.4

Source: Riinvest Institute Survey, 2024

2.2 Legal and fiscal regulations

This group of barriers includes issues related to the fiscal system (tax rates and tax administration), perceptions related to customs, as well as laws and the judicial system in general. Although most businesses consider tax rates and inefficient tax administration to be medium-intensity barriers, there has been noticeable improvement compared to 2023. This shift in business perceptions is linked to the increased efficiency and good performance of Kosovo's tax administration in tax collection and enforcement of regulations, including the adoption of the tax administration law and procedures. However, revising Kosovo's tax policy remains a challenge for the upcoming year (European Commission, 2024). As for customs, two-thirds of businesses do not view them as a barrier. Finally, laws and the judicial system present a moderate barrier, as nearly most businesses consider it a challenge for the business environment. The inefficiency of the judicial system still affects the enforcement of contracts by consumers and suppliers, a barrier that continues to have a negative impact on businesses, directly affecting transaction costs of businesses.

The Government of Kosovo has approved the **Program for the Prevention of Administrative Burdens (2020-2027),** an inter-institutional initiative aimed at reducing the administrative burden on citizens, businesses, and society (ZKM, 2022). As part of this program, in the process of reducing the burden, 152 services have been simplified and 64 others eliminated. Furthermore, the digitization of over 30 services has begun to enable easier access for citizens. Institutions have simplified service limitations related to administrative fees, documents, requests, and validity periods. In 2022, the Ministry of Industry, Entrepreneurship, and Trade (MIET) has unified 15 permits related to products such as oil and gas, standardizing the fee at 50 euros for all these permits. Similarly, the **Kosovo Business Registration Agency (ARBK)** took similar actions to simplify administrative procedures for registering and changing the status of businesses, reducing administrative burdens and fees by up to 50 percent (ZKM, 2024). However, there is still a significant amount of work to be done in addressing other obstacles and barriers within the implementation of this program.

2.3 Access to finance

Although access to finance has improved over the years, it remains one of the main obstacles to doing business for SMEs. Access to credit has decreased in intensity from 58 points in 2023 to 51.4 points out of 100 possible points in 2024. Another challenge for businesses is the cost of financing, as most businesses consider it a barrier to investment.

The limited scope of alternative financing, such as angles investors network, represents a fundamental barrier for businesses in Kosovo (European Commission, 2023; OECD, 2024). Kosovo has the lowest level compared to other Western Balkan countries in terms of alternative financing sources. The limited legal framework regulating the microfinance institutions market negatively impacts the growth and long-term sustainability of the sector (OECD, 2024). However, an important aspect of improving access to finance is linked to the Kosovo Credit Guarantee Fund (KCGF), which has become an important financial intermediary. The number of loans guaranteed by the KCGF and the diversity of funding windows, primarily six types of guaranteed loans, have increased over the years, covering five sectors (product manufacturing, construction, agriculture, forestry and fisheries, wholesale and retail trade, and services). In 2023, the intermediary loan for SMEs was 120 million euros, distributed across 2,216 loans, facilitating access to finance for 1,978 SMEs. By the end of 2023, approved loans totalled 626.4 million euros for 10,157 SMEs, with a cumulative guarantee amount of 329.47 million euros. SMEs used these loans for working capital investments (56%) and capital investments (44%) (KCGF, 2023).

2.4 Informal economy and corruption

High informality is also reflected in business perceptions, where compared to last year (63.5 percent), there has been an increase of 1.2 percentage points. Although the National Strategy for Preventing and Combating the Informal Economy, Money Laundering, Terrorism Financing, and Financial Crimes (2019-2023) has been approved (Riinvest, 2023; Government of Kosovo, 2023), the impact of these strategies in practice is still limited. According to the Balkan Business Barometer, Kosovo has a score of 2.3 out of 5 possible points, indicating that informality is seen as a major obstacle for businesses. High informality creates an unfair competitive environment, increasing operating costs and negatively impacting the growth and sustainability of micro and small businesses. It also limits access to financing, which is essential for these businesses in the early stages of development. Furthermore, participation in the informal economy discourages investment in innovation and the adoption of new technologies, thereby reducing their productivity.

The high level of corruption, as perceived by businesses, continues to be regarded as a challenge. Compared to 2023, there has been a slight increase in intensity this year (see table 12), with the majority of businesses perceiving corruption as an obstacle to development and doing business in Kosovo, ranking it among the top five barriers. As a result of the lack of up-to-date anti-corruption policies, Kosovo has the second-lowest result compared to the economies of the Western Balkans. According to the OECD's assessment (2024), Kosovo is below the average of Western Balkan countries in sub-dimensions of anti-corruption policies, such as policy and risk assessment for corruption, prevention of corruption, business integrity and corporate accountability, and criminal investigations and prosecution. According to the OECD, this is due to the lack of an updated anti-corruption policy.Furthermore, despite the adoption of a legal framework regarding the rule of law and anti-corruption policies, challenges remain regarding the progress of these reforms and achieving practical results that also aim to improve the capacity and efficiency of judicial institutions (KDI, 2024). Limited progress in the fight against corruption and the weakness of the rule of law has also been confirmed by the European Commission's Progress Report (European Commission, 2024).

2.5 Labour market

The labour market in the six Western Balkan countries (WB6) is characterized by employment in the informal sector, a mismatch between skills and abilities and the demands of the private sector, and high migration rates (World Bank, 2024a). Additionally, the labour market is marked by the continuous migration of workers, a declining working-age population, low salaries, and low labour force participation, especially among women (World Bank, 2024b). The indicators related to the labour market have been listed as the highest-intensity barriers by businesses. One of these barriers is migration, which, for the second consecutive year, despite a lower intensity in 2024, has emerged as a significant obstacle for businesses. The high migration of the workforce in Kosovo raises concerns about the loss of human capital. These labour market developments create an urgent need for a new growth model that focuses on creating higher-quality jobs and developing human capital to maintain macroeconomic stability (World Bank, 2024).

The lower score compared to the previous year may be linked to businesses' responses to the loss of workers. Data from a Riinvest study (2023) show that 79 percent of businesses increased salaries by an average of 22 percent in 2023, and one-third of businesses (37 percent) plan to raise salaries further. Almost a quarter of businesses plan to improve working conditions, 20.6 percent plan to hire more women, and 10.4 percent plan to invest in new technology for work automation.

In addition to migration, the lack of skills and abilities among workers is considered a major barrier for businesses. In the past two years, survey findings from businesses show that the majority of businesses assess that workers lack the skills and abilities required in the workplace. These findings correspond with the Riinvest and ASHAK study (2023), which adopted the World Economic Forum (WEF) methodology on the Global Competitiveness Index (GCI). The study indicates that Kosovo ranks 118th with a score of 45 out of 100 for social capital, while in terms of skills, it ranks 58th with a score of 67.4. Furthermore, Kosovo ranks 90th out of 142 countries with a score of 46.9 out of 100 for the quality of vocational training (ASHAK, 2023).

To address the skills mismatch, the government has adopted several strategies, such as the Employment Strategy 2024-2028 (GoK, 2024) and the Education Strategy 2022-2026 (MESTI, 2022), as well as measures through the Economic Reform Program (GoK, 2024) to narrow the visible skills gap in the labour market. However, so far, there have been no tangible results in terms of the implementation of these strategic documents.

2.6 Administrative barriers and infrastructure

Following the energy crisis caused by the war in Ukraine, compared to last year when most businesses considered electricity supply as a barrier, survey findings indicate that only a third of businesses now view it as a medium-intensity issue. This is also acknowledged in the European Commission's progress report as an achievement, largely thanks to the progress made under the EU-funded energy efficiency support package, which helps both households and the private sector (European Commission, 2024). Compared to 2014, there is a positive assessment from businesses regarding licensing procedures. In the transportation policy sub-dimensions of the OECD study (2024), such as planning, Kosovo is rated above the average of the Western Balkan countries, except for the sub-dimension of planning and management. As for telecommunications, in 2023, Kosovo succeeded in connecting rural settlements to internet infrastructure. These findings from the OECD study are also confirmed by survey results, where businesses assess that transportation and telecommunications constitute barriers with low intensity.

2.7 Internal barriers

In addition to external business environment barriers, businesses in Kosovo also face barriers related to internal factors within their operations. These barriers directly affect a business's ability to compete not only at the national level but also internationally. One positive change compared to previous surveys is that, in the last two years, company leaders increasingly perceive the insufficient skills and education of workers, as well as managerial skills, as significant obstacles.

In this year's survey findings, rapid technological changes have been rated as a low-intensity barrier. This is linked to the lack of an internal business strategy for responding to the rapid pace of these changes, particularly in terms of businesses' ability to adapt. Meanwhile, compared to last year, where access to information was considered a medium-intensity barrier, there has been a noticeable decline this year, with access to information now rated as a low-intensity barrier. This is a clear indication that, in order to gain access to information, businesses need to develop networking skills. In transition countries like Kosovo, networking is a vital business strategy to navigate an uncertain business environment, providing a competitive advantage through access to resources and, as a result, driving business growth. Production standards constitute a medium-intensity barrier for businesses. This is not only related to the lack of investment in the latest technologies within businesses but also to the absence of certification bodies for products intended for export. To address this, the Government's Growth Plan has outlined support for six testing laboratories and four certification bodies, which will be ready to provide international accreditation.

INVESTMENT

3

3.1 The volume, dynamics, and structure of investments

The dynamics and quality of economic growth and overall economic and social development are determined primarily by the volume and quality of investment activity. Volume refers to the depth or weight of gross investments in GDP (investments as a share of GDP), expressed as a percentage. Countries with a higher percentage of investments relative to GDP aim for a higher growth rate and are usually at a lower stage of development. However, economic growth depends not only on the volume of investments but also on their quality—that is, the efficiency of investments and their marginal contribution to GDP growth.

Efficiency depends on the quality of the preparatory process for investment decisions, cost-benefit assessments, the implementation of approved projects, and the successful exploitation during their operational period. Table 13 reflects the investment rate in Kosovo and the countries of the region.

Table 13. Gross Investments as a Share of GDP in Kosovo and Regional Countries (percent)

	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	Average
Bosnia and Herzegovina	22.5	21.7	22.7	24.6	24.4	24.8	23.1	26.1	27.4	26.8	24.4
Montenegro	20.2	20.1	26.1	30.2	31.9	32.0	31.2	26.7	30.3	27.6	27.6
North Macedonia	30.3	30.4	32.5	32.3	32.3	34.3	29.9	32.2	36.0	29.6	32.0
Albania	25.7	25.8	25.2	25.1	23.9	23.0	23.0	24.8	20.9	18.6	23.6
Serbia	16.5	18.5	18.2	19.7	22.5	24.9	24.1	24.9	26.4	24.6	22.0
Kosovo	27.8	30.4	33.5	34.7	36.3	34.6	33.4	36.0	35.2	33.9	33.6

Source: Eurostat, 2024

Kosovo has the highest average share of Gross Capital Formation (33.6 percent) in the Western Balkans for the period 2014–2023. However, this high share has not translated into high rates of economic growth, raising questions about the efficiency of these investments and their impact on productivity. North Macedonia (32.0 percent) also exhibits a high level of investments, while Montenegro (27.6 percent) shows significant variations, mainly due to large infrastructure projects. Bosnia and Herzegovina (24.4 percent) and Albania (23.6 percent) maintain relatively stable levels, whereas Serbia (22.0 percent) has the lowest level of investments as a share of GDP.

As noted earlier and further discussed in section 3.3, high investment percentages are not always sufficient to drive sustainable economic development without effective planning and management.

Overall investments include private sector investments, government and public enterprise investments, and foreign investments, including contributions from the diaspora. An overview of these investments in 2023 is presented in Table 14.

Table 14. Investments in Kosovo in 2023 (in million Euros)

	A		B	
	2023	**Proportion (%)**	**2023**	**Proportion**
Government investments	554	24	554	18
Investments of Publicly-Owned Enterprises	85	4	85	3
Private sector investments	817*	36	1600**	52
FDI	840	37	840	27
Total and structure (in %)	**2296**	**100**	**3079**	**100**

Source: 1 – Government of Kosovo; 2 – Unit for Monitoring Public Enterprises; 3 – *Tax Administration of Kosovo (TAK), **Riinvest Institute Survey; 4 – Central Bank of Kosovo (CBK)

According to these data, the level of investments in Kosovo is estimated to be around 2.3 billion euros. This calculation is based on administrative data reported by relevant institutions. If, for the level of private sector investments, we use data from the Riinvest Institute extrapolated to include the entire population, the level of investments reaches approximately 3.1 billion euros.

Although this figure is closer to the estimated level of gross investments in Kosovo as calculated by the Kosovo Agency of Statistics (KAS), the IMF, the World Bank, the Central Bank, and the Government, there is still a discrepancy. This highlights the importance of improving statistical information, particularly regarding private sector investments.

These data emphasize the need not only to increase investments but also to enhance their quality to ensure a sustainable and measurable impact on economic growth and sustainable development. Investment efficiency remains a key challenge for Kosovo and the region as a whole.

Public Investments

Data on budgeting and implementation of capital investments in Kosovo for the period 2019–2024 (discussed in detail in section 1.5) indicate that although investment budgeting has shown significant growth—from 789 million euros in 2019 to 857 million euros in 2023—the execution of these investments has lagged far behind. During this period, approximately 1.3 billion euros earmarked for capital investments remained unspent. The low implementation rate highlights significant challenges in the planning and execution processes.

The failure to execute planned capital investments has major consequences for Kosovo's economy and society. This low level of implementation limits the potential for economic growth. While the efficiency of investments in Kosovo is low, increased investment could still enable higher economic growth. Moreover, unutilized investments constrain the economy's capacity to address inflation, as improvements in infrastructure and productivity could help lower production and service costs. The lack of these investments also limits spillover effects in other economic sectors, such as construction, trade, and services, thus restricting broader economic benefits.

Furthermore, the lack of funding for projects aimed at improving public services such as education, healthcare, and transportation negatively impacts the quality of life for citizens and limits their access to basic services. To maximize economic and social benefits, it is essential to improve the capacity for implementing capital projects and address the institutional challenges that hinder the execution of the capital budget. In the last five years, private investments have been a significant driver of economic growth. Public investments, over the past five years, have recorded the lowest trend in the last decade—even when measured in monetary terms. Despite the lack of infrastructure in the country, capital investments have not been a primary focus in the state budget. In 2013, they were the main category of expenditures, but from 2014 to 2019, government spending was dominated by wages and allowances. Since 2020, subsidies and transfers have constituted the largest category of expenditures, exceeding one billion euros.

This shift toward subsidies and transfers, instead of capital investments, negatively impacts long-term economic growth. Unlike capital investments, which drive infrastructure development and improve overall economic productivity, subsidies and transfers are typically allocated for short-term expenses without creating new productive capacities. This reduces the economy's potential for sustainable growth, limiting the impact that long-term investments in strategic sectors could have.

As a result, the economy becomes less competitive and more dependent on public financing, while the direct impact on growth and development remains constrained.

Central Publicly-Owned Enterprises

Central Public Enterprises (POEs) in Kosovo generated approximately 306 million euros in revenue in 2023, accounting for around 3.2 percent of GDP.[18] Over the past five years, Kosovo's public enterprises have made significant capital investments totaling approximately 307.5 million euros (Table 15). KEK (Kosovo Energy Corporation), with investments amounting to hundreds of millions of euros, has been the enterprise with the highest level of investment, while other enterprises such as Telekom, Trainkos, Infrakos, and Kosovo Post have made more modest investments.

18 This calculation does not include revenues from KMDK due to the lack of data for 2023. The Annual Report for 2023 and financial audits have not yet been published.

Table 15. Implementation of capital projects

POE	2019	2020	2021	2022	2023
Kosovo Post	139,118.00	103,518.00	94,802.00	234,399.00	628,889.00
Ibër Lepenci	381,794.00	228,069.00	451,954.00	438,599.00	223,347.00*
Infrakos	1,419,626.82	69,542.77	40,847.16	311,138.75	278,841.67
KEK	70,151,493.00	77,046,673.00	79,315,845.00	46,275,928.00	151,985,531.00*
Telecom	3,650,000.00	-	883,000.00	16,678,000.00	7,375,000.00
Trainkos	197,577.00	245,099.00	442,840.00	247,479.00	192,124.00
Trepça	-	1,437,250.00	34,000.00	36,553,554.00	39,376,108.50
KMDK	933,305.00	666,000.00	1,005,376.00	1,441,669.00	1,012,423.00

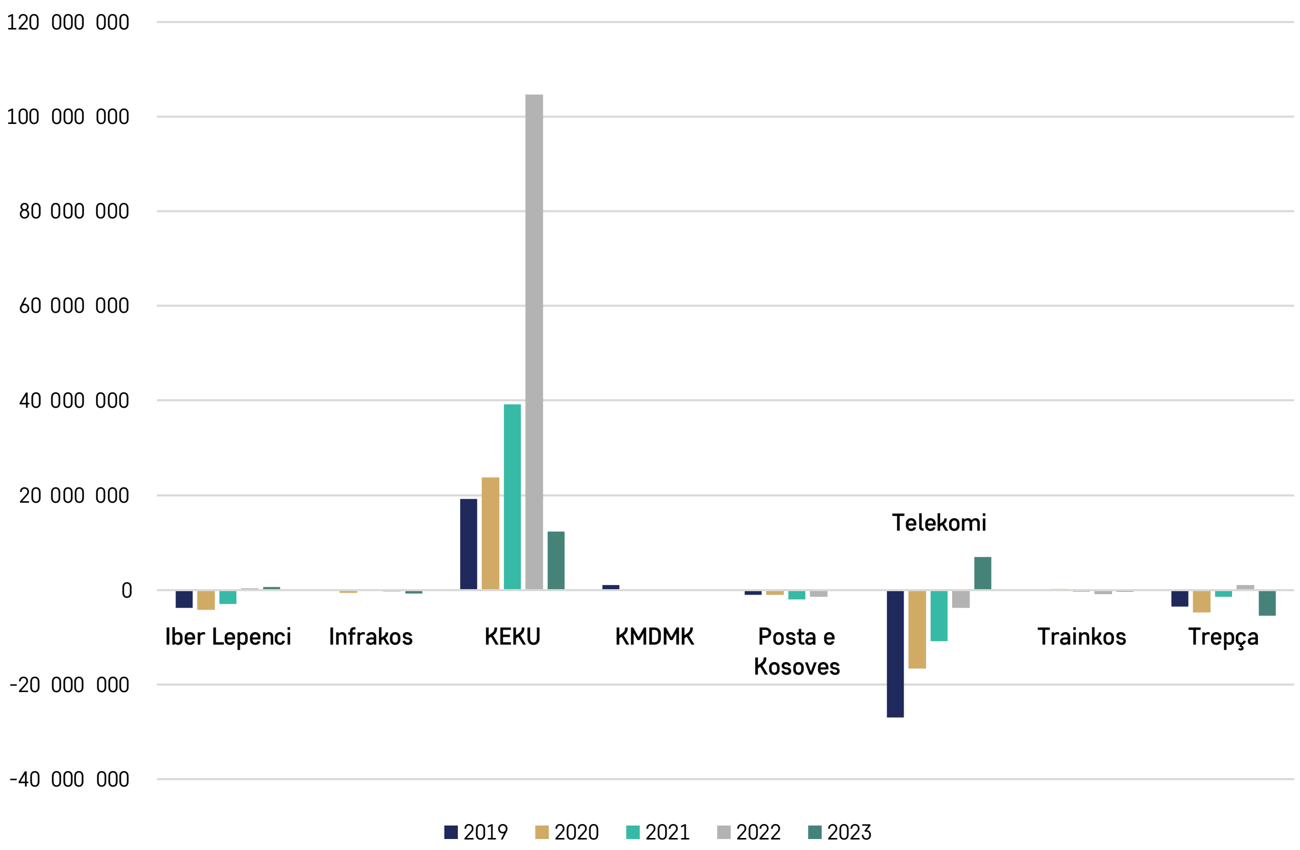
Source: Annual reports or budget plans of Central Public Enterprisesë[19]

Despite these investments, the performance of most of these enterprises has remained poor, consistently showing financial losses year after year (Figure 6). This suggests that the capital investments made have yet to improve the operational efficiency and financial sustainability of these enterprises. Contributing factors include poor corporate governance, mismanagement, and a lack of innovation.

An exception is Telekomi i Kosovës, which in 2023 recorded a profit of approximately 7 million euros—a significant achievement after several years of continuous losses. Additionally, KEK's positive financial performance is notable; however, this situation is somewhat specific due to increased demand for electricity and rising energy prices following the war in Ukraine. Geopolitical tensions have impacted global energy markets, driving up prices and creating a favorable environment for energy producers like KEK.

19 Shënim*: ***Për Ndërmarrjen Trepça dhe KMDMK, si dhe të dhënat për vitin 2023 të KEK-ut dhe Ibër Lepencit, janë evidentuar të dhënat nga buxheti i planifikuar për investimet kapitale, në mungesë të të dhënave për realizimin e tyre. Këto të dhëna nuk janë përfshirë kur është kalkuluar investimi I realizuar prej 307 milionë eurove. Nëse llogariten edhe këto investime, atëherë shuma do të arrinte vlerën prej afërsisht 390 milionë eurove.***

FIGURE 7. Summary of Net Profit/Loss for POEs (2019–2023)



Most investments by public enterprises have been financed by the companies themselves; however, a significant portion has been funded by the budget of the Republic of Kosovo. Of the approximately 59 million euros transferred by the government of Kosovo to central public enterprises over five years (2019–2023), only around 9.4 million euros were allocated as capital investments, while the remainder consisted of subsidies.

This funding structure highlights substantial support for these enterprises to cover operational costs, but with little focus on capacity building or infrastructure improvement through long-term investments. This model can create dependency on the government and limit the sustainable development of enterprises, as subsidies cover daily expenses but fail to address modernization and efficiency needs.

In the long term, the lack of capital investments can negatively impact enterprise performance, making them less competitive and increasing the pressure for continued financial support from the government.

Private sector

Data on investments in Kosovo from 2019 to the first half of 2024 indicate a significant increase over these years. According to data from the Tax Administration of Kosovo (TAK), investments grew from €392.9 million in 2019 to €817.4 million in 2023. Data for 2024, reflecting only the first six months, have already reached €449.8 million. If this trend continues, total investment for 2024 could surpass the levels of previous years. These figures are also confirmed by the Riinvest Institute survey. Furthermore, businesses' expectations for 2025 indicate that investments will increase by approximately 20 percent.

The three main sectors that have mobilized the most investments during this period are Wholesale and Retail Trade, Construction, and Manufacturing, reflecting the composition of Kosovo's economy. While the level of investments has increased significantly, the structure of private investments in Kosovo, with a heavy focus on trade and construction, poses challenges for long-term economic development. This inclination toward sectors sensitive to economic cycles may increase economic instability, creating dependence on consumer demand and remittances from the diaspora.

The lack of significant investments in other productive and value-added sectors may hinder economic diversification and limit Kosovo's capacity to build a sustainable production base. Moreover, the focus on trade and construction does not contribute significantly to innovation or long-term productivity growth. Limited investments in sectors with potential for technological development, such as manufacturing and scientific and technical activities, leave little room for sustainable growth. This lack of diversification increases the economy's risk of facing difficulties during periods of global economic crises or structural changes, making it more vulnerable to external shocks and limiting its potential for sustainable development and innovation.

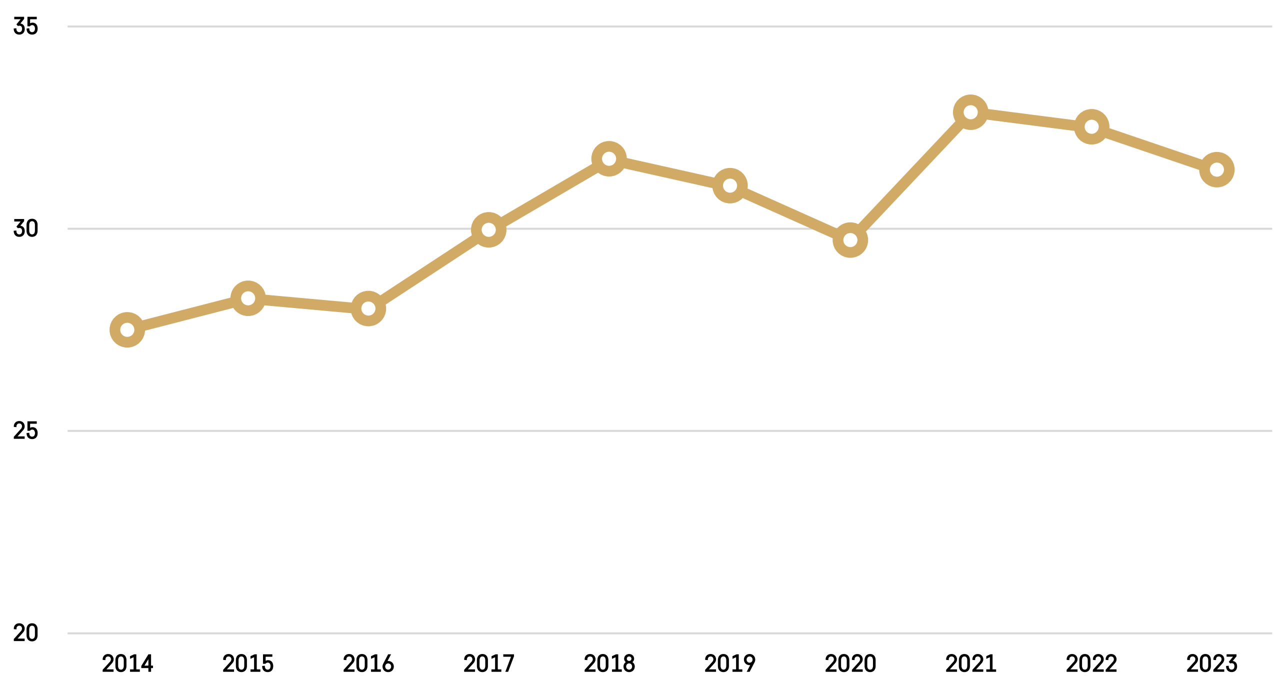
The large share of the construction sector in Kosovo's economy, representing over 17 percent of total investments, 8 percent of GDP, and 10 percent of company turnover, poses significant risks to the country's economy. The construction boom, driven by diaspora demand and supported by continuous bank financing, has pushed real estate prices to increasingly higher levels. However, according to the latest population registry, about 40 percent of housing units are vacant, which clearly indicates an oversupply in the housing market, suggesting that a large part of the demand may be speculative and not based on actual housing needs. This dynamic creates the risk of a real estate bubble, where high prices may experience a sudden drop if demand from the diaspora decreases or bank financing is restricted. Such a decline would not only harm the construction and real estate sectors but could also have consequences for the banking sector, increasing bad loans and impacting financial stability.

Additionally, since real estate prices in Kosovo are largely dictated by demand from the diaspora and foreign investors, resident locals find it difficult to afford buying a house or apartment. Furthermore, this heavy dependence on construction diverts resources from other productive sectors, which may hinder economic diversification and expose the economy to external shocks. The high rate of unused housing units, combined with rising prices, also raises concerns about inefficient capital allocation, as resources are concentrated in unused assets rather than in sectors that could generate sustainable growth and employment. Additionally, the focus on sectors like construction, which are non-tradable, worsens Kosovo's trade deficit.

3.2 Efficiency of investments and economic growth

Over the past decade, the share of Gross Fixed Capital Formation (GFCF) in Kosovo's GDP has shown a gradual increase, rising from 28 percent in 2014 to 33 percent in 2021, before stabilizing around 31 percent in the following years (Figure 7). This trend indicates that Kosovo has allocated an increasingly larger portion of its economic resources to investments in fixed capital, which are essential for long-term economic growth and infrastructure development.[20]

Figure 8. Gross Fixed Capital Formation as a Percentage of GDP in Kosovo



Source: KAS, 2024

20 The 10-year average share of GFCF as a percentage of GDP in the Western Balkan countries shows that Kosovo has the highest average share at 30 percent, followed by Montenegro and Albania at 24 percent, North Macedonia at 23 percent, Bosnia and Herzegovina at 22 percent, and Serbia with the lowest share at 20 percent.

However, despite the increase in the share of GFCF, Kosovo's overall economic growth rate has remained relatively low, with an average of 4 percent. This suggests that, although more resources are being directed towards investments, the productivity or efficiency of these investments has not improved proportionally. This indicates that there are structural challenges or inefficiencies in translating investments into faster growth.

To assess capital productivity in Kosovo, we have used the Incremental Capital-Output Ratio (ICOR)[21], which links investment levels to changes in GDP for the period from 2015 to 2023. The aim is to capture medium-term changes in the ICOR and examine the relationship between capital levels and production growth. In this context, ICOR is influenced by several factors, including the rate of technological progress, the development of professional and managerial skills, and the quality of organizational structures within the economy.

Unlike a narrow focus on new investments, ICOR not only considers the income generated from new investments but also takes into account the productivity of existing assets. This is because the change in GDP (the denominator in this case) reflects the productivity of the entire capital stock. Since existing assets are often larger than the capital added each year, ICOR reflects the efficiency of the entire capital stock and not just the most recent investments. For example, a decline in capacity utilization can lead to an increase in ICOR, even if new investments are productive. This means that ICOR in Kosovo may increase not due to inefficiencies in new investments but because of challenges in fully utilizing existing assets.

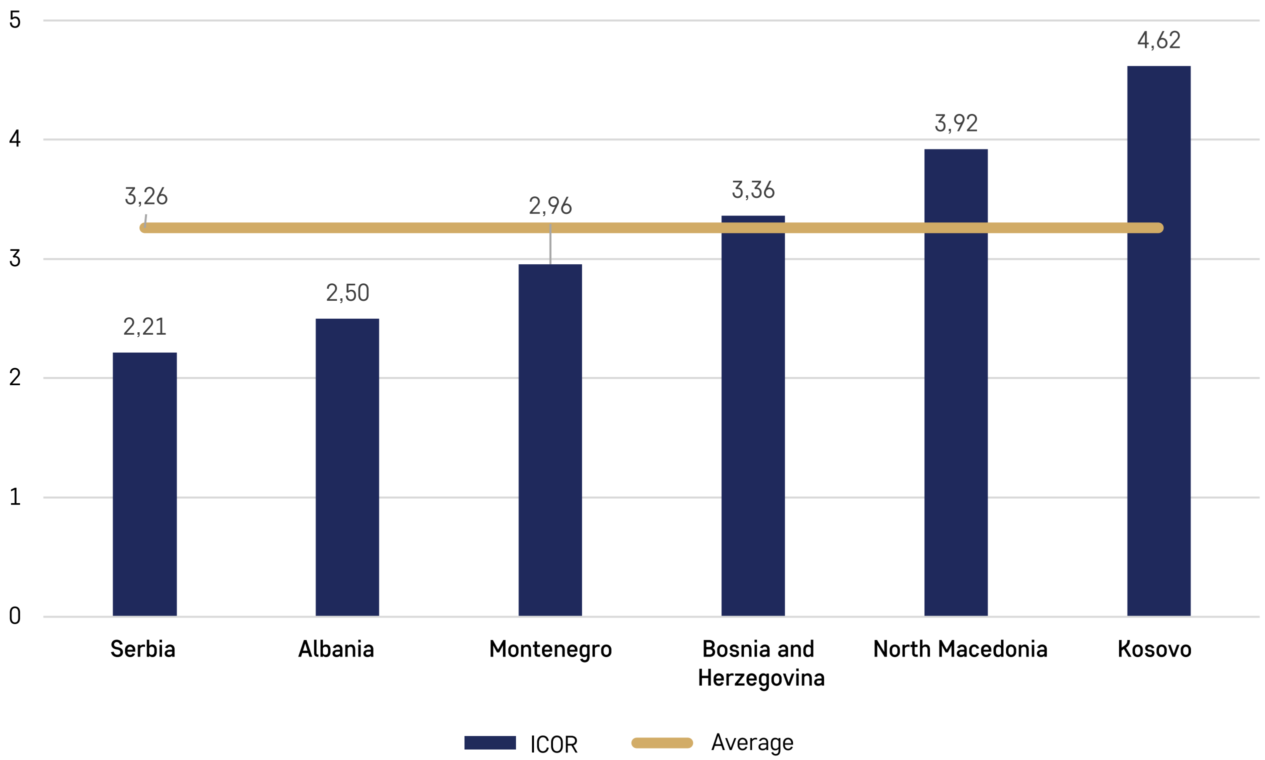
In fact, data from a survey conducted for this study shows that the average capacity utilization by businesses is around 61 percent. This suggests that many companies are not fully utilizing their existing capacity, which leads to lower investment efficiency and, consequently, a higher ICOR. This implies that more fixed capital is used to achieve a certain level of output, namely GDP. Low capacity utilization may result from challenges such as insufficient demand, lack of qualified resources, or unfavorable market conditions, indicating that improving capacity utilization could help lower ICOR and increase capital efficiency in the country.

To gain a better understanding of Kosovo's ICOR, it has been placed in a regional perspective by comparing it with other countries in the Western Balkans (Figure 8). The ICOR values highlight significant differences in capital efficiency across the region. Kosovo stands out with the highest ICOR of 4.62, indicating that it requires significantly larger capital investments to generate economic growth compared to its neighbors. On the other hand, Serbia has the lowest ICOR at 2.21, suggesting relatively high efficiency in converting investments into economic output. Albania and Montenegro also show average efficiency, with ICOR values of 2.50 and 2.96, respectively. Bosnia and Herzegovina (3.36) and North Macedonia (3.92) have higher ICORs, but remain more efficient than Kosovo.

These figures imply that Kosovo faces structural challenges in capital productivity, which could hinder its economic growth compared to other Western Balkan countries. Addressing these inefficiencies may involve measures to improve capacity utilization, enhance the technical structure of investments, improve workforce skills, and overall productivity to bring Kosovo's capital efficiency closer to regional standards.

21 ICOR (Incremental Capital-Output Ratio) for the period from i (2015) to j (2023) is defined as the ratio of the sum of investments during the period from i-1 to j-1 (expressed in terms of GFCF) to the output (expressed in terms of GDP) during the period j, minus the output in period i.

Figure 9. ICOR in the Western Balkan Countries



Source: Authors based on data published by EUROSTAT, 2024.

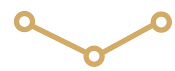
A high ICOR in Kosovo suggests internal inefficiencies in how capital is utilized, partly due to the low capacity utilization of businesses highlighted earlier or even the low labor productivity in utilizing this capital. Additionally, unlike countries with more developed infrastructure and mature sectors, Kosovo may display a relatively high ICOR due to its ongoing need for infrastructure improvements.

Furthermore, the technical structure of business investments in Kosovo during the period from 2023 to 2025, based on survey results, illustrates several reasons explaining the high ICOR (Table 16). In 2023, a large portion of investments was concentrated in less productive assets, with 58.4 percent allocated to new buildings and 29.7 percent to land, while only a small portion was directed towards machinery and equipment (4 percent) and research and development (0.16 percent). This distribution indicates that capital was directed towards assets that, although important for business expansion, do not immediately increase productivity, leading to a higher ICOR.

However, the data show that investments are expected to increase, with a shift towards more productive assets in the coming years. Specifically, the share of investments in machinery and equipment is expected to increase significantly, from 4 percent in 2023 to 22.6 percent by 2025. This shift is promising, as investments in machinery and equipment tend to have a direct impact on productivity and output, which could help reduce ICOR over time. The declining share of investments in buildings and land suggests a reallocation of resources towards assets that yield higher productivity, aligning better with Kosovo's need for efficient capital utilization.

If this focus on more productive assets is realized, it could contribute to improving capital efficiency and overall economic growth in Kosovo.

Table 16. Technical Structure of Investments in Kosovo

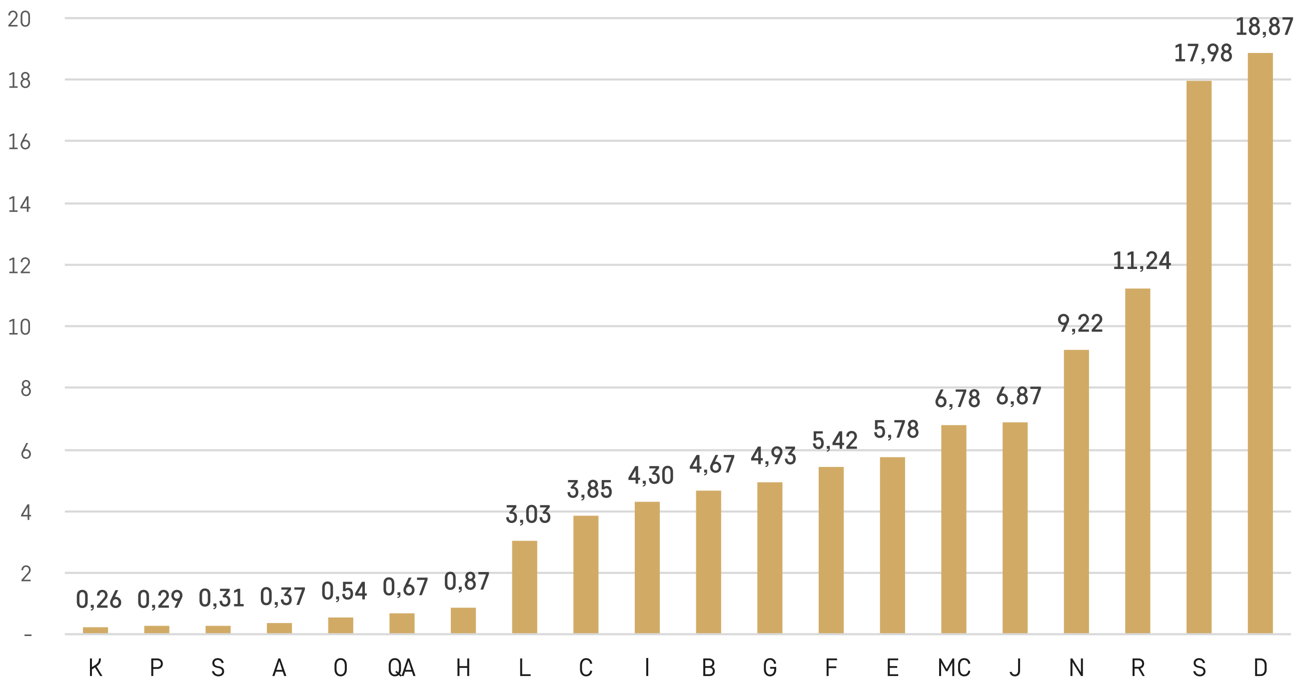
	2023	2024	2025	Trend
Land	29.69	30.33	16.72	
New Buildings	58.43	57.17	49.64	
Machinery and Equipment	4.02	8.51	22.63	
Research and Development (R&D)	0.16	0.14	0.38	
Training; Consulting	0.44	0.33	0.34	
Working Capital/Circulating Capital	6.98	3.01	7.69	
Other Investments	0.28	0.50	2.60	

BSource: Riinvest Institute Survey, 2024.

The technical structure of investments also reveals that spending on research and development (R&D) remains very low, with only 0.16 percent allocated in 2023 and a slight increase to 0.38 percent planned for 2025. Although modest, there is a positive sign with R&D investments expected to rise, suggesting an increasing awareness of the importance of R&D to foster innovation and long-term competitiveness. If this trend continues, even small increases in R&D could contribute to improved productivity and a reduction in ICOR in the future, as innovation could encourage more efficient use of capital in various sectors.

Overall, although ICOR is an informative indicator, its interpretation for Kosovo also requires analysis of the sectoral composition, which affects a better understanding of capital productivity. Based on the survey data and the data from the Tax Administration of Kosovo (TAK) on the sectoral distribution of investments, and data from the Kosovo Agency of Statistics (ASK) regarding each sector's contribution to GDP, we have calculated the ICOR for each sector based on the NACE (one-digit) classification (Figure 9)

Figure 10. ICOR according to sectors



The data suggest that there are significant differences in the level of ICOR across different sectors in Kosovo. Sectors with low ICOR and low investment-to-turnover ratios, such as the financial sector and education, are highly efficient, requiring minimal investment to generate significant output and income. On the other hand, sectors with high ICOR, such as construction, ICT, and energy, require large capital investments that are not efficiently translated into production due to high infrastructure costs, long payback periods, and operational challenges. Sectors with moderate ICOR, such as manufacturing and accommodation, require investment diversification and higher capacity utilization.

This division can inform the prioritization of investments in sectors where capital is used more efficiently, while reforms are implemented in sectors with high ICOR to reduce inefficiencies and maximize economic output. Despite the high ICOR in some sectors due to the initial infrastructure costs (e.g., energy services, transport infrastructure, and digital infrastructure), they are crucial for Kosovo's long-term development. Strategic investments in these sectors can facilitate sustainable and balanced economic growth.

Sectoral data on investments, contributions to GDP, and turnover by sector (Table 17) in Kosovo show an economy largely supported by wholesale and retail trade and construction. Trade represents 31.23% of investments, 14% of GDP, and 53% of turnover, reflecting a strong consumer market but creating a dangerous dependence on consumer demand. Construction accounts for 17.13% of investments but contributes only 8% to GDP due to its capital-intensive nature and delayed economic impact. This reliance on trade and construction makes the economy vulnerable to sectoral shocks and limits long-term diversification.

Meanwhile, the manufacturing sector, which represents 15.43% of investments, 13% of GDP, and 14% of turnover, is crucial for addressing Kosovo's structural dependency and imbalances. This can be achieved by increasing capacity utilization and directing the investment structure towards more effective elements such as machinery and equipment, research and development (R&D), and training. Focusing on these areas would help the manufacturing industry increase productivity and reduce Kosovo's high dependence on imports, contributing to a more sustainable and competitive economy.

Table 17. Sectoral participation in investments, GDP, and turnover

	Share in Investments	Share in GDP	Share in Turnover
Wholesale and Retail Trade; Repair of Motor Vehicles and Motorcycles	31.23	14	53
Construction	17.13	8	10
Manufacturing	15.43	13	14
Supply of Electricity, Gas, Steam, and Air Conditioning	8.23	4	8
Information and Communication	4.96	2	0
Accommodation and Food Service	4.89	2	2
Real Estate Activities	2.75	7	0
Professional, Scientific, and Technical Activities	2.28	1	2
Transport and Storage	1.88	4	3
Mining Industry	1.65	2	1
Agriculture; Forestry and Fishing	1.09	7	1
Financial and Insurance Activities	0.42	4	4
Human Health and Social Work Activities	0.24	2	1
Education	0.18	3	1

Source: Authors based on data from: Riinvest Institute Survey, 2024; TAK; KAS.

3.3 Investment environment

In the discussions regarding the volume, dynamics, structure, and efficiency of investment activity, special attention should be given to the impacts of the investment environment. This refers to the investment ecosystem. This environment is shaped by many economic and social actors, and here we highlight just a few of them, such as:

(1) The political-institutional level, including government economic policies, macroeconomic governance, and especially industrial policies.
(2) Access to finance and the financial sector.
(3) Information systems and technical assistance systems for investors

3.3.1 Institutional and Political Environment

In the case of Kosovo, as previously discussed, investment activity, with a higher depth of investments in gross domestic product, is higher than in regional countries. The support for investors through a favorable political environment, with expertise and other services, is of particular importance. The private sector generates more than two-thirds of the investments and is the main actor in generating investments, thus institutional collaboration should be fostered at the institutional level to facilitate and encourage investments.

Although the quality of legislation, the relatively low level of taxes, and the stability of the currency (Euro) are positive factors that should objectively encourage investment activity, the implementation of laws, the efficiency of commercial courts in protecting and enforcing contractual obligations, and the level of corruption create problematic barriers for investors. Furthermore, perceptions of political instability affect the reduction of business expectations and discourage both domestic and foreign investments.

Perceptions of private business leaders regarding the investment environment in Kosovo show neutrality, with a lack of well-formed opinions among the majority of respondents (43%) and an almost equal split between those who consider the environment very unfavorable or unfavorable and those with the opposite view (around 28.5%). Trust in institutions is more influential in shaping policies and the institutional environment, and it has a powerful impact on shaping business expectations. As such, it can either drive or inhibit investments.

In Riinvest's survey (September-October 2024), the reliability of several institutions with a direct impact on investment incentives was also assessed. The results show that trust in the central government and municipal governments is similar, with 44% and 46% respectively, out of a maximum score of 100. Customs (46%) are close to these figures, while courts perform better (49%). Over 50% trust the Tax Administration of Kosovo (ATK), suppliers, and staff they work with (76.6%).

Table 18. Overall Assessments of the Investment Environment

Assessment	%
Very Unfavorable	3.2
Unfavorable	25.3
Neutral	43.0
Favorable	22.7
Very Favorable	5.8
Total	100.0

Source: Riinvest Institute Survey, 2024.

The regulation of many areas by the relevant institutions (regulators) and economic policies, national development strategies, and sectoral strategies should serve as a starting point that, alongside market signals, can orient and stimulate investment activity. However, these important documents do not generate much interest either during the drafting process or regarding their implementation within the business community. Here, we primarily refer to industrial policies and the industrial development strategy. Kosovo has approved the Industrial Development Strategy and Business Support Policy 2023-2030, a document that, from a methodological perspective, follows the UNIDO model and marks an advancement in policies, favoring local suppliers and increasing domestic production. The document rightly includes horizontal support policies throughout the production structure and aims to create an environment where industrial sectors have non-discriminatory development conditions. However, the document highlights two sectors (stars), namely the wood industry and the plastics and rubber sector, which have shown good export results. While their importance is unquestionable, and supporting the orientation of promoting sectors that incorporate domestic inputs (raw materials and other components) is supported, we suggest that at least two additional sectors should be included – the food production and processing industry, including dairy, meat, fruit, and vegetable processing, and particularly the ICT sector.

It would be of interest to conduct a study on the performance of the production and services sectors with export performance, focusing on competitive capacity, value chains, and developmental potential, so that industrial policies in Kosovo can ensure a better cost-benefit ratio from government interventions.

It is crucial to strengthen and promote awareness of the necessity of enhancing research and innovation and creating better conditions for investment in research, development, and innovation by businesses. For this, MINT should encourage cooperation with business associations and businesses that have already reached a more advanced stage of development, to stimulate the development of research activities in the manufacturing sectors and their cooperation with academic and research institutions, both locally and internationally.

The primary goal of industrial policies is to diversify the economic structure. In the absence of this, we have seen a preservation of an inefficient economic structure for more than two decades (Table *4*). This requires a portfolio of instruments that create complementarity to achieve the desired effects. For Kosovo, projects that ensure export growth, import substitution, and simultaneously provide employment are essential. Experience shows that most of the achievements related to the diversification of production and services are the result of focused government efforts within a public-private partnership. The best interventions of these policies would be those that focus on activities, projects, not sectors, and those that have cross-sectoral effects on a broader scale. A flexible form of strategic cooperation between the private and public sectors should include dedicated political leadership. Ministers and top leaders in the government, including the Prime Minister, for example, should lead this process, having a coordinated leadership approach with the involvement of key ministers.

A public-private body (with representatives from businesses, associations) should ensure coordination of government agencies, advocate for changes, reduce transaction costs, and provide financial support, monitoring mechanisms, transparency, and accountability. Implementing agencies must have the authority to strictly monitor results and compare them with objectives. The effects of the subsidies implemented by the Kosovo government over the past few years speak volumes about this need. These now amount to hundreds of millions of euros, but there is no monitoring and auditing of performance, no accountability for the effects, and no evaluation of results achieved after project implementation. Public investments in public laboratories, research and development, physical infrastructure, sanitary infrastructure, phytopathology, vocational education, technical training, and a suitable business environment, including adequate fiscal and trade policies, would constitute a proper combination. In fact, these could be considered an integrated and complementary set of measures for portfolio diversification and, simultaneously, for increasing the competitiveness of Kosovo's products and services for export and the domestic market.

3.3.2 Access to finance

The investment environment in Kosovo is characterized by traditional financial products and low development of financial instruments to support investments in startups as well as to finance investment programs. This is clearly reflected in Table 19, which presents an overview of respondents' answers in a survey regarding the initial capital for starting a business. It shows that the dominant source of support comes from family resources (self-capital, financing from family members and friends in the country and diaspora) with 84%. The role of banks remains small, at around 14%, while the role of grants and partners in the diaspora is quite marginal, with 0.5% and 0.1%, respectively.

Table 19. Securing Initial Capital

Indicator	%
Self-capital	64.6
Debt/loans from banks	14.2
Financing from family or friends living in Kosovo	11.5
Financing from family or friends living in the diaspora	7.7
Grants from donor organizations	1.4
Participation from partners/investors from the diaspora	0.5
Other	0.1

Source: Riinvest Institute Survey, 2024.

Table 20. Sources of Investment Financing

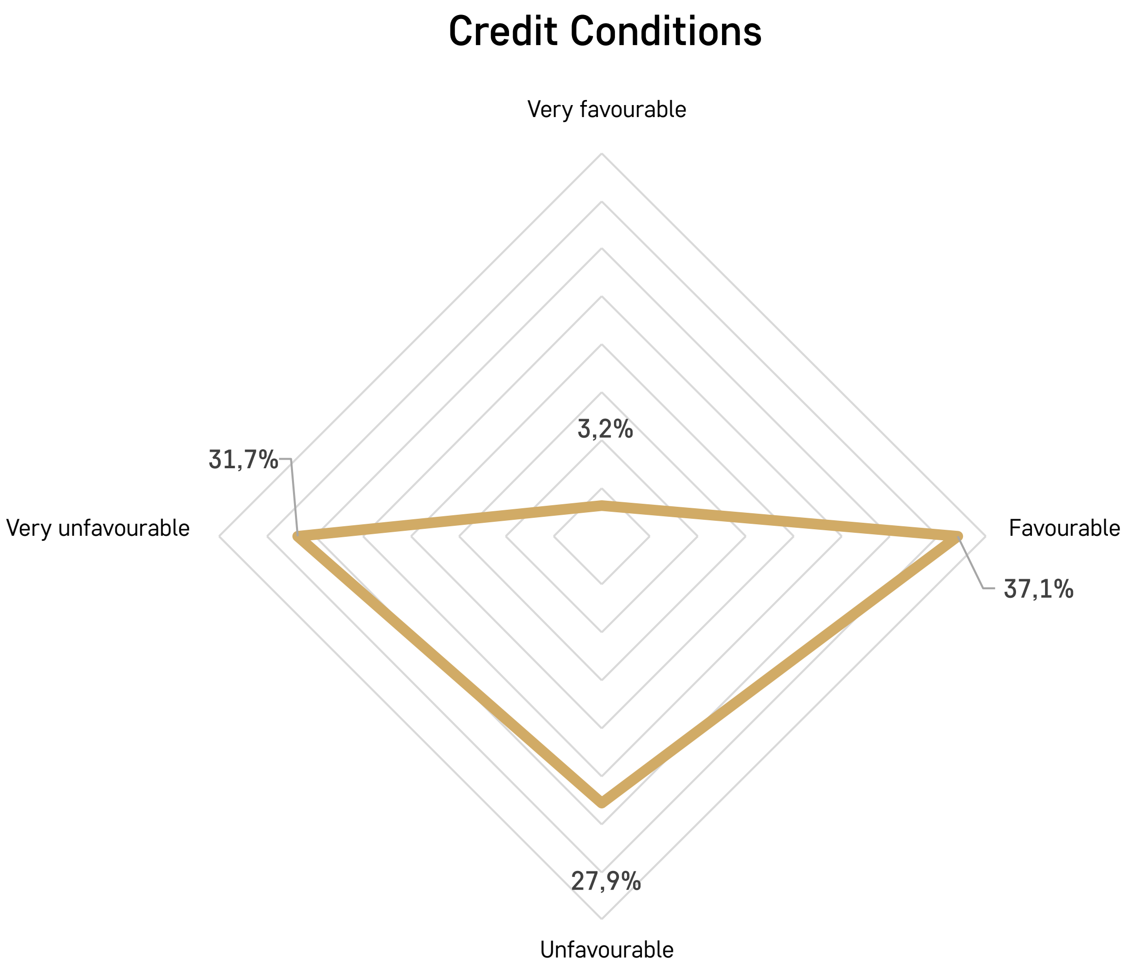
Indicator	%
Self-funds or reinvested profits for investments recorded in 2023	**72.0**
Loans from banks for investments recorded in 2023	**9.7**
Government grants for investments recorded in 2023	**1.2**
Financing from family or friends in Kosovo for investments recorded in 2023	**7.8**
Financing from family or friends from the diaspora for investments recorded in 2023	**5.4**
Financing from diaspora investments for investments recorded in 2023	**3.9**
Financing from any other option for investments recorded in 2023	**0.0**

Source: Riinvest Institute Survey, 2024.

This Riinvest Institute study shows that banks are still not a preferred option for financing investments. Only about 18% of businesses have taken loans in the years 2023-2024. As seen from the graph, nearly 60% of borrowers consider the financing conditions from banks for investments to be unfavorable, with the average interest rate reported by respondents being 7.9%, while the repayment term is 4.6 years—still unfavorable conditions for financing investments.

This indicates that investors from the private sector do not consider banks as the primary address for their investment activities. Therefore, the main option remains family and the family network in the country, and to a lesser extent, the diaspora. The Central Bank, the banking association, and the banks themselves need to review this situation and make it more favorable for investments, especially given that other financial market instruments are not well-developed. Additionally, the government should look at how to complete the legal framework to develop various elements of investment financing (factoring, leasing, investment funds). One of the possibilities that should be considered is also the cooperation between the government and international financial institutions to create special lines of investment loans for export sectors and high value-added products and services

Figure 11. Credit Conditions



Source: Riinvest Institute Survey, 2024.

3.3.3 Business Support Services and Technical Assistance

Business support services include a wide range of products that ease business operations and help them be effective and efficient in their operations, as well as achieve sustainable growth. These services typically include various aspects of business strategy planning and development, financial services and management, marketing, branding, digital marketing and web communication, product development on the web, legal and regulatory services, customer care, and more. They also offer training and educational programs for staff. These services are particularly important when it comes to investments, planning, evaluating effects, and their implementation.

Despite the gradual development of these services offered to meet the needs of businesses, it seems that when it comes to making decisions regarding investments, their use is not at the necessary level. Table 21 provides an overview of the expertise businesses use during the investment process. Based on the responses from the survey, most businesses rely on their own internal expertise (75%), while only around 16% of businesses engage consultancy services or research institutes for feasibility studies and business plans. Among the 463 businesses surveyed, only 18 (4%) received consulting and support services from donors or international organizations, and 25, or slightly more than 5%, have used expertise from business associations. Business associations need to further develop this function.

Considering the complexity of the investment process and the uncertainty that accompanies it, business associations and other actors should develop activities to raise awareness about the need to improve the quality of expertise in planning, evaluating, and implementing investment-related projects.

Table 21. Support Services and Technical Assistance for Investment Preparation and Evaluation

Indicator	%
Internal expertise (we analyzed the situation ourselves)	74.9
Engaged experts or consultancy organizations, or research institutes for feasibility studies and business plans	15.8
Expertise provided by donors, international organizations	3.9
Expertise provided by business associations	5.4
Total	100.0

Source: Riinvest Institute Survey, 2024.

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