

ECONOMY AND FINANCE

THE BIG PICTURE: A PROGRESSIVE ECONOMIC AGENDA FOR KOSOVO

**Edison Jakurti, Dita Dobranja, Dina Vllasaliu,
Lule Bahtiri, Mimozë Veliu**

December 2021



Incorporate measures to ensure a just society, with safety nets provided for vulnerable groups, as they attempt to escape the poverty trap and seize in opportunities.



Utilize a dynamic, mathematical formula for determining the minimum wage based on other wages in the economy, inflation, and economic growth rate.



Design a new industrial policy that takes into account factors such as the Revealed Comparative Advantage and productivity

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A PROGRESSIVE
ECONOMIC AGENDA
FOR KOSOVO

Publisher: Friedrich-Ebert-Stiftung Kosovo, Rr. Pashko Vasa 23, 10000 Prishtina, Republic of Kosovo

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Reviewer: Besnik Pula

Date: 2022

Design: Milky Way Creative

Printed by: Studio Forma

The authors of the individual sections take full responsibility for the contents of the publication. The opinions expressed are not necessarily those of the Friedrich Ebert Stiftung.

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FOREWORD

“The difficulty lies not so much in developing new ideas as in escaping from old ones”
– **John Maynard Keynes**

The Covid-19 pandemic exposed the fragility of the economy predominantly dependent on consumption, export of services and diaspora remittances. Kosovo, like many other developing countries, had to rely on foreign assistance and debt (fiscal policy interventions) as a way of financing the pressing requirements.

Although some of the economic fallout has been remedied in 2021 – again highlighting the influence of external factors – the need for structural reforms and innovative policies should remain a focal point in Kosovo’s development agenda. The question is “What needs to be done?”.

To this end, Friedrich-Ebert Stiftung’s Office in Kosovo has asked a panel of experts to draw “The Big Picture” for a progressive economic agenda that will offer a social-democratic perspective for the future economic development of Kosovo. As such, the proposals of our experts are clear both in their scientific merit, and their normative compass: Leading to a more just society by advancing policies that benefit many Kosovar citizens, not the few.

How to narrow the labor market-education gap? How to generate sustainable revenue for a social welfare state? Which are the industries with the largest export potential? How to transition from carbon-dependent to clean energy production?

The Big Picture Study provides answers to the principal questions and provides significant expert proposals regarding minimum wage, transition in social policy schemes, and index of comparative advantage. The study focuses on providing specific recommendations for vital areas of Kosovo’s economy such as labor market policies, social protection and fiscal policies, international trade, and industrial policies including energy security and green economy.

The results and policy proposals in this Study are interesting, stimulating, at the same time challenging for policymakers, as they contribute to the widening of the debate on effective socio-economic policies.

Kosovo’s small open economy is greatly affected by conditions and volatility in major and international

markets. The spillover effects of various crises make it difficult for small economies to find a maneuvering space to reduce the consequences of economic disruption. Nonetheless, a country should engage in a combination of macro and structural reform policies which enable economic transformation in the long run. Corresponding policies are especially important in the energy sector, as Kosovo’s current dependency on coal makes it complex to substitute for renewables in the short run. Decarbonization and clean energy are not merely obligations arising from the European integration process but of the weight our generations hold in environmental protection and reversing the trends of air pollution. It must be emphasized that a crucial factor in implementing progressive economic policies is a stable and willing political environment.

The goal of “The Big Picture” is to produce specific sector-oriented policy recommendations to facilitate public debate and democratic policymaking over the right orientation on how to build back better from the pandemic. Enjoy the read!

Rudina Nallbani Hoxha
Friedrich Ebert Stiftung

EXECUTIVE SUMMARY

The economy of Kosovo faces many challenges but, with the new Government, there are many opportunities ahead. The unprecedented victory derived by an overwhelming support by over 50% enables the current government to embark on daring projects that not only seek to reform but rather transform the economy. Its proclaimed social-democratic orientation paves the way for progressive policies to thrive. With that in mind, we have aimed to provide a big picture of Kosovo's economy by tackling some of its major issues and trying to provide progressive policies derived from rigorous economic analysis.

We first analyze some big issues in the labor market, including high unemployment rates, low labor force participation rates, inactive youth, and discriminated women. Next, we recognize that not only are there issues with the unemployed, but there are many for the employed workers. Hence, we make three policy proposals. To reduce the skill gap, as an identified cause for high unemployment especially among the youth, we propose specific steps for creating a Dual VET system which is characterized by 60-70% education and 30-40% on-the-job training for its students. To improve the workers' conditions, we strongly suggest the active support and facilitation of new trade unions, especially in the private sector. A way to achieve this is by making government's benefits towards the private sector contingent on the working conditions and workers' level of organization. Finally, after we show that raising the minimum wage in Kosovo is unlikely to have negative effects in unemployment, we provide a dynamic, mathematical formula for determining the minimum wage in Kosovo. Our formula accounts for other wages in the economy, inflation and the annual growth rate.

A chain is only as strong as its weakest link. Hence, we focus on social protection with the aim of reducing poverty and inequality. We analyze the current social assistance scheme in Kosovo, we point out its weakest spots, and propose ways to improve it, including a change in the amount allocated, an increase in the coverage rate, and a transfer in the "ownership" of the assistance from men to women. Instead of being a permanent shelter, we try to make it a temporary station that could be bridged with more prosperous sides of the economy. And, to avoid from falling in the poverty trap, we propose the establishment of a solidarity fund and the introduction of unemployment benefits to help workers in their worst days.

Next, we provide the first ever analysis of labor income inequality and distribution in Kosovo. Simultaneously we assess the current personal income tax, its progressivity degree, and its redistributive power. Because its degree of progressivity and the power of redistribution are low, we propose a new personal income tax, which is around three times more progressive, redistributive, and effective in reducing inequality. We do so by completely removing the tax burden from the "poorest" 50% and increasing the burden on the "richest" 8%. Our system has a top marginal rate of 38%, and yet it enables 92% of wage earners to receive a higher net wage than they currently do – and the Government to generate more revenues than it currently does. Along with this tax, we propose a 100% increase in the corporate income tax – from 10% to 20%; and, the introduction of a 30% dividend tax – which is currently absent in Kosovo but present in almost all countries in Europe.

We then turn to the macroeconomic aspects of Kosovo's economy by decomposing its Gross Domestic Product. We analyze factors that help the economy grow and stagnate and identify trade deficit to be a major issue. To address that, we propose the beginnings of a new industrial policy that is based on economic analysis rather than some ad hoc measures that are unfocused and ineffective. Hence, for the first time, we estimate the revealed comparative advantage for Kosovo's exports. Next, we analyze the productivity of different sectors to determine industries that can thrive and patterns that can inform further policy regarding industrial potentials of the country.

Last but not least, we recognize that while, the COVID-19 pandemic has cost many lives and caused numerous disruptions, the humanity faces an even more existential crisis – the climate crisis. For that, every country must do its part and Kosovo should take its share of responsibility. Hence, we analyze the energy transition with the aim of evaluating the current conditions, learning from best practices, and proposing big steps for decarbonization done in a just way for the workers, in particular, and the society, in general.

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SECTION I. LABOR MARKET ANALYSIS AND POLICY

CHAPTER 1. LABOR MARKET ANALYSIS

Dita Dobranja

1. INTRODUCTION

This chapter provides a general analysis of Kosovo's labour market, with specific focus on youth and women, as groups that face the most difficult labour market conditions. The first section aims to provide a broad overview of the main labour market trends through the lens of the most problematic indicators – unemployment and labour market participation rates. Focusing on youth, especially youth who are currently not in education, employment, or training, these sections show the need for interventions to address a growing challenge in activating youth in the labour market. On the other hand, women's low labour force participation, stemming from numerous socio-economic, cultural, and legislative constraints are also elaborated in the need for a multi-faceted approach to solving labour market problems in Kosovo.

The following sections focus on sectoral analysis of the labour force, showing the concentration of labour force in less productive sectors while more productive sectors claim to face shortage of qualified workforce. Additionally, a skills gap analysis is provided, as one of the main causes of the current stagnation in employment and labour market development.

Finally, the last two sections of the chapter offer policy solutions to vocational education development and to trade union empowerment. Establishment of a dual VET system and the creation of sector skill councils can improve the current mismatches in the labour market and lack of cooperation between the private and public sector in addressing these shortcomings.

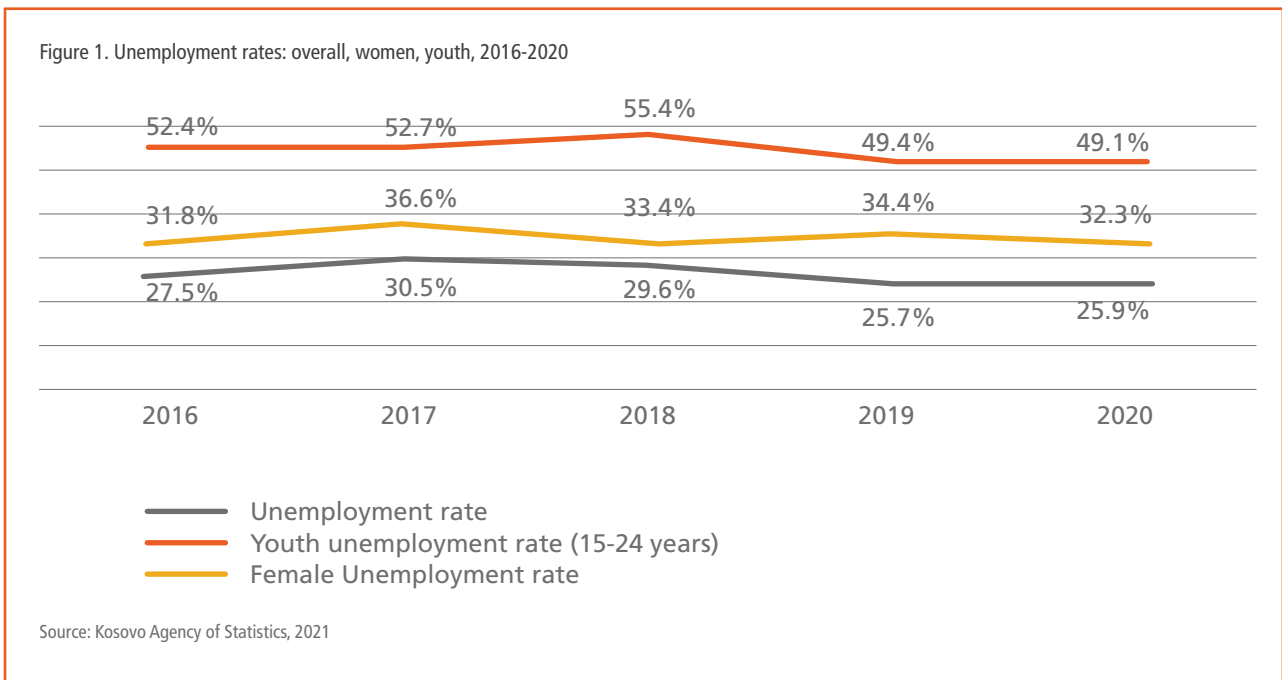
Improving the conditions for unionization of the labour force, especially at the sectoral level, through conditional and direct engagement of trade unions in different modalities, such as inclusion of worker's organizations as provisions for investments and as eligibility criteria for government incentive programmes.

2. UNEMPLOYMENT TRENDS

Kosovo’s most concerning labour market indicator is the unemployment rate which has not shown significant improvements, especially not corresponding to levels of economic growth registered throughout the years. The rapid economic growth that Kosovo has recorded in early 2000s has been fuelled by a considerable level of international aid (including spending and incomes of the international presence in Kosovo) as well as steady remittance inflows, which accounted for more than 10% of GDP continuously since

early 2000s.¹ The latter is considered to have the highest impact on labour market outcomes in Kosovo.

The overall levels of unemployment have continuously stayed above 25%, even in periods of economic growth. The unemployment levels are significantly higher for youth (continuously around 50%) and for women (continuously above 32%).² The trends of unemployment for the past five years for youth and women are shown in Figure.



Studies in developing countries show that high and especially steady inflows of remittances impact labour force participation negatively, especially for women.³ Considering remittances as direct and simple transfers of income, households that receive remittances (and expect to continue receiving remittances) are more likely to substitute income from remittances for unearned labour market income, thus increasing leisure and reducing active participation in the labour market.

Moreover, empirical analysis from Kosovo, show that higher levels of income from remittances, as expected, increase the reservation wage of household members, thus negatively impacting likelihood of employment.⁴

However, higher levels of remittances are also linked to increased investment in human capital, especially in health and education.⁵ Theoretically, investment in human capital is expected to increase labour force participation. However, Azizi, studying the impact of remittances in developing countries, including Kosovo, finds that despite the positive impact remittances have on investment in human capital, it is offset by the increase in reservation wage, and thus willingness to participate in the labour force, especially for women.⁶ This finding is significant especially in economies such as Kosovo’s, given the low base of women’s labour force participation.

¹ Central Bank of Kosovo, Remittances by Channel, 2021.

² Kosovo Agency of Statistics, Labour Force Survey, 2016-2021

³ Valerie Kozel and Harold Alderman, Factors Determining Work Participation and Labour Supply Decisions in Pakistan’s Urban Areas, The Pakistan Development Review, 1990, vol. 29, issue 1, 1-18

⁴ Jeta Rudi, Remittances and Labour Supply: The Case of Kosovo, 2014, Working Paper

⁵ Seyed Soroosh Azizi, The impacts of workers’ remittances on human capital and labour supply in developing countries, 2018, Economic Modelling, 75 (2018) 377-396

⁶ SeyedSoroosh Azizi, The impacts of workers’ remittances on human capital and labour supply in developing countries, 2018, Eco-

2.1. YOUTH UNEMPLOYMENT AND NEET

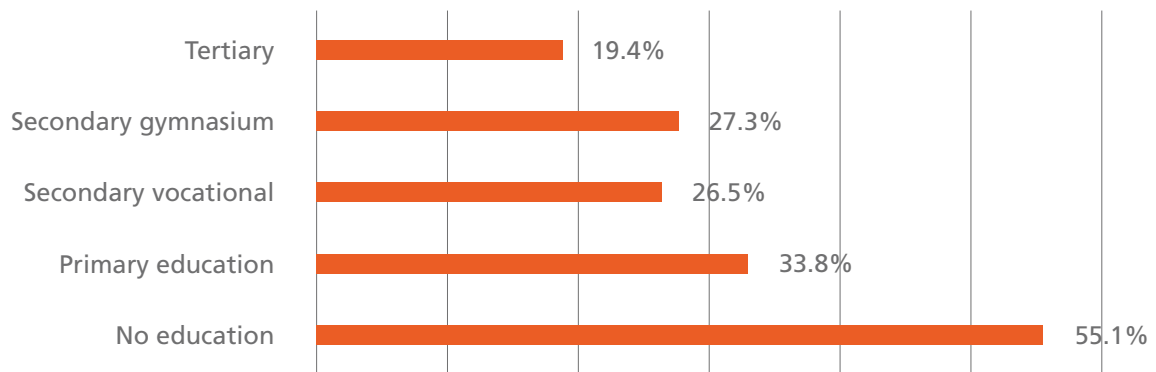
Although youth in Kosovo make up the largest share of the population, they make up the lowest share of those employed. Lack of vacancies along with the skills mismatch between education and the needs of labour market leave Kosovo youth at crossroads in terms of their labour market activities. For youth 15-24, only around a quarter are active in the labour market (22.5%, and only 15.3% for women) and around 50% are unemployed (65.4% for women).

An even more worrying problem is the large share of youth who are currently not in education, employment, or training (NEET), at around 35% of all youth 15-24.⁷ One third of youth not active in the labour-market of any sort of skills building activities implicat-

ions span beyond the current labour market outcomes. Based on the high level of skills mismatch observed in Kosovo's labour market, lack of involvement in any skills building programmes will cause an even bigger gap to be bridged in the future.

Data from the Labour Force Survey show that unemployment rates are highest for those with no education completed, followed by those who have completed only primary education, as Figure shows. However, for those with vocational education, the unemployment level stands at similar levels to Kosovo wide unemployment at 26.5%. The lowest unemployment levels are recorded for people who have completed tertiary education.

Figure 2. Unemployment levels by levels of education



Source: Kosovo Agency of Statistics, 2021

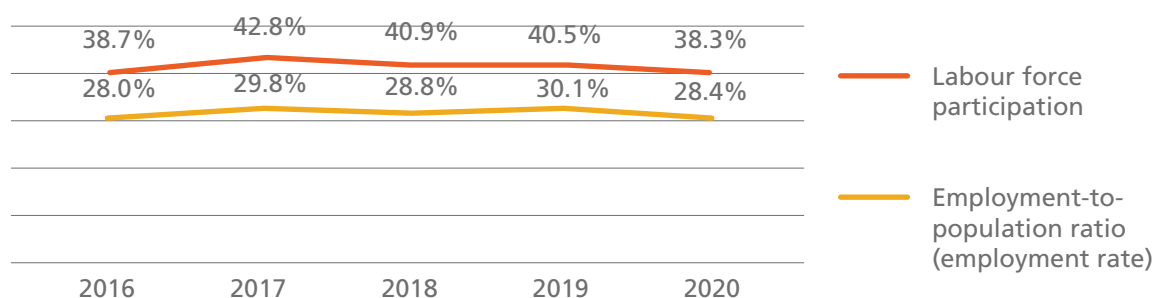
⁷ Kosovo Agency of Statistics, Labour Force Survey, 2016-2021

3. EMPLOYMENT AND LABOR FORCE PARTICIPATION RATES

Kosovo's economic growth in the past two decades, starting from rebuilding in the early 2000s to a more nuanced approach to economic development through international cooperation and adhering to EU standards in the 2010s, has not translated into equal improvement in labour market conditions. Despite growth across sectors in Kosovo, the rate of employment has remained low, with less than 1/3 of the working age population employed during the past 5 years.

Low employment rates combined with a high level of inactivity amongst working age population, show a clear need for a transformation in Kosovo's labour market. Currently, only 38.3% of working age population are active in the labour force, this figure staggeringly lower for women, at only 20.8%.⁸ The gender differences in the labour market have considerable consequences in the overall orientation of Kosovo's economy and especially in tapping into the potential for inclusive growth.

Figure 3. Labour force participation and employment rate trends in Kosovo



Source: Kosovo Agency of Statistics, 2020

The COVID-19 pandemic found Kosovo in an improving economic trend, however, the unemployment levels continued to be high, especially among youth and women. A steady decline in the unemployment rate, although not a highly significant one, was reversed by the pandemic. The overall unemployment rate in 2019 was 25.7%, increasing to around 27% in the second quarter of 2020, however declining back to 25.9% by the end of 2020.

Specific sectors suffered higher losses, given the different impact the pandemic as well as restrictive measures had on these sectors. However, in the second half of 2020 and beginning of 2021, labour market indicators for women and youth have shown significant improvements, both in terms of activity rates and in terms of employment.

Table 1. Main Labour Market Indicators

	2016	2017	2018	2019	2020
Labour force participation rate	38.7%	42.8%	40.9%	40.5%	38.3%
Employment-to-population ratio (employment rate)	28.0%	29.8%	28.8%	30.1%	28.4%
Unemployment rate	27.5%	30.5%	29.6%	25.7%	25.9%
Youth unemployment rate (15-24 years)	52.4%	52.7%	55.4%	49.4%	49.1%
NEET share of youth population (15-24 years)	30.1%	27.4%	30.1%	32.7%	33.6%
Share of vulnerable in total employment	22.9%	23.1%	19.6%	18.8%	17.0%

Source: Kosovo Agency of Statistics, 2021

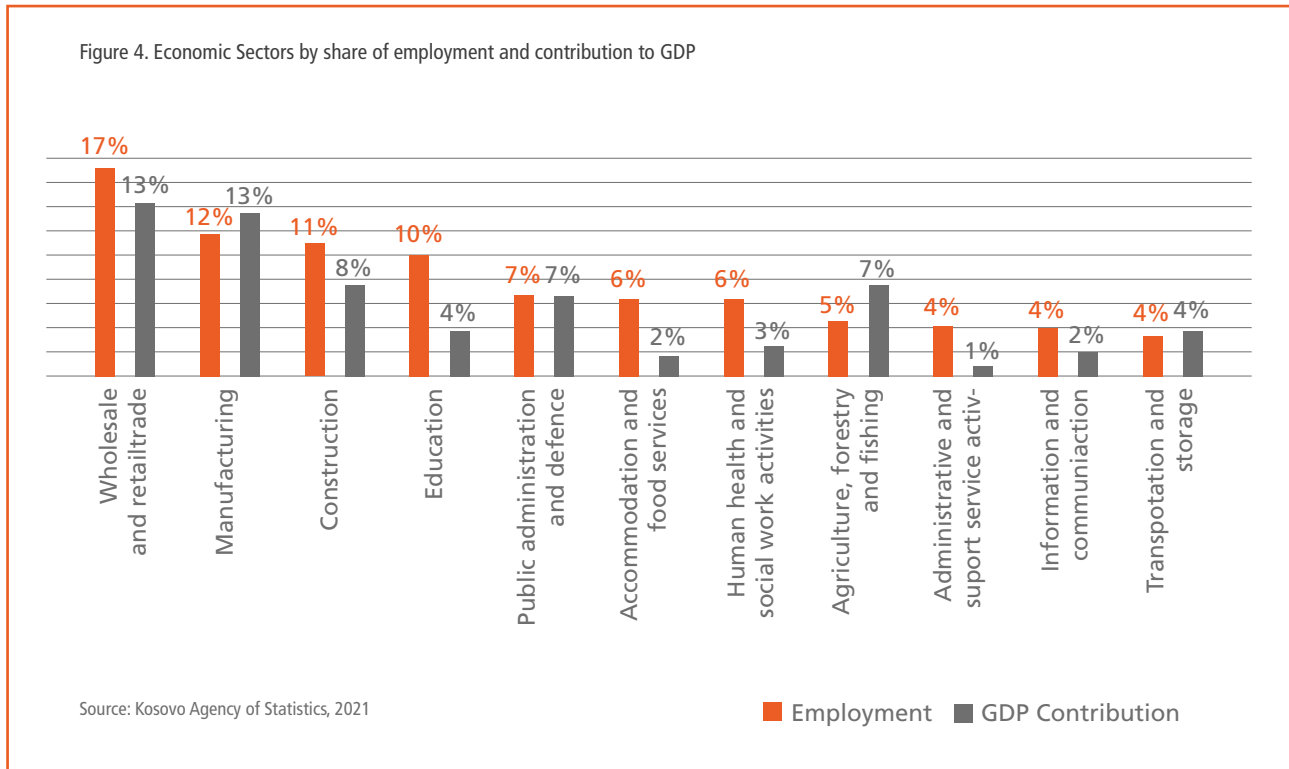
⁸ Kosovo Agency of Statistics, Labour Force Survey, 2016-2020

3.1. SECTORAL ANALYSIS OF EMPLOYMENT

Economic sectors in which employment is concentrated show another important facet of the labour market in Kosovo. Wholesale and retail trade have continuously been the biggest employer as a sector, currently employing around 17% of all employed. In 2020, for the first time since 2017, manufacturing has surpassed construction as the second largest employer, employing 12% of those currently employed. Construction employs 11%, followed by education at 10% and public administration at 7%. In terms of GDP contribution, however, there is discrepancy between the share of employment and share of GDP contribution for most of these sectors.

As shown in Figure 4, manufacturing and agriculture have a significantly higher contribution to Kosovo’s annual GDP compared to their share of employment. The contribution of the education to the society’s wellbeing is larger than its contribution to GDP, therefore the discrepancy between share of employment and traditional measures of contribution to economy are not surprising.

However, the accommodation and food services industry, as one of the sectors with the highest workforce turnover and a difference between employment (6%) and GDP contribution (2%) is an important sector to look at in terms of likelihood of informality.



Keeping the COVID-19 pandemic impact in mind, data from the Kosovo Tax Administration (KTA) show that, while there have been cuts in employment in general, in the sectors that employ the largest number of people this has been more evident. The three sectors that employ the largest number of employees, wholesale and retail trade, manufacturing, and construction have experienced the most significant decrease in employees between March 2019 and March

2020, with the level of employed in the wholesale and retail trade dropping by 45%, in manufacturing by 36% and construction by 50%.⁹ These numbers have recovered in the following quarters, however, the lockdown measures have shown a high level of volatility in employment in these sectors, a concerning observation that has implications for policy development and sector prioritization.

⁹ Kosovo Tax Administration, Employment Data, April 2020

3.2. SKILLS GAP

One of the main findings of continuous labour market analysis for Kosovo remains the skills mismatch. According to the 2019 World Bank STEP survey, skills mismatch is prevalent in Kosovo, especially for firms who implemented innovative and improved approaches to services, manufacturing, or any form of offering activities.¹⁰ Even though manufacturing and construction are two of the three largest employing sectors, these sectors also claim to face the most difficulties in finding workers who were adequately skilled for their needs.¹¹ According to this UNDP study, the majority of firms (65%) end up hiring less qualified staff, whereas others (19%) assign duties to existing staff.

Furthermore, based on data from the Employment Agency of Kosovo, the vacancies filled through the unemployment program run by the Agency has averaged 30% in the past five years, with the highest level of vacancies filled reached in 2019, at 44%.¹² A high level of vacancies remaining unfilled is an important indicator to a mismatch in the labour market.

The mismatch in skills stems from lack of a substantial analysis of Kosovo's labour market needs and lack of clear strategies and action plans to path the way for Kosovo's labour market outcomes in the future. Continuous neglect in skills and job forecasting, combined with lack of reforms in the education sector, have severely impaired Kosovo's labour market. Without a clear vision of future needs of the labour market, Kosovo's education institutions offer concentrations and specializations in areas which are decreasingly needed by employers, not only in Kosovo, but globally.

One attempt at bridging the skills gap has come in the form of vocational education and training. However, introducing a different level of education had not addressed the needs of the labour market. Based on data from students with a vocational education degree, one third (33%) have specialized in economics, around 17% in medicine, and less than 10% have completed their vocational education in technical schools.¹³ The overcrowding effect in social sciences which is prevalent in tertiary education is also common in professional education.

Apart from an overall tendency to have social sciences dominate the education system, the fact that vocational schools and centres of competence have undergone little to no reform since their establishment has impacted career choices of youth.

Currently there are 60 vocational schools and 4 centres of competence operating in Kosovo, which offer 33 occupational standards, 140 profiles, and 60 modular qualifications.¹⁴ Private sector companies, especially those operating in the manufacturing industry place an importance on vocational education.

3.3. WOMEN'S POSITION IN THE LABOUR MARKET

Reducing economic inequalities spans beyond bridging the gap between the rural-urban income divide, overcoming the differences in economic outcomes depending on education levels. In Kosovo's labour market, one of the biggest gaps is the gender gap. Women's labour force participation is the lowest in the Western Balkans region, at only 20.8%, compared to 56% for men.

According to a 2018 study by Riinvest Institute, more than half of women consider inability to find a suitable job, lack of suitable jobs altogether and their own inadequate qualifications, as one of the main reasons for being unemployed/inactive.¹⁵ However, 1 in 4 women state that care obligations, such as childcare, elderly care, as well as household work, as the main reasons for not working.¹⁶

Similarly, inability to find suitable (full-time) jobs and personal and family reasons are also the main reasons stated by women who are currently working part time. It is notable that although remittances impact the general decisions of joining the labour market, empirical studies show no impact of remittances in terms of hours worked. This can be a result of the lack of part time employment in Kosovo, where only 7% of those employed work less than 40 hours a week.

The stark differences in labour force participation, which are graphically displayed in FIGURE 6 combined with the societal expectations for women to carry out the lion's share of care obligations impact the decisions women face in terms of their activity in the labour market! Reference source not found., combined with the societal expectations for women to carry out the lion's share of care obligations impact the decisions women face in terms of their activity in the labour market. These figures show a need for institutional support in childcare alternatives for women, as well as for interventions to support skills-building schemes targeting marginalized groups, and especially women.

¹⁰ World Bank, Kosovo country report: Findings from the Skills towards Employment and Productivity Survey, World Bank, Washington, DC, 2019.

¹¹ UNDP Kosovo, Public pulse analysis: Correlation between labour market of Kosovo and outmigration, 2020

¹² Employment Agency of the Republic of Kosovo: Work and labour, 2019

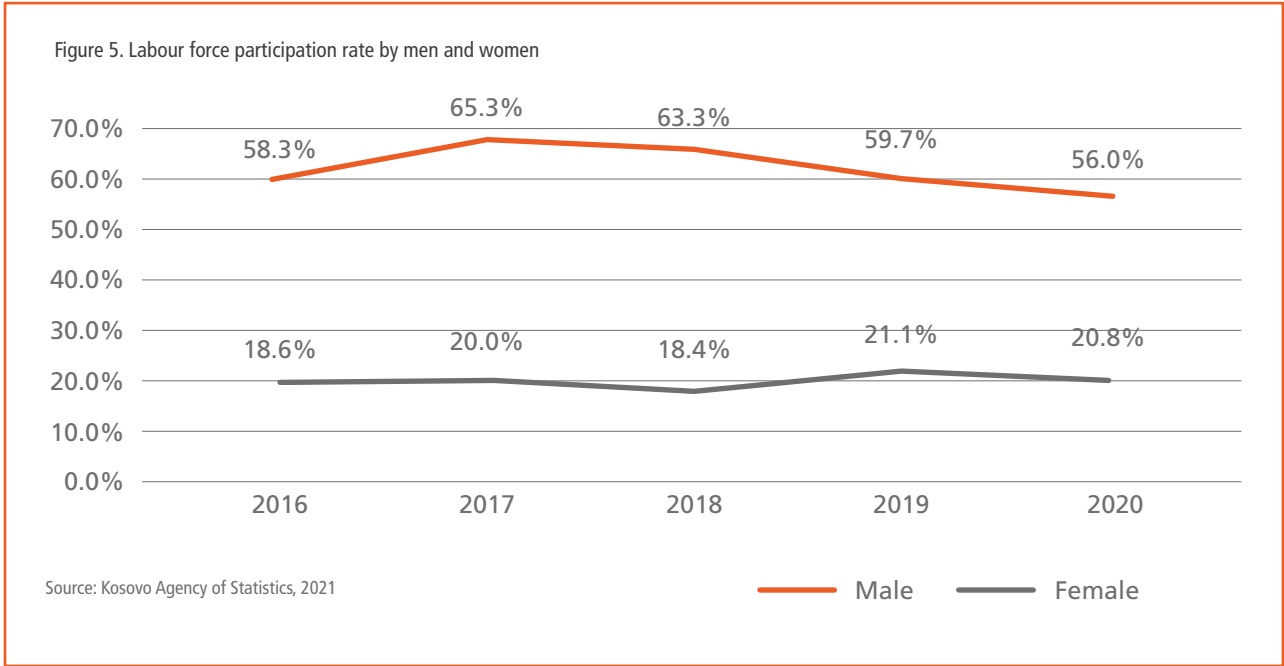
¹³ LMIS data on supply and demand in the labour market: <http://sitp.rks-gov.net>

¹⁴ Kosovo National Qualifications Authority, Accessed October 2020,

¹⁵ <https://akkks.rks-gov.net/en/nqa/about-us>
Riinvest Institute, Facilitating Empowerment: Factors Influencing Women's Economic Decisions in Kosovo, 2018

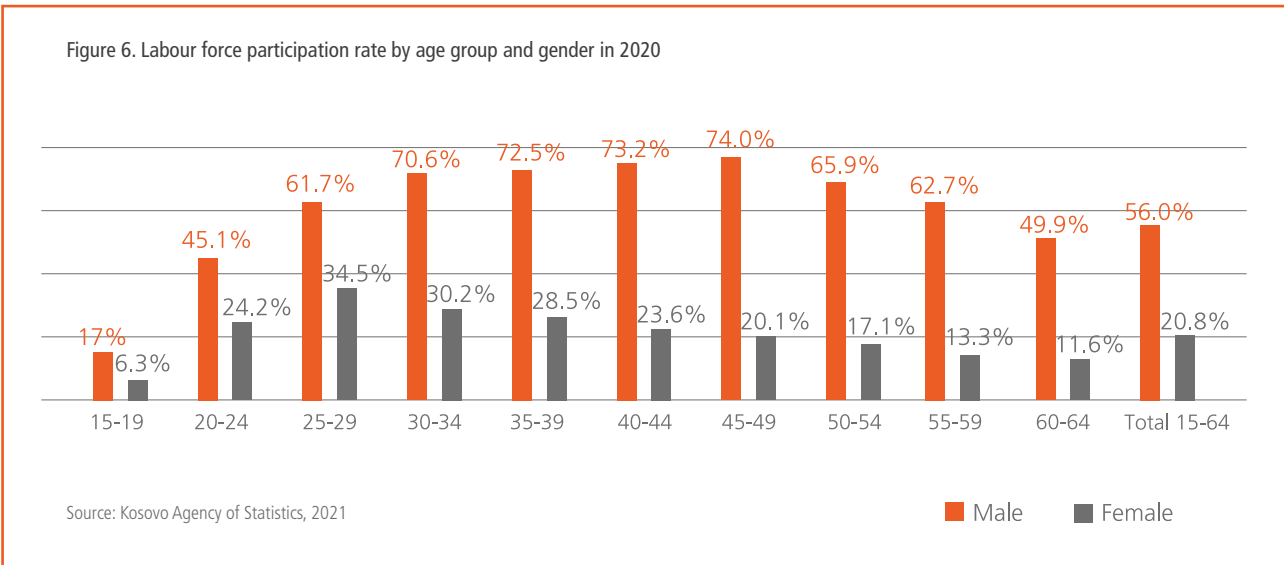
¹⁶ Ibid.

¹⁷ Kosovo Agency of Statistics, Labour Force Survey, 2016-2021



Labour force participation peaks for women in the 25-29 age group, declining steadily as women age, as shown in Figure 6. For men, labour force participation increases steadily until the 45-49 age group, where it peaks, at more than double the level of the peak for women.

This further highlights the problems in women’s role in the labour market, considering that their labour force participation reaches its peak only in the first couple of years following university graduations and only ten years following their eligibility to join the labour market.



One of the main barriers women face in employment is also linked to the maternity and paternity leave provisions of the labour law, which only provide women with substantial leave. This, in turn, impacts hiring decisions of employers, creating the potential for a taste for discrimination. The legal framework should ensure a model of balanced family leave, in

line with the EU Directive 2010/18/EU where mothers are guaranteed 8 months of paid leave and fathers are guaranteed 5 months of paid leave. Compensation provisions need to be developed in stages, transitory in cooperation with employers, and gradually transfer to completely be covered through an ear-market tax or social protection fund.

Inactivity rates are also impacted by a high level of discouraged workers, who remain unemployed for periods usually longer than one year. In Kosovo, the share of those who are unemployed for longer than a year, within those unemployed has increased from around 64% in 2019, to around 72% in 2020¹⁸. However, the increase is more significant among men than among women, and for women aged 40 to 44, the share of those unemployed for longer than one year has decreased.

However, due to the COVID-19 pandemic, the differences in duration of unemployment remain impacted by the lockdown and other restrictive measures, thus can be clearly analysed with data from 2021 and onwards.

3.4. A PROPOSAL FOR KOSOVO'S APPROACH TO VOCATIONAL EDUCATION AND TRAINING

Vocational Education and Training (VET) programs are often considered as systems that play the role of developing skills needed in the labour market. However, the way VET programs are organized differs from country to country and these differences determine the strongest programs. The main differentiation has been found to be the "level of linkage between actors from the education and employment systems."¹⁹

Labour market characteristics are the main determinants of the VET systems therefore specific models or curricula that have been successful in certain countries are not necessarily models for success in others. Moreover, considering the most important aspect of VET programs is linking workers to the labour market, work experience and practical experience offered through VET programs is crucial for the success.

Renold et. al. in the analysis conducted to compare VET programs find that the most successful VET programs are ones that include both classical education and on-the-job trainings.²⁰ In cases when the education-system actors are dominant, such as the current case in Kosovo, the VET program is a school-based skills and career education. In the other extreme, when actors in employment systems dominate the program, the VET program is on-the-job training programs offered by employers. A combination of the two has been the most successful model, however, the balance is not easy to find.

The KOF Education-Employment Linkage Index measures the link between the education-system and the employment-system, throughout three phases of the Curriculum Value Chain – design, application, and updating.²¹ The analysis has yielded results showing that the Dual VET systems score best in all the aspects of the analysis.

Review of concentrations and specializations offered by Kosovo's education system, both at vocational education level and at tertiary level is crucial to ensure improved skills attainment to match the needs of the labour market. Moreover, close cooperation of Kosovo institutions with employers to determine the needs of the labour market, not only in the present, but even more so in the future, is inevitable to avoid a continuous skills mismatch, which in turns impacts high levels of unemployment and inactivity.

Kosovo's current VET system has not successfully bridged the skills gap in the labour market, particularly due to a weak link between employers and the education system. Re-designing the VET programs to better fit both education and apprenticeship/on-the-job trainings as equally important aspects of VET education.

While a Dual VET system takes time to be developed and implemented, making this model the one to follow is crucial. Using existing models as frameworks for developing Kosovo's own system, that best fits our labour market characteristics, results in a Dual VET system which is characterized by 60-70% education and 30-40% on-the-job training for its students. The system, however, needs to plan for a gradual movement towards higher share of on-the-job trainings and lower share of classical education.

The first step in achieving this is to identify priority sectors for employment growth. Kosovo institutions need to identify the main sectors of interest in which they want to channel resources, especially channel employment efforts. Through analysis of revealed comparative advantage or by targeting sectors with the highest export productivity, or by selecting sectors based on a specific political and economic vision of the government, the Kosovo government needs to identify 3-5 priority sectors, both for growth and employment. These sectors can be ones that show most promise in exporting, sectors that link to international markets, or sectors with the lowest cost of training and upskilling of the labour force.

¹⁸ Data for 2020 are only available until Q3.

¹⁹ Ursula Renold, Thomas Bolli, Katherine Caves, Jutta Bürgi, Maria Esther Egg, Johanna Kemper and Ladina Raeth, "Comparing International Vocational Education and Training Programs: The KOF Education-Employment Linkage Index" (Washington, DC: National Center on Education and the Economy, 2018).

²⁰ Ibid.

²¹ In the first phase, the standards of qualification and evaluation are developed, along with the identification of the main areas of necessary focus. In the second phase, practical and application-level issues are addressed, including examinations. In the third phase, employers provide feedback on graduates but also on the current demand, to be used as information for potential curriculum changes.

Following the identification of these sectors, the ministry responsible for industry and private sector development would, through engagement of private sector representatives identify private sector enterprises within those sectors that are willing to participate in VET programs. This is the most difficult step, considering both the overall reluctance of the private sector to engage with public vocational education system but also given that most enterprises in Kosovo are small and medium enterprises, for which it is difficult to engage in long term staffing planning. However, depending on the level of willingness to engage, incentives from the Kosovo institutions can be developed, to start engaging enterprises in the program.²²

The third step is to develop councils on skills for each sector that serve as the mechanism for the public (especially education) sector and the private sector to collaborate. Sector skill councils would serve not only in identifying the skills needed in the market, but also to contribute to curriculum development, training module selection, and most importantly to provide opportunities for on-the-job training and apprenticeships.

Sector skills councils would serve as advisory bodies and would have representative members from (1) main employers in the sector (private sector firms with highest employment capacities), (2) relevant government institutions (ministry responsible for labour, ministry responsible for education, ministry responsible for industry development, employment agency), and (3) unions or professional organizations of the employees in the sector.

As a tripartite body, sector skills councils will enable employers from the sector to play a key role in providing specific recommendations on skills requirements for their sector, will offer government institutions direct insights into the needs of the labour market, and will empower employee organizations to represent the needs and expectations of the labour force in the sector.

Finally, develop a strict monitoring system, which enables revision of the curricula and career orientation opportunities in three-year cycles. The monitoring system needs to have data collection instruments for the performance in the vocational education system, data collection instruments for tracking of graduates and assessing their performance in the workplace and match the scores to identify gaps and successes in the system. New data collection instruments should be integrated into the statistical system of the education sector in Kosovo and be published on an annual basis. However, tracing surveys and workplace performance data need to be ensured by the sector skills councils.

The data analysis will allow the institutions to track progress, identify shortcomings and gaps to address, and identify strong aspects of the system.

²² Incentives can range from offering government/donor paid apprenticeships, to limited time tax breaks for engaging in VET programs and hiring from these programs.

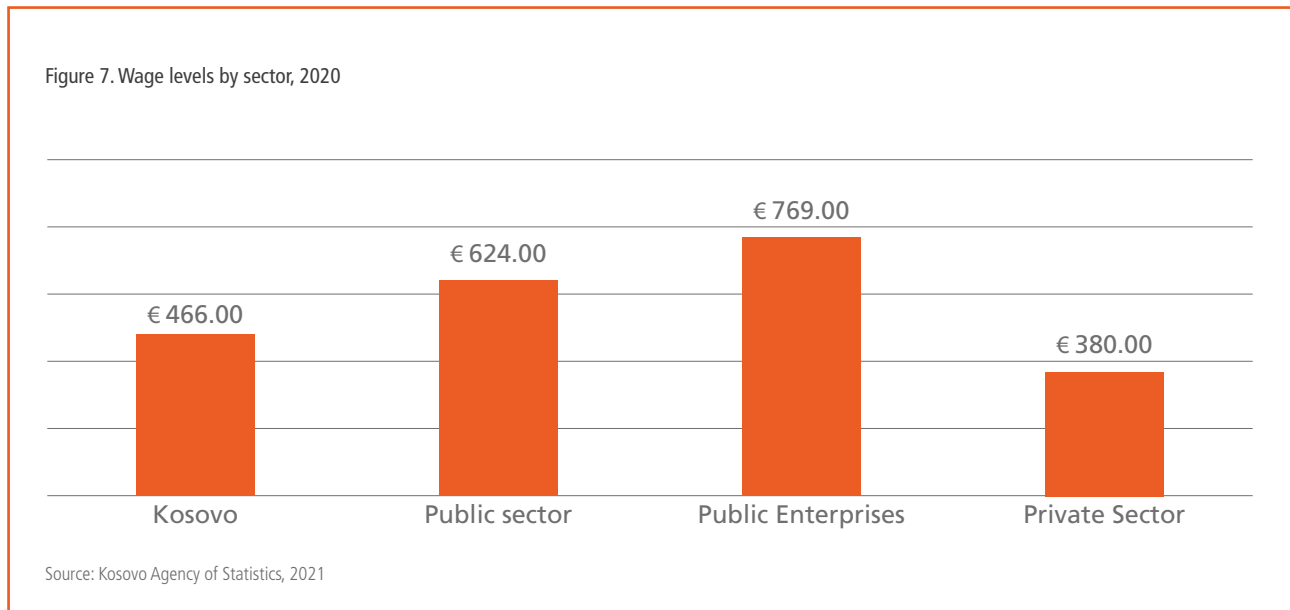
3.5. A PROPOSAL FOR THE TRADE UNIONS

Kosovo's collective bargaining system remains fragile, especially for workers in the private sector. There are a dozen of trade unions operating in Kosovo, representing workers in the public sector or public enterprises. Workers in the public sector are represented through the Union of Independent Trade Unions, the umbrella organization, affiliated to the International Trade Union Confederation (ITUC).

Trade Unions representing employees of privatized SOEs have undergone crisis due to the change in

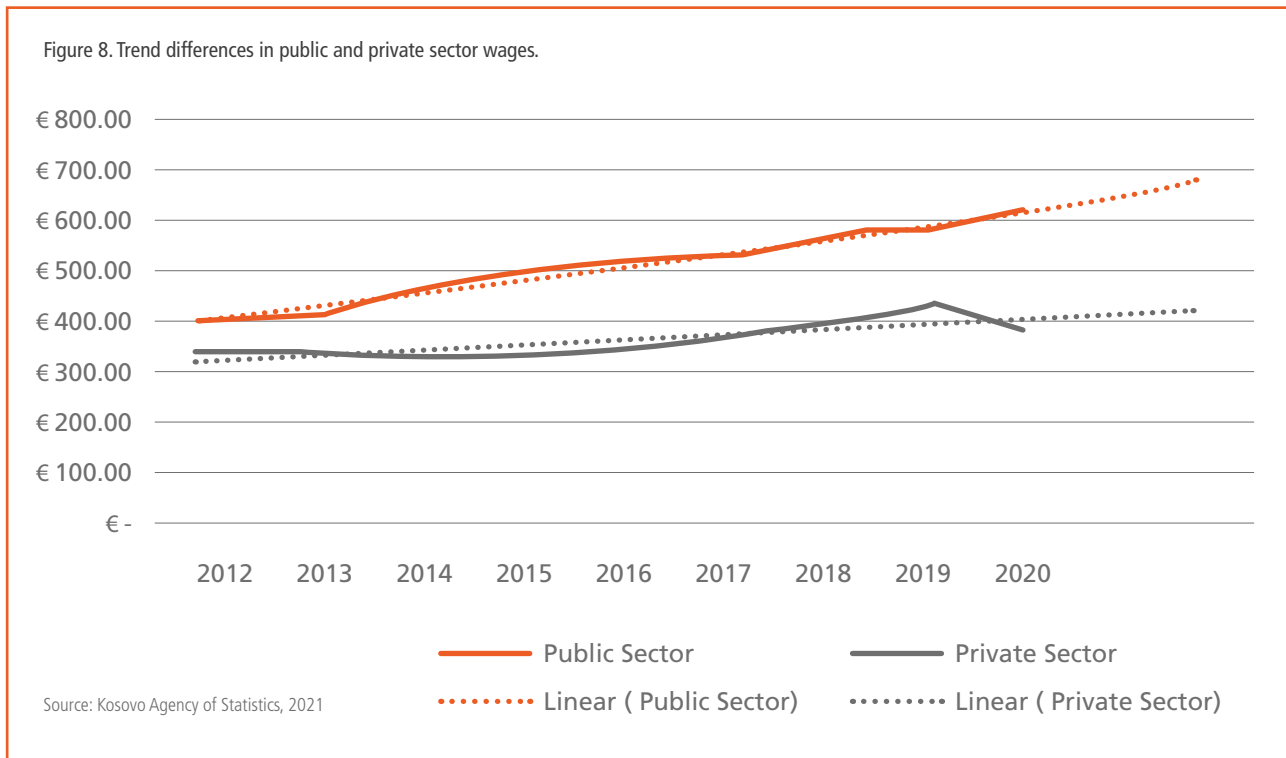
leadership as well the expected transformation of the workplace that often never came. However, overall trade unions in Kosovo have been heavily politicized, using their impact to influence government decisions but even more so to secure political promises. As a result, the gap between private sector and public sector employees has widened, especially in terms of wages.

In 2020, the average gross wage in the public sector is recorded at €624, compared to only €380 in the private sector, as is shown in Figure 7.



More importantly, the trend of changes in the wage levels in the private and public sectors has widened in the past decade. Public sector wages were about 20% higher in 2012, jumped to 43% higher in 2014, due to a government decision to raise public sector wages,

as seen Figure 8. The private sector did not follow the increase in public sector wages, and the gap between private and public sector wages is at around 65% in 2020.



The lack of trade union coverage in the private sector has not only impacted the wage levels, but also working conditions. Workers in the private sector work longer hours, on average a full day of work longer than workers in the public sector (35 hours in the public sector compared to 42 hours in the private sector). It is estimated that 30% of workers in the private sector work without a contract, and as such without legal protection. For women workers in the private sector, 1 in 3 does not hold a contract, while the number is 1 in 2 for those employed for the first time.²³ Even more so, most workers that hold contracts in the private sector, work under contracts with limited duration, usually set at less than a year.

These uncertainties in private sector employment show the clear need for establishment of trade unions and increase coverage of trade unions, especially in the industries with the highest employment and those with highest levels of risk, such as the construction industry.

For trade unions to have success, however, there needs to be numerous conditions in place, including but not limited to effective social dialogue mechanisms, strong institutional attachments for the trade unions, as well as inclusion as strategic partners. Kosovo institutions need to create a strong legislative framework that protects workers and their right to establish and be part of trade unions, be it within the firms, or the industry.

Inclusion of worker representatives, with specific designation of organized representation, in public-private dialogue for working conditions, including working hours, overtime and holiday pay and compensation, health insurance and on-the-job security, can dramatically increase the power of worker representatives and the interest of workers to organize.

In order to improve trade union membership and representation of workers in the labour dialogues, Kosovo institutions should develop legislative provisions that strengthen the role of trade unions in improved economic outcomes.

The Law on Investments, while offering incentives for foreign direct investors, needs also to safeguard worker's rights and working conditions. Legislation on investments should have provisions that require investors to guarantee worker's rights through workers organizations and trade unions. Moreover, worker's organizations need to be included in negotiations for any changes in investment conditions. Legislation should further prevent company agreements from undercutting sectoral trade unions and any collective bargaining agreements reached by the sectoral worker's organizations.

All benefits from Kosovo government to private sector firms should be contingent on worker's organizations through trade unions, be it at the company or sectoral level.

²³ Riinvest Institute, Facilitating Empowerment: Factors Influencing Women's Economic Decisions in Kosovo, 2018

Through such provisions place importance on the workers and working conditions as key to private sector development. Moreover, such contingencies may impact firms in developing their own social standard guidelines, especially when dealing with suppliers or when they are part of value chains.²⁴

In specific sectors, such as agriculture, where the ministry responsible for agricultural development supports producers through continuous grants and subsidies, eligibility for such programmes can be made contingent on worker's organizations.

Finally, the current Law on Labour, specifies the freedom of worker's organizing and of trade unions, with specifics of trade unions and organizing stipulated in the Law on Organizing Trade Union in Kosovo. None of the laws, condition trade unions in certain sectors. Establishment of sectoral bodies, such as the sector skills council, for vocational education curriculum development, which require representatives of sectoral trade unions to be represented, can serve as guarantees for establishing sectoral trade unions. These provisions can be stipulated in the Law on Labour or other legislation that establishes such sectoral collaboration bodies.

Collective bargaining and other sectoral bargaining dialogues need to be defined in terms of participation and legitimacy of representation. Currently, the collective bargaining agreement is reached between the Union of Independent Trade Unions, as the representative body of private sector workers and employer representative bodies and the government. Nonetheless, the market structure, with a limited number of large employers, also impacts the number of employees that are covered by a collective bargaining agreement, potentially leaving a considerable number of employees uncovered by this agreement.

As such, regulating representation of workers in terms of industries and sectors is an important way to distinctly encourage organization of workers into sectoral or industry unions. Moreover, at the company level, requirements such as a worker council where unions are non-existent provide a strong basis for employee organization at this level.

4. CONCLUSIONS

Kosovo's labour market is still in a fragile state. Issues stemming from high levels of unemployment to high levels of inactivity, to a skills mismatch gap that has been a cause of concern for the past decade. However, to date, little real actions has been taken to overcome these issues. Clear preferences for public sector employment, a sector that is already saturated, have resulted from superior work conditions in the public sector, while at the same time facing significant inequalities in the private sector.

To address these issues, there is a necessity to foster the establishment of labour and trade unions in the private sector, to improve social dialogue and enhance workers' rights. Moreover, it is crucial to improve the effectiveness of the labour inspectorate, through more thorough inspections and a higher number of inspectors, to align with the needs of the labour market.

Furthermore, the legal framework regulating the labour market needs to ensure flexible work, part-time work, as well as shared work, in professions where this is possible, as schemes to increase employment and improve the participation, especially of youth and women, in the labour market. Similarly, legal provisions regulating work from home need to be enacted, especially considering the COVID-19 pandemic. Strategic orientation of the economy along with the labour market needs to be translated into a clear action plan that envisions the future orientation of work.

Such that it includes education and training reform, collaboration with private sector in determining the needs of the market and ensuring that the bridging of the skills gap happens from the mutual development of the economy and the labour market.

Through periodic targeted data collection, the Government can identify sectors with development potential and those with potential for job creation. Stimulation of sectors with potential for job creation can inform fiscal policies, such as tax breaks for companies that create new jobs - not just retaining existing ones, in specific sectors with potential for development.

Labour market data needs to be collected and published with sectoral, gender, and age disaggregation, to make it possible for proper analysis to be conducted that enables detailed strategic orientation of the economy, which aims to improve economic opportunities for all groups of the society.

²⁴ In Italy, the fashion design house Gucci, as means of maintaining quality control, requires suppliers to observe social standards – including collective agreements.

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CHAPTER 2. A NEW WAY TO DETERMINE THE MINIMUM WAGE IN KOSOVO

DITA DOBRANJA & EDISON JAKURTI

1. INTRODUCTION

While high unemployment remains the key problem of the labour market in Kosovo, there are many issues that the employed face, as well. One of them is the wage levels, especially for the low-wage earners. It has been over a decade full of change in the economy, but one indicator has not changed in nominal terms – the minimum wage. Given that it is a cushion for the poorest workers, the level of the minimum wage is also a reflection of a government's priorities and its ideological compass. Such a stagnation in increasing the minimum wage has had negative impacts in the labour market and as such needs to be addressed. The approach to minimum wage determination should reflect the dynamic and rapid changes in the economy, through periodic adjustments and while considering multiple facets of the economy.

Since there is an ongoing debate on the potential, adverse effects of the minimum wage on other factors such as unemployment and given that this is a particularly important issue in Kosovo's context, we bring new evidence on this relationship. Albeit that our baseline model is very simple and constraint to several limitations, it still enables us to provide some insights on the potential effects of raising the minimum wage on unemployment. The verdict is clear: there is no adverse effect.

Further, in this chapter we present a novel approach for determining the minimum wage in Kosovo. Specifically, we have developed a simple mathematical formula which is intuitive and easy to use. There are three main features of our model. First, it accounts for other wages in the economy by linking the minimum wage to the median wage. Second, it accounts for the overall "health" of the economy by adjusting it for economic growth in real terms. And third, it is dynamic given that it enables a reflection of changes in these aforementioned factors in the last 3 years.

²⁵ Administrative instruction no. 09/2017 on setting a minimum wage in the Republic of Kosovo

2. CRITERIA FOR DETERMINING THE MINIMUM WAGE

Minimum wages have been subject to discussions across the world, with both supporters and opponents offering solutions to the issues. In Kosovo, the minimum wage calculations are based on the following: (1) Cost of living; (2) Unemployment rate; (3) Job market situation; (4) Level of competitiveness and productivity.²⁵ While the cost of living, based on the Consumer Price Index (CPI) and the rate of unemployment, based on Labour Force Surveys, are easily determined, the factors foreseen to impact the determination of the minimum wage leave room for interpretation.

The collective agreement agreed upon at the Social Economic Council²⁶, establishes a different set of criteria, including the cost of living, needs of workers and their families, living standard of workers, as well as the level of economic development. These criteria again allow for interpretation.

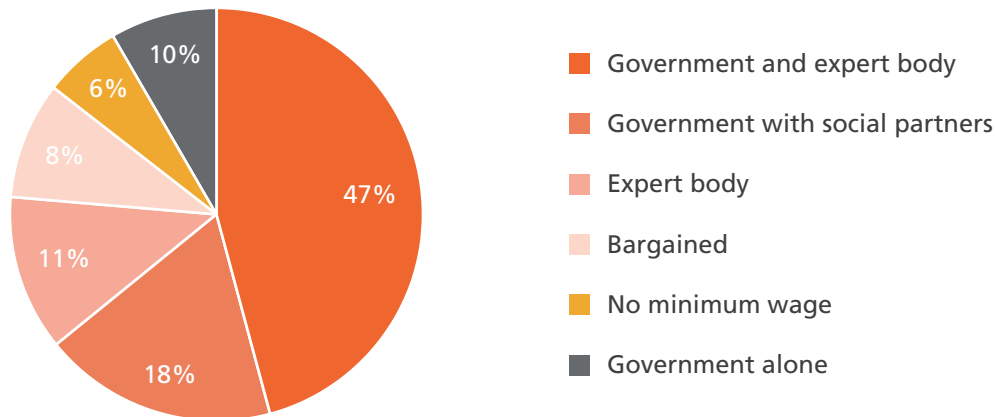
Globally, there are numerous methods that are used to set the level of the minimum wage. In the US, the Federal Government sets the minimum wage, which currently is set at \$7.25/hour, however, many states have their own minimum wage laws. In the case when employees are subject to the state and federal minimum wages, they are entitled to the minimum wage that is the higher of the two.²⁷ Countries like Austria and Germany determine the minimum wage based on a collective bargaining system.²⁸ About 6% of countries in the world do not have a minimum wage system in place at all. A more detailed breakdown of different approaches to minimum wage setting can be seen in Figure 1.

²⁶ The Social Economic Council consists of fifteen (15) members, who, in this body, represent the interests of Employees' Organizations, Employers' Organizations and Government.

²⁷ US Department of Labor, Minimum Wage, Accessed October 2021, <https://www.dol.gov/general/topic/wages/minimumwage>

²⁸ Richard Dickens, How are Minimum Wages Set, IZA, World of Labour, 2015

Figure 1. Wage setting across the world



Source: ILO, 2013

Minimum wage determination also differs between countries depending on whether they use a single minimum wage or different wages for different worker groups. Kosovo has a different minimum wage depending on the age, set at a lower rate for workers under 35, and higher for those above. Other approaches to differentiating workers include setting minimum wages by sector or by occupation. The main aim of setting different wages for different groups of workers is to allow the government to tailor policy responses to these different groups. This is especially important in times of economic or social crises, when the government can choose to alleviate minimum wages for certain groups (for example sectors not impacted by the economic downturn) while keeping them in place for other sectors. However, the downside of setting different wages for different groups lies in the risk of non-compliance or complexity to administer.

3. DIFFERENT FORMS OF MINIMUM WAGE SETTING

The International Labour Organization (ILO) recommends a general set of criteria and approached to be followed by countries setting the minimum wages. Based on the Minimum Wage Fixing Convention, minimum wages should include both social and economic aspects.²⁹ Most notably, the minimum wage, as per the convention, needs to keep ensure that cost of living, overall levels of wage compensation, as well as the rate of economic and productivity growth, are taken into account.³⁰

According to the ILO, the list is not exhaustive and the level of inclusion of these indicators depends on the type of minimum wage setting mechanisms the country uses. While there is no one size fits all approach, mechanisms that involve a higher number of stakeholders and experts in determining the minimum wage, have a higher likelihood of incorporating the necessary perspectives in setting the minimum wage.

3.1. GOVERNMENT ONLY

Setting minimum wages through government issues decisions and voted in government bodies, while considered more efficient, is often exposed to criticism for not considering the perspective of other stakeholders, especially of trade unions. In the US, minimum wage setting has been stagnant and subject to political agendas of the two major parties. Problems linked to the political agendas in wage setting in countries where government alone determined the minimum wage are prevalent.

²⁹ ILO, Chapter 5 – Setting and adjusting minimum wage levels, 2015

³⁰ In terms of social aspects, the ILO determines that the minimum wage setting should at least consider: (1) needs of workers and their families, (2) overall wage levels in the economy, (3) cost of living, (4) social security benefits, as well as the (5) living standards of other social group. Economic factors to be considered include: (1) economic development, (2) productivity levels; as well as the (3) desirability of attaining and maintaining a high employment level.

3.2. EXPERT BODY

The most common approach to minimum wage determination has been that of using expert bodies. The way this is regulated depends on the country, however, in most countries, expert bodies are comprised of relevant stakeholders and experts of the field, who in dialogue with the government bodies, recommend the minimum wage levels. The composition of expert bodies is important for objectivity and not to serve any political or trade union interests.

3.3. MATHEMATICAL FORMULA

Many countries use mathematical formulas for determining minimum wage levels. This method ensures rigidity in setting minimum wages and in most cases automatically compensates for inflation, which in turn ensures that minimum wages maintain their purchasing power. However, adjusting solely for inflation does not provide a comprehensive approach to minimum wage setting. Some countries use more complicated mathematical formulas, to adjust for economic growth, other sector wages, as well as poverty levels.

Malaysia³¹ uses one of the most comprehensive and complicated mathematical formulas for determining minimum wages. Given that Malaysia sets different minimum wages based on regions, the formula for determining the minimum wage accounts for that, as well as for the poverty line income, growth in productivity, consumer price index, and the real unemployment rate. Currently, minimum wage in Malaysia is calculated as the average of poverty line income in terms of average workers per household adding the median wage. All this is then calculated in terms of the productivity growth, the consumer price index, and the real unemployment rate, in different regions.

On the other hand, in France³², the annual change in minimum wage is directly linked to inflation (calculated through year-on-year CPI) and to the purchasing power of blue-collar workers' hourly wages. Through this, France intends to consider both the cost of living, but also keep minimum wage linked to wages of lower paid workforce in the economy. However, collective bargaining agreements have in the past impacted sectoral minimum wages, setting them higher than the calculated minimum wage.

Different countries consider different aspects to incorporate in their calculations of minimum wages, however, using mathematical formulas leaves little to no flexibility for policy response to changing labour market conditions.

Moreover, even in countries where mathematical formulas are used, expert bodies need to be consulted when determining the formulas for setting the minimum wages.

3.4. COLLECTIVE BARGAINING

Using collective bargaining as a method of setting the minimum wage depends on the influence that trade unions and employee organizations have in the country. Moreover, given that trade unions often operate at a sectoral level, collective agreements for setting minimum wages are also decided at sectoral levels. While this approach guarantees a comprehensive approach it also is difficult to implement and requires high levels of institutional capacities. Countries such as Sweden, Finland, and Denmark, implement this approach, with sectoral set minimum wages.

4. KOSOVO MINIMUM WAGE SETTING

Currently the minimum wage in Kosovo is set through legislative framework, which was adopted in 2011. In 2011, the law on minimum wage established that the minimum wage is mandatory throughout Kosovo, has no difference between regions or professions, with the only differentiation in the level of the minimum wage being that of age. The minimum wage is €130 for those under 35 years of age; €170 for those over the age of 35.

Kosovo's approach to setting the minimum wage needs reform, not least because ambiguities stemming from loosely defined criteria, combined with influences from collective agreements, are a cause for concern. Moreover, the stagnation in updating the minimum wage in Kosovo has caused discontent from workers and their representatives. However, considering the uneven power that trade unions representing workers in public institutions exert, compared to the little to no collective organizing of workers in the private sector, it is crucial to develop a system of determining minimum wages that does not allow for undue influence.

Using an expert body to develop a mathematical formula for determining the minimum wage, such that adjustments are made based on economic, social, and labour market trends, is the approach with the highest likelihood of succeeding. However, indicators that are included in the determination of the minimum wage need to be aligned with data that is continuously collected, such that the determination of minimum wage does not fail due to lack of data.

³¹ See International Labor Organization Website: https://www.ilo.org/global/topics/wages/minimum-wages/setting-adjusting/WCMS_439264/lang--en/index.htm

³² Ibid

The main issues Kosovo’s minimum wage determination needs to address are the existing income and wage inequality, which can skew the minimum wage; real growth, which adjusts for changes in prices and the standard of living; as well as regulate the adjustment periods, to ensure that the minimum wage is adjusted to reflect changes in the economy, rather than remain as an institutional or political will.

4.1. EFFECTS OF MINIMUM WAGE CHANGES IN UNEMPLOYMENT – AN EMPIRICAL ANALYSIS FOR KOSOVO

To address concerns about the impact that the minimum wage has on unemployment, among other factors, a simple Ordinary Least Squared (OLS) regression analysis between the minimum wage and unemployment was conducted for Kosovo’s labour market, beginning in 2016, with quarterly data reporting from the Kosovo Agency of Statistics. The minimum wage levels, based on the legislation, were reported accordingly to the age limits in the data set

(€130 for those under 35 years of age; €170 for those over the age of 35).

The lone interaction between minimum wage and unemployment was assessed through a simple regression analysis, as per the following model:

$$\text{unemployment} = \beta_0 + \beta_1 (\text{minWage})$$

where β_1 is the proportional unit for unit change between minimum wage and unemployment.

For this regression analysis, the null hypothesis was that the minimum wage would have no effect on unemployment rate.

$$H_0 : \beta_1 = 0$$

$$H_A : \beta_1 \neq 0$$

However, the alternate hypothesis states that $\beta_1 \neq 0$, indicating a direct relationship between minimum wage and unemployment. Table 1 contains the results of the simple linear regression analysis, with robust standard errors.

Table 1. Simple OLS regression model results

Independent variables	General Model Results	Women’s Unemployment Results
Minimum Wage	-717.8947** (40.96643)	-301.3377** (12.9006)
Intercept	137505.3** (6268.093)	54313.38** (2023.168)
Observations	95	95
R-sq	0.7591	0.8587

Standard error of estimated coefficients are reported in parentheses.

* Significant at the 0.05 level

** Significant at the 0.01 level

*** Significant at the 0.001 level

For the general model, determining the impact of minimum wage on overall unemployment the determination coefficient, R-squared is 0.7591, showing that showing that 76% of variation in unemployment, since 2016, is explained by the minimum wage. P-value results show that the result of the regression as a 0% value to be at random, therefore indicating a high significance of the results.

$$\text{unemployment(Thousands)} = 137505.3 - 717.8947(\text{minWage})$$

Meaning that, if the country has no minimum wage set (that is, minimum wage is €0), the number of the unemployment will be 137,505; however, a €1 increase in minimum wage is expected to decrease unemployment by 718.

Given the high unemployment and inactivity levels of women in Kosovo’s labour market, it is also important to determine whether the minimum wage has an impact on women’s unemployment levels.

The R-squared for the second regression is 0.8587, showing that showing that 86% of variation in women’s unemployment, since 2016, is explained by the minimum wage. P-value results show that the result of the regression as a 0% value to be at random, therefore indicating a high significance of the results.

$$\text{unemployment women(Thousands)} = 54313.38 - 301.3377(\text{minWage})$$

Meaning that, with no minimum wage, the women’s unemployment in thousands will be 54,313; however,

with an €1 increase in minimum wage women’s unemployment is expected to decrease by 301.

Moreover, given the 2020 COVID-19 pandemic has caused a disruption in the overall economy and the labour market as well, this model looks at the relationship between unemployment and minimum wage with pre-COVID-19 data and data during the pandemic in 2020. The results are shown in Table 2.

Table 2. Simple OLS regression analysis pre-pandemic and during the pandemics

Independent variables	Pre-COVID19 Pandemic (2016-2019)	During COVID19 Pandemic (Q1-Q3 2020)
Minimum Wage	-745** (46.59796)	-573.333** (70.78996)
Intercept	142375** (7233.949)	111533** (10989.56)
Observations	80	15
R-sq	0.7632	0.8219
Standard error of estimated coefficients are reported in parentheses. * Significant at the 0.05 level ** Significant at the 0.01 level *** Significant at the 0.001 level		

Pre pandemic:

$$\text{unemployment(Thousands)} = 142375 - 745(\text{minWage})$$

Prior to the COVID-19 pandemic, with a minimum wage of €0, the unemployment levels in thousands are estimated at 142,375; however, with an €1 increase in minimum wage the unemployment is expected to decrease by 745.

During the pandemic:

$$\text{unemployment(Thousands)} = 111533 - 573.333(\text{minWage})$$

The disturbance of the COVID-19 pandemic in the labour market shows that having no minimum wage the unemployment levels in thousands are estimated at 111,533; however, with an €1 increase in minimum wage the unemployment is expected to decrease by 573. However, the results for the analysis during the COVID-19 pandemic include only 15 observations, making it difficult to generalize based on only a small sample size.

However, it is important for the analysis to include the disturbance in the economy and labour markets that has resulted from the COVID-19 pandemic, as a reference point, even if the results cannot be generalized.

This analysis clearly shows that the minimum wage currently does not impact the unemployment level negatively. Looking at the Kosovo labour market for the past five years the regression models show that minimum wage has a negative effect on unemployment. The impact of minimum wage on unemployment is different for different dependent variables, initially analysing unemployment as a whole and following by women’s unemployment. Moreover, during 2020, the COVID-19 pandemic has impacted the labour market and it reflects in the model as well, showing that the reduction in unemployment from the minimum wage has been hired prior to the pandemic. However, in all models treated, the impact of the minimum wage has been identified as reducing unemployment.

Shortcomings of the model, that stem from the simplicity of the model, a small sample size, and lack of more variables included, remain valid. The model does not address an important aspect of the minimum wage, that of the differences between youth under 35 and the rest of the population over 35, which is included as difference in the minimum wage itself. A stronger model would control for youth, while at the same time controlling for differences in the gender outcomes, and other disturbances in the market. Lack of data to differentiate the impact between the public and the private sector limit the options for analysis as well.

4.2. A PROPOSAL FOR KOSOVO'S APPROACH TO THE MINIMUM WAGE

One proposed model that can address these issues and serve as Kosovo's minimum wage setting formula, is the following:

$$MW = \frac{4}{5} \times [(Average\ Inflation - Adjusted\ Median\ Wage_{t-3}) \times (1 + Average\ Real\ GDP_{t-3})]$$

Where:

$$Average\ Inflation - Adjusted\ Median\ Wage = \frac{IAMW_{t-3} + IAMW_{t-2} + IAMW_{t-1}}{3}$$

where

$$IAMW = Inflation - Adjusted\ Median\ Wage$$

and

$$IAMW_{t-3} = \frac{Nominal\ Median\ Wage_{t-3} \times CPI_t}{CPI_{t-3}}$$

$$IAMW_{t-2} = \frac{Nominal\ Median\ Wage_{t-2} \times CPI_t}{CPI_{t-2}}$$

$$IAMW_{t-1} = \frac{Nominal\ Median\ Wage_{t-1} \times CPI_t}{CPI_{t-1}}$$

and

$$Average\ Real\ GDP\ Growth\ Rate = \frac{RGGR_{t-3} + RGGR_{t-2} + RGGR_{t-1}}{3}$$

where

$$RGGR = Real\ GDP\ Growth\ Rate$$

and

$$Real\ GDP\ Growth\ Rate = \frac{Real\ GDP_t - Real\ GDP_{t-1}}{Real\ GDP_{t-1}}$$

and

$$Real\ GDP_t = \frac{Nominal\ GDP_t}{\frac{CPI_t}{100}}$$

and

$$CPI_t = \frac{C_t}{C_0} \times 100$$

This minimum wage fulfils the main ILO criteria for minimum wage setting, addressing issues of efficiency and equity, by using median wages, rather than the mean. Using median average wages are a more accurate point of reference for setting the minimum wage in economies such as Kosovo's. Furthermore, given that wage levels for women and youth are lower, using the median average wage tends to address the inequalities stemming from this as well.

However, the drawback of adjusting median wages in current year's prices is that the calculation will always end up using either a particular month's annual inflation rate (e.g., September 2021) or the average inflation rate up to that month (average of inflation rates between January and September 2021). Making it impossible to use annual average simply because we want current year's prices.

Following ILO, to take living standard into consideration when setting the minimum wage, this model addresses both economic growth and the living standard, through price changes, thus using is the real GDP growth rather than the nominal growth.

Moreover, given the current situation where the minimum wage adjustments are long overdue, a dynamic model that is self-adjusting is important. Considering the current labour market dynamic, the proposed period for adjustment is 3 years. However, this period can be extended to a maximum of 5 years, if the economy shows a stable growth with not many fluctuations, in the future.

Finally, since changes are high that the number yielded might include decimal points i.e., euro cents, for practical reasons, we recommend that the final minimum wage is rounded up to the next value of the second digit before the decimal point. For example, if the minimum wage determined by the formula is €218.52 euro, we recommend that it becomes €220 euros.

4.3. A NUMERICAL EXAMPLE OF THIS MODEL

In order to show the exact level of the minimum wage derived from this model, we provide a numerical example as shown in Table 3. Data for the average median wage were retrieved from the Tax Administration of Kosovo (TAK) and include all wage earners. Real GDP growth rates were retrieved from the publicly available World Bank database.

If our last recommendation is followed, for practical reasons, then this would be rounded up to €260. Inflation adjustments are done using the annual rate of CPI reported in September (2018, 2019, 2020, and 2021) since the last one published by KAS is from September 2021. Here, median wages in 2018, 2019, and 2020, are adjusted for prices in September 2021.

So, if the minimum wage were to change this year, based on our formula, it should be at least €254.1.

Table 3. Determining the minimum wage for 2021 based on our model

Coefficient	Average of 2018, 2019, 2020		Minimum wage in 2021
	Median (inflation-adjusted)	Growth rate	
0.8	€315.6	0.62%	€254.1

Source: Authors' own calculations based on data from TAK and World Bank

5. CONCLUSIONS

While unemployment is a long-lasting issue which needs to be constantly addressed by the Government, improving the conditions of the employed workers should too be a vivid policy of any progressive Government. The nominal minimum wage in Kosovo has stagnated ever since it was introduced, and we recommend that the Government raises it now and periodically. After analyzing the different criteria and approaches for determining it, we have also addressed an important question.

With a simple OLS model, we analyzed the potential effects of raising the minimum wage on unemployment. Results show that raising minimum wage in Kosovo will not have a negative impact on unemployment. Hence, we propose a specific mathematical formula, which is dynamic and considers other wages and the overall economic growth. Based on our formula and rounding up procedure, the minimum wage in 2021 should be €260. The formula, as is seen, considers inflation adjusted median wages, as well as inflation adjusted economic growth.

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SECTION II: SOCIAL PROTECTION AND FISCAL POLICY

CHAPTER 3. SOCIAL ASSISTANCE AND UNEMPLOYMENT BENEFITS

DINA VLLASALIU

1. INTRODUCTION

This chapter covers information on Kosovo's current social assistance schemes and unemployment benefits. The first section starts off with an explanation of what social assistance schemes are in general, different pillars of social assistance, as well as how are they set up in Kosovo, with specific emphasis on the Social Assistance Schemes (SAS), despite the existence of other schemes such as support for foster families, electricity subsidies, support for families with children that have permanent disabilities, and alike. It further goes on to discuss the country's social assistance eligibility criteria and pitfalls associated with the current criteria in place.

The Study proposes a series of recommendations regarding the betterment of social assistance:

- Increasing the coverage of eligible people through outreach programs and the lowering of administrative costs of applying
- Establishing a solidarity fund through progressive contributory mechanisms with the employer and the employee as the two key contributing actors, followed by charity and crowdfunding initiatives, whereby people/businesses that contribute to the solidarity fund voluntarily would become eligible for business tax break schemes or potential government subsidies for their businesses.
- Establishing of in-kind or cash transfers to the woman of the household qualifying for social assistance, as studies have shown that allocating funds to the mother can increase the likelihood of proper allocation of funds, especially when it comes to the children's well-being. Furthermore, the Study suggests that in-kind transfers could be targeted toward purchasing of domestic products to simultaneously incentivize domestic production
- Presenting a numerical amount of social assistance allocated to families depending on whether families belong to Category I, whereby all members are considered dependent and/or unable to work, or Category II, where at least one family member is capable of working.

- Establishing mechanisms to exit the social assistance program through re-skilling programs, focus group establishment to identify rural labor market needs, government subsidies to employers if they hire social assistance beneficiaries, and tailored help to families receiving assistance.

The second section covers information on what unemployment benefits are, how are they set up in different countries, as well as the rationale behind why Kosovo needs an establishment of unemployment benefits, keeping in mind that these benefits are considered a transitional period from unemployment to employment. To ensure that, the Study puts forth a series of recommendations:

- In order to qualify for unemployment benefits, citizens should apply for benefits through the employment agency and be willing to participate in vocational training to help them in skill-matching with labor demand.
- The Study proposes that the benefits received should not exceed the monthly minimum wage in Kosovo, as doing so might serve as an incentive to remain unemployed
- Following best practices from developing countries, benefit duration should range between 5-7 months.
- Sanctions should be applied to individuals matched to a job but refuse one. Additionally, voluntary resignation should generally not qualify one for unemployment benefits as it could serve as an incentive for other individuals quitting as well.

2. WHAT ARE SOCIAL ASSISTANCE SCHEMES? ARE THEY EFFECTIVE IN TARGETING THE POOR?

Social protection schemes are set in place to protect the vulnerable groups of societies. These schemes can vary in nature, on whether they are contributory or non-contributory. Governance and Social Development Resource Centre (GSDRC) divides these schemes into social assistance, social care, social insurance, and labor market policies and interventions.³³

Social assistance schemes are targeted to reach the poorest and/or most vulnerable groups of society. Across nations, social assistance is reported to have the highest level of coverage, covering around 46% of the population in lower middle-income countries and around 15% in low-income countries. However, ironic to its purpose, data shows that the poorest of the poor do not get to benefit from these schemes.

For example, once social transfers are considered, the total number of people living in poverty reduced by only 3% in low-income countries whereas these percentages were 6%, 8%, and 16% in lower middle-income, upper middle-income and high-income countries, respectively³⁴. International Growth Care, deriving information from several countries, stipulates that this could partly be due to poor data quality and updated information on formal employment³⁵.

3. SOCIAL ASSISTANCE SCHEME IN KOSOVO: HOW ARE THEY SET UP

In Kosovo, the Social Assistance pillar is divided into several components including a) last resort social assistance - the Social Assistance Scheme (SAS), b) material support for foster families, c) assistance for exceptional needs, d) energy/electricity subsidy, e) material support for families with children (of age 0-18 years) with permanent disability, and f) social and family services³⁶. Generally, only the Social Assistance Scheme (SAS) is aimed specifically toward poverty reduction in the country, through cash transfers as well as other in-kind benefits and fee exemptions (coverage of a certain amount of electricity bill, exemption from payments of primary and secondary health care services, free books for primary and secondary education, exemption from tuition fee for higher education students, exemption from payment of municipal administrative taxes, and exemption from payment of other utilities)^{37,38}.

In order to qualify for social assistance in Kosovo, there is a two-fold procedure for each family— a categorical criteria under one of which each family must fall to qualify, and if that is fulfilled, a poverty test is also utilized, based on an econometric method known as the proxy means test³⁹.

3.1. THE EFFECTIVENESS OF SAS IN KOSOVO, ITS PITFALLS, AND CURRENT PROGRESS

Social assistance schemes, even though designed to alleviate poverty, do not always end up doing so especially in countries that are developing. Kosovo is no exception to this rule. According to World Bank, there are discrepancies between the country's poverty profile and the households receiving social assistance. As the report states, around 20% of households with more than 5 members are considered poor, and yet only around 5%-8% of them receive social assistance funds.

The report further stipulates that this untargeted coverage may be due to a myriad of reasons, some of them including a) the criterion of having a child younger than 5 in order to qualify excludes many families with school age children, b) employment of one family member may result in exclusion but the individual may not be making enough to pass the poverty threshold, and c) the poverty test does not necessarily target the poorest of the households as the formula currently used may require statistical accuracy.

As of 2020, the Ministry of Labor and Social Welfare (now under Ministry of Finance) has updated the "Concept-Document" aiming to reorganize the SAS in Kosovo. If the plan is to move forward, there are a series of goals it would try to achieve, resulting chiefly from the World Bank report of 2019:

- Removal of category-based filters
- Selection of beneficiaries through a new poverty test
- Introduction of a more equivalence scale and increase of child allowance from 5 EUR to 10 EUR a month for every child below 18 years of age

³³ Types of Social Protection. Governance and Social Development Resource Centre. <https://gsdrc.org/topic-guides/social-protection/types-of-social-protection/>

³⁴ Do Social Assistance Programs Reach the Poor? Micro-Evidence from 123 Countries. International Growth Care (2020). <https://www.theigc.org/reader/do-social-assistance-programmes-reach-the-poor-micro-evidence-from-123-countries/yes-the-poorest-are-left-behind/>

³⁵ Ibid.

³⁶ Legislation in the Official Gazette of the Republic of Kosovo

³⁷ Administrative Instruction No.15/2012 on the Calculation of Monthly Social Assistance Amount

³⁸ Kosovo Social Assistance Scheme Study. World Bank Group (2019) <https://documents1.worldbank.org/curated/en/994991557470271998/pdf/Kosovo-Social-Assistance-Scheme-Study-Assessment-and-Reform-Options.pdf>

³⁹ Ibid.

⁴⁰ Ibid.

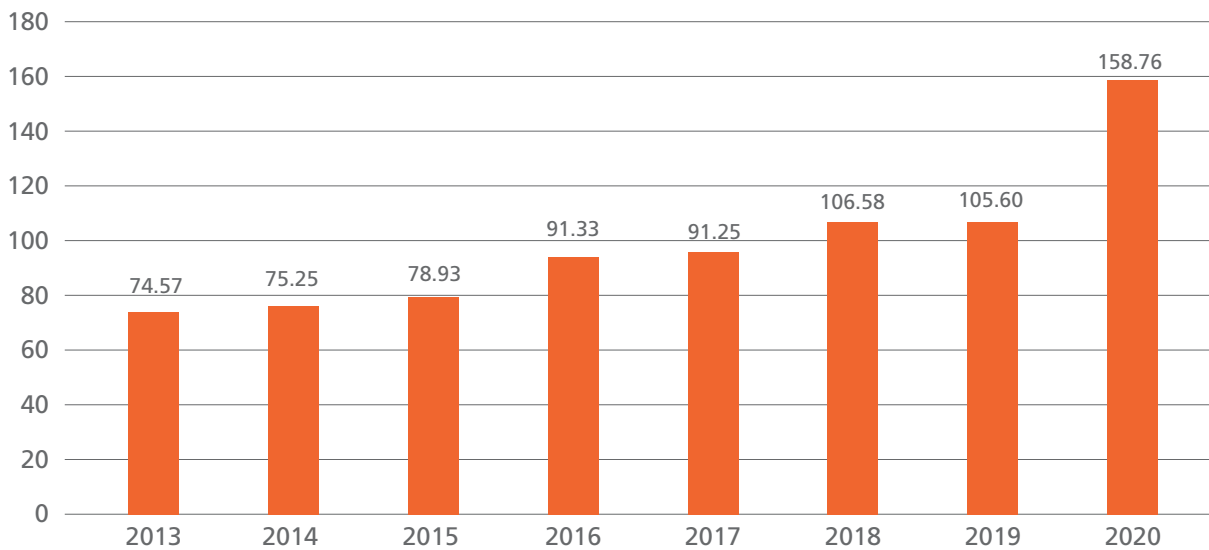
- Engage those in SAS with employment programs, vocational training, government programs and alike to ensure they escape the cycle of being on social benefits for an extended period⁴¹.

The chart below presents a breakdown of the average monthly income received by families as social assistance, from 2013 to 2020. In 2013 for example, a family receiving social assistance was allotted an average of 74.52 EUR, whereas in 2020 this number was 158.25 EUR. Though this is evidence for increased allocation throughout the years, the fact that the formula doesn't account for inflation, deems the social

assistance program not as effective in combating poverty.

Additionally, a recent study conducted by the Kosovo Democratic Institute (KDI)⁴², shows that as of July 2020, there have been around 20,876 individuals (out of 3,000,000 EUR allocated from the budget, 2,713,880 EUR have been used up) that have applied for 130 EUR monthly assistance under Measure 15 of the Fiscal Emergency Package. With this additional information at hand, it becomes crucial to prioritize social assistance schemes.

Figure 1. Average monthly income of families receiving social assistance (in €)



Source: Author's Calculations. Data retrieved from Ministry of Finance and Transfers

4. A PROPOSAL FOR REFORMING THE SOCIAL ASSISTANCE SCHEME

With this state of play at hand, this Study puts forth a series of policy recommendations to ensure a better allocation, targeting, and coverage for the poor in need of social assistance, while instituting efficient programs to help these vulnerable groups escape the poverty trap. These include increasing the coverage of eligible people, establishing an assistance program that serves as a boost off social assistance, escaping the poverty trap through conditional cash transfers, and ensuring appropriate allocation of funds.

4.1. NUMERICAL AMOUNT ALLOCATED

With the current economic situation and price level at play, this Study puts forth the idea that there should be a minimum amount of social assistance received by each family, depending on what category they belong to. Below is a brief outline:

- For families belonging to Category I where all family members are considered dependent and unable to work, a minimum of 3 EUR/day should be allocated to each family member, for a total of 90 EUR/month per member. If the family unit comprises of minors, the funds will be transferred on the mother's financial account.

⁴¹ Ibid.

⁴² Pakoja Fiskale Emergjente. Analize e Shkurter. KDI (2020) <https://kdi-kosova.org/wp-content/uploads/2020/08/50-Analiz%C3%AB-e-Shkurt%C3%ABr-e-Pakos-Fiskale-Emergjente-ALB-02.pdf>

- For families belonging to Category II, where at least one person is capable of working, minimum of 3 EUR/day should be allocated to each family member, for a total of 90 EUR/month per member, if the total per family does not surpass the value of 220 EUR/month, with the rationale that the assistance should still be less than the minimum wage. If the family unit comprises of minors, the funds should be transferred on the mother's financial account. Additionally, if the capable family member(s) find employment, they should nonetheless receive social assistance if their monthly pay is less than the minimum wage, whereby the total income guaranteed from both assistance and employment equals a minimum income guarantee threshold (MIG). If a family member however finds employment that pays up to 33% above minimum wage (around 300 EUR/month), the social assistance allocated is to be terminated only to the recently employed but should continue for other members remaining unemployed.⁴³

4.2. INCREASE COVERAGE OF ELIGIBLE PEOPLE

In Kosovo, there is evidence of discrepancy between the population living in poverty and those that receive social assistance⁴⁴. Generally, discrepancies might arise from several reasons, including lack of information about the existence of social assistance programs, a complicated application process, fear of stigmatization, as well as the refusal to change the current state of being (also known as the status quo bias)⁴⁵. This becomes even more difficult among the vulnerable minority groups in Kosovo, some of whom might also be illiterate. To target this problem, a series of undertakings outlined below can be implemented:

- Outreach efforts to increase people's awareness about the assistance programs. These can be done through awareness raising campaigns, especially nearby dwellings of vulnerable communities, TV ads, or also as information ad messages as part of utility bills
- Lower administrative burdens such as assistance with application forms (especially for those with limited literacy levels), convenient office hours, mobile application centers scattered across

municipalities as well as the enabling of digital applications for those that have the means to apply online. Another possibility here could also be the establishment of community-level NGOs which would help spread information about social assistance application procedure as well as help these individuals with the application process itself.

4.3. ESTABLISHMENT OF A SOLIDARITY FUND/INCOME

People who have been employed before but suddenly find themselves without a job, a program could be established- a solidarity fund- whereby whenever an employee finds oneself trapped in poverty (income below minimum wage for example), one can withdraw funds from the solidarity fund. For these people, this could be considered as contributory assistance.

The solidarity fund could additionally extend to also include individuals who are incapable of working due to some terminal illness (mental disorders, chronic illness, intellectual disability)⁴⁶. This way, the fund can serve as an additional safety net for the most vulnerable groups of society. For this category, the funding would be non-contributory assistance.

Unlike other social assistance programs for which funding is mainly sponsored by the government, the solidarity fund can get its majority of funding from a progressive contribution scheme, whereby both employers and employees can contribute a progressive-to-salary percentage of the employee's pay into the fund. Careful attention needs to be paid to the fact that the percentages allocated toward the fund should be small enough to avoid any boomerang effects in terms of increasing hiring costs for the employers. Additionally, only people that are paid above the minimum wage would be considered eligible for contributing to the fund.

Moreover, other stemming sources of funding can also come from crowdfunding events and charity initiatives. Contributors to the fund (i.e., entrepreneurial companies) could then be encouraged to continue contributing via possible schemes of tax breaks or subsidy programs that they could enroll in to help their business prosper.

⁴³ The rationale behind the calculations is based on prior group discussions of the authors as well as supported by literature as in the following: RSA: Providing Income Security and Supporting Return to Work. Case of France. <https://www.social-protection.org/gimi/gess/RessourcePDF.action?ressource.ressourceId=53361>

⁴⁴ Kosovo Social Assistance Scheme Study. World Bank Group (2019) <https://documents1.worldbank.org/curated/en/994991557470271998/pdf/Kosovo-Social-Assistance-Scheme-Study-Assessment-and-Reform-Options.pdf>

⁴⁵ David, Ribar. How To Improve Participation in Social Assistance Programs? (2014) <https://wol.iza.org/uploads/articles/104/pdfs/how-to-improve-participation-in-social-assistance-programs.pdf>

⁴⁶ Social Assistance and Social Solidarity. Quebec. <https://www.quebec.ca/en/family-and-support-for-individuals/social-assistance-social-solidarity#c67410>

4.4. WELFARE PAYMENT- DIFFERENTIATING BY GENDER: OPPORTUNITIES AND PITFALLS

Traditionally, welfare payments especially in developing nations are given to the head of the household, which by societal norms, has always been the father. In a study conducted in Brazil, beginning in the early 1990s, there is evidence that unearned income given to the mothers, has a stronger effect in money allocation going toward the child's well-being and development, thereby increasing the latter's probability of survival⁴⁷. The Brazilian government has also introduced a 10-year conditional cash program named Bolsa Família which transfers welfare finances to the mother of a household. This gender-oriented allocation has proven effective in Brazil and has shown positive results in increased school attendance and improved regular health check-ups of children⁴⁸.

Another study conducted using randomized controlled trials in rural Burkina Faso, shows evidence that while allocating welfare to mothers leads to higher school enrollment, giving cash to the father leads to increased livestock ownership, higher agricultural production, and increased investment into a house's equipment⁴⁹.

However, the existing evidence of the positive correlation between women recipients of welfare and a) improved probability of a child's survival, b) higher rate of school attendance, and c) health check-up visits, could serve as a motivating ground to implement such a policy with the Social Assistance Scheme (SAS) in Kosovo. Given that recently the government has established a channel of support for young mothers and child allowance schemes, implementing this policy is a feasible idea.

Nonetheless, one must keep in mind that the studies, the results of which are extrapolated here, have been implemented in different cultures with different social norms. One should consider the implications that such a cash transfer could have in the family unit/stability in Kosovo. Traditionally, the father in Kosovo is seen as the breadwinner and is deemed such by cultural norms as well. Any challenge of that authority might backfire in potential domestic violence and result in creating ground for instability within the family. While empowering women financially is a great step forward and one that should be encouraged, it is also worthy to discuss the fact that social assistance transfers are merely a sustenance income and might not give mothers complete financial autonomy in decision making.

⁴⁷ Duncan Thomas. Intra-Household Resource Allocation: An Inferential Approach (1990). <https://ideas.repec.org/a/uwp/jhriss/v25y-1990i4p635-664.html>

⁴⁸ Olga Khazan. Brazil's Government Gives Money to Women Because 'They're More Reliable'. (2014). <https://www.theatlantic.com/international/archive/2014/04/brazils-government-gives-money-to-women-because-theyre-more-reliable/360336/>

As such, this Study proposes that, keeping cultural implications and risks in mind, it is perhaps time to consider the transfer of social assistance to the mothers of the household, with the reasoning being that it could ultimately lead to a targeted fund allocation toward the children, their health, and education.

4.5. ENSURING APPROPRIATE ALLOCATION OF FUNDS- IN-KIND VS. CASH TRANSFERS

There is also another route to consider when it comes to proper allocation of social assistance. While traditionally it is argued that social assistance is best distributed in forms of cash transfers rather than in-kind, it is worth exploring in-kind⁵⁰ transfers as a possibility to ensure appropriate fund allocation.

A possibility could be that families which qualify for social assistance could receive "stamps" or cards like the food stamp program in different countries. These stamps could then be used to buy only domestically produced goods. This policy's purpose would be two-fold: a) make sure that families in need have this type of social net, and b) encourage domestic producers and help them in competing with the international market by boosting national demand.

4.6. GETTING OFF SOCIAL ASSISTANCE: ESCAPING THE POVERTY TRAP

One of the key criticisms of social assistance programs is that people receiving such benefits are stuck in a poverty cycle. To tackle this, one must understand the reasons behind poverty. Chronic poverty is assumed to stem from a combination of poor work opportunities, limited citizenship, insecurity, spatial disadvantages, and social discrimination⁵¹.

⁴⁹ De Walque, Damien B. C. M. ; Akresh, Richard ; Kazianga, Harounan.

Evidence from a randomized evaluation of the household welfare impacts of conditional and unconditional cash transfers given to mothers or fathers (English). Policy Research working paper, no. WPS 7730, Impact Evaluation series, Paper is funded by the Knowledge for Change Program (KCP) Washington, D.C.: World Bank Group. <http://documents.worldbank.org/curated/en/944741467047531083/Evidence-from-a-randomized-evaluation-of-the-household-welfare-impacts-of-conditional-and-unconditional-cash-transfers-given-to-mothers-or-fathers>

⁵⁰ Jesse M. Cunha. Testing Paternalism: Cash vs. in-kind Transfers. American Economic Journal (2014). <https://www.aeaweb.org/articles?id=10.1257/app.6.2.195>

⁵¹ Chronic Poverty Research Centre. Social Assistance and the Dependency Syndrome (2011). <https://www.files.ethz.ch/isn/127203/PB%2022.pdf>

While some of the aforementioned are beyond the scope of this Study, additional policies will be proposed. For example, active labor measures including retraining and job centers that match people with jobs can be implemented to tackle the poor work opportunities component. Every able-to-work individual that receives social assistance can undergo mandatory regular training programs/vocational training to hone their professional skills.

Additionally, focus groups can be formed to identify labor demand needs for specific regions and in return offer training opportunities to the citizens that live nearby in order to skill-match regionally. This would not only help shrink the labor demand-supply gap, but it would also aid in alleviating spatial disadvantages that arise due to lack of work opportunities in rural areas.

Thirdly, the government of Kosovo can provide subsidies to employers that are willing and able to hire social assistance beneficiaries. This subsidy could come in the form of the government paying the employer's monthly share of contribution payments for the employee for a period of up to a year, with possibility of extension. This way, hiring costs to an employer would decrease and as a result they might find it more lucrative to hire people under social assistance. This could further contribute to the reduction of the stigma associated with hiring people living on assistance but at the same time it is an ideal way of ensuring that social assistance recipients do not become dependent on assistance. A similar policy has been adopted in Turkey and so far, has proven fruitful⁵².

Lastly, tailored help is also necessary for social assistance schemes to be temporary. Representatives working with individual families to understand their exact situation that traps them in poverty can help shed light in identifying common themes of impoverishment, which could as a result aid policymaking in better understanding the poverty factors in the country and addressing them.

5. UNEMPLOYMENT BENEFITS

5.1. WHAT ARE UNEMPLOYMENT BENEFITS? ARE THEY EFFECTIVE?

Unemployment benefits are also one of the types of social protection. Depending on how the country has structured them, these benefits can be contributory or non-contributory.

If they are non-contributory, they are often financed from citizens' taxes or employers' taxes and then redistributed to low-income families with unemployed workers. If they are contributory, they are of the form of unemployment insurance, whereby the unemployed contributes financially toward his/her unemployment insurance⁵³.

As such, unemployment benefits can either be of the form of a) Unemployment Assistance- UA (or benefits) are targeted toward poverty reduction for households and b) Unemployment Insurance- UI are targeted toward an individual that has been recently out of the labor market⁵⁴. Because they are fundamentally different from one another, there are sharp contrasts between their effects, especially in the short-term duration. Recipients of UI can be high-income earners but still receive unemployment insurance if they find themselves unemployed. Recipients of UA on the other hand, are limited only to families that are considered low-income after having gone through a means test. However, these differences tend to blur over the longer a person remains unemployed. Because of this, usually a country implements both UI and UA to ensure against poverty⁵⁵.

Unemployment benefits serve as safety net for the society not to fall under a poverty trap. However, one must keep in mind that these benefits need to be targeted and implemented in such a way so as not to risk the possibility of beneficiaries falling into an unemployment spell and losing their incentive to work. Studies point out to a different set of policy solutions to ensure effective unemployment benefits that accurately target the poor. Some of them include a) duration of unemployment benefits and directly linking them to the tenure of employment for the beneficiary and b) net replacement rate of previous earnings when making unemployment redistributions⁵⁶.

5.2. KOSOVO'S LABOR MARKET AND THE INEXISTENCE OF UNEMPLOYMENT BENEFITS

Kosovo is characterized by a high unemployment rate, especially among the youth and women. When compared to the Western Balkan region, Kosovo has the lowest women participation rate (20.8%) and highest youth unemployment rate (49.4%).

⁵² Fikret Adaman and Burcay Erus. New legislation in Turkey to strengthen the link between social assistance and the labour market. (2016). <file:///C:/Users/dvllasaliu/Downloads/ESPN%20-%20Flash%20Report%202016-40%20-%20TR%20-%20July%202016.pdf>

⁵³ Types of Social Protection. Governance and Social Development Resource Centre. <https://gsdrc.org/topic-guides/social-protection/types-of-social-protection/>

⁵⁴ Wayne Vroman. Unemployment Insurance and Unemployment Assistance. (2002). <https://documents1.worldbank.org/curated/en/411271468769849695/pdf/multi0page.pdf>

⁵⁵ Ibid.

⁵⁶ European Semester Thematic Factsheet. Unemployment Benefits. https://ec.europa.eu/info/sites/default/files/file_import/european-semester_thematic-factsheet_unemployment-benefits_en_0.pdf

Moreover, a high share of people working in under-skilled jobs and those not in employment, education, or training -NEET- (32.7%) creates an unstable job market and skilled human capital development⁵⁷. Since the on-set of COVID-19, this situation has probably exacerbated, and its spillover effects are still to be fully observed in Kosovo’s labor market.

The country has made some attempts to target the vulnerable groups when it comes to boosting employment. For example, it has adopted a Youth Employment Action Plan 2018-2020 which partly due to the pandemic and partly to implementation measures has not resulted in any effective measures toward reducing unemployment. There are individuals however that have benefited from Active Labor Market Policies (ALMP)- around 8,694- and in 2019 around 5,138 individuals benefited from Vocational Training Centers (VTC) via their internship programs. However, these numbers are miniscule in targeting unemployment in Kosovo and ensuring those that are in a poverty trap can indeed escape it.

What is even more concerning is the fact that Kosovo does not have passive labor market measures in place- be it unemployment assistance or unemployment insurance- to provide a safety net for those that are suddenly unemployed or have been so for some time⁵⁹. When considering the latest developments in the economy attributed to COVID-19 and quarantine

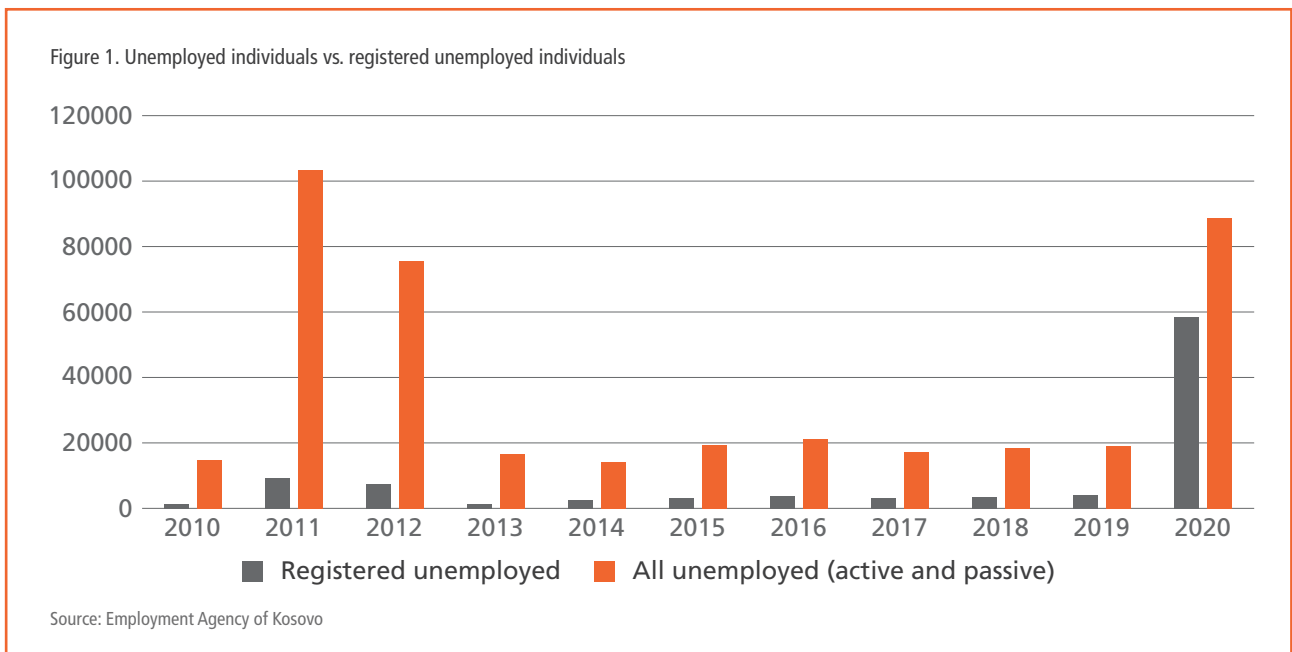
measures, the lack of unemployment benefits has only worsened the vulnerable groups of society and has exposed these groups to even more vulnerability and no income to rely on⁶⁰.

5.3. A PROPOSAL FOR INTRODUCING UNEMPLOYMENT BENEFITS IN KOSOVO

Because unemployment benefits are absent in the country, this Study firstly proposes that such a fund should be established in order to aid the temporarily (as well as the longer-term) unemployed reach some financial security. This is especially the case post-2020 with COVID-19 causing a surge in the unemployment rate.

However, as a first step, it is crucial to ensure that every unemployed person is registered with the unemployment office before they become eligible for benefits.

This is especially necessary given the unemployed dynamics in Kosovo. As Figure 1 shows, while the number of s unemployed individuals in 2020 reached 90,250, only 58,488 (64.8%) are registered as unemployed with the Employment Agency in Kosovo. While this percentage is quite inclusive relative to other years (in 2019, 26% of the unemployed were registered; in 2018, 24.4%, in 2010 only 0.08%), there is still room for improvement.



⁵⁷Evelyn Viertel., Policies for human capital development, Kosovo. A Torino Process assessment, ETF, Turin (2020) available at <https://www.etf.europa.eu/en/publications-andresources/publications/policies-human-capital-development-kosovo-etf-torino>.

⁵⁸Artane Rizvanolli, Ardiana Gashi, and Laurie Joshua. Active labour market measures: Are they effective tools for addressing Kosovo’s skills and employment challenges? Gesellschaft für Internationale Zusammenarbeit (GIZ) Prishtina (2019). Available at <https://yesforkosovo.org/wp-content/uploads/2019/12/Report-ENG.pdf>

⁵⁹ Kosovo. Education, Training, and Employment Developments 2020. European Training Foundation. <https://www.etf.europa.eu/sites/default/files/document/Country%20Fiche%202020%20Kosovo%20Education%20Training%20and%20Employment%20Developments.pdf>

⁶⁰ COVID-19 has challenged Kosovo’s households and businesses in many ways – UN Kosovo Team’s second Socio-Economic Impact Assessment. UNDP (2020). <https://kosovoteam.un.org/en/108425-covid-19-has-challenged-kosovos-households-and-businesses-many-ways-un-kosovo-teams-second>

If established correctly, it can also help the unemployed not to stay unemployed for a long time via skill upgrading for the registered as well as job matching to potential labor demand. The setting up scheme could follow the procedure below:

- 1 Setting the qualifying conditions for the benefit: a) length of previous employment and b) reason behind previous' employment termination, assuming that it was one-sided termination from the employer's side. Quitting should generally not qualify for receiving unemployment benefits as it can create contrary effects on incentives to quit.
- 2 Mandatory registration for the qualifying unemployed with the Employment Agency.
- 3 Skill-matching phase: enrollment and attendance of the unemployed to vocational trainings as a necessary condition to qualify for assistance.
- 4 Implementations of sanctions if an unemployed person is matched to a job but refuses the job and/or if they don't participate in skill-enhancing activities/trainings. Sanctions can range from reducing unemployment benefits to ineligibility for further benefits.
- 5 Re-application for assistance if necessary.

6. CONCLUSION

This chapter has elaborated on Kosovo's current social assistance programs, their pitfalls, as well as has proposed ways which could aid in a better, more efficient distribution of financial resources to those in need. The proposed recommendations include a) increase in eligibility coverage, b) establishment of in-kind and cash transfers with allocation of funds targeted toward the mother as the key unit of the household, and with in-kind transfers being used toward purchase of domestic produce, c) formation of mechanisms such as re-skilling programs and focus group market surveying to identify gaps in labor supply-demand to ensure social assistance is a short-term solution rather than a lifetime choice, d) establishment of a solidarity fund through progressive contributory mechanisms and voluntary donations, and e) a proposed allocation amount for monthly social assistance depending on qualifying criteria.

Next, the chapter has expanded on the need to establish unemployment benefits for Kosovo, focusing on best practices from other countries.

It should be noted that prior to allocation, there are decisions to be made firstly on the replacement rate- the compensation amount of unemployment benefits received as a percentage of average salary when the person was employed. Caution should be applied here when calculating monthly unemployment benefits- it is advisable that benefits received are lower than Kosovo's minimum wage, regardless of recipients' incomes in their previous jobs. The reasoning behind this is simple: workers are encouraged to seek employment, even one that pays a minimum wage, rather than stay idle under the safety of unemployment benefits.

Attention should also be paid to the unemployment benefit duration -median values for developing nations range from 5.8-6.4 months⁶¹. Kosovo can start by applying best practices from other countries. The funding of unemployment benefits can be both from the government as well as from the employer and employee in terms of an unemployment insurance (UI) if the employee is ever out of the job market.

The section has emphasized the need to enroll the unemployed with the employment agency, while ensuring that everyone receiving unemployment benefits is also actively looking for a job and attending vocational trainings to match with a potential job. It has also elaborated on the need to make these benefits a short-term solution by implementing sanctions/ reduction of benefits as well as making them expirable (developing countries' average unemployment benefits last between 5-7 months). Lastly, the proposal includes the need to make sure that unemployment benefits received monthly are lower than the minimum wage of the country in order to stimulate active job seeking.

Overall, the Study sheds light on mechanisms that could be implemented in order to ensure a more just society, with safety nets provided for vulnerable groups, as they attempt to escape the poverty trap and seize in opportunities.

⁶¹ Antonia Asenjo and Clemente Pignatti. Unemployment Insurance Schemes Around the World: Evidence and Policy Options. International Labour Office. (2019) <http://sarkoups.free.fr/lo723778.pdf>

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CHAPTER 4. INCOME INEQUALITY AND FISCAL POLICY

EDISON JAKURTI

1. INTRODUCTION

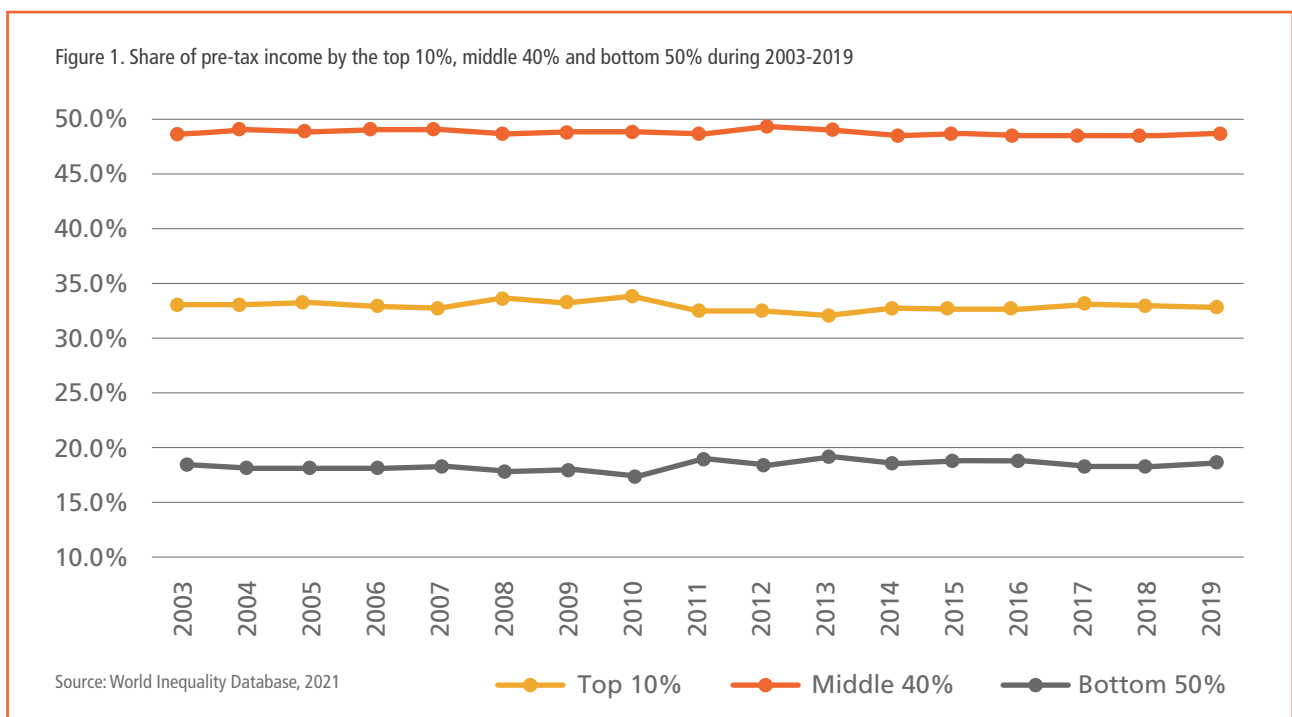
Rising income inequality is a common phenomenon in many countries around the world. There is a growing literature that shows both its magnitude and severity and attempts to diagnose its causes. Unfortunately, such a debate has not found a place in the sphere of public discussions in Kosovo. Indeed, here poverty remains more pronounced as a topic. But poverty is often accompanied by high levels of economic inequality, too. Hence, it should be the duty of any progressive Government to use all its powers to address not only the symptoms but especially the causes of both wealth and income inequality.

In this chapter, for the first time, we provide a detailed picture of income inequality in Kosovo. Specifically, given the data availability, we focus on labor income inequality and distribution. Further, we analyze the degree of progressivity and the redistributive power of the current personal income tax system. Given that all indicators show that there is plenty of room for improvement, we propose a new personal income tax (for both primary and secondary wage earners), a new corporate income tax (for all levels of income), and the introduction of a dividend tax.

2. INCOME INEQUALITY TRENDS IN KOSOVO

While data unavailability or difficulty to obtain remains challenging, there have been attempts to estimate the trends in income inequality in Kosovo. For example, World Inequality Database (WID) includes several statistics about income inequality in Kosovo, too. Figure 1 below shows the trend of the pre-tax income shares by the top 10%, middle 40%, and bottom 50% (of adults) as estimated by WID.

The trends for all three groups have been fairly stable. The bottom 50% has shared around 18%, the middle 40% has shared around 49%, and the top 10% has shared around 33%. If we use these three groups to proxy classes, then one can see that the middle class (i.e., middle 40%) is doing well, the rich (top 10%) are doing extremely well, and the poor (i.e., 50% or half of the adult population) are not doing well at all.



However, these estimates and extrapolations by WID were based on survey data on consumption only, and even the authors give a “Medium Low” score regarding their quality⁶². Moreover, in order to take into account, the redistribute power of the current tax system, post-tax trends are needed as well. Thus, better data are paramount for estimating inequality.

3. LABOR INCOME INEQUALITY

To have a better understanding of inequality in Kosovo, we have obtained detailed tax data on wages, both primary and secondary employers, from the Tax Administration of Kosovo (TAK). While the concept for inequality in Kosovo given the quality⁶² (i.e., tax administration data), the coverage (i.e., around 300 thousand individuals), and its importance in overall income (i.e., salaries constitute for the highest source of income for households and individuals in Kosovo)⁶³. A drawback though is that it covers only the formal economy, hence leaving the informal economy out – which is perceived to be a non-negligible portion. Nevertheless, these data are crucial for assessing not only inequality, with the aforementioned caveat, but also to assess the current personal income tax system from the perspective of progressivity and distribution.

3.1. DISTRIBUTION OF LABOR INCOME

Table 1 below presents the average and the median annual wages, both gross and net, for the period 2016-2020, and the number of wage receivers through TAK. The first observation here is that both the average and the median wage have fluctuated from one year to another⁶⁴. Overall, the average wage has been increasing, while the median has not.

In the case where the average wage is greater than the median, the distribution of wages is positively skewed (or right skewed). That means that we have more than half of the workers earning a wage that is less than the average. In other words, there are some high-wage workers that are raising the average. Such a relation is especially important for tax policy, when progressivity and redistribution are concerned.

Further, the number of wage-earners through the Tax Administration has been increasing. From an optimistic perspective, this could be due to either an increase in employment or in formalization – or both. From a pessimistic perspective, these could be more part-time workers, seasonal workers, or workers that are employed shortly but do not obtain long term contracts. This issue is covered in the robustness check section.

Table 1. Average and median annual wages 2016-2020

	2016		2017		2018		2019		2020	
Wage	Mean	Median	Mean	Median	Mean	Median	Mean	Median	Mean	Median
Gross	€4,903	€3,636	€4,548	€3,291	€5,145	€3,675	€5,006	€3,600	€5,026	€3,507
Net	€4,391	€3,331	€4,073	€3,018	€4,601	€3,360	€4,474	€3,299	€4,492	€3,214
N	280,722		323,600		315,857		350,353		372,607	

Source: Author's own calculations based on data from TAK

3.2. SHARE OF LABOR INCOME BY THE BOTTOM 50%, MIDDLE 40%, AND TOP 10%

Next, we conduct another analysis to see the portions of labor income that go to the bottom 50%, middle 40%, and top 10%⁶⁵. This is shown in Figure 2 below which, again, covers the period between 2016 and 2020. It is remarkable how close these values are to

the ones retrieved from the World Inequality Database, which aims to measure the overall income inequality. Again, this confirms that the labor income inequality is a good proxy for the overall income inequality in Kosovo.

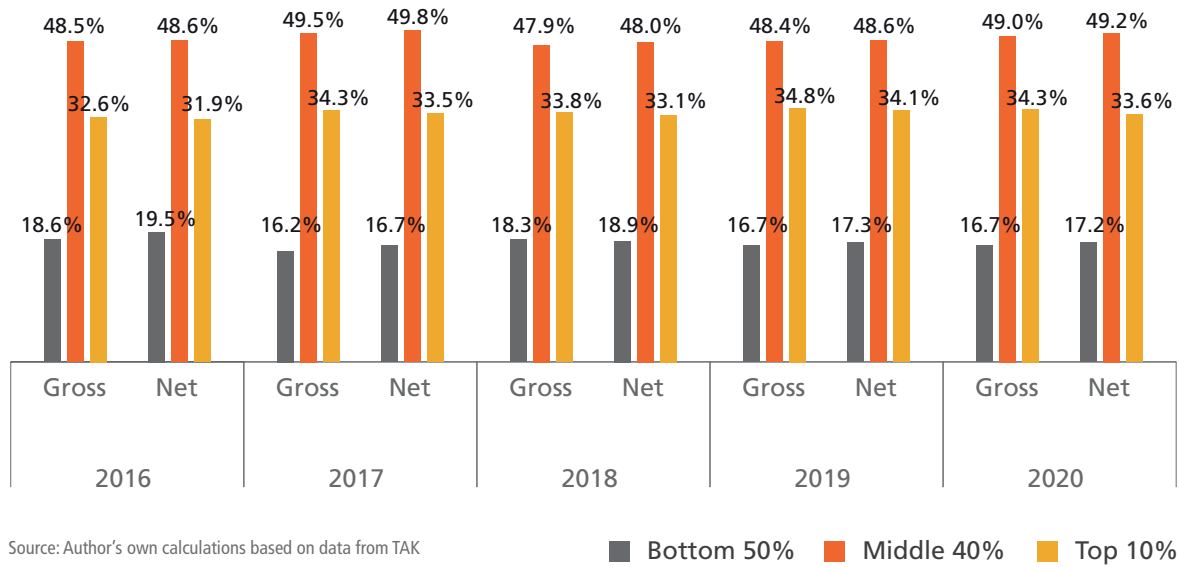
⁶² See Blanchet, Chancel and Gethin (2020).

⁶³ Based on the latest Results of the Household Budget Survey 2017, conducted by Kosovo Agency of Statistics, in 2016 and 2017, wages (from both the private and public sector) were the most important source of income for 51% and 52% of the households, respectively. Also, in 2017, 55% of individuals' income was comprised of wages from the public and private sector.

⁶⁴ The author recognizes the differences between salaries and wages but, for consistency with the terminology used by the Tax Administration, wages is throughout the chapter.

⁶⁵ Labor income in this chapter is defined as the sum of wages earned from both primary (i.e., main job) and secondary employers (i.e., additional, usually short-term work). Data provided by Tax Administration to us did not include information about any other benefits.

Figure 2. Labor income share by the bottom 50%, middle 40%, and top 10%



Over this period, on average, the bottom 50% has shared 17.4% of gross and 17.9% of net labor income. The middle 40% has shared 48.7% of gross and 48.8% of net labor income. And the top 10% has shared 34% of gross and 33.3% of net labor income. So, the personal income tax raises the labor income shared by the bottom 50% by 3.1%, raises the labor income shared by the middle 40% by 0.4%, and lowers the labor income shared by the top 10% by 2.1%. Again, a degree of redistribution is expected from every progressive tax system, however its magnitude, in this case, is quite small.

3.3. ESTIMATING LABOR INCOME INEQUALITY - GINI COEFFICIENT

After analyzing the distribution, we measure inequality by estimating the Gini coefficient, which is one of the most widely used methods for measuring income inequality. Formally, Gini coefficient is defined as:

$$G_x = 1 - 2 \int_0^1 L_x(p) dp$$

where x denotes income and L is the Lorenz curve, which indicates the distribution of income i.e., the proportion of income going to the lowest percentile of population which is arranged from the lowest to

highest income earner. Gini coefficient can take a value between 0 and 1, where the first would indicate perfect equality and the latter perfect inequality. While theoretically possible even at the extremes, in practice, coefficients are between these two values with higher figures indicating more inequality.

Table 2 below measures Gini coefficients for both gross and net salary and the percentage difference between the two for the period 2016-2020. The first observation here is that inequality of labor income has been already high and generally increasing over this period. Second, the difference between the Gini coefficient of gross and net labor income is very small. As expected, unless it is a regressive tax system, the Gini coefficient of net income is expected to be smaller than that of gross income. However, the percentage difference is very small, hence indicating that the current personal tax system has been decreasing inequality but by almost negligible degrees.

Table 2. Gini coefficients of gross and net labor income between 2016-2020

Year	Gross	Net	Change in %
2016	0.4568	0.4478	-1.97%
2017	0.4967	0.4884	-1.67%
2018	0.4692	0.4603	-1.90%
2019	0.4927	0.4842	-1.73%
2020	0.492	0.4832	-1.79%

Source: Author's own calculations based on data from TAK

4. ASSESSING THE PROGRESSIVITY AND THE REDISTRIBUTIVE EFFECT OF THE CURRENT PERSONAL INCOME TAX SYSTEM

Based on the analysis so far, there are several indications that the current personal tax system has not been very effective in reducing inequality. These indications came from the analysis of labor income inequality which, when compared to before and after tax, is reduced by thin magnitudes. So, we now conduct a direct analysis of the progressivity and redistributive effect of the current personal income tax system. To do that, we use two indices: the Kakwani index⁶⁶ and the Reynolds-Smolensky index⁶⁷.

To measure the progressivity of the current personal income tax system, we use the Kakwani index which is formally defined:

$$K_t = C_t - G_x = 2 \int_0^1 [L_x(p) - C_t(p)] dp$$

where C is the concentration index of taxes t and G is the Gini coefficient of pre-tax income x . Kakwani index can take a value between -2 and 1 . Signs show the type of the tax system: negative indicates regressive while positive indicates progressive. The magnitude shows the degree of inequality and tax burden: the lower the value means that there is higher income inequality and a higher tax burden falling on the poorest while the higher the value means that there is lower income inequality and a higher tax burden on the richest.

To measure the redistributive effect of the current personal income tax system, we use the Reynolds-Smolensky index which is also known as the redistributive effect (RE). Basically, it is the difference between the pre-tax and post-tax Gini coefficients. Formally, RE is defined:

$$RE = G_x - G_{x-t} = 2 \int_0^1 [L_{x-t}(p) - L_x(p)] dp$$

where the G_{x-t} is the post-tax Gini coefficient. RE can take values between -1 and 1 . The negative values indicate a regressive tax system, while positive values indicate a progressive tax system. The magnitudes of each indicate the degree to which the system is redistributing to the higher-income earners (if the values are negative) or lower-income earners (if the values are positive).

Table 3 below shows the Kakwani index and the Reynolds-Smolensky index for the period 2016-2020. First, the Kakwani index is positive, which confirms that the current personal tax system is progressive. Also, the Reynolds-Smolensky index re-affirms that given that it is positive. However, in both cases magnitudes are very small. While the potential maximum value of progressivity is 1 , the current personal tax system has had a progressivity value ranging between 0.0715 (the lowest) and 0.0779 (the highest). And, while the potential maximum value of a redistributive system is 1 , over the given period, the current personal income tax system has had a redistributive value ranging between 0.0083 and 0.0091 . Hence, in order to reduce inequality, a more progressive and redistributive system of personal income taxation is needed.

⁶⁶ See Kakwani (1977).

⁶⁷ See Reynolds and Smolensky (1977).

Table 3. The Kakwani and Reynolds-Smolensky indexes of personal income tax system between 2016-2020

Year	Kakwani Index	Reynolds-Smolensky Index
2016	0.0779	0.0091
2017	0.0717	0.0083
2018	0.0756	0.0089
2019	0.0715	0.0085
2020	0.0751	0.0089

Source: Author's own calculations based on data from TAK

5. ROBUSTNESS CHECK

To check the robustness of our results, we modify the sample. In the previous analysis, we included all workers as provided by the Tax Administration. That means that even if someone was paid just once per year, was included. Seasonal workers and those employed short-term might have been included also. This means that there could be a bias in our results. For example, if there were many low-paid workers, who were paid once or twice per month, then our estimations could show a higher magnitude of inequality than it actually is. And this may result in wrong conclusions about the current personal income tax system.

In order to address issues of those nature, we decided to only keep workers who had been paid at least 9 months per year.

This eliminated seasonal workers (who usually work for 3 months) and others who might have been employed short-term. Table 4 below shows the annual average and median wage (both gross and net), the number of workers in the sample, and their portion to the original sample size (i.e., with all the labor income earners). Here we see that, on average, around 72% of the workers met the criteria of having been paid for 9 months or more. More information would be needed to correctly determine about the reason to why the rest 28% worked only 3 months or less. Next, we see that both the annual average and the median are higher, indicating that we have removed some lower-paid workers. Also, over the years, the general trend of both shows an increase. However, their relation remains the same: the average is still higher than the median, indicating a positively skewed distribution.

Table 4. Average and median annual wages of workers who were paid 9 months or more per year

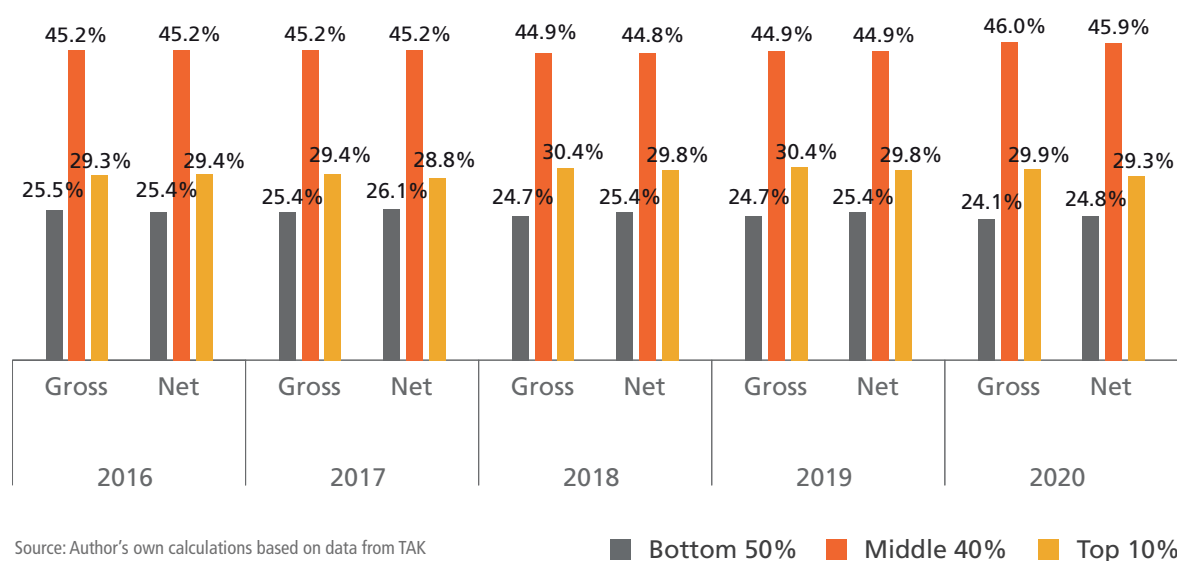
	2016		2017		2018		2019		2020	
	Mean	Median	Mean	Median	Mean	Median	Mean	Median	Mean	Median
Gross	€6,008	€ 5,070	€ 6,056	€ 5,057	€ 6,372	€ 5,240	€ 6,526	€ 5,311	€ 6,532	€ 5,165
Net	€ 5,376	€ 4,588	€ 5,420	€ 4,573	€ 5,693	€ 4,735	€ 5,827	€ 4,800	€ 5,832	€ 4,675
N	212,095		222,435		234,776		245,001		263,549	
%	75.55%		68.74%		74.33%		69.93%		70.73%	

Source: Author's own calculations based on data from TAK

The composition of distribution among the bottom 50%, middle 40%, and top 10% has remained stable also. As shown in Figure 3 below, over this period, on average, the bottom 50% has shared 24.9% of gross and 25.4% of net labor income. The middle 40% has shared 45.2% of gross and 45.2% of net labor income. And the top 10% has shared 29.9% of gross and 29.4% of net labor income.

So, the personal income tax raises the labor income share of the bottom 50% by 2.1% (it was 3.1% in the full sample), does not affect much the labor income shared by the middle 40% (it raised by 0.4% in the full sample), and lowers the labor income shared by the top 10% by 1.3% (it lowered by 2.1% in the full sample).

Figure 3. The share of labor income held by the bottom 50%, middle 40%, and top 10% among workers who were paid 9 months or more per year



So, indeed the share held by the top 50% has increased but, given that the change in net income lowered, it happened so because of the removal of some lower-paid workers. On the other hand, the share held by the top 10% decreased, but so did the difference between their gross and net income. These results indicate once again that the progressivity degree and the redistributive effect of the current personal income tax system are low.

Further, another indication that we have removed some outliers can be seen in the Gini coefficients. As shown in Table 5 below, both the gross and net coefficients are lower. While the percentage difference between the two has increased compared to the previous analysis, it still remains low. Yet again indicating that there is room for enhancing the redistributive power of the current personal tax system.

Table 5. Gini coefficients of gross and net labor income of workers who were paid 9 months or more per year

Year	Gross	Net	Difference
2016	0.3666	0.3561	-2.86%
2017	0.3687	0.3582	-2.85%
2018	0.3812	0.3708	-2.73%
2019	0.3816	0.3713	-2.70%
2020	0.3854	0.3748	-2.75%

Source: Author's own calculations based on data from the TAK

Finally, Table 6 below shows the Kakwani and Reynolds-Smolensky indices. Unsurprisingly, given the previous checks, both indices have slightly increased. They indicate a slightly higher progressive and redistributive tax system.

Nevertheless, the miniscule magnitudes still indicate that, if one aims to reduce labor income inequality, then there is plenty of room to enhance both progressivity and redistributive effect of the personal income tax system.

Table 6. The Kakwani and Reynolds-Smolensky indices of personal income tax system between 2016-2020

Year	Kakwani Index	Reynolds-Smolensky Index
2016	0.0898	0.0105
2017	0.0891	0.0104
2018	0.0873	0.0104
2019	0.0862	0.0103
2020	0.0886	0.0106

Source: Author's own calculations based on data from Tax Administration

6. A NEW FISCAL POLICY

Reducing income inequality and concentration should be a key fiscal policy of any progressive Government. From our analysis, based on the data from TAK, we have estimated labor income inequality and distribution, and we have assessed the progressivity degree and the redistributive power of the current Personal Income Tax policy.

Differences between Gini coefficients of gross versus net labor income indicate a not-so-effective system in terms of inequality reduction. Such an indication becomes more vivid when we analyze the progressivity degree measured by the Kakwani Index and the redistributive power measured by the Reynolds-Smolensky Index. Albeit the tax schedule is progressive, the degree of progressivity is relatively low and the redistribution power even lower.

Further, the analysis including all labor income earners shows that, while the share of gross income by middle 40% is robust, the income shared by the 10% is around double the share owned by the bottom 50%. The post-tax structure shows small changes, with a small degree of increase of the share owned by the bottom 50%, a miniscule increase of the share owned by the middle 40%, and a negligible decrease of the share owned by the top 10%.

In order to reduce such high levels of inequality and concentration of income at the top, we propose a new Personal Income Tax policy which is more progressive, more effective in reducing inequality and redistributes more. In order to provide a comprehensive approach, we propose a new Corporate Income Tax policy along with the introduction of a Dividend Tax.

6.1. A NEW PERSONAL INCOME TAX

The current Personal Income Tax in Kosovo, with a few exceptions, applies to all sources of income, with wages being one of the main ones. For that reason, and given the data provided by TAK, we focus here on labor income.

There are a few simple details that make the whole system fairly easy to comprehend. Gross income consists of a 5% pension contribution made by the

employer and a 5% pension contribution made by the worker. The remaining after a 5% deduction from gross income is then considered taxable income. For wages from primary employers i.e., main jobs, a progressive tax with brackets and margins as shown in Table 7 applies. For wages from secondary employers i.e., additional, mostly short-term jobs, a proportional tax of 10% applies.

Table 7. Current Personal Income Tax schedule

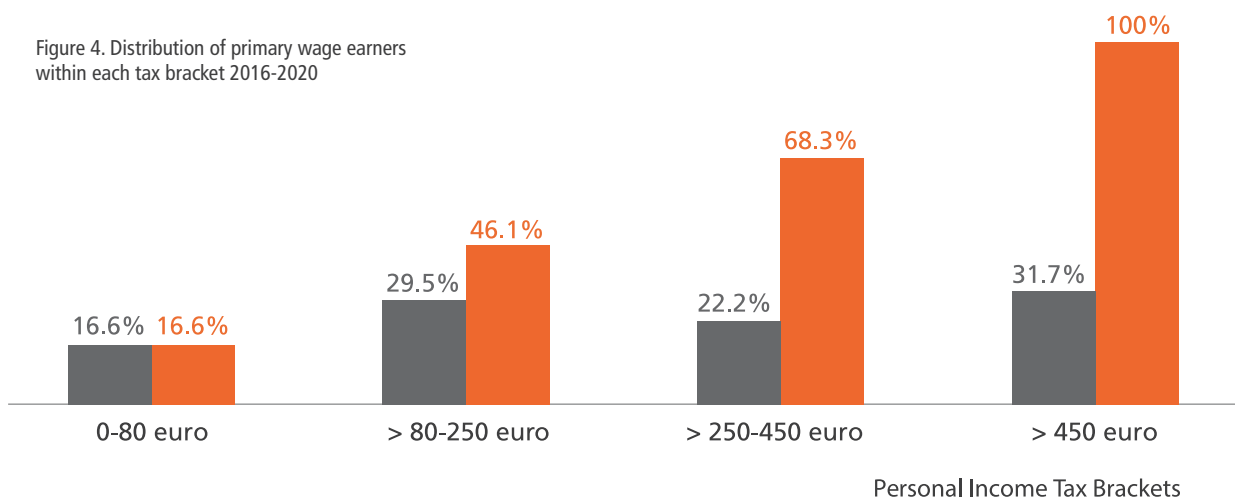
Monthly taxable labor income	Tax rate
€0 – €80	0%
> €80 – €250	4%
> €250 – €450	8%
> €450	10%

Source: Tax Administration

Figure 4 below shows the distribution and cumulative distribution of wage earners that fall within each tax bracket. There are two important observations regarding the extremes. On one hand, the current Personal Income Tax exempts only 16.6% of primary wage earners, which consists of workers than earn up to €80 per month – a very low threshold.

On the other hand, the top marginal rate, which is 10%, applies to 31.7% of primary wage earners who earn a wage of more than €450 per month – again, a very low threshold. These are additional indications that this tax schedule is not designed to reduce inequality since it exempts very few very-low earners and levies the top marginal rate above a very low threshold, too.

Figure 4. Distribution of primary wage earners within each tax bracket 2016-2020



Source: Tax Administration

■ Distribution of wage earners ■ Cumulative distribution of wage earners

As all the analyses done so far have shown, the current tax policy has not been very effective in reducing income inequality and concentration. Hence, we set a number of objectives which must be fulfilled by a new tax. A new Personal Income Tax should:

1. Be more progressive for wages from primary employers and progressive (instead of proportional) for wages from secondary employers;
2. Reduce income inequality more than the current tax;
3. Reduce concentration/increase redistribution more (i.e., post-tax income share increases for the poor and the middle class, and decreases for the rich);

4. Not reduce revenues;
5. Result in a net gain (i.e., “winners” >50%).

A tax schedule that fits all of these objectives is presented in Table 8. This is our proposal for wages from primary employers. As can be noted, there are major differences in the number and width of the brackets, and marginal rates. While the “old” tax schedule is progressive in, mostly, the bottom half of the distribution, it lets the upper half “enjoy” most of their labor income through a proportional tax of 10%. The proposed tax schedule follows the opposite logic: the bottom half of the labor income earners are completely exempt from tax, and progressivity begins approximately on the upper half of the distribution.

Table 8. New Personal Income Tax schedule for wages from primary employers

Monthly taxable income	Tax rate
€0 – €300	0%
> €300 – €550	8%
> €550 – €800	14%
> €800 – €1,050	20%
> €1,050 – €1,300	26%
> €1,300 – €1,800	32%
> €1,800	38%

Source: Author’s own calculations based on data from the Tax Administration

As explained earlier, wages from secondary employers are currently taxed proportionally at 10%. We propose a new tax that is progressive. Because there are much fewer earners of these wages – only 8% of the earners in the last 5 years, and because these

is secondary income, we propose narrower brackets and higher rates. Again, we exempt from tax the overwhelming majority and target the very-high income earners.

Table 9. New Personal Income Tax schedule for wages from secondary employers

Monthly taxable income	Tax rate
€0 – €100	0%
> €100 – €250	9%
> €250 – €400	15%
> €400 – €550	21%
> €550 – €700	27%
> €700 – €850	33%
> €850	39%

Source: Author's own calculations based on data from the Tax Administration

An example of what would this mean in practical terms is given in Table 10 below. The first column shows the rates. The second shows gross income brackets. The third shows pre-tax (i.e., taxable income) which is gross income less the employer's contributions. The fifth column shows the net labor income of the highest earner (i.e., upper bracket) in the "old" tax schedule.

The sixth column shows what the same person would earn in the "new" tax schedule. The seventh column shows the difference between net labor income from the "new" tax less the one from the "old" tax. And the eighth column shows the cumulative distribution of labor income earners in each bracket for the period 2016-2020.

Table 10. Effects of new tax on income from primary wages

Tax rate	Gross		Pre-tax	Net BEFORE	Net AFTER	Difference in Net	Cumulative Distribution
0%	€ -	€ 315.8	€ 300.0	€ 289.2	€ 300.0	€ 10.8	53.3%
8%	€ 315.8	€ 579.0	€ 550.0	€ 517.2	€ 530.0	€ 12.8	80.5%
14%	€ 579.0	€ 842.1	€ 800.0	€ 742.2	€ 745.0	€ 2.8	91.8%
20%	€ 842.1	€ 1,105.3	€ 1,050.0	€ 967.2	€ 945.0	€ (22.2)	95.9%
26%	€ 1,105.3	€ 1,368.4	€ 1,300.0	€ 1,192.2	€ 1,130.0	€ (62.2)	97.5%
32%	€ 1,368.4	€ 1,894.7	€ 1,800.0	€ 1,642.2	€ 1,470.0	€ (172.2)	98.9%
38%	€ 1,894.7	€ -	€ -	€ -	€ -	€ -	100.0%

Source: Author's own calculations based on data from the Tax Administration

The last two columns show the most important statistics of this table. First, with our proposal, over half (53.3%) of the labor income earners would be exempted from tax. Second, earners of gross wages up to €842.1 would receive a higher net wage than in the "old" tax schedule. In other words, 91.8% of the labor income earners would receive higher net wages than they currently do. The next 4.1% would receive a net wage that could, at the maximum, be €20.2 lower than the one they currently receive. And it would be the top 4.1% i.e., the ones whose gross monthly wages begin at €1,368.4 that would bear a heavier burden of this new tax policy.

Table 11 below mimics the previous one but now with statistics for wages earned from secondary employers. Again, the last two columns show the most important figures. Here, 99.1% of the distribution would earn a higher net wage than they currently do. It would be only the top 0.9% or the ones whose monthly secondary wage is €421.1 or higher that would receive a lower net wage than they currently do.

Table 11. Effects of new tax on income from secondary wages

Tax rate	Gross		Pre-tax	Net BEFORE	Net AFTER	Difference in Net	Cumulative Distribution
0%	€ -	€ 105.3	€ 100	€ 90	€ 100.0	€ 10.0	97.1%
9%	€ 105.3	€ 263.2	€ 250	€ 225	€ 250.0	€ 11.5	98.5%
15%	€ 263.2	€ 421.1	€ 400	€ 360	€ 400.0	€ 4.0	99.1%
21%	€ 421.1	€ 579.0	€ 550	€ 495	€ 550.0	€ (12.5)	99.4%
27%	€ 579.0	€ 736.8	€ 700	€ 630	€ 700.0	€ (38.0)	99.6%
33%	€ 736.8	€ 894.7	€ 850	€ 765	€ 850.0	€ (72.5)	99.7%
39%	€ 894.7	€ -	€ -	€ -	€ -	€ -	100.0%

Source: Author's own calculations based on data from the Tax Administration

What is the effect of this new tax on income inequality? To answer that, we have empirically estimated Gini coefficients for gross labor income, pre-tax income i.e., taxable income, net before, and net after the implementation of the new tax, as shown in Table 12. The last two columns show percentage changes of Gini coefficients between pre-tax and net before, and pre-tax and net after, respectively.

The difference is obvious: differences between net labor income before and after show that the new tax is much more effective in reducing income inequality than the current tax. If we divide the percentage change of the Gini coefficient after the new tax with the change in coefficient before the new tax, we see that the new tax is 3 times more effective in reducing inequality.

Table 12. Comparison of Gini coefficients before and after new tax

Year	Gross	Pre-tax	Net Before	Net After	Change Before	Change After
2016	0.4568	0.4573	0.4478	0.4302	-2.1%	-5.9%
2017	0.4967	0.4973	0.4884	0.4716	-1.8%	-5.2%
2018	0.4692	0.4699	0.4603	0.4401	-2.0%	-6.3%
2019	0.4927	0.4932	0.4842	0.4646	-1.8%	-5.8%
2020	0.492	0.4925	0.4832	0.4643	-1.9%	-5.7%
Overall	0.4832	0.4837	0.4744	0.4557	-1.9%	-5.8%

Source: Author's own calculations based on data from the Tax Administration

Moreover, we estimate the Kakwani Index and Reynolds-Smolensky Index of the current versus new tax. The ratio of Kakwani Indices shows that the new tax is around 3 times more progressive than the current one. Also, the ratio of Reynolds-Smolensky Indices shows that the new tax is almost 3 times more redistributive than the current one.

Table 13. Comparison of progressive degree and redistributive power of the old and new tax

Year	Before		After		Ratios	
	Kakwani Index	Reynolds-Smolensky Index	Kakwani Index	Reynolds-Smolensky Index	New Kakw. / Old Kakw.	New RS/ Old RS
2016	0.1542	0.0096	0.4016	0.0271	2.6	2.8
2017	0.1425	0.0088	0.3755	0.0257	2.6	2.9
2018	0.1491	0.0095	0.3934	0.0297	2.6	3.1
2019	0.1396	0.009	0.3735	0.0286	2.7	3.2
2020	0.1456	0.0093	0.3709	0.0282	2.5	3.0
Overall	0.146	0.0093	0.382	0.028	2.6	3.0

Source: Author's own calculations based on data from the Tax Administration

After confirming that the new tax is more progressive and redistributive than the old one, we estimate changes in income concentration. This is another way to see the redistributive power of the tax. Again, our aim is to reduce income concentration at the top by redistributing it to lower-income earners.

Table 14 below shows the pre-tax, net (current) and net (before) income shared by the bottom 50%, middle 40% and top 10% - as three proxies for low-income, middle-income, and high-income class. As shown in the fourth column, the current tax reduces the income shared by the top 10% by 2.3% and

increases the income of middle 40% and bottom 50% by 0.5% and 3.2%. The new tax, on the other hand, as shown in the fifth column, reduces the income shared by the top 10% by 9.2%, and raises the income of middle 40% and bottom 50% by 3.9% and 7.3%, respectively. Finally, the last column shows the difference between the two tax policies. The new tax raises the income share of the bottom 50% by 3.9% more than the current tax; it raises the income of the middle 40% by 3.4% more than the current tax; and it reduces the income of the top 10% by 7% more than the current tax.

Table 14. Comparison of changes in income concentration by different income groups

Tax rate	Pre-tax	Net (Before)	Net (After)	Change in percent		
	(A)	(B)	(C)	(B-A)/A	(C-A)/A	(C-B)/B
Bottom 50%	17.3%	17.8%	18.5%	3.2%	7.3%	3.9%
Middle 40%	48.6%	48.8%	50.4%	0.5%	3.9%	3.4%
Top 10%	34.2%	33.4%	31.0%	-2.3%	-9.2%	-7.0%

Source: Author's own calculations based on data from the Tax Administration

The last criteria for evaluating our tax policy is to determine its effects on revenues. When we apply this system for each year from 2016 to 2020, we find that actually revenues would have been higher if this system had been in place. For each year, revenues would have been 7.6%, 8.9%, 16.2%, 16.6%, and 17.1%,

respectively, higher than they were with the current tax schedule. So, we can conclude that besides being more progressive, reducing inequality and increasing redistribution more than the current system, our tax policy proposal would also raise more revenues.

6.2. A NEW CORPORATE INCOME TAX

In our proposal, the top marginal tax rates for primary increases from 10% to 38% - which is 3.8 times higher. For secondary income, which has a proportional tax of 10%, we change it into a progressive tax with a top marginal rate of 39% - which is 3.9 times higher. The average tax rate increases from around 6% to around 6.8%. And the average statutory tax increases from 5.5% to around 19.7%.

The current Corporate Income Tax is 10% for businesses with an annual income of over €50,000; 3% and 9% (depending on the sector) for those with an income of €50,000 or lower. The changes in corporate income tax should also reflect the changes proposed for the personal income tax.

Hence, we suggest that the top corporate tax rate should be no lower than the average statutory personal income tax rate. In this case, the corporate income tax would increase from 10% to 20%. Given that the two other rates apply to smaller businesses, the increase should be lower. So, we suggest a 50% increase of the top rate for the lowest rate and approximately 75% for the middle rate. That means that the lowest rate would increase to 4.5% and the middle would increase to 16%.

6.3. INTRODUCING A DIVIDEND TAX

Currently there is no dividend tax in Kosovo. The only two countries that do not have a dividend tax in the EU are Estonia and Latvia⁶⁸. All other OECD European countries and all other Western Balkan-6 countries have a dividend tax. As shown earlier, labor income inequality in Kosovo has been persistently high. And overall income inequality, which includes other types of income such as capital, could be even higher knowing that these other types are usually concentrated in fewer hands than those of wages. So, both from examples in other countries and from an egalitarian perspective, given that even low-income earners and small business have been paying taxes, but super-rich shareholders have been exempted, a dividend tax should be introduced. Again, it should be no lower than the average statutory personal income tax, which means that no lower than the corporate income tax, either. As such, we suggest that the dividend tax to be 50% higher than the corporate income tax, which would make it 30%. Combined with the Corporate Income Tax we proposed, this rate ensures that a dividend-earner would pay more taxes than a wage-earner.

7. CONCLUSIONS

Small differences in Gini coefficients between gross and net labor income are an indication that the current personal income tax is not an adequate mechanism for reducing inequality. Moreover, the ratio of income shares between the rich (e.g., top 10%) and the poor (e.g., bottom 50%) is around two, indicating a high concentration of labor income at the top. The Kakwani and the Reynolds-Smolensky indices further confirm the low progressive degree and the impotency of the current personal income tax system to redistribute.

In order to reduce labor income inequality and increase redistribution, without hurting revenues and resulting in a net gain, we proposed a new personal income tax that follows a different logic, utilizes different brackets and applies different marginal rates from the current one. Further, we ensured that these changes in the personal income tax are paralleled with changes in corporate income tax. As such, we proposed a 100% increase of that. Lastly, both based on practices in almost all countries around, and from an egalitarian perspective, we proposed the introduction of a dividend tax which would both help reduce the overall inequality and generate a new stream of revenues for the Government.

⁶⁸ See Elke (2021).

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SECTION III: ECONOMIC STRUCTURE AND INDUSTRIAL POLICY

CHAPTER 5. GDP AND TRADE BALANCE STRUCTURE OVERVIEW

LULE BAHTIRI

1. INTRODUCTION

Gross Domestic Product is considered one of the most important measures regarding the performance of the economy in Kosovo. GDP⁶⁹ contains the market value of all final goods and services produced within a country for a certain period, usually a year. Although, there are numerous pitfalls that can be addressed to GDP regarding the real presentation of an economy, it is one of the only comprehensive measures of national output.

There are three different approaches to calculating the GDP: expenditure approach, value-added approach, and income approach. For the purposes of this chapter, only the first two approaches will be elaborated. The two approaches provide a deeper understanding of the industry and trade balance in Kosovo,

which remains negative throughout the years. An important factor in the Kosovo economy is aggregate spending, which will provide an understanding of the importance of diaspora and their remittances.

2. THE EXPENDITURE APPROACH TO GDP

The Expenditure Approach⁷⁰ to calculating GDP consists of overall purchases in a resident economy for a certain period, usually a year. Specifically, it includes consumption of goods and services, gross capital formation, government expenditure, and net exports. Due to data availability, this is the most popular approach used in Kosovo.

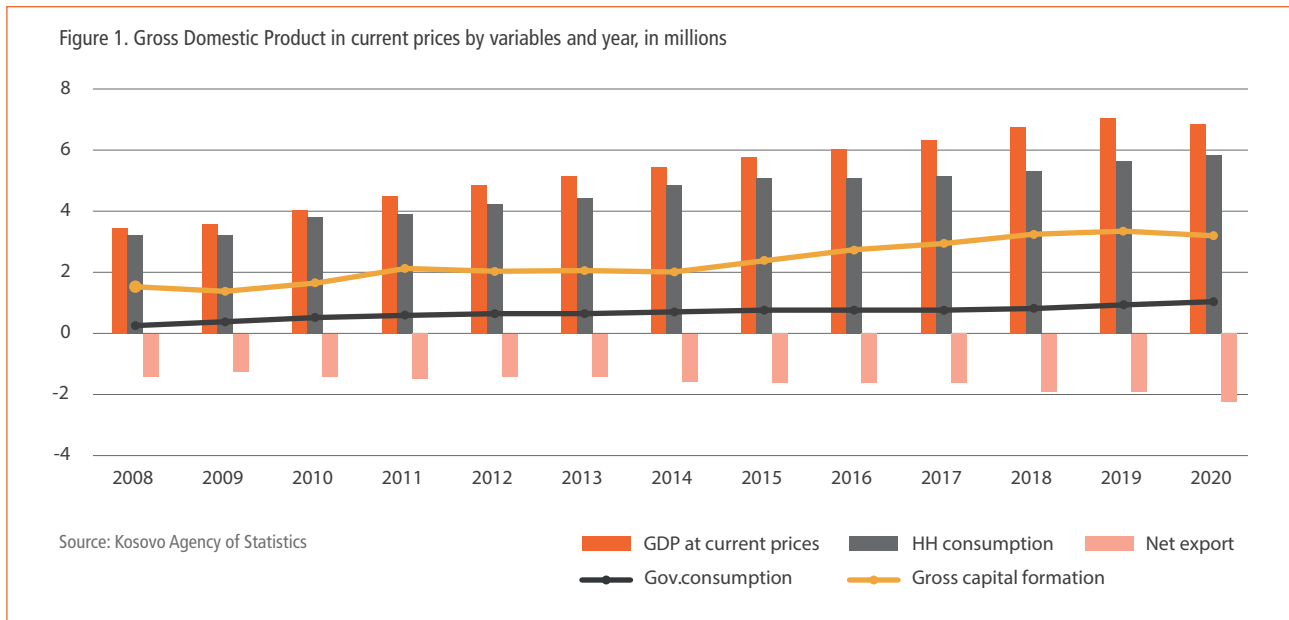


Figure 1 shows time series values for GDP⁷¹ measured through the expenditure lens. As theory suggests, consumption is the largest component in Kosovo’s

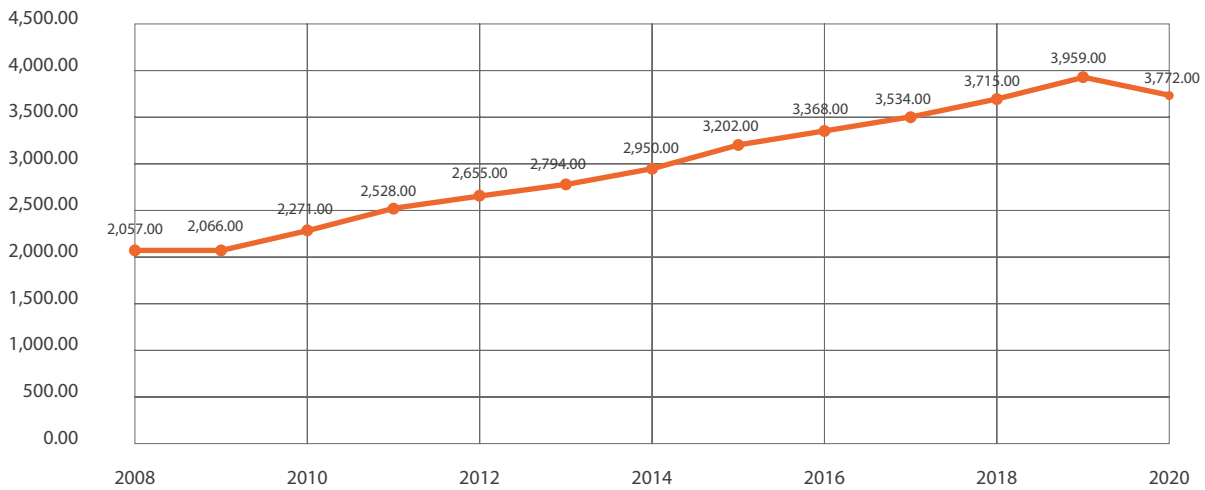
GDP. However, although final consumption remains the dominant category, it has experienced a downwards trajectory through 2010-2019. Second component, government expenditures, have remained stable through the period, with very small fluctuations.

⁶⁹ GDP always includes nominal GDP, unless stated otherwise.
⁷⁰ See more detailed explanation on GDP measurement approaches at Lumen Boundless Economics <https://courses.lumenlearning.com/boundless-economics/chapter/measuring-output-using-gdp/>

Finally, net exports balance is constantly negative in Kosovo, implicating that for a period of one year, Kosovo's imports of goods and services outweigh the value of exports. Although the Figure shows improvement for the period of 2010-2017, there is another downfall which begins in 2018. This implies a strong dependency of Kosovo on foreign products and makes our market especially vulnerable to any international crisis.

The expenditure approach provides a general view of a country's economy, and it goes as far as providing an average expenditure value for every citizen in the country (GDP per capita⁷², shown in Figure 2). Nevertheless, it does not provide the real impact of the GDP's growth or decline over the years. Other components such as real growth rate will provide a different picture regarding the standard of living in Kosovo.

Figure 2. Gross Domestic Product per capita in €, 2008-2020

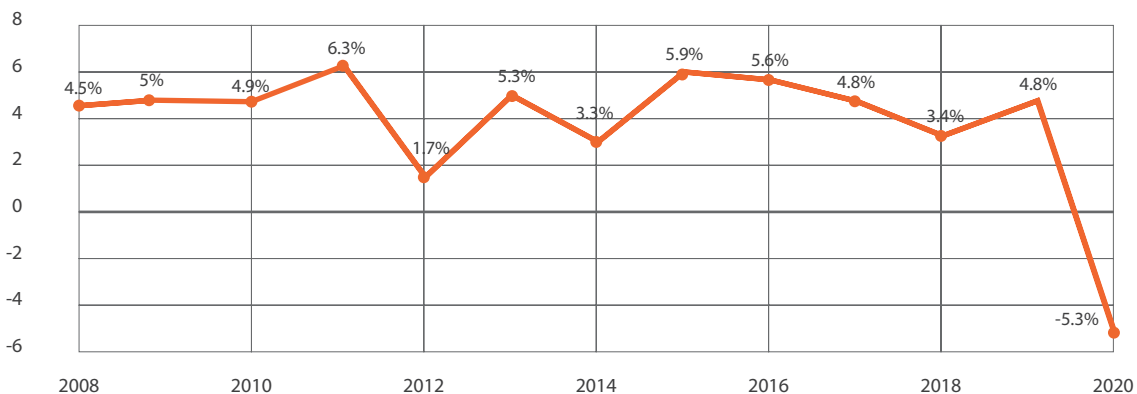


Source: Kosovo Agency of Statistics

The increase of GDP per capita has been stable through the years, excluding 2020. Based on these data and according to World Bank classifications, Kosovo is now an upper-middle income country. However, these values are presented in nominal

values and do not represent the real growth or real effect of GDP values in people's lives. According to the numbers published by the Kosovo Agency of Statistics (KAS), the real growth trajectory follows a less linear path and even experiences decrease at times.

Figure 3. Real growth rate, 2008-2020



Source: Kosovo Agency of Statistics

⁷¹Kosovo Agency of Statistics, Gross Domestic Product in current prices by variables and year, from 2008-2020, <https://ask.rks-gov.net/en/kosovo-agency-of-statistics/add-news/gross-domestic-product-by-economic-activities-and-expenditure-approach-2008-2020>

⁷²Kosovo Agency of Statistics, Gross Domestic Product in current prices by variables and year, from 2008-2020, <https://ask.rks-gov.net/en/kosovo-agency-of-statistics/add-news/gross-domestic-product-by-economic-activities-and-expenditure-approach-2008-2020>

Variations in GDP⁷³ imply that although in nominal terms the Kosovo GDP increased steadily, the real growth received quite some hits during the years, meaning the quality of life in Kosovo got worse during this period.

3. THE VALUE-ADDED APPROACH TO GDP

The value-added approach⁷⁴ to measuring GDP includes the sum of gross value added for all economic activity and calculated with base prices, plus taxes minus product subsidies⁷⁵. In other words, value added approach measures an industry's production value minus intermediate consumption. This is an important approach for Kosovo's future policies in industry development. The numbers show how large, in terms of GDP, different industries are in Kosovo. In this way, in times of crisis, the industries that are larger in size will have a bigger impact as compared to the smaller ones. However, the smaller industries are also crucial and must be supported in growth.

According to KAS data, the three largest industries/sectors in Kosovo are the processing industry and wholesale and retail trade, and agriculture, hunting, forestry, and fishing. Although the trend for these industries seems stable, production/output in these industries decreases slowly through the years.

Moreover, according to a recent study measuring the impact of COVID-19 in the private sector, the first two industries have been hit the hardest by the pandemic (Jakurti et al., 2020), implying that the impact in the GDP will be significant. For policy purposes, it is important to know whether these industries are being replaced and if yes, by what, and how can we balance other industries' growth without harming the existing ones.

4. REMITTANCES

Worker's remittances are considered financial flows from Kosovar citizens living abroad to their families in Kosovo. Although remittances do not count directly towards GDP, they carry a significant importance in the economy. The consumption category in the GDP formula is significantly influenced by remittances. In fact, the average annual inflow of remittances in Kosovo nears 15% of the total GDP.

Compared to regional countries during 2019, Kosovo tops the list, followed by Bosnia and Herzegovina (11.2%), Montenegro (10.54%), Albania (9.63%), Serbia (8.23%), Croatia (6.64%), and North Macedonia (2.53%)⁷⁶. During 2020, remittances reached record values in Kosovo. For the first time, the monthly value of inflows from diaspora surpassed 100 million euros in April 2020. Significant portion of this value was provided to help families overcome the COVID-19 crisis. Nevertheless, remittances are mostly spent on consumption and real estate, with little to no prior institutional effort to alter this behavior, and direct diaspora money to other investments that promote real growth.

5. FOREIGN DIRECT INVESTMENT

Foreign Direct Investment (FDI) fluctuates more than other categories elaborated in previous sections. Very often, especially for developing countries, theories suggest that FDI affects growth positively. Along with capital inflow, FDI also brings management know-how and technological innovation. In Kosovo, in terms of flows, real estate dominates FDI comprising more than half of the total value. Moreover, Central Bank of Kosovo (CBK) data show that Germany and Switzerland are the largest partners investing in Kosovo. This reveals additional importance of Kosovar diaspora, who invest in their home country. While it is important to invest in real estate, the fact that it dominates FDI diminishes its role in creating sustainable jobs, sharing management know-how or bring innovation. Real estate category is followed by financial services as well as mining and quarreling. On the other hand, investment of Kosovars abroad never surpasses 20% of investments in Kosovo. Therefore, the real impact of FDI in Kosovo is smaller than its value.

6. TRADE BALANCE

Current Account balance in Kosovo is negative from 2004, when the state started quantifying it. The current account is comprised of goods, services, primary and secondary income (income from general government and financial and nonfinancial corporations, households, etc.). Nevertheless, the major contributor of the negative value in current account balance remains balance in goods.

⁷³ Kosovo Agency of Statistics (2021). Review of National Accounts 2008-2020, <https://ask.rks-gov.net/media/6311/bpv-2008-2020.pdf>

⁷⁴ Detailed explanation on GDP measurement approaches can be found at Lumen Boundless Economics <https://courses.lumenlearning.com/boundless-economics/chapter/measuring-output-using-gdp/>

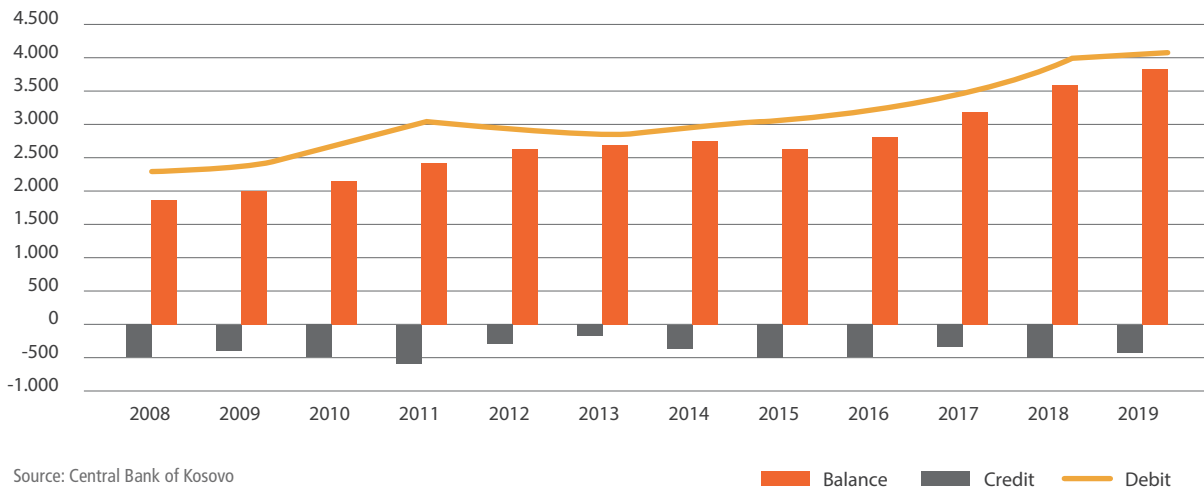
⁷⁵ Kosovo Agency of Statistics (2021). Review of National Accounts 2008-2019, <https://ask.rks-gov.net/media/6003/publikimi-i-revidim-it-te-2008-2019.pdf>

⁷⁶ The Global Economy. (2019 data). Remittances, percent of GDP - Country rankings, https://www.theglobaleconomy.com/rankings/remittances_percent_gdp/

Although exports are less than imports every year since 2004, they haven't been increasing at a much higher rate than imports. A slight break in the cycle occurred during 2020, when exports increased by more than usual. For instance, while exports only covered 12 or 13% of imports until 2019, in 2020 exports covered around 17% of imports. Moreover, a short

analysis for country partners shows a huge increase of exports in the United States (644%), China (444%), Egypt (185%) and Hungary (98%). Provided that the increase in exports occurred during the year of the pandemic, it remains to be seen whether this was a one-time thing or a stable, positive trend.

Figure 4. Current Account Transactions, 2008-2019⁷⁷ (in millions €)



Trade balance in services has been positive from 2006 implying an increasing trend in export of services. We temporarily exclude 2020 from the analysis, due to COVID-19 restrictive measures which immediately affected reduction in the travel category and does not provide a real indicator of a repetitive pattern in exports of services. Recent World Bank research indicates that for developing countries, investment in services is positive towards growth, as services can help in developing manufacturing as well through improved technology and know-how⁷⁸.

6.1. THE IMPACT OF COVID-19 ON THE TRADE BALANCE

While the effect of COVID-19 in general seems to be negative, the data on trade balance tell a somewhat different story. Speaking in GDP terms, Kosovo appears to have gone back almost three years, and the private sector reports significant losses in annual turnover and profits, as well as significant layoffs (Jakurti et al., 2020). Trade balance of goods on the other hand, has improved.

According to official statistics, exports of goods has increased by 21%⁷⁹ during 2020- one the largest increases in this category; while import of goods has decreased by 6%- the largest decrease in imports in over six years. Meanwhile services category experienced a record decrease of almost 60%. While almost all items in the services category decreased slightly, travel services seem to have been hit the hardest with 60% downfall. This is within reason, as during the second quarter, Kosovo was in total or in part isolated. One of the only categories that experienced a significant increase of 155% is telecommunication, computer, and information services. This was witnessed around the world, as isolation incentivized use of on-line platforms. The good news is that Kosovo keeps exporting services that rely on high-skilled labor and should make use of it for domestic economy as well.

6.2. TYPES OF EXPORTS AND IMPORTS

To understand the growth model of a country, one must look beyond the numbers regarding exports or imports. What is also crucial is the structure of export and import. In research conducted by Levy Institute, richer countries export mostly "good" products, which include goods that are mainly man-made and require high-skilled labor; while poorer countries

⁷⁷ Central Bank of Kosovo (2020). Balance of Payments Current Account, <https://bqk-kos.org/statistics/time-series/?lang=en>

⁷⁸ Nayyar, Gaurav; Hallward-Driemeier, Mary; Davies, Elwyn (2021). At Your Service? The Promise of Services-Led Development. Washington, DC: World Bank. © World Bank. <https://openknowledge.worldbank.org/handle/10986/35599>

⁷⁹ Includes re-exports

export mostly “bad” products which include goods that are mainly nature-made and require low-skilled labor⁸⁰. According to the research, the latter countries find it very difficult to achieve sustained growth in the long term and remain caught in a middle-income trap. Throughout this section, we will explore the nature of exports and understand that Kosovo’s main basket of export goods is comprised of “bad” products, with a smaller number a goods exported belonging to the “good” category. We also explore the “good” products that Kosovo imports as well as the main trade partners.

6.2.1. EXPORTS AND IMPORT CLASSIFICATION

According to the data published by the Central Bank of Kosovo and based on EU categorization, there are 11 main categories of exports. The biggest export categories in Kosovo include (i) base metals and articles of base metal, (ii) plastics, rubber, and articles thereof, (iii) prepared foodstuffs, beverages, and tobacco. In other words, Kosovo mainly exports raw materials, or goods with no added value. It is important to note that raw materials are sold at their lowest price; trade partners who import these goods then process them and sell them at a much higher price.

As for trade partners, the European Union is Kosovo’s biggest exporting partner, based on the total value sold annually. Specifically, Germany, Italy and the United Kingdom are the countries Kosovo sells most goods to, followed by Western Balkan region. Kosovo’s main partners are Albania, North Macedonia, and Serbia. Finally, from non-European countries Kosovo exports most to the United States of America and India.

With regards to services, the main categories which contribute to Kosovo’s exports are travel, telecommunications, computer and information services, and government goods and services. In other words, it is mainly Kosovo’s diaspora through travel expenses along with other tourists, and youngsters providing computer services abroad that have continued to maintain services in a surplus for years. Kosovo policy makers must review the possibility of investing more in the second category⁸¹ and find ways of also using the development of this highly skilled labor into helping manufacturing sector as well.

The main categories of goods Kosovo imports include prepared (i) foodstuffs, beverages, and tobacco, (ii) machinery, appliances, etc., and (iii) mineral products. Practically, most of the food and beverages consumed by Kosovars are foreign. In comparison, Kosovo only exports about 10% of what it imports in consumption goods.

Kosovo’s main trading partners include the EU, CEFTA countries, and Asia. In EU, main partners are Germany, Greece, and Italy; in CEFTA, main partners include Serbia, Albania, North Macedonia; while the country we export the least in the region is Serbia, it remains the country we import from the most. In other European countries, Turkey is a strong partner, while with non-European countries, China dominates our market.

7. CONCLUSIONS

According to World Bank classifications, Kosovo is an upper-middle income country which has experienced a stable economic growth during the last 10 years. While Kosovo’s GDP has been increasing steadily over the years, the real growth rate has been less linear with significant variability through the years, implying the standard of living didn’t improve much. While exports have also experienced a somewhat positive trend, the main exporting categories do not show promise for sustainable growth. However, there is potential for growth in the service industry, and backed by recent research, investment in services can help in establishing sustainable economic growth. Furthermore, diaspora contribution is the largest in the region; however, majority of this value is spent on consumption or real estate. This year’s decision of the Ministry of Finance to provide opportunities for diaspora to invest in treasury bonds was an important move in altering the direction of diaspora contributions from consumption to investment. Although the value of investment was relatively small (10 million euros), it is crucial in changing future behavior, as any good policy should.

⁸⁰ Felipe, J. et al. (2010). How Rich Countries Became Rich and Why Poor Countries Remain Poor: It’s the Economic Structure . . . Duh! Asian Development Bank, https://www.levyinstitute.org/pubs/wp_644.pdf

⁸¹ Assuming the computer and information services are the dominant item in this category.

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CHAPTER 6. THE BEGINNINGS OF A NEW INDUSTRIAL POLICY

EDISON JAKURTI

1. INTRODUCTION

Large trade deficits indicate a change that needs to take place in industrial policy, especially when there are high unemployment rates as is the case in Kosovo. Given the small size of the economy and the deindustrialization history, it is impossible for Kosovo – or any country for that matter – to specialize in all commodities. Thus, a specific strategy of specialization in goods and services with the lowest opportunity costs is paramount.

In this chapter, we estimate the revealed comparative advantage for Kosovo's exported goods in the last 11 years. There are important patterns that could serve as a beginning for a new industrial policy that is actually based on economic analysis – and not in ad hoc manners or via cronyism. Moreover, we estimate the productivity associated with each exported good along with the overall productivity of the basket of exports. While the first shows certain productive industries that could further grow and thrive, the latter indicates that besides strategic planning, enhancing other components such as human capital are crucial for improving the overall industrial capacities.

2. REVEALED COMPARATIVE ADVANTAGE

One good place to start is by estimating the comparative advantage, which is a notion attributed to David Ricardo, a classical political economist, who discussed this concept in his 1817's book *On the Principles of Political Economy and Taxation*. Basically, a country is said to have a comparative advantage in producing a good or a service when that production is done at a lower opportunity cost than in other countries.

Comparative advantage is a very widely mentioned notion in discussion on economic issues of Kosovo, yet there are no official statistics revealing it. While it is a relatively easy-to-comprehend notion, it is not so when it comes to estimation. Nonetheless, there are ways in which this can be done, especially given its importance as a first step for re-assessing the current and past trends in this regard.

A common and fairly simple way to do that is by estimating the revealed comparative advantage (RCA) index suggested by Balassa (1965)⁸². The RCA of country k for good i is defined as,

$$RCA_k^i = \frac{X_k^i / X^i}{X_k / X}$$

where X_k^i denotes the exports of good k by country i , X^i denotes the aggregate value of exports of country i , X_k is world's total exports of good k , and X is the aggregate value of world's exports (i.e., of all goods). In other words, it is a ratio of a country's exports of a certain good to world's share of exports of that same good.

The cutoff that determines whether a country has a revealed comparative advantage for exporting a certain good is 1. If the $RCA > 1$ then that good is said to have a revealed comparative advantage. A drawback of this index though is that it is unbounded in the upper end (i.e., for goods where there is a comparative advantage), but the lower bound (i.e., for goods with a comparative disadvantage) is 0. For that reason, and for a more intuitive approach when comparing different goods or sectors, one can normalize the RCA as suggested by Laursen (2000)⁸³ and utilized by World Trade Organization publications⁸⁴. So, the Normalized RCA (NRCA) is:

$$NRCA_k^i = \frac{RCA_k^i - 1}{RCA_k^i + 1}$$

The cutoff now is 0, the lower bound is -1 and an the upper bound of 1. In other words, goods for which $NRCA > 0$, it is said to have a comparative advantage, while the ones where $NRCA < 0$, have a comparative disadvantage.

⁸² See Balassa (1965).

⁸³ See Laursen (2000).

⁸⁴ See World Trade Organization (2012).

2.1. DATA

To estimate the NRCA for Kosovo, we use export data of goods for the period 2010-2020. Exports are structured through the Harmonized System (HS) codes and we use the 2-digit (HS-2) disaggregation level i.e., Chapter 1 through 99. These data were retrieved from the public database of the Kosovo Agency of Statistics. The same data, for the same period and level of disaggregation, for the rest of the world were retrieved from the United Nations Comtrade Database, which is also publicly available. Because the data from UN Comtrade was in United States dollars, export values were converted to euros using the annual average exchange rates as listed by the European Central Bank⁸⁵.

2.2. RESULTS

Figure 1 below shows the top 5 chapters of commodities with the highest revealed comparative advantage for each year between 2010 and 2020. An exhaustive list of all commodities with a revealed comparative advantage (and disadvantage) can be found in Appendix A. The first column is the code of the chapter of goods as per the HS classification at 2 digits, the second column describes the set of commodities included in the chapter, and the last column shows the normalized revealed comparative advantage. Again, as described earlier, the revealed comparative advantages were normalized in order for the indices to be bounded on both the lower and upper side. As such, the range of values lies between -1 and 1, and 0 is the cutoff i.e., indicating the revealed comparative advantage of that good.

Figure 1. Top-5 commodities with the highest comparative advantage 2010-2020

2010

No.	Commodity	NRCA
72	Iron and steel	0.93
41	Raw hides and skins (other than furskins) and leather	0.91
11	Products of the milling industry; malt, starches, inulin, wheat gluten	0.90
78	Lead and articles thereof	0.87
26	Ores, slag and ash	0.82

2011

No.	Commodity	NRCA
11	Products of the milling industry; malt, starches, inulin, wheat gluten	0.91
72	Iron and steel	0.90
41	Raw hides and skins (other than furskins) and leather	0.88
55	Man-made staple fibres	0.75
51	Wool, fine or coarse animal hair; horsehair yarn and woven fabric	0.75

2012

No.	Commodity	NRCA
11	Products of the milling industry; malt, starches, inulin, wheat gluten	0.93
41	Raw hides and skins (other than furskins) and leather	0.91
78	Lead and articles thereof	0.90
72	Iron and steel	0.89
55	Man-made staple fibres	0.84

2013

No.	Commodity	NRCA
11	Products of the milling industry; malt, starches, inulin, wheat gluten	0.93
41	Raw hides and skins (other than furskins) and leather	0.91
72	Iron and steel	0.90
55	Man-made staple fibres	0.85
78	Lead and articles thereof	0.83

⁸⁵ See the "Euro foreign exchange reference rates" as part of the "ECB/Eurosystem policy and exchange rates" section in the Statistics tab of the European Central Bank website: https://www.ecb.europa.eu/stats/policy_and_exchange_rates/euro_reference_exchange_rates/html/eurofxref-graph-usd.en.html.

2014

No.	Commodity	NRCA
11	Products of the milling industry; malt, starches, inulin, wheat gluten	0.90
72	Iron and steel	0.90
41	Raw hides and skins (other than furskins) and leather	0.89
55	Man-made staple fibres	0.84
26	Ores, slag and ash	0.73

2015

No.	Commodity	NRCA
72	Iron and steel	0.89
41	Raw hides and skins (other than furskins) and leather	0.89
78	Lead and articles thereof	0.88
11	Products of the milling industry; malt, starches, inulin, wheat gluten	0.84
22	Beverages, spirits and vinegar	0.77

2016

No.	Commodity	NRCA
41	Raw hides and skins (other than furskins) and leather	0.90
76	Aluminium and articles thereof	0.87
11	Products of the milling industry; malt, starches, inulin, wheat gluten	0.85
26	Ores, slag and ash	0.81
22	Beverages, spirits and vinegar	0.78

2017

No.	Commodity	NRCA
41	Raw hides and skins (other than furskins) and leather	0.90
11	Products of the milling industry; malt, starches, inulin, wheat gluten	0.83
72	Iron and steel	0.82
78	Lead and articles thereof	0.81
22	Beverages, spirits and vinegar	0.81

2018

No.	Commodity	NRCA
41	Raw hides and skins (other than furskins) and leather	0.91
78	Lead and articles thereof	0.84
22	Beverages, spirits and vinegar	0.84
72	Iron and steel	0.77
26	Ores, slag and ash	0.73

2019

No.	Commodity	NRCA
41	Raw hides and skins (other than furskins) and leather	0.87
78	Lead and articles thereof	0.84
22	Beverages, spirits and vinegar	0.83
72	Iron and steel	0.82
73	Iron or steel articles	0.68

2020

No.	Commodity	NRCA
78	Lead and articles thereof	0.92
72	Iron and steel	0.87
41	Raw hides and skins (other than furskins) and leather	0.85
22	Beverages, spirits and vinegar	0.83
26	Soap, organic surface-active agents; washing, lubricating, polishing or scouring preparations; artificial or prepared waxes, candles and similar articles, modelling pastes, dental waxes and dental preparations with a basis of plaster	0.77

Source: Author's own calculations based on data from KAS and UN Comtrade

As revealed in Figure 1 and the tables in Appendix A, there are certain chapters of commodities that appear year after year. If the index of revealed comparative advantage from the past is taken as an initial indication to think of sectors that should be taken into account, when thinking about export support and promotion, then it is paramount to conduct a deeper analysis on the commodities with the highest NRCA and the ones that have repeatedly been on the list. Specifically, commodities that have had a comparative advantage every year in the past decade include (listed in a descending order based on their code and not their NRCA):

- 7. Edible vegetables and certain roots and tubers;
- 8. Edible fruit and nuts; peel of citrus fruit or melons;
- 9. Coffee, tea, mate and spices;
- 11. Products of the milling industry; malt; starches; inulin; wheat gluten;
- 18. Cocoa and cocoa preparations.
- 20. Preparations of vegetables, fruit, nuts or other parts of plants.
- 22. Beverages, spirits and vinegar.
- 26. Ores, slag and ash.
- 41. Raw hides and skins (other than furskins) and leather.
- 59. Impregnated, coated, covered or laminated textile fabrics; textile articles of a kind suitable for industrial use.
- 72. Iron and steel.
- 73. Articles of iron or steel.
- 74. Copper and articles thereof
- 76. Aluminum and articles thereof
- 78. Lead and articles thereof
- 79. Zinc and articles thereof.

3. DETERMINING EXPORTS' PRODUCTIVITY

RCA is an important index, but its drawback is that it does not inform one about the most productive sectors that have been exporting. In order to determine the productivity level associated with a product, Hausmann, Hwang and Rodrik (2007) propose the construction of PRODY and EXPY⁸⁶. Basically, PRODY is the productivity level associated with a good and it is a product of the RCA of country j and the GDP per capita of that country denoted by Y_j . Formally, it is defined as:

$$\text{PRODY}_k = \sum_j \frac{(x_{jk}/x_j)}{\sum_i (x_{ik}/x_i)} Y_j$$

In other words, it is the weighted average of the GDP per capita, where the weights are determined by each country's RCA. This way, PRODY represents the income level of exports. Then, to determine the productivity level associated with the basket of exports, Hausmann, Hwang and Rodrik (2007) suggest EXPY which is formally defined as:

$$\text{EXPY}_i = \left(\frac{X_{ii}}{X_i} \right) \text{PRODY}_i$$

where the PRODY index is multiplied by the share of each export in total exports of country i . While PRODY and EXPY are usually used to compare different countries' productivity of exports, they can still reveal some important information regarding patterns and trends in single countries. Hausmann, Hwang and Rodrik (2007) show that there is a high correlation between economic growth and EXPY.

3.1. RESULTS

To estimate PRODY we use the RCA indices calculated earlier and the GDP per capita (constant, in euro) from the public database of KAS. Then, as the formula shows, PRODY values are multiplied by export shares, using also the same data that was used to construct the RCA indices, to derive the EXPY indices.

Table 1 below shows the top-5 largest and smallest exports arranged by the average PRODY from the period 2010-2020. The first three lowest values are zero because Kosovo did not export any commodities in these chapters. Then, some negligible amounts are recorded in the "Aircraft, spacecraft and parts thereof" and "Arms and ammunition parts and accessories thereof". It is quite expected given that Kosovo does not produce these types of goods. Then, the highest value of PRODY is associated with several categories that are not surprising either. Yet, while metals and minerals have been crucial exports – mostly as raw material – for many years, it is optimistic to see the beverages industry – which involves processing and adding value – in the list.

⁸⁶ See Hausmann, Hwang and Rodrik (2007).

Table 1. Smallest and largest PRODY values for the period 2010-2020

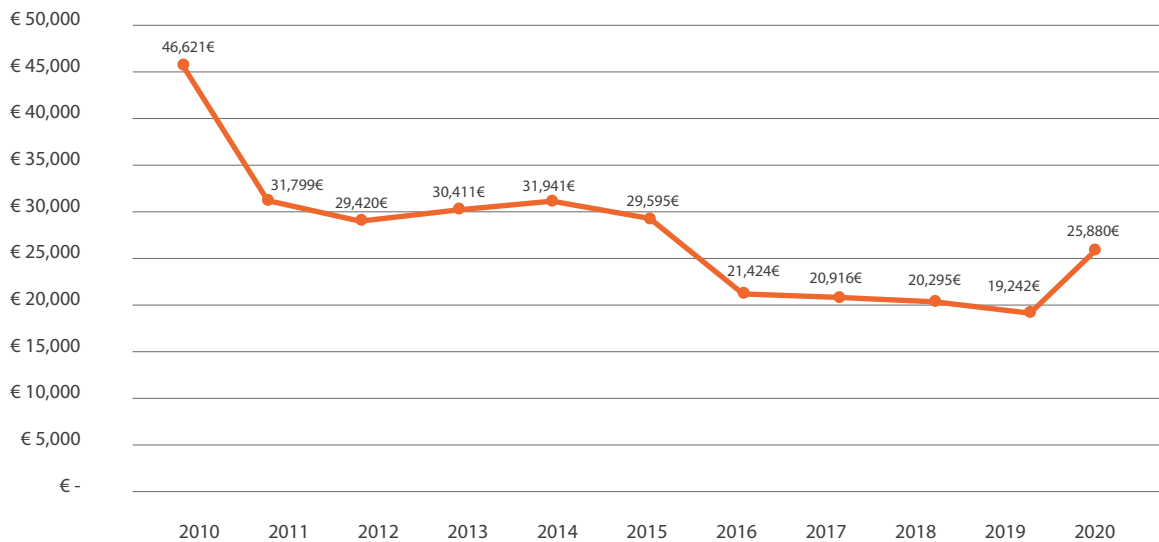
	Code	Commodity	Mean PRODY 2010-2020	
Smallest	43	Furskins and artificial fur; manufactures thereof	€	-
	45	Cork and articles of cork	€	-
	50	Silk	€	-
	88	Aircraft, spacecraft and parts thereof	€	2.69
	93	Arms and ammunition; parts and accessories thereof	€	3.51
Largest	41	Raw hides and skins (other than furskins) and leather	€	59,862
	72	Iron and steel	€	47,702
	11	Products of the milling industry; malt, starches, inulin, wheat gluten	€	44,911
	78	Lead and articles thereof	€	39,043
	22	Beverages, spirits and vinegar	€	27,349

Source: Author's own calculations based on data from KAS and UN Comtrade

What is more concerning though is that the EXPY values show a downward trend between 2010 and 2019, and then a turning point in 2020, as shown in Figure 2

below. This indicates that the overall productivity of exports has been falling.

Figure 2. Productivity of the basket of exports 2010-2020



Source: Author's own calculations based on data from KAS and UN Comtrade

More data and analyses are needed to determine the reason why but, Hausmann, Hwang and Rodrik (2007) suggest theoretically and provide empirical evidence for human capital and the size of the labor market to be key determinants for the level of a country's EXPY. While they indicate for potential endogeneity issues when it comes to the relation between human capital and EXPY, they recognize that a causal rela-

tionship between the country size and EXPY is more plausible. Understanding the high correlation between EXPY and growth that Hausmann, Hwang and Rodrik (2007) find, and bearing in mind Kosovo's large trade deficits, it is imperative to address the issue of increasing exports productivity when designing industrial policy.

4. CONCLUSIONS

Persistent trade deficits are an indication that industrial policy, among other policies, needs a major reform. Such a reform must follow a scientific approach rather than creating ad hoc responses or considering all industries as strategic and equally important. While it is crucial for this new industrial policy to focus on import substitutions too, we have provided here a beginning for focusing on export promotion. Further analyses are needed to understand the difficulties and strengths of each industry, yet the revealed comparative advantage index is a way to start.

Moreover, besides knowing the lowest opportunity cost, it is important to also know the level of productivity in each industry. Hence, we used PRODY and EXPY as methods which can inform industrial policy regarding both individual industries and the overall trends. While there are certain sectors that have been thriving, the overall trend of productivity has been falling. This should alarm the Government to seriously consider drafting a much more thorough and focused industrial policy that would boost the overall productivity in exporting industries.

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APPENDIX A

Figure A.1 Normalized Revealed Comparative Advantage of Kosovo 2010-2020

No.	Commodity	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020
1.	Animals; live	0.20	-0.56	-0.67	-1.00	-1.00	-1.00	-1.00	-1.00	-0.93	-1.00	-1.00
2.	Meat and edible meat offal	-0.94	-0.99	-0.99	-0.98	-0.91	-0.86	-0.80	-0.87	-0.90	-0.79	-0.81
3.	Fish and crustaceans, mollusks and other aquatic invertebrates	-0.97	-0.97	-0.85	-1.00	-1.00	-0.97	-0.97	-0.87	-0.91	-0.92	-0.90
4.	Dairy produce; birds' eggs; natural honey; edible products of animal origin, not elsewhere specified or included	-0.36	-0.68	-0.79	-0.83	-0.79	-0.54	-0.49	-0.59	-0.57	-0.42	-0.43
5.	Animal originated products; not elsewhere specified or included	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-0.27	-0.97
6.	Trees and other plants, live; bulbs, roots and the like; cut flowers and ornamental foliage	-0.57	-0.96	-0.92	-0.56	-0.89	-0.80	-0.74	-0.46	-0.31	0.43	0.53
7.	Vegetables and certain roots and tubers; edible	0.64	0.41	0.53	0.44	0.62	0.41	0.55	0.51	0.61	0.56	0.68
8.	Fruit and nuts, edible; peel of citrus fruit or melons	-0.24	0.05	0.09	0.16	0.17	0.17	0.28	0.54	0.57	0.49	0.58
9.	Coffee, tea, mate and spices	0.31	-0.20	0.01	0.34	0.54	0.54	0.40	0.54	0.63	0.63	0.69
10.	Cereals	-0.78	-0.89	-0.92	-0.97	-0.67	-0.49	-0.70	-0.79	-0.70	-0.90	-0.67
11.	Products of the milling industry; malt, starches, inulin, wheat gluten	0.90	0.91	0.93	0.93	0.90	0.84	0.85	0.83	0.72	0.37	0.44
12.	Oil seeds and oleaginous fruits; miscellaneous grains, seeds and fruit, industrial or medicinal plants; straw and fodder	-0.44	-0.50	-0.36	-0.39	-0.13	-0.16	-0.12	-0.16	0.11	0.27	0.25
13.	Lac; gums, resins and other vegetable saps and extracts	-1.00	-1.00	-1.00	-0.89	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00
14.	Vegetable plaiting materials: vegetable products not elsewhere specified or included	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-0.38	-1.00	-0.89	-0.63	-1.00
15.	Animal or vegetable fats and oils and their cleavage products; prepared animal fats; animal or vegetable waxes	-0.87	-0.95	-0.93	-0.94	-0.98	-0.95	-0.99	-0.85	-0.68	-0.15	-0.21
16.	Meat, fish or crustaceans, mollusks or other aquatic invertebrates; preparations thereof	-0.99	-1.00	-0.98	-0.77	-0.49	-0.28	-0.29	-0.26	-0.14	-0.11	0.22
17.	Sugars and sugar confectionery	-0.73	-0.74	-0.71	-0.65	-0.67	-0.07	-0.05	-0.24	-0.07	-0.08	-0.05
18.	Cocoa and cocoa preparations	0.26	-0.44	0.35	0.45	0.52	0.50	0.45	0.31	0.31	0.29	0.23
19.	Preparations of cereals, flour, starch or milk; pastrycooks' products	-0.53	-0.17	-0.12	0.00	0.11	0.25	0.19	0.11	0.12	0.04	-0.05
20.	Preparations of vegetables, fruit, nuts or other parts of plants	0.52	0.49	0.49	0.25	0.24	0.32	0.53	0.64	0.57	0.55	0.63
21.	Miscellaneous edible preparations	-0.45	-0.75	-0.68	-0.71	-0.57	-0.58	-0.49	-0.62	-0.42	-0.47	-0.50
22.	Beverages, spirits and vinegar	0.62	0.63	0.72	0.77	0.73	0.77	0.78	0.81	0.84	0.83	0.83
23.	Food industries, residues and wastes thereof; prepared animal fodder	-0.31	-0.24	-0.10	-0.10	-0.05	-0.32	-0.20	-0.18	-0.11	-0.38	-0.25
24.	Tobacco and manufactured tobacco substitutes	-0.76	-1.00	-0.81	-0.77	-1.00	-1.00	-1.00	-1.00	-1.00	-0.76	-0.99
25.	Salt; sulphur; earths, stone; plastering materials, lime and cement	-0.01	0.55	0.22	0.60	0.49	0.53	-0.39	-0.74	-0.37	-0.47	0.33
26.	Ores, slag and ash	0.82	0.64	0.71	0.71	0.73	0.68	0.81	0.79	0.73	0.64	0.60
27.	Mineral fuels, mineral oils and products of their distillation; bituminous substances; mineral waxes	-0.50	-0.52	-0.52	-0.35	-0.47	-0.22	0.10	-0.03	-0.28	-0.41	-0.55

28.	Inorganic chemicals; organic and inorganic compounds of precious metals; of rare earth metals, of radio-active elements and of isotopes	-0.84	-0.48	-0.42	-0.98	-0.84	-0.93	-0.34	-0.61	-0.99	-0.88	-0.47
29.	Organic chemicals	-0.98	-1.00	-0.99	-1.00	-1.00	-1.00	-1.00	-0.99	-0.99	-0.98	-0.98
30.	Pharmaceutical products	-0.93	-0.90	-0.91	-0.94	-0.97	-0.98	-0.97	-0.88	-0.71	-0.86	-0.91
31.	Fertilizers	-0.99	-0.94	-0.95	-1.00	-0.90	-0.99	-0.86	-0.79	-0.81	-0.61	-0.52
32.	Tanning or dyeing extracts; tannins and their derivatives; dyes, pigments and other coloring matter; paints, varnishes; putty, other mastics; inks	-0.70	-0.61	-0.37	-0.25	-0.26	-0.18	-0.12	-0.04	0.05	0.18	0.33
33.	Essential oils and resinoids; perfumery, cosmetic or toilet preparations	-0.88	-0.91	-0.92	-0.93	-0.90	-0.98	-0.93	-0.77	-0.83	-0.84	-0.73
34.	Soap, organic surface-active agents; washing, lubricating, polishing or scouring preparations; artificial or prepared waxes, candles and similar articles, modelling pastes, dental waxes and dental preparations with a basis of plasters	-0.61	-0.83	-0.61	-0.25	-0.04	0.13	0.28	0.24	0.37	0.45	0.77
35.	Albuminoidal substances; modified starches; glues; enzymes	-0.56	-0.59	-0.71	-0.93	-0.69	-0.70	-0.66	-0.75	-0.55	-0.64	-0.48
36.	Explosives; pyrotechnic products; matches; pyrophoric alloys; certain combustible preparations	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-0.86	-1.00	-1.00	-1.00
37.	Photographic or cinematographic goods	-0.97	-0.98	-0.98	-0.96	-0.99	-0.91	-0.86	-0.97	-1.00	-1.00	-0.96
38.	Chemical products n.e.c.	-0.66	-0.82	-0.72	-0.94	-0.86	-0.91	-0.82	-0.86	-1.00	-1.00	-0.82
39.	Plastics and articles thereof	-0.34	-0.36	-0.07	0.12	0.03	0.28	0.42	0.44	0.54	0.58	0.59
40.	Rubber and articles thereof	0.33	0.31	0.33	0.32	0.19	0.12	0.00	-0.21	-0.17	-0.20	0.01
41.	Raw hides and skins (other than furskins) and leather	0.91	0.88	0.91	0.91	0.89	0.89	0.90	0.90	0.91	0.87	0.85
42.	Articles of leather; saddlery and harness; travel goods, handbags and similar containers; articles of animal gut (other than silk-worm gut)	-0.90	-0.99	-0.98	-0.76	-0.32	-0.66	-0.07	-0.27	-0.26	-0.37	-0.87
43.	Furskins and artificial fur; manufactures thereof	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00
44.	Wood and articles of wood; wood charcoal	-0.08	-0.13	0.00	0.03	0.07	0.00	0.19	0.21	0.34	0.35	0.31
45.	Cork and articles of cork	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00
46.	Manufactures of straw, esparto or other plaiting materials; basketware and wickerwork	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00
47.	Pulp of wood or other fibrous cellulosic material; recovered (waste and scrap) paper or paperboard	-0.45	-0.10	0.10	0.06	0.33	0.28	0.43	0.42	0.42	0.35	0.24
48.	Paper and paperboard; articles of paper pulp, of paper or paperboard	-0.68	-0.74	-0.60	-0.59	-0.59	-0.55	-0.30	-0.16	-0.18	-0.28	-0.14
49.	Printed books, newspapers, pictures and other products of the printing industry; manuscripts, typescripts and plans	-0.43	-0.69	-0.61	-0.44	-0.65	-0.31	-0.42	-0.59	-0.29	-0.34	-0.52
50.	Silk	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00
51.	Wool, fine or coarse animal hair; horsehair yarn and woven fabric	0.41	0.75	-0.07	0.01	-0.18	-0.34	-0.56	-0.34	-0.69	-0.48	0.54
52.	Cotton	-1.00	-0.99	-0.99	-0.72	-0.99	-0.98	-1.00	-1.00	-0.95	-0.98	-0.92
53.	Vegetable textile fibres; paper yarn and woven fabrics of paper yarn	-1.00	-1.00	-0.97	-1.00	-0.24	-0.35	-1.00	-1.00	-1.00	-1.00	-1.00
54.	Man-made filaments; strip and the like of man-made textile materials	-0.88	-0.97	-0.98	-0.90	-0.99	-0.98	-0.82	-0.81	-0.84	-0.88	-0.93
55.	Man-made staple fibres	0.80	0.75	0.84	0.85	0.80	0.70	-0.15	0.14	-0.18	-0.67	-0.77

56.	Wadding, felt and nonwovens, special yarns; twine, cordage, ropes and cables and articles thereof	-0.92	-0.97	-0.92	-0.89	-0.87	-0.94	-0.96	-0.98	-0.93	-0.95	-0.80
57.	Carpets and other textile floor coverings	0.07	0.15	0.26	0.01	0.04	-0.07	-0.03	-0.17	0.38	0.37	0.38
58.	Fabrics; special woven fabrics, tufted textile fabrics, lace, tapestries, trimmings, embroidery	-1.00	-1.00	0.34	-0.80	-1.00	-0.98	-0.99	-0.99	-0.89	-0.99	-0.74
59.	Textile fabrics; impregnated, coated, covered or laminated; textile articles of a kind suitable for industrial use	0.78	0.72	0.69	0.69	0.68	0.74	0.74	0.67	0.71	0.63	0.66
60.	Fabrics; knitted or crocheted	-1.00	-0.96	-1.00	-1.00	-1.00	-0.99	-1.00	-1.00	-0.99	-0.94	-0.92
61.	Apparel and clothing accessories; knitted or crocheted	-0.96	-0.97	-0.83	-0.87	-0.88	-0.89	-0.92	-0.69	-0.56	-0.51	-0.52
62.	Apparel and clothing accessories; not knitted or crocheted	-0.73	-0.55	-0.50	-0.32	-0.32	-0.38	-0.53	-0.76	-0.61	-0.43	-0.07
63.	Textiles, made up articles; sets; worn clothing and worn textile articles; rags	-0.81	-0.82	-0.68	-0.71	0.07	0.12	0.49	0.51	0.53	0.56	0.33
64.	Footwear; gaiters and the like; parts of such articles	-0.95	-0.92	-0.85	-0.51	-0.16	0.06	0.14	-0.06	-0.20	-0.13	-0.11
65.	Headgear and parts thereof	-1.00	-1.00	-1.00	-0.96	-0.96	-0.77	-0.81	-0.82	-0.98	-0.87	-0.92
66.	Umbrellas, sun umbrellas, walking-sticks, seat sticks, whips, riding crops; and parts thereof	-0.53	-0.83	-0.59	-0.53	-0.23	-0.07	0.12	0.27	0.60	0.45	0.62
67.	Feathers and down, prepared; and articles made of feather or of down; artificial flowers; articles of human hair	-1.00	-1.00	-1.00	-0.98	-1.00	-1.00	-1.00	-0.87	-0.92	-0.97	-0.98
68.	Stone, plaster, cement, asbestos, mica or similar materials; articles thereof	0.38	0.05	-0.10	-0.06	-0.12	0.02	0.45	0.54	0.56	0.52	0.52
69.	Ceramic products	-0.47	-0.52	-0.56	-0.60	-0.37	-0.48	-0.27	0.00	0.14	0.09	0.10
70.	Glass and glassware	-0.91	-0.93	-0.90	-0.59	0.15	-0.16	-0.47	0.03	0.25	0.37	0.48
71.	Natural, cultured pearls; precious, semi-precious stones; precious metals, metals clad with precious metal, and articles thereof; imitation jewelry; coin	-0.99	-1.00	-0.98	-0.98	-1.00	-0.42	-1.00	-0.55	-0.55	-0.59	-0.74
72.	Iron and steel	0.93	0.90	0.89	0.90	0.90	0.89	0.72	0.82	0.77	0.82	0.87
73.	Iron or steel articles	0.32	0.19	0.35	0.44	0.51	0.54	0.63	0.64	0.70	0.68	0.74
74.	Copper and articles thereof	0.69	0.64	0.65	0.60	0.54	0.46	0.51	0.60	0.51	0.47	0.44
75.	Nickel and articles thereof	-0.88	-0.97	-0.91	-0.88	-0.97	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00
76.	Aluminium and articles thereof	0.52	0.43	0.56	0.44	0.53	0.59	0.87	0.47	0.58	0.51	0.55
77.	Lead and articles thereof	0.87	0.49	0.90	0.83	0.68	0.88	0.65	0.81	0.84	0.84	0.92
78.	Zinc and articles thereof	0.42	0.47	0.54	0.64	0.53	0.50	0.59	0.58	0.72	0.62	0.76
79.	Tin; articles thereof	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00
80.	Metals; n.e.c., cermets and articles thereof	-0.73	-0.61	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-0.98
81.	Tools, implements, cutlery, spoons and forks, of base metal; parts thereof, of base metal	-0.95	-0.90	-0.96	-0.91	-0.91	-0.88	-0.89	-0.88	-0.54	-0.10	0.13
82.	Metal; miscellaneous products of base metal	-0.97	-0.93	-0.95	-0.86	-0.90	-0.85	-0.68	-0.64	-0.38	-0.29	-0.17
83.	Nuclear reactors, boilers, machinery and mechanical appliances; parts thereof	-0.78	-0.47	-0.41	-0.62	-0.60	-0.61	-0.73	-0.79	-0.74	-0.69	-0.67
84.	Electrical machinery and equipment and parts thereof; sound recorders and reproducers; television image and sound recorders and reproducers, parts and accessories of such articles	-0.80	-0.89	-0.82	-0.76	-0.82	-0.88	-0.86	-0.86	-0.83	-0.74	-0.73

85.	Railway, tramway locomotives, rolling-stock and parts thereof; railway or tramway track fixtures and fittings and parts thereof; mechanical (including electro-mechanical) traffic signalling equipment of all kinds	-0.87	-0.35	-0.72	-1.00	-0.98	-1.00	-1.00	-1.00	-0.99	-0.99	-0.89
86.	Vehicles; other than railway or tramway rolling stock, and parts and accessories thereof	-0.93	-0.94	-0.95	-0.95	-0.93	-0.88	-0.89	-0.89	-0.81	-0.77	-0.71
87.	Aircraft, spacecraft and parts thereof	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00
88.	Ships, boats and floating structures	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-0.99
89.	Optical, photographic, cinematographic, measuring, checking, medical or surgical instruments and apparatus; parts and accessories	-0.92	-0.88	-0.93	-0.88	-0.94	-0.94	-0.92	-0.94	-0.90	-0.94	-0.94
90.	Clocks and watches and parts thereof	-1.00	-0.99	-1.00	-1.00	-0.99	-0.99	-0.82	-0.71	-0.57	-0.25	-0.40
91.	Musical instruments; parts and accessories of such articles	-1.00	-1.00	-1.00	-0.98	-0.98	-0.95	-0.95	-0.96	-0.91	-0.96	-0.94
92.	Arms and ammunition; parts and accessories thereof	-1.00	-0.99	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00
93.	Furniture: bedding, mattresses, mattress supports, cushions and similar stuffed furnishings; lamps and lighting fittings, n.e.c.; illuminated signs, illuminated name-plates and the like; prefabricated buildings	-0.44	-0.32	-0.22	-0.30	-0.18	-0.09	0.33	0.29	0.42	0.55	0.77
94.	Toys, games and sports requisites; parts and accessories thereof	-0.72	-0.78	-0.78	-0.66	-0.74	-0.88	-0.81	-0.83	-0.83	-0.72	-0.82
95.	Miscellaneous manufactured articles	-0.83	-0.60	-0.48	-0.28	-0.41	-0.32	-0.29	-0.38	-0.16	-0.17	-0.19
96.	Works of art; collectors' pieces and antiques	-0.99	-0.99	-1.00	-1.00	-0.98	-0.99	-0.99	-0.97	-0.98	-0.98	-0.73
97.	Commodities not specified according to kind	-0.98	-0.96	-0.97	-0.96	-0.99	-0.96	-0.96	-0.96	-0.97	-0.99	-0.96

Source: Author's own calculations based on data from KAS and UN Comtrade

SECTION III: ECONOMIC STRUCTURE AND INDUSTRIAL POLICY

CHAPTER 7. JUST ENERGY TRANSITION

MIMOZË VELIU & DINA VLLASALIU

1. INTRODUCTION

This chapter provides an overview of the electricity sector in Kosovo by identifying key issues the country faces in this sector, and it aims to provide ideas on how the transition to a clean electricity system can be completed in a just way. The first section gives an overview of the country's electricity generation mix and the implications the current fossil fuel-based energy system poses for the health of citizens and for the environment. The second segment lays out Kosovo's position with respect to the EU integration process and to the overall global climate crisis by discussing key developments in the EU and in the world with respect to climate change and energy policy. We continue by focusing on Kosovo's technical potential to increase the share of renewable energy in electricity consumption and on the main technical and financial barriers the country faces in this process. The fourth part provides an analysis of how Kosovo can achieve a just energy transition, by discussing examples from three different countries. Finally, we offer conclusions and recommendations for just energy transition in Kosovo.

From analysis of three cases, the study proposes the following:

1. Plan early by setting a clear long-term decarbonization target. This will be the first step which will define key issues such as the expected energy mix as well as the expected coal-phase out dates. Early planning and communication to the public will be key to lowering any potential adverse impacts on vulnerable groups such as coal workers and other communities. While working on defining the future energy mix, strive to take immediate action in implementing no regret projects such as expanding district heating network and investing in energy efficiency measures.
2. Facilitate the involvement of the private sector in the transition to a clean energy system by offering financial incentives and implementing other policy interventions such as establishment of innovation centers to stimulate entrepreneurship development in the sector. Accelerate the establishment of a market-based support scheme (renewable energy auctions) to encourage cost-effective investments in renewable energy generation.
3. Intervene in the education system to reduce the mismatch between skills acquired in schools and those demanded by the labor market, keeping in mind that the demand for professionals in the field of renewable energy will increase as coal phases out globally.
4. Develop economic diversification strategies now to combat the anticipated economic losses from the shutdown of coal-fired power plants and coal mines, thus minimizing economic shocks attributed to the transition.
5. Depending on the decision regarding the coal-phase out date, work on identifying the number of coal workers and their main characteristics. Based on these data, develop retirement or re-skilling programmes.
6. Engage in close dialogue with donors to secure financial support and transfer of know-how in order to smooth the transitioning process.

2. KOSOVO'S ELECTRICITY SECTOR

Almost all of Kosovo's electricity is generated by two ageing Thermal Power Plants (TPPs), Kosovo A and Kosovo B, which have been in operation for 51-37 years respectively⁸⁷. Most TPP units are at the end of their operating life, with Kosova A already passing its decommissioning deadline.

⁸⁷ Energy Regulatory Office (ERO). (2020). Electricity and Thermal Energy Balance 2020. Prishtina: ERO. Retrieved from: <http://ero-ks.org/2020/Sektoret/ELECTRICITY%20AND%20THERMAL%20ENERGY%20ANNUAL%20BALANCE%202020.pdf>

Deemed as a country abundant with coal reserves (ranking it second in Europe and fifth in the world⁸⁸) and with an average per capita income around one tenth of that of the EU⁸⁹, Kosovo has been traditionally labelled as problematic in phasing out coal due to the latter's abundance. To account for the ageing TPPs and to improve security of supply, Kosovo planned to construct a new 450 MW TPP. This sparked huge debates among civil society and in Energy Community due to issues of state aid, climate change as well as high electricity prices. Currently the construction plans are on halt as the company which was selected to construct the TPP has withdrawn from the project⁹⁰.

As of 2020, the country's electricity production was planned to be as follows: 88.99% of electricity generation was to come from the two TPP - Kosova A and Kosova B; 5.12% from renewable sources connected to the grid- HPP Ujmani, HPP Kaskada e Lumbardhit, and Wind Park KITKA; and 5.89% from other sources connected to transmission⁹¹. In terms of GWh, Energy Regulatory Office (ERO) estimated a holistic generation capacity of 5,051.1 GWh.

In terms of demand, ERO estimated that in 2020, the total demand for electricity in Kosovo territory would be 6,404 GWh. The overall electricity demand includes household and business sector, as well as distribution and transmission losses (electricity flows from point of generation to the point of consumption). As a common practice, ERO planned to cover the shortage in demand with electricity import of around 1451 GWh. The available electricity at the end of 2020 will not only cover domestic demand but will at the same time serve to cover unplanned electricity flow interruptions.⁹²

The current electricity system poses major health and environmental consequences. Kosovo's air pollution is often compared to overpopulated cities like Beijing and New Delhi, especially during the winter months when smog sets in the capital, Prishtina. The World Bank reports that the air in Kosovo is characterized by ambient concentrations of particulate

matter with a diameter of 2.5 micrometers or less (PM_{2.5}), far exceeding the European Union standards and guidelines set by World Health Organization (WHO)⁹³. Energy sector is considered as the main contributor to this situation. According to reports, power plants in Kosovo exceed the allowed levels of dust emissions, sulfur oxides (SO_x) emissions, as well as nitrogen oxides (NO_x) emissions⁹⁴.

Apart from the pollution of air, Kosovo's fossil fuel-based electricity system is a major contributor to land contamination and to the contamination of surface and underground water resources. According to Kosovo Environmental Protection Agency (KEPA), Kosovo's TPPs "during 2018/2019...generated waste in the form of oils containing PCB (polychlorinated biphenyls), other waste oils -17800 l (2018), radioactive waste, asbestos, metal waste and other wastes". One of the most infamous environmental impact emerging from the power plants is the so called "blue lake". The ash, which is produced as a result of coal combustion, is mixed with water and is discharged in a former open pit mine creating the so-called blue lake⁹⁵. This lake is toxic as the acidity of the water exceeds the legally allowed values and there are worries that the water is already contaminating the nearby surface and underground river streams⁹⁶.

The environmental degradation creates a health burden for the citizens. The World Bank estimates that Ambient Air Pollution (AAP) exposure leads to around 760 premature deaths on an annual basis⁹⁷, with 11% of this weight concentrated on the capital city. High levels of air pollution are responsible for an increase in cases of people with chronic heart and lung diseases such as chronic obstructive pulmonary diseases (COPDs) and ischemic heart disease (IHD). Even more worrying is the fact that 53% of cases with IHD and 63% of strokes occur in people younger than 70 years of age.

These health implications not only cause pain for the ones involved but they also lead to economic costs including hospital admission, treatment, and general loss in labor productivity on the patients' part. The World Bank estimates that the economic costs amount to around US\$160–US\$310 million, which put into perspective is around 2.5 percent–4.7 percent of gross domestic product (GDP) in 2016⁹⁸.

⁸⁸ Lajqi, S., Durin, B., Berisha, X., & Plantak, L. (2020). Analysis of the Potential for Renewable Utilization in Kosovo Power Sector. *Environments*. doi:10.3390/environments7060049

⁸⁹ The World Bank (2018, October). *Energy in Kosovo*. Retrieved from [worldbank.org: https://www.worldbank.org/en/country/kosovo/brief/energy-in-kosovo](https://www.worldbank.org/en/country/kosovo/brief/energy-in-kosovo)

⁹⁰ European Commission. (2020). *Kosovo 2020 Report*. Brussels: European Commission.

⁹¹ Energy Regulatory Office (ERO). E. R. (2020). *Electricity and Thermal Energy Balance 2020*. Pristina: ERO. Retrieved from <http://ero-ks.org/2020/Sektoret/ELECTRICITY%20AND%20THERMAL%20ENERGY%20ANNUAL%20BALANCE%202020.pdf>

⁹² Ibid.

⁹³ The World Bank. (2019). *Air Pollution Management in Kosovo*. Washington DC: The World Bank.

⁹⁴ Kosovo Environmental Protection Agency. (2020). *Annual Report on the State of Air 2019*. Pristina: Kosovo Environmental Protection Agency.

⁹⁵ Techene, F. (2017, June). Next to KEK, a toxic blue lake that could spell disaster. Retrieved from [prishtinainsight.com: https://prishtinainsight.com/next-kek-toxic-blue-lake-spell-disaster-mag/](https://prishtinainsight.com/next-kek-toxic-blue-lake-spell-disaster-mag/)

⁹⁶ Ibid

⁹⁷ The World Bank. (2019). *Air Pollution Management in Kosovo*. Washington DC: The World Bank.

⁹⁸ Ibid.

3. KOSOVO'S POSITION VIS À VIS EU INTEGRATION AND GLOBAL CLIMATE CHANGE POLICIES

In addition to environmental degradation, Kosovo's energy system is responsible for most of the greenhouse gas (GHG) emissions. It is estimated that above 80% of all GHG emitted in Kosovo come from the energy sector. Worldwide, GHG emissions continue to rise having a direct impact in the global average temperature increase. As of 2021, at least 38 countries have declared a climate emergency, noting the urgency to take concrete steps towards climate change mitigation⁹⁹. Kosovo is not a party of the United Nations Framework Convention on Climate Change (UNFCCC) as a result it is not a signatory of the Paris Agreement. However, as a member of the Energy Community and as a signatory of the Stabilization Association Agreement (SAA), Kosovo has pledged to gradually transpose and implement the EU Acquis with respect to energy and environment. Hence, developments in the EU with respect to these two sectors have a direct impact for Kosovo.

In response to the global climate crisis, the EU has recently adopted the Green Deal as a new growth strategy through which it aims to decouple economic growth from resource use and to transform itself into the world's first continent with net-zero greenhouse gas emissions by 2050. The Green Deal lays out key policies and measures which will be taken to reach this ambitious transformation. Cooperation with and inclusion of Western Balkan countries (Kosovo, Albania, North Macedonia, Montenegro, and Serbia) is considered as important to reach this objective, hence, the Commission adopted the Green Agenda for Western Balkans.

The Green Agenda serves as blueprint for possible measures to be adopted jointly by the EU and each of the Western Balkan partners across five different pillars, namely:

1. climate action, including decarbonization, energy and mobility;
2. circular economy, addressing in particular waste, recycling, sustainable production and efficient use of resources;
3. biodiversity, aiming to protect and restore the natural wealth of the region;
4. fighting pollution of air, water, and soil; and
5. sustainable food systems and rural areas.

This agenda was endorsed by Western Balkan leaders in the Sofia Summit in November 2020¹⁰⁰, whereby the leaders have agreed to **“work towards the 2050 target of a carbon-neutral continent together with the EU through mainstreaming a strict climate policy and reforming energy and transport sectors”**. Within this they have agreed to, inter alia:

- Align with the EU Climate Law once it is adopted with a vision of achieving climate neutrality by 2050;
- Set forward-looking 2030 energy and climate targets in line with the Energy Community framework and EU Acquis, as well as develop and implement integrated Energy and Climate Plans with clear measures designed to reduce greenhouse gas emissions in the Western Balkans economies by integrating climate action into all relevant sectorial policies;
- Continue alignment with the EU Emissions Trading Scheme, as well as work towards introducing other carbon pricing instruments to promote decarbonization in the region.

EU's aim to becoming climate neutral by 2050 is expected to be reflected in the EU's bilateral relations and accession negotiations with the Western Balkans. To illustrate, the EU plans to introduce mechanisms such as carbon border adjustment to reduce carbon leakages. Depending on how the mechanism is designed, this could lead to price adjustment of imports from Western Balkans to reflect the cost of greenhouse gas emissions. In the case where energy remains heavily reliant on fossil fuels, the region will be impacted negatively. The overall global climate emergency will also have an impact on availability of financing. Several International Financial Institutions (IFIs) have already decided to phase out fossil fuel/coal financing with the European Investment Bank (EIB), most notably, deciding for a complete fossil fuel investment phase out by 2021. The European Commission which is by far the largest provider of development assistance to Kosovo has already stopped financing coal related projects and the new Instrument for Pre-Accession Assistance III (IPA) is expected to have a much more enhanced focus on climate change and on the transition to a low carbon economy¹⁰¹.

⁹⁹ Harvey, F. (2020, December). UN secretary general urges all countries to declare climate emergencies. Retrieved from theguardian.com: <https://www.theguardian.com/environment/2020/dec/12/un-secretary-general-all-countries-declare-climate-emergencies-antonio-guterres-climate-ambition-summit>

¹⁰⁰ Sofia Declaration on the Green Agenda for Western Balkans. (2020). Retrieved from berlinprocess.info: <https://berlinprocess.info/wp-content/uploads/2021/02/Leaders-Declaration-on-the-Green-Agenda-for-the-WB.pdf>

¹⁰¹ European Commission (2018). Proposal for the Regulation of the European Parliament and of the Council Establishing the Instrument for Pre-Accession Assistance (IPA III). Retrieved from eur-lex.europa.eu: https://eur-lex.europa.eu/resource.html?uri=cellar:827c66b8-6fb3-11e8-9483-01aa75ed71a1.0002.03/DOC_1&format=PDF01aa75ed71a1.0002.03/DOC_1&format=PDF

Considering these developments, Kosovo is urged to increase the share of renewable energy in final energy consumption and to gradually start the process of coal-phase out¹⁰².

4. KOSOVO'S RES POTENTIAL

Though the need to decarbonize the country and diversify its energy mix is evident, there is a need to analyze the overall potential to decarbonize as well as the main challenges Kosovo is expected to face when it comes to the transitioning of its energy system.

4.1. KOSOVO'S CURRENT DECARBONIZATION PLANS

Two key documents have defined Kosovo's policies and targets with regard to renewable energy: the Energy Strategy (2016-2027) and the National Renewable Energy Action Plan (2011-2020) (NREAP). The Energy Strategy foresees a gradual increase in the share of RES in final energy consumption without specifying this share in terms of total energy consumption by 2027¹⁰³. NREAP on the other hand, has set a target of 25% of energy from renewable sources to be achieved by 2020. In terms of specific sectors, the plan has defined the following targets:

1. Electricity: 25.64% of RES in gross final consumption;
2. Transport: 10% of RES in final consumption;
3. Heating and Cooling: 45.65% of RES in gross final consumption.

For reaching the electricity target, the plan has foreseen the installment of 545 MW hydropower, 150 MW wind power, and 10 MW solar power¹⁰⁴. According to the latest evaluations, the overall RES share in 2019 was 25.6%, however this was mainly achieved via the use of biomass for domestic heating¹⁰⁵, hence the planned target in the electricity consumption was not realized.

Strategically speaking, Kosovo is at a crossroads with respect to energy policy. As mentioned before, the country has endorsed the Green Agenda for Western Balkans and has pledged to join the efforts with the EU to becoming climate neutral by 2050.

Nevertheless, NREAP has expired in 2020 and the country does not have a long-term decarbonization plan. The Energy Strategy still foresees the construction of a new 450 MW coal-based power plant to improve security of supply. This, however, is not likely to happen given that the company which was selected to construct the plant has withdrawn from the project. Currently, the Energy Strategy is being revised and the National Energy and Climate Plan (NECP) is being developed. NECP is expected to set three important targets to be reached by 2030: GHG reduction target, renewable energy share in gross energy consumption, and energy efficiency in final energy consumption. As such, NECP together with the strategy will be the first documents to define Kosovo's decarbonization path.

4.2. RES POTENTIAL

Kosovo has a considerable renewable energy potential which can be tapped to decarbonize the electricity sector. Key potentials rely on solar and wind energy, with less potential in hydro given that the country faces water scarcity. As far as solar energy is concerned, there are several factors considered when assessing potential: a) solar irradiation, which in Kosovo ranges from 1,200 kWh/m² for mountainous parts, to 1,500 kWh/m² in the southern part near Gjakova and b) technical factors such as terrain consideration, available ha of land, and consideration of protected areas¹⁰⁶. When these two factors are considered together, Kosovo's technically usable area amounts to 7,400 ha whereby realizable potential of PV is calculated by assuming 2 ha/MW and is estimated at **3,600 MW**.

As far as wind energy potential is concerned, the factors that must be considered when estimating include a) wind speed, b) suitability of the terrain for the construction of the wind farm, c) distance from grid connection, and d) restrictions due to environmentally protected areas or heritage areas. When all of these are considered, Kosovo's wind potential amounts to **1,200 MW-1,781 MW**, depending on whether further technical restrictions are imposed¹⁰⁷.

Lastly, when considering the hydro potential of the country, one must be aware that Kosovo's main renewable energy source already accounts for hydro, with an installed capacity of 108.24 MW. Because Kosovo is already affected by water scarcity, therefore relying on hydropower will come at a costs. However, according to studies, the north-western

¹⁰² European Commission. (2020). Kosovo 2020 Report. Brussels: European Commission.

¹⁰³ Ministry of Economy. (2017). Energy Strategy of the Republic of Kosovo. Retrieved from me.rks-gov.net: https://me.rks-gov.net/repository/docs/Energy_Strategy_of_the_Republic_of_Kosovo_2017_-_2026.pdf

¹⁰⁴ Ministry of Economy (2013). National Renewable Action Plan of Kosovo. Retrieved from <https://www.energy-community.org/implementation/Kosovo/reporting.html>

¹⁰⁵ Ministry of Economy. (2021). Kosovo's Fourth Progress Report on promotion and use of energy from renewable energy sources, 2018-2019. Retrieved from [www.energy-community.org](https://www.energy-community.org/implementation/Kosovo/reporting.html): <https://www.energy-community.org/implementation/Kosovo/reporting.html>

¹⁰⁶ The World Bank (2020). Energy Efficiency and Renewable Energy Project. Support for Grid Integrated Renewable Energy Generation. The World Bank.

¹⁰⁷ Ibid.

part of the country has a higher potential compared to south-eastern part. Considering the available sources, studies estimated an allocated potential of 136 MW of Small Hydro Power Plant (SHPP), with respected electricity generation of 657.40 GWh. Lastly, the pump storage hydropower plant project Zhur is estimated to have a stored capacity of 250 MW which is to be used during peak demand in winter months¹⁰⁸

4.3. ENERGY EFFICIENCY AS A DEMAND SIDE RESPONSE

In terms of demand, energy efficiency improvements are key considerations that aid in shrinking energy consumption while at the same time minimizing energy losses. Kosovo's final energy consumption has increased in the past years, relative to the years prior 2016, and is expected to grow with more economic growth. Kosovo has adopted energy efficiency action plans, has established most of the legal framework for energy efficiency improvements, and has established the Kosovo Energy Efficiency Fund (KEEF)¹⁰⁹. In terms of implementations however, there is much room for improvement. Nearly 40% of the energy is used by the building sector (followed by transport, industry, services, and agriculture) which is two times more use per square meter when compared to the EU average¹¹⁰. This comes as a result of lack of insulation measures in buildings both in the residential and industrial sector. Coupled with the fact that most of these houses rely on electricity for heating, it is inevitable that the energy demand peaks in the winter months. Moreover, transmission and distribution losses due to the obsolete network, add further to losses as the electricity is transported from point of production to that of consumption¹¹¹.

4.4. KEY IDENTIFIED ISSUES

Currently, around 1,185 MW of solar and wind projects are under various stages of development in Kosovo¹¹². The estimated generation capacity of these projects is 1,300 GWh of electricity which would increase current generation by 40%¹¹³. Latest evaluations suggest that lack of RES is not considered an

issue when it comes to the decarbonization of the electricity system. Renewable energy deployment becomes challenging due to the inability of the system to manage the intermittent nature of renewable energy supply as well as due to the lack of a clear financial supporting mechanism. Regional market integration as well as development of back up and reserve capacity remain essential.

In terms of regional integration, a key milestone has been reached with Kosovo entering a new deal with the association of European transmission system operators (TSOs) which allows the country to form a new interconnection line with central Europe. This way, Kosovo will partner with Albania and fully invoke the 400 kV line, covering the required demand during the winter months¹¹⁴. This agreement has fully disentangled Kosovo's Transmission System Operator (KOSTT) from the Serbian Regulatory Area (EMS) in the Serbia-Montenegro-North Macedonia block. In terms of financial difficulties, a barrier which is currently blocking development of new renewable energy generators is the lack of a support mechanism. Kosovo has cancelled the feed in tariff scheme and is currently working on developing a new market-based support scheme. The development of such scheme is welcomed given that it will enable the construction of renewable generators at market competitive prices, and this will reflect the global trend of price decrease in this sector.

In addition to addressing technical challenges for RES deployment, Kosovo should also deal with the socio-economic impacts of the transition. Energy transitions are characterized by uncertainties when it comes to the wellbeing of the people and the general welfare of the country. With plans to decommission TPPs, many fear job losses. Some find comfort in the construction of a new TPP (Kosova e Re), hoping that during its construction phase at least, it will create many jobs, ranging from unskilled to skilled labor. However, research shows that falling costs of renewables has aided job creation in many EU countries, whereby an estimated 1.2 million people across EU are employed in the renewables sector¹¹⁵. The good news is that the green energy sector has proven to create sustainable jobs across a range of skills and sectors, including manufacturing, engineering, instal-

¹⁰⁸ Ibid.

¹⁰⁹ Kosovo Energy Efficiency Agency (2019). National Energy Efficiency Action Plan 2019 - 2021. Pristina: Kosovo Energy Efficiency Agency.

¹¹⁰ Deutsche Gesellschaft für Internationale Zusammenarbeit (GIZ). (2018). Kosovo Energy Efficiency Project. Retrieved from [www.giz.de: https://www.giz.de/en/downloads/Factsheet%20KEEP_EN_final.pdf](https://www.giz.de/en/downloads/Factsheet%20KEEP_EN_final.pdf)

¹¹¹ Kosovo Energy Efficiency Agency (2019). National Energy Efficiency Action Plan 2019 - 2021. Pristina: Kosovo Energy Efficiency Agency.

¹¹² Krejci, M., & Božidar Radovic, A. G. (2020). Assessment of the potential to deliver utility-scale dispatchable renewable power to Kosovo.

¹¹³ Ibid

¹¹⁴ Ibid and Spasic, V. (2019). KOSTT, OST sign deal to establish Kosovo-Albania regulatory block. Retrieved from [balkan-greenenergynews.com: https://balkan-greenenergynews.com/kostt-ost-sign-deal-to-establish-kosovo-albania-regulatory-block/](https://balkan-greenenergynews.com/kostt-ost-sign-deal-to-establish-kosovo-albania-regulatory-block/)

¹¹⁵ IRENA. (2017). Renewable Energy and Jobs – Annual Review 2017. Retrieved from [www.irena.org: https://www.irena.org/publications/2017/may/renewable-energy-and-jobs--annual-review-2017](https://www.irena.org/publications/2017/may/renewable-energy-and-jobs--annual-review-2017) and Matthias Buck, K. G. (2018). Phasing in Renewables Towards a prosperous and sustainable energy future in Kosovo: challenges and possible solutions. Bonn: Germanwatch e.V.

lations, research and development (R&D), operations and service, as well as consulting and financial services¹¹⁶. Furthermore, the World Bank estimates that investments in energy efficiency in Kosovo would not only create local jobs but would also save the public budget around 18 million EUR annually¹¹⁷. The benefits of decarbonization outweigh the costs, however, countries must ensure that these costs will not be disproportionately borne by vulnerable groups and communities, in other words, countries must ensure that the transitioning to a decarbonized energy system must happen in a just way. The next sections will focus on exploring successful just transition cases and on providing recommendations for Kosovo.

5. ACHIEVING A JUST ENERGY TRANSITION

The term “just transition” was initially coined by the North American unions during 1990s. Initially “just transition” was understood as a support system for workers who lost their jobs due to the implementation of various environmental policies¹¹⁸. Gradually, the term became broader and more tied to climate change activities. The idea of just transition is now embedded in the preamble of the Paris Agreement highlighting the need to consider the impact of the shift to a low carbon economy on the workforce in terms of both quantity as well as quality of jobs. In addition to the impact on the workforce, just transition encompasses other issues of fairness and equity¹¹⁹. One important aspect of just transition is ensuring that the costs of climate change policies do not disproportionately affect those who are more vulnerable and least responsible for GHG emissions¹²⁰. This is valid for both the national scale as well as the global one. To illustrate, developing countries are least responsible for GHG emissions and they are usually more at risk from adverse climate impacts. These countries also face challenges when it comes to combating poverty and improving the livelihoods of their citizens. For this reason, the Paris Agreement foresees support for these countries to reach their decarbonization targets.

In 2015 the International Labor Organization (ILO) developed “Guidelines for a just transition towards environmentally sustainable economies and societies for all”¹²¹. According to this document “a just transition for all towards an environmentally sustainable

economy...needs to be well managed and contribute to the goals of decent work for all, social inclusion and the eradication of poverty”¹²². ILO has defined the main principles that should guide the transition to environmentally sustainable economies and societies¹²³. These principles highlight the importance of engaging and consulting all the affected parties and working on providing decent solutions to potential displacements or negative effects that can emerge from the shift to a low carbon economy. Because no country has yet decarbonized completely, it is difficult to find examples of a successful transition. However, certain regions in Canada, Germany and Czech Republic, have designed and implemented concrete just transition policies from which we can learn. The Study will now turn in analyzing these cases in more detail.

5.1. CANADA

Canada is not reliant on coal for electricity generation. In 2016, only 9% of the total produced electricity was coal based. Nevertheless, the energy mix is not the same throughout the country. Canada is comprised of ten provinces and three territories¹²⁴. In four provinces: Alberta, Saskatchewan, New Brunswick, and Nova Scotia, the share of RES in electricity consumption is lower. This is not the case for Alberta as in 2017 approximately 59% of electricity was generated from coal¹²⁵. As of 2018, the number of coal power plants and coal thermal mines in all these provinces combined, was 24 with 11 being located in Alberta¹²⁶. The total estimated number of employees in the coal sector (coal mines and power plants) ranges between: 3,080-3,900¹²⁷. In response to the overall global climate crisis the Federal Government has decided to complete the coal phase out for electricity production by 2030. In the Province of Alberta, the transition is already underway due to specific decisions taken by the local government, hence in this province all coal fired power plants are expected to be closed by 2023¹²⁸.

5.1.1. PLANNED/IMPLEMENTED POLICIES TO ENSURE A JUST ENERGY TRANSITION

In light of the decision for a complete coal phase out for electricity production by 2030, the federal

¹¹⁶ Ibid.

¹¹⁷ The World Bank. (2019). Energy Efficiency in Kosovo. Retrieved from [www.worldbank.org: https://www.worldbank.org/en/country/kosovo/brief/ee-in-kosovo](https://www.worldbank.org/en/country/kosovo/brief/ee-in-kosovo)

¹¹⁸ Smith, S. (2017). Just Transition: A report for the OECD. Just Transition Centre.

¹¹⁹ Emden, J., Ahmad, H., Murphy, L., & Cameron, C. (2020). LESSONS LEARNED: JUST TRANSITIONS FROM AROUND THE WORLD. Institute for Public Policy Research (IPPR). <http://www.jstor.org/stable/resrep32562>

¹²⁰ Ibid

¹²¹ ILO. (2015). Guidelines for a just transition towards environmentally sustainable economies and societies for all. Geneva: ILO

¹²² Ibid

¹²³ For more information on the principles please consult the Guidelines for a just transition towards environmentally sustainable economies and societies for all published by ILO. ¹¹⁸ Smith, S. (2017). Just Transition: A report for the OECD. Just Transition Centre.

¹²⁴ Government of Canada (2021). Provinces and territories. Retrieved from [www.canada.ca: https://www.canada.ca/en/intergovernmental-affairs/services/provinces-territories.html](https://www.canada.ca/en/intergovernmental-affairs/services/provinces-territories.html)

¹²⁵ Task Force on Just Transition for Canadian Coal Workers (2018). A Just and Fair Transition for Canadian Coal Workers and Communities. Government of Canada.

¹²⁶ Ibid

¹²⁷ Ibid

¹²⁸ Ibid

government as well as the provincial governments have taken concrete steps to ensure that the cost of the transition is not disproportionately borne by coal workers and by the communities where coal mines and power plants are located. A Task Force on Just Transition for Canadian Coal Workers was formed at the federal level with the aim of identifying the main issues and providing recommendations on ensuring a just energy transition. During 2018, the Task Force visited all the concerned provinces, held several meetings with coal workers and other impacted parties and visited several affected communities. Based on these engagements it provided recommendations to the Government to offer just transition support¹²⁹. Majority of these recommendations revolved around development of various support schemes for impacted coal workers.

These schemes were related to either early retirement or to offering financial and educational support to those who are young enough to remain in the labor market. For coal communities, the Task Force recommended the establishment of a just transition funding programme and investment in local infrastructure projects to spur economic growth. The government was also advised to develop a comprehensive just transition plan, to dedicate funding to researching the impacts of the transition, and to enshrine just transition provisions in labor and environmental legislation.

In Alberta the transition started earlier due to a decision taken by the provincial government to accelerate the coal phase out and increase the share of RES in the overall electricity consumption¹³⁰. Initially, the provincial government failed to involve the affected workers and communities. The Advisory Panel which was tasked with identifying the impact of the coal phase out on workers and communities was formed a year after the decision for the acceleration of the coal phase out was made. The panel engaged in discussions with all the affected parties and provided numerous recommendations to the provincial government on supporting workers and the impacted communities. In addition, labor unions in Alberta formed their own Coal Transition Coalition to advocate for the rights of impacted employees and they too provided recommendations which were considered¹³¹

Considering the recommendations emerging from the above-mentioned bodies, the federal and provincial governments in Canada designed and started to implement concrete projects with the aim of reducing the burden of coal workers and communities.

As such, in 2018 the federal government allocated \$35 million for skills development and economic diversification projects¹³². A year later, \$105 were allocated for funding infrastructure needs in coal-affected communities through the so-called Canada Coal Transition Initiative¹³³. In Alberta, the provincial government allocated a \$40-million transition fund to finance support programs for Alberta's coal workers. The fund provides support for coal workers in various ways starting from financing various trainings to providing career counselling and job matching services. More specifically, the fund offers support in the following forms¹³⁴:

1. Workers who seek re-employment are entitled to re-employment financing in the amount of 75% of weekly earnings when combined with employment insurance benefits. This support is available up to 45 weeks or until the worker finds a new full-time job;
2. Workers who are close to retirement but who are still not eligible for the pension are entitled to a grant covering of 75% of their previous weekly earnings until they become eligible for the pension;
3. Workers who are forced to move more than 40 km in order to be re-employed are entitled to a lump sum of \$5,000 for their relocation expenses;
4. Workers who wish to enter training programs are entitled to tuition coverage up to \$12,000;
5. Career counselling and other employment services for coal workers;
6. Qualified facilitators who can be hired to assist employers, workers, and unions with setting up a workforce adjustment committee to create a tailored transition plan for individual worksites using labour market research.

The fund became operational in 2018 and in addition to it, Alberta also allocated \$35 million to support affected communities via implementation of various projects which will lead to economic diversification in areas where coal mines and coal power plants were located¹³⁵. This was done via the Coal Transition Fund and via a regional economic program. While the Coal Transition Fund mainly focused on financing studies and plans for economic diversification the government of Alberta also decided to construct two new highways which will open new economic prospects and will lead to employing around 800 people¹³⁶. In addition to programs rolled out by the provincial government, there are cases when local governments themselves initiated studies on economic potential and started to work on attracting new private investments to account for the expected job losses in their territories¹³⁷.

¹²⁹ *ibid*

¹³⁰ Labour Education Centre (2020). *Just Transition: Exactly What's in it for Workers?* Alberta: Labour Education Centre.

¹³¹ *Ibid*

¹³² Jackson, E., & Hussey, I. (2019). *Alberta's Coal Phase-Out: A Just Transition?* . Alberta: Parkland Institute.

¹³³ *Ibid*.

¹³⁴ *Ibid*.

¹³⁵ *Ibid*.

¹³⁶ *Ibid*.

¹³⁷ *Ibid*.

5.2. RUHR AREA, GERMANY

Germany has traditionally relied on two types of coal: hard coal and brown coal, also referred to as lignite. While the former was mined in heavy industrial areas, the latter was mostly centralized in rural areas with low population, making energy and mining the key industry there¹³⁸.

In 2018 however, the mining of hard coal in Germany came to an end. This was not a sudden decision but rather a planned path from 2007. The reasoning behind the undertaking is mainly two-fold: a) due to cheaper coal in the region, it didn't make sense for the country to rely on hard coal, and b) because of Germany's pledges to diversifying the energy mix, reliance on hard coal would pose a hindrance to fulfilling of international treaties¹³⁹. Germany has also committed to phasing out lignite and all coal-fired power generation, with a "Coal-Exit" commission in place to monitor the whole process¹⁴⁰. The country's energy mix now constitutes of oil, lignite, natural gas, nuclear, biofuels and waste, as well as wind and solar energy¹⁴¹.

5.2.1 RUHR'S AREA AND LESSONS LEARNT

If there is one overarching lesson that is to be taken away from Ruhr's case is that a just transition is a lengthy process which requires the collaboration of multifaceted actors, stemming from a) the role of educational institutions, b) the role of the government, and c) the role of trade unions, businesses, local communities, and NGOs. Below are key areas of focus that should be kept in mind in order to ensure a just transition.

Lost jobs and re-skilling through educational reforms: The main concern regarding phasing out of coal in any country undoubtedly regards the workers of the coal sector and what will happen to them. Lessons learnt from the Ruhr area include the following:

- Depending on the age composition of the workers, the country can rely on both early retirements, if such a thing is deemed feasible, as well as skill repurposing to other sectors for those workers that are relatively young and remain in the job market. For example, when the coal was

phased out in Ruhr area, people were re-employed in other sectors, including the renewable sector as well as the metal one.

- In order to aid the transition from one industry to another, educational policies can be targeted to either a) provide early vocational reskilling in the job for those that are employed in the coal sector, and b) large-scale public investment to develop strong university and technical educational systems¹⁴².
- Heavy focus on funding research and development within universities- a factor that has enabled Ruhr to switch from an industrial society to a knowledge-based one and has increased demand for retaining and attracting skilled workers.

Economical and industrial reforms: Ruhr's economic and industrial independence from coal has been a lengthy process, especially due to the subsidies provided to the mining and coal companies which blocked the development of new sectors:

- Instead of targeting subsidies and other support systems toward financing coal-based sectors, the same funding can be used to strengthen companies and sectors that appear to be "leading" in the market in terms of comparative advantage.
- Identification, monitoring, and distribution of funds has been effectively managed when the system of governance leading the transition has been one of a regional level rather than a federal one.

Financial conundrum and the security of funds: In Ruhr's example, because the phasing out of hard coal was a governmental decision resulting from climate change concerns, the transition has been mainly financed from a national level, rather than based on donors and short-term financing from others.

Decisiveness on a phase-out date and cooperation of all key stakeholders: Determining a phase-out date early on resulted to be crucial for the Ruhr area and should be kept in mind when determining similar deadlines for Kosovo- deadlines that are not to depend on myopic political business cycles but span on a more long-term outlook. Moreover, should Kosovo decarbonize as smoothly as possible, it is necessary to have all actors on board, from the government to the civil society, to the average citizen.

¹³⁸ National Economic and Social Council. (2020). Four Case Studies on Just Transition. Lessons for Ireland

¹³⁹ European Commission (2019a), Coal Regions in Transition. <https://ec.europa.eu/energy/en/topics/oil-gasand-coal/EU-coalregions/coal-regionstransition> 12/12/19.

¹⁴⁰ National Economic and Social Council. (2020). Four Case Studies on Just Transition. Lessons for Ireland

¹⁴¹ IEA. (2021). Germany. Retrieved from <https://www.iea.org/countries/germany>

¹⁴² Cooke, P. (1995a), 'Introduction' in P. Cooke (Ed.), The Rise of the Rustbelt, London: University College London. 1-19.

5.3. CZECH REPUBLIC

Czech Republic is considerably reliant on coal with 35.43% of all energy and 39.74% of electricity being generated from this source¹⁴³. Approximately 50% of all electricity production in the country is based on fossil fuels¹⁴⁴. Coal mining activity takes place in three coal regions: Ústecký, Karlovarský and Moravskoslezský. During the past 15 years coal production has been declining and the number of employees has reduced considerably due to cheaper coal imports from abroad and mining limits placed as part of environmental legislation¹⁴⁵. The current energy strategy foresees a gradual replacement of coal with nuclear energy and renewables in the electricity sector by 2040¹⁴⁶. Czech Republic does not have a definitive coal phase out date, initially the country was considering completing the phase-out by 2038, however, earlier dates are being considered in the light of expected price increases resulting from the emission allowance limits¹⁴⁷. With the Green Deal in force and with the new commitments to reduce GHG emissions by 2030, the country is facing pressure to accelerate the transition to a clean energy system.

5.3.1. PLANNED/IMPLEMENTED POLICIES TO ENSURE A JUST ENERGY TRANSITION

Even though the government is yet to decide a final coal phase out date, Czech Republic has already developed a transition strategy for its coal regions. The strategy, referred to as RE:START was developed as a response to the decline in coal production and coal jobs¹⁴⁸. The development of the strategy was led by the Ministry of Regional Development, however, in informing the strategy and the specific measures, the national level collaborated closely with the local stakeholders to gather input and to design solutions tailored to the needs of the regions in transition¹⁴⁹. In addition to regional and local authorities, business sector, labor offices and NGOs are also part of the contributing team in the development of RE:START. RE:START is backed by a mix of national and EU funds and until 2030 it foresees to deploy 1.5 billion EUR for development of various projects¹⁵⁰. Apart from this, the three coal regions in the country are already implementing activities such as: establishment of innovation centers for stimulating local business development, development of education programs for the local population, and development of platforms for developing regional transformation models¹⁵¹

¹⁴³ Ritchie, H., & Roser, M. (n.d.). Czechia: Energy Country Profile. Retrieved from <https://ourworldindata.org/energy/country/czech-republic>

¹⁴⁴ *ibid*

¹⁴⁵ European Commission (2019). Re-Start: Strategy for economic restructuring of Czech coal regions. https://ec.europa.eu/energy/sites/default/files/documents/restartstrategy_for_economic_restructuring_of_czech_coal_regions.pdf

¹⁴⁶ *ibid*

¹⁴⁷ *ibid*

5.4. JUST TRANSITION AT THE EU LEVEL

In light of the adopted goal of becoming climate neutral by 2050, the EU has established the Just Transition Mechanism (JTM) which will serve as the key tool to lower the burden of the transition in the most affected regions of the EU. JTM is expected to mobilize up to €65-75 billion over the period 2021-2027¹⁵². The funds will be provided in the form of grants, budget guarantees and loans from the European Investment Bank (EIB). Member States will have to define their most affected regions and draft territorial just transition plans to be able to benefit from the mechanism. JTM¹⁵³ is expected to provide assistance in the following forms:

- Vulnerable people and citizens will be supported in re-employment facilitation, re-skilling, improving energy efficiency housing, fighting energy poverty and facilitating access to clean and affordable energy;
- Companies and sectors active in carbon intensive industries will be supported in transition to low-carbon technologies and economic diversification based on climate-resilient investments and jobs, creating attractive conditions for public and private investors, providing easier access to loans and financial support, investing in the creation of new firms, SMEs and start-ups, and in investing in research and innovation activities.
- Regions highly dependent on fossil fuels and carbon intensive industries will be supported in transition to low-carbon and climate-resilient activities, creating new jobs in the green economy, investing in public and sustainable transport, providing technical assistance, investing in renewable energy sources, improving digital connectivity, providing affordable loans to local public authorities, improving energy infrastructure, district heating and transportation networks.

5.5 MAIN TAKE AWAY FROM THE THREE CASES

Energy transitions differ from one case to another as both the technical capacities but also the economic and social situations are unique to the given area of concern. However, broadly speaking there are some similar patterns as to how the countries concerned are handling these transformations.

¹⁴⁸ *ibid*

¹⁴⁹ *ibid*

¹⁵⁰ *ibid*

¹⁵¹ R. Dudcu, G. G.-Y.-C. (2019). Transformation Experiences of Coal Regions: Recommendations for Ukraine and other European countries. Center for Environmental Initiatives Ecoaction.

¹⁵² European Commission. (2020). The Just Transition Mechanism: making sure no one is left behind https://ec.europa.eu/info/strategy/priorities-2019-2024/european-green-deal/finance-and-green-deal/just-transition-mechanism_en

¹⁵³ *ibid*

Clear strategies and targets adopted by the Government

Canada and Germany have established coal-phase out dates ahead of time and have adopted strategies which delineate the future expected energy mixes. Czech Republic is yet to adopt the coal phase out date, nevertheless the strategy for energy diversification exists. Making these decisions and communicating them to the public as early as possible is necessary because the concerned parties will have a clearer understanding as to where the sector is headed.

Establishment of specific just transition bodies

The governments in all three cases were willing to ensure a just energy transition. As such all of them formed specific bodies who were tasked with scanning the situation in the field, analyzing data and providing tailored recommendations to the governments on ensuring that no one is left behind.

Involvement of all impacted parties early in the planning process

The input from coal workers, coal communities, labor unions and agencies, business sector and NGOs, was central when it came to designing specific policies and interventions. Through this, both Canada and Czech Republic were able to tailor programs to the needs of the people in the ground.

Targeting the needs of the laid-off workers as well as the needs of the impacted regions

Both Canada and Germany put a lot of effort in identifying the needs of the impacted coal workers as well as the needs of the coal regions. Governments formed specific funds through which they provided support for laid-off workers in the form of employment benefits, early retirement, reallocation and re-skilling. In addition, large amounts of funds were allocated in the coal regions with the aim of diversifying them economically. One important factor to be mentioned here is that these interventions did not always emerge from the top, there were cases when affected regions themselves took concrete measures to diversify economically. In the case of Germany, concrete educational policies as well as funding of research and development, facilitated the transition of Ruhr area from a coal region to a knowledge-based economy.

6. CONCLUSIONS AND RECOMMENDATIONS

Almost all the electricity in Kosovo is produced from two ageing coal power plants, one of which is well beyond its decommissioning deadline. This poses major environmental and health threats. In addition, energy in Kosovo is responsible for well above 80% of GHG emissions. Kosovo is not a signatory of the Paris Agreement, nevertheless it is part of the Energy Community, and it aims to integrate in the European Union. Due to this, developments in the EU regarding energy have direct implications for the country. In response to the overall global climate crisis the EU has decided to become carbon-neutral by 2050. The Western Balkan countries have adopted the Sofia Declaration, through which they pledged to join the EU in the efforts of decarbonizing the economy by mid-century. Kosovo has a considerable RES potential which can be tapped, this is especially the case for solar and for wind energy. However, there are challenges which the country needs to solve. At a technical level, key challenges for increasing the share of RES in the final energy consumption are lack of regional energy market integration as well as lack of storage and back-up capacity. At a financial level, there is a need for establishing a market based financial support mechanism to spur the investment in this field. Finally, in completing a successful energy transition, Kosovo should ensure that the burden should be shared equally, and the needs of vulnerable groups and communities must be taken into account. Based on the experience from the countries which are already transitioning to a clean energy system, Kosovo should:

1. Set a clear long-term decarbonization target. This is the first step which will define key issues such as the expected energy mix as well as the expected coal-phase out dates. Experience from other countries shows that early planning will be key to lowering any potential adverse impacts on vulnerable groups such as coal workers and other communities. The definition of a future energy mix should be preceded by a rigorous technical and financial analysis. However, no regret actions which can be taken immediately include investments in energy efficiency and investments in expansion of district heating systems. It was stated previously that many citizens in Kosovo rely on electricity for heating, this is especially the case in urban areas. Residential buildings are also responsible for a large share of energy consumption. The central government and municipalities should focus on expanding district heating networks and on introducing energy efficiency financial incentives for the residential sector. Investments in these sectors will also lead to positive economic impacts.

2. Work on creating an enabling environment for involvement of the private sector in the transition to a clean energy system. As fossil fuels are gradually replaced by renewable energy sources, the demand for renewable energy products and related renewable energy services will increase. The first company which produces and exports solar panels in the region was established in Kosovo. Having in mind the future of the energy system, the country should focus on providing the necessary support to similar businesses to improve their comparative advantage. This support can be provided in the form of financial incentives or in the form of other policy interventions such as establishment of innovation centers to stimulate entrepreneurship development in the sector. As a first step, the government should strive to assess the needs of businesses which operate in this area based on which it can define a tailored package of interventions aimed at assisting these businesses to improve their performance.

When it comes to the private sector, an important intervention is the acceleration of the establishment of a market-based support scheme (in the form of renewable energy auctions) to encourage cost-effective investments in renewable energy generation.

3. Intervene in the education system to reduce the mismatch between skills acquired in schools and those demanded by the labor market. These interventions could focus on establishing new training programs offered in vocational education centers keeping in mind that the demand for professionals in the field of renewable energy will increase as coal phases out globally. This is especially important when considering the comparative advantage Kosovo has due to its young population. Similar interventions can also be carried out at higher education levels where the country could focus on improving research and innovation in the field of renewables. The first step in achieving this transformation is the evaluation of the situation on the ground. A gap assessment could be carried out to evaluate the mismatch between acquired skills and labor market demand (including projected demand). Based on this, the government could design specific interventions in the education system.
4. Start to develop economic diversification strategies now to combat the anticipated economic losses from the shutdown of coal-fired power plants and coal mines, thus minimizing economic shocks attributed to the transition. This is specifically valid for coal regions such as Obiliq. The government could, as in the case of Canada, conduct evaluations on the economic potential of the region.
5. Depending on the decision regarding the coal-phase out date, Kosovo should start to work on identifying the number of the affected individuals that are directly employed in the coal sector and their main characteristics such as education background, age and skills. Depending on these characteristics different interventions can be carried out. For workers who will be close to retirement, early retirement can be considered as an option. For those who are relatively younger, there are needs for specific training or re-skilling programs to enable them to transition in other professions. Employment benefits should be provided to workers in this transitioning process. In designing these policies, integrating the input of the impacted citizens is of an utmost importance.
6. Engage in close dialogue with donors to secure financial support and transfer of know-how in order to smooth the transitioning process. As a potential EU candidate, Kosovo is eligible to receive funding under the Instrument for Pre-Accession Assistance (IPA). With the adoption of the Sofia Declaration, IPA III (which covers the period 2021-2027) is expected to have a much more enhanced focus on climate change and on the transition to a low carbon economy. Therefore, it is imperative for Kosovo to work on developing clear project proposals which could be supported by this instrument. Kosovo can use IPA to finance infrastructure projects as well as for capacity building and transfer of know-how. IPA funds can also be blended with soft loans from various International Financial Institutions (IFIs) under the Western Balkans Investment Framework (WBIF) to finance large infrastructure projects which are a priority for the country. Additionally, the country should also work on identifying cooperation possibilities with other bilateral donors who are active in the energy sector.

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Dina Vllasaliu holds a Bachelor's Degree in Applied Arts and Sciences from Rochester Institute of Technology, Kosovo and a MSc in Resource Economics and Policy degree from the University of Maine. Dina started her career working at KOSID as a Research Assistant where she was involved in researching Kosovo's renewable energy potential and energy efficiency policies. She continued working as research and a teaching assistant at the University of Maine from 2016 to 2018, exploring green consumerism and factors that influence Mainers to buy green energy and engage in eco-friendly behaviors. Dina currently works as a Statistics and Economics teacher at Prishtina High School and teaches classes for standardized tests of TOEFL and SAT part-time.

Dina has published her undergraduate paper "Factors Affecting Payment of Electricity Bills in Hajvali"; authored "Factors Affecting Mainers' Preferences for Renewable Energy Sources and Energy Efficiency Measures" and co-authored "Where Are We Headed After the COP-21 Agreement in Paris". This paper examines the position of Kosovo in terms of its legislative basis and implementation roadblocks when it comes to fulfilling the Green Paris Agenda 2015. Lastly, Dina was involved in "Economic Effects of COVID-19: An Analysis of the Private Sector in Kosovo" aimed to assessing Kosovo's economic situation during COVID-19 pandemic.

Lule Bahtiri works as a Statistician for the Central Bank of the Republic of Kosovo. She holds a Bachelor degree in Economics and Statistics from Rochester Institute of Technology, and a Master's degree in Economic Development from Vanderbilt University. Her most recent works include a research paper measuring the Impact of COVID-19 in the Private Sector in Kosovo, a paper assessing Perceptions of Kosovar Youth Regarding Environmental Situation in Kosovo, as well as an impact analysis report for 800 grant beneficiaries in the fields of agriculture, crafts and services.

Lule's prior work experience includes both the NGO and private sector. She is also engaged as a member of the board for the Transformational Leadership Program Alumni Association.



Mimoze Veliu is a development assistance specialist with more than three years of experience in the public sector. She completed her bachelor's degree at Rochester Institute of Technology with a focus in economics and management. In 2016 she was elected as one of the recipients of the Young Cell Scheme scholarship through which she pursued her master's degree in development studies at University of Sussex. Her areas of interest comprise environment and energy. In addition to her experience in the public sector, Mimoze has also worked with different NGOs and has served as the president of the European Young Cell Scheme Alumni. In her free time, she likes to explore nature by walking or hiking and her favorite hobby is photography.

THE BIG PICTURE: A PROGRESSIVE ECONOMIC AGENDA FOR KOSOVO



A dual VET system and the creation of sector skill councils can improve the current mismatches in the labor market and lack of cooperation between the private and public sector in addressing these shortcomings. Establishing labor and trade unions in the private sector, improves social dialogue and enhances workers' rights. The legal framework regulating the labor market needs to ensure flexible work, part-time work, as well as shared work, in professions where this is possible, as schemes to increase employment and improve the participation, especially of youth and women. Through periodic targeted data collection, the Government can identify sectors with development potential and for job creation capacity



In completing a successful energy transition, Kosovo should ensure that the burden is shared equally, and the needs of vulnerable groups and communities are taken into account. The definition of a future energy mix should be preceded by a rigorous technical and financial analysis. Policy intervention support should be provided to RES private sector companies to improve their comparative advantage. This support can be provided in the form of financial incentives or policy interventions such as establishment of innovation centers to stimulate entrepreneurship development in the sector.