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INTERNATIONAL DEVELOPMENT ASSOCIATION

INTERNATIONAL FINANCE CORPORATION

AND

MULTILATERAL INVESTMENT GUARANTEE AGENCY

COUNTRY PARTNERSHIP STRATEGY

FOR

THE REPUBLIC OF KOSOVO

FOR THE PERIOD FY12–FY15

May 1, 2012

South East Europe Country Unit
Europe and Central Asia

Europe and Central Asia
International Finance Corporation

CURRENCY EQUIVALENTS
(Exchange Rate Effective April 16, 2012)
Currency Unit = Euro (€)
€1.00=US$1.30
SDR 1.00=US$1.54

GOVERNMENT'S FISCAL YEAR
January 1 – December 31

ABBREVIATIONS AND ACRONYMS

AAA	Analytical and advisory activities
ARDP	Agriculture and Rural Development Plan
BEEPS	Business Environment and Enterprise Performance Survey
CBK	Central Bank of the Republic of Kosovo
CEFTA	Central European Free Trade Agreement
CEM	Country Economic Memorandum
CPS	Country Partnership Strategy
DPO	Development Policy Operation
EC	European Commission
ECA	Europe and Central Asia Region
EIB	European Investment Bank
EPAP	European Partnership Action Plan
ESW	Economic and sector work
EU	European Union
EULEX	EU Rule of Law Mission in Kosovo
EUSR	EU Special Representative
FDI	Foreign direct investment
FY	Fiscal year
GDP	Gross domestic product
GOK	Government of the Republic of Kosovo
IBRD	International Bank for Reconstruction and Development
ICR	International Civilian Office
IFC	International Finance Corporation
IFI	International financial institution
IMF	International Monetary Fund
IPARD	Instrument for Pre-Accession for Rural Development
ISG	International Steering Group for Kosovo
ISN	Interim Strategy Note
KEDS	Kosovo Electricity Distribution and Supply
KEK	Public Electricity Company
KEP	Kosovo Enterprise Program
KES	Kosovo Environment Strategy
KFOR	Kosovo Force
KRPP	Kosova e Re Power Plant
MDGs	Millennium Development Goals
MESP	Ministry of Environment and Spatial Planning
MSMEs	Micro, small, and medium-sized enterprises

LITS	Life in Transition Survey
MDRI	Multilateral Debt Relief Initiative
MIGA	Multilateral Investment Guarantee Agency
MIP	Mitrovica Industrial Park
MTEF	Medium-Term Expenditure Framework
MW	Megawatt
NEAP	National Environment Action Plan
OECD	Organisation for Economic Co-operation and Development
PCH	Pro Credit Holding
PIU	Project Implementation Unit
PM	Particulate matter
PPIAF	Public-Private Infrastructure Advisory Facility
PPP	Public-Private Partnerships
PRG	Partial Risk Guarantee
PSD	Private Sector Development
PTK	Kosovo Post and Telecommunications Company
QA	Quality assurance
R&D	Research and development
ROSC	Report on the Observance of Standards and Codes
SAP	Stabilization and Association Process
SBA	Stand-By Arrangement
SEDPP	Sustainable Employment Development Policy Program
SEE	South East Europe
SME	Small and medium-sized enterprises
SMP	Staff-Monitored Program
SOK	Statistical Office of Kosovo
SPF	State and Peace-Building Fund
STM	Stability Tracking Mechanism
TA	Technical assistance
TBD	To be determined
TF	Trust fund
UNDP	United Nations Development Programme
WBI	World Bank Institute
WBIF	Western Balkans Investment Framework
y-o-y	Year-on-year

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EXECUTIVE SUMMARY

i. **This Country Partnership Strategy (CPS) for FY12-15 is the first to be prepared since Kosovo declared independence in February 2008 and became a member of the World Bank Group (WBG) in mid-2009.** The CPS follows a series of Interim Strategy Notes (ISNs) implemented over the last decade and is closely aligned with the national development priorities set by the Government.

ii. **With high and persistent rates of poverty and unemployment (particularly among youth and women), the central development challenge confronting Kosovo today concerns how to forge an economic growth path that sustainably creates more opportunity and high-quality jobs for its growing, youthful population.** Kosovo's growth model has thus far been based largely on public investment and the availability of external sources of financing—especially donor assistance and remittances. This model is likely to be unsustainable for the longer term, implying the need for a viable alternative approach. Private-sector investment, which has begun to emerge, is the most promising avenue for generating accelerated growth and jobs in the future but is affected critically by infrastructure bottlenecks, especially persistent shortages of energy. Besides acting as a brake on business growth, frequent load shedding (power cuts) deprives people of light, space heating, refrigeration and cooking fuel—with obvious implications for health, education, and the overall quality of life. Addressing the energy crisis in a comprehensive way is thus a critical component of Government's strategy for creating a hospitable climate for investment, jobs, and better living standards.

iii. **Taking into account both the limited IDA resources available and Kosovo's implementation constraints, the proposed new lending program is highly selective.** The aim is to support fewer, larger operations in sectors/sub-sectors where the WBG has a comparative advantage by virtue of previous experience and analytical work in Kosovo and synergies between IDA, IFC and MIGA. The choice of operations included in the CPS program takes into account Government ownership of the agenda and alignment with the country's overarching goal of closer integration with the EU.

iv. **The main objectives of the CPS are to support Kosovo to (i) accelerate broad-based economic growth and employment generation; and (ii) improve environmental management.** The goal of accelerating growth and employment creation is a continuation of the priorities established in previous interim strategies, which emphasized the need to promote growth via targeted attention to macro-stability, infrastructure development (especially energy), an improved business environment, better governance and investments in agriculture and human capital. The second objective was less prominent in previous strategies. It is being given higher priority now because of wider recognition that environmentally-sensitive use of Kosovo's major natural resources—including investments in energy efficiency and renewables, as well as better management/clean-up of environmental hazards—are critical elements of the effort to improve the population's health and living standards.

v. **Support for Kosovo under this CPS is organized into two pillars corresponding to the two main objectives given above.** Pillar I aims at accelerating broad-based and sustained growth through actions in six main areas: (i) supporting infrastructure, particularly energy, (ii) improving the business climate, supporting the private sector, and increasing access to finance; (iii) supporting agriculture development; (iv) continuing to invest in education and skills; (v) strengthening the regulatory and institutional frameworks for labor and social protection; and (vi) reinforcing public financial management and anti-corruption efforts. Pillar II seeks to support the Government to increase energy efficiency and the use of renewables, reduce environmental hazards, enhance water supply, and move towards harmonization with EU environmental standards.

vi. **It is expected that IDA funding for the CPS would be around SDR 48.1 million, i.e., about US$76 million or US$19 million annually, supplemented by about US$66 million in grant funds**

channeled through IDA by donors. **In addition, IFC will aim to provide around US$40–50 million in the form of direct financing to the private sector as well as additional funds for advisory services. MIGA could provide political risk guarantees** in support of the energy sector. The CPS envisages five new IDA operations, a grant-financed DPL operation and IFC and MIGA transactions.

vii. **A main focus of the new lending under the CPS program is the energy sector with the aim of addressing Kosovo's energy crisis in a comprehensive way, taking full account of environmental considerations and mitigating adverse impacts**. Proposed support would comprise a Partial Risk Guarantee (FY13/FY14) to private investors bidding on construction of a new (replacement) coal-fired power plant, where IFC would also consider to contribute with its own financing and through mobilization of additional funds, as well as transaction advice from IFC for privatization of electricity distribution. To support construction of the power plant, MIGA would consider providing an investment guarantee against non-commercial risks. A large Energy Efficiency and Renewables project (FY13) under CPS Pillar II would also help to implement the country's energy strategy. In addition, a small additional financing operation for the ongoing Energy Sector Clean up and Land Reclamation project would help build Government's environmental and social impact monitoring capacity, as well as carry out additional clean up of the legacy waste at the site of Kosovo's existing thermal power plants. The program also includes three other operations, including the second in a two-part program of grant-funded DPL operations for Sustainable Employment (FY12), an Education Improvement project (FY14) and a Water Supply project (FY15).

viii. **While new lending will be selective, the WBG will continue to support a broader development agenda through a robust program of AAA and technical assistance/capacity building**. In addition to annual analysis and monitoring of the macro-fiscal framework, financial sector, poverty and gender, and ongoing IFC advisory support for the investment climate and PPPs in infrastructure, the CPS includes a Financial Sector Assessment (FSAP) and three ROSCs, a Country Environmental Analysis and programmatic assistance to strengthen public expenditure management, the fiduciary framework and anti-corruption efforts. In addition, Kosovo benefits from AAA activities covering the Western Balkans, including analytical work on Smart Safety Nets, Energy Strategy, Employment and Jobs, Health Finance and Climate Change, as well as several Trust Funds financed by the EC, in areas such as Science, Technology and Innovation, Monitoring and Evaluation and Public Financial Management.

ix. **The implementation of the FY12-15 CPS entails four main risks as follows:**

- Kosovo's uneven track record in fiscal management in the past raises some questions about **medium-term macroeconomic stability**, especially if further economic deterioration occurs in Europe. Recent improvements in fiscal management and the new Stand-By Arrangement (covering a 20 month period from April 2012) with the IMF should help to reduce this risk.
- While investment in Kosovo's energy sector is critical to growth, job creation, and poverty reduction, the Bank's involvement in the new lignite-fuelled **power generation** plant will likely generate controversy among some civil society groups. This risk is being addressed through ensuring transparent processes and regular dialogue/outreach throughout project development.
- An additional risk is that, given continued turmoil in financial markets (especially in Europe), **power project financing** may not be easy to obtain. The availability of WBG guarantees should help to mitigate this risk. Credit enhancement from other multilateral lenders would also help to catalyze needed funds from the private sector.
- Kosovo's **governance** and political structures could destabilize in the event of significant shocks. Also, Kosovo's governance systems still lack full transparency, accountability, and viability. Actions to support improved public financial management included in the DPL and in the ongoing Public Sector Management Project should help to reduce this risk. The Bank will also carry out programmatic AAA to follow on the recommendations of the Country Fiduciary Assessment, including support for anti-corruption initiatives.

I. INTRODUCTION

1. **This Country Partnership Strategy (CPS) is the first to be prepared since Kosovo declared independence in February 2008 and became a member of the International Monetary Fund (IMF) and the World Bank Group (WBG) in mid-2009.** The CPS, which covers FY12–15, follows a series of Interim Strategy Notes (ISNs) implemented over the last decade—the most recent one being a two-year ISN for FY10–11. This CPS is being prepared after Kosovo's 2011 general election to ensure close alignment with the Government's national development priorities in the context of the country's aspirations for integration with the European Union (EU). As Kosovo is an IDA-only country, the strategy will be financed principally by an allocation from IDA-16 for FY12–14 and from IDA-17 for FY15. At this stage, it is expected that the total funds available for Kosovo for the CPS period would be around SDR 48.1 million (or about US$76 million), i.e., about US$19 million annually. It should be noted, however, that in accordance with IDA rules, all the amounts beyond FY12 are indicative only. Actual allocations will depend on (i) the country's own performance; (ii) its performance relative to that of other IDA recipients; (iii) the amount of overall resources available to IDA; (iv) changes in the list of active IDA-eligible countries; (v) terms of financial assistance provided (grants or loans); and (vi) the amount of compensatory resources received for Multilateral Debt Relief Initiative (MDRI). Since IDA allocations are made in SDRs, the US dollar equivalent is dependent upon the prevailing exchange rate. The International Finance Corporation (IFC) will provide about US$40–50 million in the form of direct financing to the private sector as well as additional funds for advisory services. To support private sector participation in the power sector, MIGA would consider providing an investment guarantee against non-commercial risks and IFC would consider providing financing for its own account as well as mobilize additional funding from other financial institutions. In addition, substantial grant resources—about US$66 million—will complement WBG funds in financing the CPS program.

2. **The FY12–15 CPS proposes a selective and targeted support program aimed at (i) promoting growth and employment, and (ii) improving environmental management.** Building on the direction set by the FY10–11 ISN, the CPS consolidates the shift in the Bank's focus from post-conflict reconstruction support towards a clear emphasis on addressing medium-term development challenges. The strategy pays due attention to lessons learned from the WBG's involvement in Kosovo in the decade since the end of the 1998–99 conflict, the execution of ongoing Government or donor-sponsored programs, and consultations with the Government of Kosovo, Parliament, the private sector, civil society, and the community of bilateral and multilateral development partners.

3. **The main objectives of the CPS are to support Kosovo to (i) accelerate broad-based economic growth and employment generation; and (ii) improve environmental management.** The proposed strategic focus of this CPS stems from the Government's own policy priorities anchored in the need to build a stable society following years of conflict, and the objective of preparing the country for eventual EU membership. The CPS is fully aligned with the Government's national development plan and the Medium-Term Expenditure Framework (MTEF) for 2011–14. Fostering employment-generating, inclusive growth is critical for a young, multiethnic country with high unemployment and, as such, could help to reduce the strains that exist within the society from years of ethnic conflicts. In parallel, there is a need to increase energy efficiency and the use of renewables, strengthen environmental management, and improve access to good quality water.

II. COUNTRY CONTEXT

A. Political Context

4. **Kosovo is a potential candidate for EU membership, now with a clear perspective in the *Stabilization and Association Process*** (SAP). The February 2012 agreements in the EU-moderated talks with Serbia on Kosovo's regional representation[1] and integrated border management (the "footnote compromise") appears to have enabled the European Commission (EC) to establish contractual relations[2] and, on that basis, (i) take the first steps in the SAP, starting with the feasibility study; and (ii) advance membership in European (financial) institutions. As per assurance contained in the EC's October 2011 *Enlargement Package*, the EU has opened the visa liberalization dialogue in January 2012, with the aim of enabling visa-free travel to the Schengen area in due course. The EC has reiterated its commitment to full EU membership "once conditions are met." Progress towards integration is monitored regularly via annual Progress Reports. The EC's 2011 Progress Report called for considerable reforms and investments to enable Kosovo to cope with competitive pressure and market forces within the EU.

5. **The period of "supervised independence" ends in December 2012.** In early 2012, the 25-country International Steering Group (ISG), set up in 2008 to guide democratic development, promote good governance, multi-ethnicity, and the rule of law, announced its plans—with subsequent support from Parliament—to close the International Civilian Office (ICO), thus far the final authority regarding the interpretation of the Comprehensive Settlement Proposal ("Ahtisaari Plan").[3] The appointment of the new head of the EU Office in early 2012 marked the end of the personal union between the EU Special Representative (EUSR) and the International Civilian Representative (ICR), in preparation of the latter position's abolishment. However, both the EU's rule-of-law mission (EULEX), which performs some police, judicial, and customs functions, and the NATO-led peacekeeping force (KFOR), with more than 6,000 soldiers from 30 countries, are expected to continue to play important—if gradually declining—roles in the foreseeable future. KFOR's main objectives are to (i) provide a safe and secure environment; (ii) maintain security in northern Kosovo; and (iii) oversee the newly established Kosovo Security Force.

6. **Although there has been a steady increase in international recognition of Kosovo, the country is not yet a member of the United Nations, in turn hindering Kosovo's overarching objectives of political integration and socio-economic development.** As of March 20, 2012, 89 countries have recognized Kosovo's independence, including all neighbors except Serbia (which regards Kosovo as a UN-governed entity within its sovereign territory). The prospect for UN membership[4] remains dim as two veto-holding permanent members of the UN Security Council have called for the statehood issue to be settled in direct negotiations between Pristina and Belgrade. Following the violent escalation of the trade tit-for-tat over the recognition of Kosovo's customs stamps in 2011-S2, the status of northern Kosovo—comprising three Serb-majority municipalities and the city of Mitrovica that have refused to accept the authority of the central authorities in Pristina—has been placed on the political agenda, albeit without a clear perspective of a political settlement.

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[1] With this agreement, Kosovo will represent and sign for itself in regional fora and not require any longer the representation through UNMIK. However, it does so not under its Constitutional name ("Republic of Kosovo") but as "Kosovo*" with a footnote stating, "This designation is without prejudice to positions on status and is in line with UNSC 1244 and the ICJ Opinion on the Kosovo Declaration of Independence."

[2] The "footnote compromise" appears to have unblocked obstacles in the formal progress in advancing the integration agenda that has been constrained by the non-recognition of Kosovo by five EU members.

[3] In April 2008, UN Special Envoy Martti Ahtisaari had presented to the UN Security Council a "Comprehensive Proposal for the Kosovo Status Settlement" with a recommendation of eventual independence, following a period of international supervision.

[4] For a "peace-loving State" to become a member of the UN, it would have to (i) garner the recommendation from 9 of the 15 members of the Security Council (without any of the five permanent members vetoing such a decision); and (ii) secure a two-third majority of currently 193 member states.

7. **Kosovo's political system is a representative democracy with a unicameral legislature**. The Parliament of Kosovo has 120 members, of which 10 are reserved for ethnic Serbs and another 10 for other minority parties. Electoral laws also require that at least every third candidate on the electoral lists of all parties is female. There are currently five major political parties represented in Parliament and twelve smaller ones representing ethnic minorities. The largest parties include the center-left Democratic Party of Kosovo (PDK), the center-right Democratic League of Kosovo (LDK), the nationalist youth movement Self-Determination (*Vetëvendosja*), and the center-right Alliance for the Future of Kosovo (AAK). The Government coalition is formed between the PDK and two other political parties represented in Parliament, viz., the pro-business New Kosovo Alliance (AKR) and the Serb-minority Independent Liberal Party (SLS). Following two presidential crises in 2010 and 2011 and a subsequent compromise across all major parties, President Atifete Jahjaga—Kosovo's first female, first non-partisan president—is expected to be the last head of state elected indirectly by Parliament. Two commissions are currently finalizing a broad-based overhaul of the Constitution and the Electoral Law to allow, *inter alia*, for the direct election of the President. On this basis, the next rounds of presidential and general elections are foreseen in 2013.

B. Recent Macroeconomic Developments

8. **Kosovo's economic growth has averaged over 4 percent since the end of the conflict in 1999, and remained positive throughout the global economic crisis. Growth peaked at 6.9 percent in 2008 before declining to 3 percent in 2009 in the wake of the crisis** (see Table 1). The overall impact of the crisis was smaller in Kosovo than in neighboring countries, largely because of Kosovo's limited integration into the global economy. Growth is estimated to have reached around 4 percent in 2010 and 5 percent in 2011, with preliminary data suggesting that growth was driven by increased public spending, and, to a lesser extent, by private investment and a surge in commodity exports. The IMF projects that GDP growth will be around 3–4 percent in the medium-term, because Kosovo is somewhat insulated from the global economy. However, a sharper-than-expected downturn in Europe would lower growth through declines in exports and remittances.

9. **Having adopted the euro as the local currency, Kosovo has to rely on fiscal policy as the main anchor for macroeconomic stability.** However, Kosovo's fiscal position has become strained as expenditures have risen rapidly since 2008. The savings from fiscal surpluses accumulated up until 2007, reflecting conservative spending policy and over-performing revenues, began to erode in 2008 and the fiscal deficit widened in successive years. The Government concluded an 18-month, €104-million Stand-By Arrangement (SBA) with the IMF in July 2010. However, the program went off-track, largely due to the failure of an attempt to privatize the telecommunications company (PTK) and an (unplanned) increase of 27 percent in civil servant wages to fulfill an electoral campaign promise. In July 2011, the authorities and the IMF agreed on a six-month staff-monitored program (SMP). Although the non-realization of revenues from the sale of PTK could have been covered by existing accumulated bank balances, the Government, in agreement with the IMF, decided instead to make cuts of about €60 million to the budget to preserve a higher level of bank balances.

10. **Since July 2011, macroeconomic policies have been broadly satisfactory and the implementation of structural measures under the SMP has remained on track leading to the agreement on a new IMF SBA**. The two SMP reviews were successfully concluded with fiscal targets met; the 2011 budget deficit (1.8 percent of GDP) was 1 percentage point lower than projected. The process of privatizing PTK (originally expected to be completed in 2011 and part of the SMP) is ongoing in 2012 and the financial transaction is expected to close in 2013. due to waning investors' interest, which, in turn, put pressure on the Government's ability to finance the deficit. In this context, the

Government cut expenditure by about €60 million in the 2011 budget and adopted a more restrained budget for 2012. In terms of structural measures, solid reform progress was achieved on tax administration, banking, and energy reforms. As a result of the successful implementation of the SMP, the authorities and the IMF reached agreement on a 20-month, €107-million SBA, starting in April 2012.

Table 1: Kosovo Macroeconomic Indicators

	2008	2009	2010	2011	2012	2013	2014
		Actual		Estimate		Projections	
Population, in thousands*	1,662	1,687	1,712	1,738	1,764	1,791	1,817
GDP, in millions of euro	3,851	3,912	,216	4,637	4,911	5,234	5,508
GDP per capita, in euro	2,317	2,319	2,462	2,668	2,784	2,923	3,031
Investment, in percent of GDP	28.6	32.3	33.9	33.2	32.6	33.9	32.3
Real GDP growth, in percent	6.9	2.9	3.9	5.0	3.8	4.1	3.2
CPI (period average), in percent	9.4	-2.4	3.5	7.3	0.6	1.2	1.4
Fiscal accounts, in percent of GDP							
Revenues	24.5	29.3	27.6	28.1	28.1	27.1	27.8
of which: official grants	0.0	0.0	0.7	0.4	0.7	0.0	0.0
Primary expenditures	24.7	29.9	30.0	29.8	30.5	30.2	28.6
Interest income, net	0.0	-0.2	0.3	-0.1	-0.1	0.0	-0.1
Overall balance	-0.2	-0.7	-2.6	-1.8	-2.7	-3.3	-1.1
Stock of Government bank balances	10.8	8.7	5.8	3.5	3.8	8.8	8.7
Public debt	0.0	6.7	6.9	5.6	6.9	8.5	9.0
External accounts, in percent of GDP							
Current account	-15.3	-15.4	-17.4	-20.3	-18.3	-18.3	-16.1
Exports of goods	5.6	4.5	7.2	6.9	7.2	7.5	8.0
Imports of goods	-49.0	-47.3	-49.4	-52.0	-49.7	-48.9	-47.8
Services receipts	9.1	11.0	11.3	13.1	13.3	13.4	13.6
Services payments	-7.0	-7.9	-9.7	-9.1	-8.8	-8.4	-7.9
Transfers	21.5	22.1	21.1	18.1	17.3	15.6	15.6
Official transfers	7.5	10.2	8.6	5.9	5.4	3.9	3.5
Private transfers	14.0	11.9	12.5	12.2	11.9	11.8	12.0
Capital account	0.0	2.8	0.6	0.1	0.0	0.0	0.0
Financial account, including CBK	12.9	11.1	12.5	15.9	12.3	14.2	12.4
Net errors and omissions	2.5	1.6	4.3	4.3	4.1	3.8	3.6

* Population number here does not include Serbs living in the northern part of Kosovo

Sources: Kosovo authorities, IMF and WB staff estimates.

11. **The authorities are committed to maintaining medium-term fiscal sustainability**. The fiscal deficit is expected to increase to 2.7 percent of GDP in 2012 and to peak at 3.3 percent of GDP in 2013, due to high spending on the Route 7 motorway. It is then projected to decline in 2014 when the motorway project is planned to be completed. At the same time, improvements in tax administration are expected to improve tax collection and tax revenue over the medium-term. The commitment to a sustainable medium-

term fiscal framework was supported by actions taken by the authorities in the second half of 2011. First, the construction of the Route 6 motorway to FYR Macedonia will start only after a cost-benefit analysis is carried out and financing secured. Second, additional war-related benefits, defined by the law on war values of December 2011, will be introduced based on a fiscal impact assessment and consider affordability and economic incentives criteria. This implies that the authorities would first define the amount of spending and only then define the benefits, so that spending limits are not breached.

12. **Kosovo's public debt—at 5.6 percent of GDP at end-2011—is very low and largely comprised of the inherited share of ex-Yugoslav debt to IBRD**.[5] There are two legal mechanisms to preclude public debt from rising to unsustainable levels. First, Kosovo's public debt law sets a maximum public debt ratio of 40 percent of GDP and, second, the Constitution requires that any external borrowing by the Government requires Parliamentary ratification with a two-thirds majority. The public debt stock was entirely external until 2011, as the Government securities market had not yet been developed. As of January 2012, the Ministry of Finance has successfully issued the first rounds of 3-month T-bills, in the amount of €10 million each, with preparations being made for 6-month T-bills later on in 2012. Commercial banks, which have good liquidity (including non-interest earning excess reserves at the CBK) are expected to be the main investors in the domestic securities market. While data on private external borrowing is not fully available, such borrowing is likely to be very small (below 1 percent of GDP), given Kosovo firms' very limited access to international financial markets. Therefore, total external debt, though not officially published, is estimated to be only slightly higher than the public debt.

13. **Despite its low external and public debt, Kosovo's debt sustainability could be jeopardized by worsening fiscal deficits or growth moderation**. The IMF's debt sustainability analysis in the 2011 Article IV report shows that all debt indicators remain on a sustainable path over the next two decades in the baseline fiscal and external scenarios shown in Table 1 (Annex 2). However, the debt trajectory is subject to prominent risks that could derive either from fiscal issues and/or growth shocks. Maintaining the primary deficit as a share of GDP at the 2011 budgeted level of 4.8 percent of GDP over a two decade period would put debt on an unsustainable path. Debt would also become unsustainable if growth is lower by one standard deviation (2.3 percentage points) in 2012 and 2013. In terms of external debt, the main weakness lies with the high debt and debt service to exports ratios. This is a result of Kosovo's small export base, a weakness which is somewhat rectified by Kosovo's large and stable remittance flows.[6]

14. **With limited room to maneuver in monetary policy, maintaining macroeconomic stability must rely on sound fiscal policy.** On the revenue side, the main priorities for policymakers are to broaden the tax base and continue to improve revenue collection. Making fiscal spending more efficient and sustainable will depend on the timely implementation of structural reforms in key sectors, including energy, transport, and health. In addition, maintaining control over recurrent expenditures—in particular, salaries and social transfers—will be essential for fiscal sustainability. Given Kosovo's unilateral euroization, monetary policy is constrained, and ensuring stability of the banking sector will remain a priority especially in the prevailing environment of uncertainty in European financial markets. Setting up the "emergency liquidity assistance" fund for the banking sector represents an important step.

C. Socio-Economic Environment

15. **Although Kosovo has come a long way in re-establishing peace and social stability, a few municipalities with sizeable minority populations—mainly those in the Serb-dominated**

[5] Up to 2009, Kosovo had no public debt. In 2009, Kosovo took over its share of former Yugoslavia's debt to IBRD, in the amount of €381 million (9.7 percent of GDP). Kosovo has not participated in the division of other assets and liabilities of former Yugoslavia; if this process takes place, it may inherit additional debt owed to the Paris and London Clubs.

[6] The IMF's debt sustainability analysis includes the potential additional liabilities referred to in footnote 5.

municipalities in northern Kosovo—continue to experience unrest. While considerable progress has been made in overcoming the tensions in mixed areas, the three Serb-dominated municipalities in northern Kosovo remain prone to localized outbreaks of violence. Other minorities tend to keep a low profile in terms of ethnic conflict but sometimes suffer economic and social discrimination, and are disproportionately represented among Kosovo's poorest households. The Government of Kosovo and civil society groups have put in place a number of initiatives to promote inclusion of all minorities including through affirmative action.

16. **With a per-capita GDP of about €2,600, Kosovo is one of the poorest countries in Europe.** With 34.5 percent of its population of 1.8 million[7] living below the poverty line, i.e., on less than €1.55 per day (and about 12 percent living on less than €1 per day), poverty is widespread. However, Kosovo has a relatively low Gini index (about 0.3 in 2009) and a relatively flat consumption distribution. No significant differences exist between urban and rural poverty, but there are notable regional differences, with poverty rates varying from 53.8 percent to 18 percent among districts. Young people are disproportionately poor, accounting for about 60 percent of people living below the poverty line. Kosovo's ethnic minorities—especially the Roma, Ashkali, and Egyptian ethnic groups, which comprise about 2–3 percent of the population—are particularly vulnerable to income poverty besides frequently being marginalized in socio-political and economic life. As in many other countries, there is a strong negative correlation between education and poverty, with those having secondary or higher education much less likely to be poor.

17. **Widespread unemployment and a lack of quality jobs have contributed significantly to poverty and income insecurity as well as to gender inequality, social instability, and ethnic tensions.** With a 45-percent unemployment rate and a low employment rate (29 percent), Kosovo has the weakest employment track record in Europe. Kosovo's 53 percent labor participation rate among the working-age population is substantially below the ECA average (65 percent). Obviously, the lack of jobs has direct consequences on income, and empirical evidence suggests that the risk of poverty is 20 percent higher for the unemployed than the employed. Households with unemployed heads have the highest extreme poverty indices. In addition, many households with adult members in precarious or unsteady jobs are also below the poverty line. Many of these households are dependent on small, informal enterprises for the majority of their income, reflecting the high degree of informality in Kosovo's economy.

18. **Kosovo's difficult labor market conditions have been especially severe for youth and women.** Unemployment among the population 15–25-year-olds reaches 76 percent—a figure that is more alarming considering that 21 percent of Kosovo's population is between the ages of 15 and 25. The poor quality of the education system, coupled with limited employment opportunities, makes it difficult for young people to access and retain jobs. Moreover, young people who do find employment are typically hired into low-skilled, low-productivity positions, often in the informal sector. According to survey data, about 20 percent of employed youth did not have an employment contract, 37 percent were not entitled to paid leave, and 73 percent were not registered in the social security system. At 56 percent, unemployment is also unacceptably high among Kosovo's women. Only 11 percent of working age women are employed, compared with 68 percent of men, in part because of lower educational opportunities and achievement (see Box 1).

[7] According to the data from the 2011 census, Kosovo's resident population stands at about 1.73 million, excluding the population in northern Kosovo. The World Bank thus estimates the entire population at close to 1.8 million.

Box 1: Gender Disparity in Kosovo

Kosovo has made progress in tackling gender inequalities over time, but substantial gender gaps persist. Focusing on gender inequalities in human capital and economic opportunities, a gender diagnostic, undertaken to inform the CPS, identified significant disparities: (i) large gender gaps in literacy, educational attainment and secondary school enrollment; (ii) overall low life expectancy, more pronounced for women, and high maternal mortality (iii) exceptionally low women's labor force participation and employment rates; and (iv) low representation of women in entrepreneurship and management, as well as in senior Government positions.

Gender gaps in human capital. Kosovo has achieved near universal primary school enrollment and the country has made significant progress in improving literacy rates. However, significant gender gaps persist. Women are more than twice as likely as men to be illiterate, with illiteracy rates of 7.2 percent for females, compared to 2.2 for males. However, some progress has been made in recent years, given that the gender gap widens with age (in rural areas, the literacy gender gap reaches 34 percentage points among the elderly in rural areas. Women have lower educational attainment than men in Kosovo and recent figures show that girls are underrepresented in educational institutions at all levels—except for university education. In terms of enrollment, large gender gaps appear in secondary level, with fewer girls enrolled than boys. Drop-out rates for girls in primary education are relatively higher and, while boys' drop-out rates have decreased since 2004, they have increased for girls.

Maternal mortality is estimated at 43.3 per 100,000 births, which is one of the highest rates in the ECA region. Inadequate quality of antenatal care, pregnancy and labor complications, and unsafe abortions are among leading causes of maternal deaths. Poor nutrition and anemia are also important contributing factors. Life expectancy has increased slightly in Kosovo in the past decades for both men and women. Nevertheless, life expectancy for both groups is the lowest of the Western Balkans countries (71.8 and 67.6 years for women and men, respectively) and women's advantage in life expectancy is smaller than that seen in global averages, mainly due to lower life expectancy for women. Other important gender-related concerns in Kosovo are the high rate of miscarriages, stillbirths and abortions, and evidence of a sex imbalance at birth in favor of boys.

Gender gaps in economic opportunities. Labor market outcomes in Kosovo are among the poorest in the region, particularly for women. Women's labor force participation is significantly lower than for men (26 percent compared to 58 percent in 2009, respectively) and has decreased since 2002. This low activity rate for women, the lowest in the Western Balkans, is partly related to a disproportionate share of household responsibilities or because they are discouraged by the absence of opportunities for paid employment outside the home. Other closely related factors are the lack of childcare facilities and an inadequate access to flexible work arrangements. In addition, unemployment rates are significantly higher for females (56 percent) than for males (41 percent) in Kosovo, and are the highest, for both sexes, of countries in the region. Unemployment rates reach very high levels for the younger population (15–24 years), at 82 percent for women and 69 percent for men. Among the low share of employed women, they are considerably underrepresented in leading positions in firms, comprising less than ten percent of all entrepreneurs and with the lowest representation in private firms' top management (0.3 percent) of all ECA countries. Finally, although Kosovo has made significant progress in increasing women's voice in political decision-making, the share of women in leading Government positions remains low.

19. **Besides facing challenges of widespread income poverty, Kosovo's citizens have insufficient opportunity for investment in education and health as evidenced by relatively low social indicators.** While Kosovo's net primary enrollment rate reaches 96 percent, the country's secondary and higher education enrollment lags behind rates in South East Europe (SEE). For example, Kosovo's 75 percent net secondary enrollment rate trails the 82 percent rate in neighboring FYR Macedonia, and drop-out rates remain high in rural areas, especially among girls. The gender gap in secondary enrollments has not yet narrowed tangibly, with women in their twenties being much less likely than men to have completed secondary education (60 percent versus 76 percent). Moreover, Kosovo's education system does not provide to its nearly one-half million students adequate curricula and instruction to produce the skills that the evolving labor market requires. The National Qualification Authority recently adopted a new National Qualification Framework (NQF) which aims to strengthen standards in pre-university and vocational/technical education. Health outcomes in Kosovo are extremely low. According to UNDP data, Kosovo had the highest child and infant mortality rates and the lowest life expectancy (70 years in 2009)

in SEE. Major investments in the quality of basic healthcare services are needed to improve outcomes in tuberculosis, immunization, and reproductive care. Access to health care also faces significant barriers. Within Europe, Kosovo has the lowest rate for hospital admissions and the second lowest rate for outpatient visits. Shortages of essential drugs are widespread, and out-of-pocket payments constitute 80 percent of the expenditures on pharmaceuticals.

III. KEY DEVELOPMENT CHALLENGES AND GOVERNMENT STRATEGY

20. **The central development challenge relates to an economic growth path that (i) creates high-quality jobs; and (ii) uses key natural resources in a sustainable and environmentally sensitive manner.** Kosovo's growth model in recent years has largely been based on the availability of external sources of financing, especially donor assistance and remittances. The Government of Kosovo recognizes that this model cannot be the foundation of a sustainable growth strategy, especially in the current economic environment. Donor support has already declined considerably from its peak and is expected to decline even further. By contrast, private-sector investment has begun to emerge and could be the principal engine for accelerated growth and employment-creation. Creating a hospitable climate for investment is thus a critical component of Government's current strategy -- Vision of Economic Development Priorities and associated Action Plan and Medium-term Expenditure Framework (2011-2014) -- for creating jobs for the large proportion of unemployed Kosovars, and accelerating the convergence to SEE and European income levels. In addition, Government attaches high priority to agriculture sector development as the sector currently accounts for 35 percent of total employment. Kosovo is also increasingly aware of the need to pay more attention to environmental problems and to move towards EU environmental standards and requirements. The remainder of this section provides a more in-depth look at the challenges faced by Kosovo in each of these areas.

A. Key Challenges in Promoting Private Investment and Employment

21. **Kosovo has considerable potential to shift towards rapid and sustainable private sector-led growth and job creation if it can address existing obstacles to investment.** As noted in the Bank's 2010 Country Economic Memorandum (CEM), the country enjoys several comparative advantages that are important to the creation of a flourishing export sector as well as to attracting local and foreign investment in the tradable sectors. Indeed, Kosovo is endowed with several key assets, viz., abundant natural resources, a young and growing (albeit underutilized) labor force, good quality agricultural land, and virtually free access to the EU and regional markets. In some respects, the policy environment is also favorable, including (i) a tax system that is simple and has low rates; (ii) a labor market that is more flexible than in neighboring countries; and (iii) comparatively low wages for (semi-)skilled workers. Nonetheless, there are a number of serious obstacles to investment that need to be addressed if Kosovo is to realize its potential as an attractive destination for local and foreign private investment.

22. **The 2010 BEEPS[8] report for Kosovo points to five sets of obstacles to doing business**. While in some areas the business climate in Kosovo is better than that in neighboring countries (or even in the EU10+1), main challenges include severe infrastructure gaps, deficiencies in the rule of law, shortages of appropriately skilled labor, limited access to finance, and onerous regulatory procedures for business entry and operations. Challenges and the Government's strategies in each of these areas are described below.

[8] See EBRD and World Bank Group, 2010, "BEEPS At-A-Glance 2008: Kosovo."

Infrastructure

23. **Surveys of private firms (BEEPS 2010) indicate that infrastructure problems are perhaps the most serious constraint faced by businesses in Kosovo**—with power, transport, and telecommunication cited most frequently. Over 98 percent of Kosovo firms surveyed by BEEPS cited unreliable electricity supply as a major obstacle to day-to-day operations and a constraint both to investment in new equipment and business expansion, in turn affecting job and employment creation. Frequent power outages both increase costs by necessitating the use of expensive and polluting diesel-fired power generation and prevent investment in sophisticated equipment. Moreover, the power sector is currently both a major drain on public funds—absorbing €70 million in public subsidies annually—and highly polluting. To address these critical issues, Government—working in close concert with the EC, USAID, and the World Bank Group—has developed a multi-pronged approach aimed at ensuring adequate and reliable energy supplies, reducing the need for public subsidies to energy, and limiting the negative environmental impacts of power generation. The strategy also aims at significantly enhancing the involvement of the private sector in generation and distribution, while strengthening Government's regulatory and supervisory capacity. The implementation of the strategy will depend on continued support from Kosovo's external development partners as well as interest from private energy firms, which could be an issue in the current uncertain global economic climate. More details concerning the energy situation and Government's strategy are given in Box 2 below.

24. **Kosovo's transport system is also inadequate in relation to business and trade needs and is incompatible with European standards in many respects.** Adequate road transport and its integration with the networks of neighboring countries are of critical importance, given Kosovo's landlocked geographical position. Currently, the costs of goods transported between Kosovo and key trading partners are among the highest in the region and a major deterrent to the achievement of greater trade integration and the development of export-oriented businesses. In this context, Government has embarked on major road investments, notably construction of a €660-million highway to Albania (providing businesses with sea access and a route to Western Europe) which is now under way, and has plans for another major highway to FYR Macedonia. Within Kosovo the road network density (3.3 km per 1,000 people) lags behind the ECA average (8.6 km per 1,000 people) and quality is poor due to poor construction and inadequate maintenance.

Governance and Rule of Law

25. **Kosovo ranks poorly on many dimensions of governance.** The EC's latest Progress Report highlighted that perceptions of widespread corruption and weaknesses in the rule of law inhibited private investment and, in turn, job creation. Other governance sources reinforced these findings (Table 2). The 2010 World Governance Indicators placed Kosovo below the Europe and Central Asia averages for Government effectiveness, regulatory quality, and control of corruption. The Global Integrity Index rated Kosovo as "very weak" on Government accountability, administration, and civil service. Weak administration manifests itself directly in poor service delivery. A 2010 Life in Transition (LIT) Survey ranked Kosovo lower than the SEE average on satisfaction with public services ranging from social services to police and the courts. The Government has initiated many reforms and enacted some laws, but implementation is slow. The Government's revised public administration strategy for the period 2010–13, adopted in September 2010, has not yet been implemented. In civil service reform, some

Table 2: Rankings for Key Governance Indicators
(lower ranks indicate better performance)

	Doing Business Index 2012 (of 183 countries)	Transparency International Corruption Perceptions Index 2011 (of 183 countries)
Kosovo Rank	117	112
ECA Average Rank	72.4	93.1
SEE Average Rank	82	83.6
EU-25 Average Rank	36.3	32.4

Sources: Doing Business 2012, Transparency International, 2011

Box 2: Energy in Kosovo

Demand for energy has been growing rapidly in Kosovo over the past decade, with actual energy consumption and peak demand growing by more than 90 percent between 2000 and 2010—despite being constrained by supply limitations and consequent frequent load shedding. As seen in many countries, these problems have multiple adverse impacts. First, prolonged electricity load shedding (power cuts) deprives people of light, space heating, refrigeration, and cooking fuel—with obvious implications for their health, access to education, and overall quality of life. Second, there is convincing evidence that Kosovo's unreliable power supply is a major constraint to business development and, hence, badly-needed employment opportunities. As the population grows, demand for electricity is continuing to climb by about 4.6 percent a year.

Most of Kosovo's domestic electricity generation comes from two coal-fired power plants (Kosovo A and B) with net operating capacity of about 840–900 MW. Additional supply, amounting to 5–17 percent of annual consumption over the past decade, is derived largely from imports of electricity via regional interconnections. The availability of electricity imports for base power is unreliable and subject to price volatility because it is affected by supply conditions in neighboring exporting countries (e.g., hydrological conditions in the region). A KfW funded 400kV transmission line between Kosovo and Albania should help to facilitate an exchange of power, given that Albania relies principally on hydroelectric generation while Kosovo has predominantly thermal power. This power exchange should result in operational, economic, and environmental benefits to both countries. In general, however the regional market is shallow. Moreover imported power is also frequently generated from thermal sources. With regard to generation as well, the current situation is unsatisfactory: both thermal power plants are antiquated and unreliable and operating well below their installed capacity. For example, two of five units at Kosovo A, the oldest and largest plant, are out of operation and the remaining three produce only up to about 350 MW, well below their installed capacity. The Kosovo B plant (net capacity of about 540 MW), though newer (about 25 years old), is affected by damage to the turbine rotors of its two units and deterioration of other critical components, resulting in frequent forced outages. Both plants are highly polluting, with Kosovo A being the worst single-point source of pollution in SEE. Its high emissions of sulfur and nitrogen oxides and particulate matter (PM) have significant negative health impacts for the population in the vicinity of the plants, which includes the capital city Pristina.

In this context, Government, with support from several external partners, has proposed a multi-pronged approach to addressing Kosovo's energy crisis and related environmental issues. It seeks to (i) close Kosovo A by 2017 and replace it with a new, state-of-the-art, privately operated 600-MW power plant termed the "Kosova e Re" Power Plant (KRPP); (ii) attract private investment to rehabilitate and upgrade Kosovo B, including ensuring conformity with EU environmental standards; (iii) privatize electricity distribution *inter alia* to reduce technical and commercial losses; (iv) step up payment enforcement and raise tariffs to levels consistent with full cost recovery; (v) expeditiously address environmental legacy issues associated with Kosovo A and B; (vi) invest significantly greater resources in energy efficiency in the near term; and (vii) maximize the use of renewable energy (hydro, solar, wind, geothermal). Implementation of the above strategy is expected to reduce PM emissions by over 90 percent, sulfur and nitrogen oxides by over 70 percent and lower carbon emissions per unit of electricity produced.

Several studies of Kosovo's energy options have been conducted with donor assistance over the last ten years. A 2004 Regional Generation Investment Study for the Western Balkans and its 2007 Update indicated an emerging shortage of 10,000 -12,000 MW by 2025. More recently, the Bank conducted a study entitled Development and Evaluation of Power Supply Options for Kosovo (2011), whose findings broadly support the strategy being proposed by the Kosovo Government. The Options Study considered ways of meeting Kosovo's current and future energy needs taking into account economic, financial, and environmental costs, including the potential contributions of efficiency improvements, demand-side management, construction of small hydropower plants, and other renewable sources, importing electricity from neighboring countries and additional thermal generation. The study found that the lowest-cost reliable energy supply that would meet Kosovo's base load and peak demand is a mix of thermal and renewable energy sources. This mix would include (i) a hydropower plant (Zhur) of about 300-MW and, according to a DANIDA study, at least 60 MW from small hydropower plants; (ii) a preliminary estimate of 395 MW in wind, biomass and biogas-fired power generation (to be confirmed through technical studies); (iii) upgrading of Kosovo B plant; and (iv) construction of the new 600-MW coal power plant which has been proposed by Government to replace Kosovo A. The study is premised on continued investment in energy efficiency improvements, rapid reduction of technical and commercial losses and development of renewable energy sources. In the longer term (10–15 years) it is expected that construction of a Balkans gas-ring could enable Kosovo to import gas to meet its growing energy demand.

important regulations and administrative instructions have been adopted, such as the regulation on working hours, on job descriptions, the appointment of senior civil servants, and the register of civil servants. However, the legal framework necessary to implement the primary civil service legislation has not been adopted. Judicial reform has been initiated, but has not improved court efficiency or assured the safety and independence of the judiciary yet. An anti-corruption agency has been established and some legal reforms taken to strengthen the anti-corruption legal framework, but implementation remains a challenge. Considerable support is being provided by the EU's ("technical") Rule of Law Mission to Kosovo (EULEX)—with around 3,200 staff (of which 1,950 international)—in helping Kosovo's Government to strengthen police, judiciary, and customs.

Education and Labor Markets

26. **Appropriately educated, skilled human resources are critical to private investment, growth, and employment**. The education system needs to improve quality and relevance throughout the system and address access issues at secondary and post-secondary levels where students from the poorest households and women/girls from all income quintiles are clearly underrepresented. Indeed, 45 percent of businesses surveyed reported difficulties in recruiting skilled workers; in turn, more than 50 percent of unemployed men cited lack of appropriate education and skills as a reason for their inability to find work. Kosovo's school infrastructure is dramatically insufficient: more than half of schools operate on double shifts and about 5 percent on triple shifts. School and university management is weak, particularly with respect to monitoring of enrollment, performance, and institutional finances. At the same time, the education system remains poorly regulated, resulting in the low quality of services and weak linkages with labor demand, including apprenticeships for youth. Importantly, and within the framework of moving towards universal access to secondary education, targeted strategies are needed to increase girls' and women's access to secondary and post-secondary education and significantly raise enrollment. Similarly, attention needs to be paid to means of raising secondary school enrollments for children from the poorest households, of which only about two-thirds attend secondary school. The Government is placing high priority on strengthening the education system and has prepared a multi-year strategy for developing both general and higher education. The strategy, which addresses quality, implementation, and management issues, should help to alleviate sector deficiencies.

27. **While Kosovo's considerable labor market flexibility should be sustained and labor taxes kept low to promote labor demand, active labor market programs need to be strengthened to facilitate the transition to work.** Employment rigidity is among the lowest in the region and labor taxes are low. Kosovo faces the challenge of maintaining these favorable conditions in the face of pressures to increase worker protection and social services. It has done so successfully, for example, by passing a health insurance law that transforms the financing of health services without threatening the financial sustainability of the health system or increasing labor taxes. At the same time, however, major efforts are needed to improve the transition from welfare and long-term unemployment to work. Currently, more than 63 percent of unemployed people remain without work for over a year. To help to address this issue, the Government has introduced public works programs aimed at reducing joblessness in the short term and providing beneficiaries with the work experience needed to maintain/improve their employability. Employment services, however, remain ineffective, largely due to the inadequacy of information systems and low local capacities. Government has recently begun addressing this gap. As a first, immediate step, the Government has started to digitize the records system, which, in turn, will allow for better case management. It has also initiated a comprehensive, functional review of the employment services.

Strengthening the Financial Sector and Improving Access to Finance

28. **Kosovo's financial system has proven quite resilient to the global financial crisis, and its regulatory and institutional framework has been substantially strengthened.** The financial system is

dominated by foreign-owned banks and is largely deposit-funded, mostly from large and relatively stable remittance inflows. However, structural financial sector vulnerabilities exist as bank assets are highly concentrated, leading to a lack of competition and high interest rates. As a result, Kosovo's banking system has one of the lowest loan-to-deposit ratios in the region. Additionally, banks rely excessively on Government deposits. In recent years, Kosovo's regulatory and supervisory framework has been gradually improved to meet EU standards, both for banks and non-bank financial institutions. A new Banking Law has been drafted that is expected to strengthen governance standards, limit related party lending, authorize consolidated supervision of banking groups, and support bank resolution, when needed. The new Banking Law also assigns the CBK responsibility for licensing of micro-finance institutions.

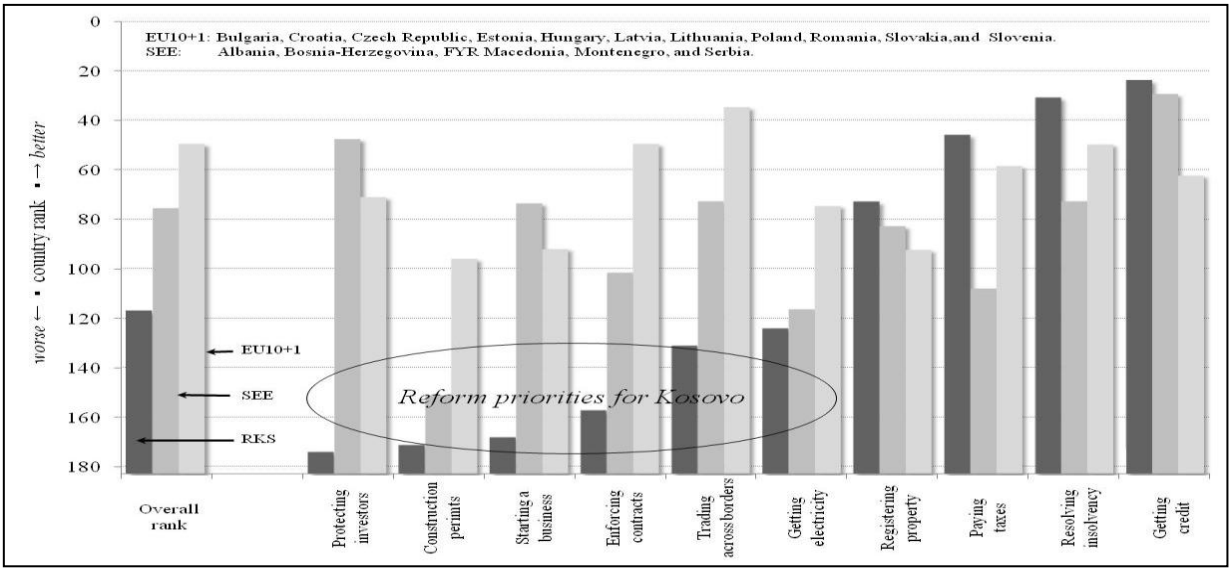
29. **In addition to strengthening financial system supervision, there is a need to improve access to affordable financial services, especially outside the capital city and for small enterprises.** BEEPS results indicate that access to credit is seen as a major obstacle by businesses in Kosovo. Only about 10 percent of investment is financed by credit, and over 85 percent of investment is financed from own resources. Further strengthening of banks' risk management practices is a necessary step in order to increase banks' willingness to lend. In addition, it is critical to develop and strengthen micro-finance institutions that have the potential to lend to farmers and other rural entrepreneurs. This would involve, inter alia, transforming existing non-profit foundations into more sustainable, for-profit financial intermediaries and raising awareness of the potential roles of small entrepreneurs in mainstream economic activities.

Legal and Institutional Framework for Business

30. **Although Kosovo's business climate has a number of strengths, the acceleration of private sector-led growth will involve addressing key institutional issues including ineffective licensing regimes and weak property rights.** Significant progress was made in Kosovo to put in place the basic legal framework and institutional structures necessary for a market-oriented economy. Moreover, Kosovo's business climate has several features that could make the country attractive to investors vis-à-vis its neighbors. Kosovo's labor markets are very flexible, the trade regime is open and liberal, and the banking sector is relatively dynamic, following the entry of foreign banks and gradually rising depositor confidence. However, weak institutional capacity, unclear property rights, and a complicated and fragmented licensing regime create fertile ground for growth of the grey economy. There is room for streamlining red tape and the Government is moving forward with the establishment of a one-stop shop, which should help potential investors to better navigate the requirements for investing in Kosovo.

31. **Improvement of the business environment is a key priority for Government and a Task Force has been formed with the mandate of improving Kosovo's DBR ranking** (currently 117th overall, see Figure 1). As a result of the task force's efforts, Kosovo recently passed amendments to relevant laws on business associations and internal trade to reduce the costs, number of steps and time involved to start a business and eliminate work permits and the charter capital requirement for limited liability companies.

Figure 1: Doing Business in Kosovo, the Western Balkans, and the EU10+1 Countries



Source: World Bank Group, *Doing Business* 2012.

Agriculture

32. **In addition to addressing the constraints present in the business environment that affect all sectors of the economy, special attention should be paid to addressing issues in agriculture, given its high potential.** Kosovo—endowed with good quality agricultural land—had been largely food self-sufficient in the past. At present, the sector currently contributes about 12 percent to GDP and is the largest employer in post-conflict Kosovo, accounting for approximately 35 percent of total employment. With its relatively abundant and underutilized labor, Kosovo has competitive potential in the horticulture sector, i.e., the production of fruits and vegetables as well as in the livestock sub-sector since domestic demand for horticulture and livestock products is expected to grow as purchasing power increases. Over the last decade, demand for high-value horticulture products has surged more than any other food category. However, while there is great potential for growth and expansion of productivity in agriculture, the sector faces several challenges that are reducing competitiveness and preventing it from meeting its potential. Unfavorable farm structures, outdated farm technologies and farm management practices, sub-optimal use of inputs, weak rural infrastructure, a rudimentary rural advisory system, and limited access to credit and investment capital are all limiting factors. In addition, Kosovo's farmers are placed at a competitive disadvantage as agricultural imports originate in neighboring and EU member states in which farmers receive production and export subsidies.

33. **The Government strategy to promote growth and competitiveness in the agriculture sector is elaborated in the Agricultural and Rural Development Plan (ARDP) 2007–13** (which was updated in 2009). The fundamental objectives are to (i) undertake actions to overcome the bottlenecks holding back sustainable rural development in the country; and (ii) align Kosovo's rural sector with the four axes of the Instrument for Pre-Accession for Rural Development (IPARD). The Government is undertaking several significant and strategic initiatives in this direction. It is also putting in place institutional structures in line with EU accession requirements. It recently established the Paying Unit within the Ministry which is expected to evolve into the IPARD Paying Agency.

B. Issues in Environmental Management

34. **Although environmental management has not been high on Government's agenda in the past, there is now growing recognition of the high costs of environmental neglect and the need to move ahead more rapidly towards meeting EU standards and requirements in environment**. The Government's Kosovo Environmental Action Plan (2011 draft) and the State of the Environment Report as well as the Bank's draft Country Environmental Assessment focus on three main areas problem areas—viz., (i) air pollution; (ii) water availability and quality; and (iii) hazardous and municipal waste. Key issues in each of these areas are discussed below, followed by a brief description of Government's strategy for addressing environmental problems in the country.

Air Pollution

35. **Air pollution is a significant problem in Kosovo's urban areas and a moderate problem for the country as a whole.** Urban ambient air quality is poor particularly in Pristina, the Obiliq area, the Drenas area, and in Mitrovica. The principal sources of pollution include (i) energy and mining production activities and the burning of wood and lignite for household heating purposes; (ii) smoke and emissions from large industrial complexes; (iii) landfills of urban and industrial waste which tend to have more specific local impacts; and (iv) vehicular emissions. Key health impacts from air pollution are related to the high levels of particulate matter (PM), also known as fine particles or dust. For the 2010–11 period, monthly average PM concentration values in Pristina fluctuated between 40–130 $\mu g/m^3$—nearly always above the 40 $\mu g/m^3$ average concentration determined by the EU as being consistent with human health. The key sources of PM emissions in Pristina are the power plant and household use of wood and coal for heating purposes during winter. High PM levels are responsible for increases in cardiopulmonary and lung cancer mortality in the case of long-term exposure as well as chronic bronchitis and respiratory diseases, particularly in children.

Water Availability and Quality

36. **Kosovo has limited water resources, divided into four main water basins: the Drini i Bardh, Ibri, Morava e Binçës, and Lepeneci.** There is unequal water distribution throughout the country, and–given the limited and insufficient water resources—water is expected to be a limiting factor for economic and social development in the future, particularly given rising demand for water due to increases in urban, industrial, and agricultural development. With regard to water quality, the percentage of the population with access to piped water supply is just 70–75 percent, while an even smaller proportion (50–55 percent) of the population is connected to the sewerage systems. Data from the Institute of Public Health on the quality of drinking water show that the pollution of drinking water is generally associated with bacterial rather than chemical contamination. Much of this bacterial (fecal) contamination occurs in the water supply systems of small cities and rural areas where a large proportion of wells and springs are thought to be contaminated, although no firm numbers exist. Given that there are no wastewater treatment plants in operation in Kosovo, it is not surprising that water contamination is a major issue.

Untreated Hazardous and Municipal Waste

37. **Environmental impacts from former mining and mineral processing are a substantial problem in Kosovo due to the lack of adequate environmental protection measures.** Historical and current industrial waste has remained—for long periods of time—in production sites, storage areas, and industrial hot spots. Mining and industry activities generate about 1.3 million tons per year of waste (commercial, hazardous and non-hazardous). Moreover, an estimated 395,000 tons of municipal solid waste is generated yearly. At present, there is a near-total lack of proper waste management in Kosovo for all waste types—domestic, industrial, healthcare, and hazardous waste—as well as for legacy pollution

from historical contamination. Current waste management practice, if left unchanged, will lead to high levels of pollution of groundwater and air (e.g., through methane or landfill gas), but also dioxins and fine particles when burned. In line with the municipal waste management policy, IFC has been working towards the concessioning of the Pristina landfill, for which there is strong private sector investors' interest.

Government Strategy for the Environment

38. **The Ministry of Environment and Spatial Planning (MESP) is preparing an update of the Kosovo Environmental Strategy (KES) and an associated National Environment Action Plan (NEAP) for 2011–15,** in close cooperation with other ministries, NGOs, and other development partners. The NEAP identifies short and long term objectives in the environment area aimed at meeting EU requirements. For the short term, the focus is on more rigorous implementation of existing legislation, continued efforts to modify legislation and institutions to conform with EU requirements and integration of environmental requirements into the sectoral development policies of relevant ministries. For the longer term the KES/NEAP sets goals and/or strategies for the following four areas: (i) reduction in pollution (including environmental degradation) and the prohibition of economic activities that harm human health or the environment; (ii) bio-diversity protection and the preservation of ecological balance; (iii) the rational and sustainable use of natural resources, including agricultural land; and (iv) the protection of valuable natural landscapes. In addition, the NEAP identifies needed investments in water and air quality, waste (including chemical waste) management, biodiversity preservation, and environmental policy development, categorizing them by priority, cost, and likely sources of funding.

IV. KOSOVO-WORLD BANK GROUP PARTNERSHIP

A. Active Portfolio, Lessons Learned and Partnerships

39. **The last ISN for Kosovo, covering FY10-11, was the first to cover a period of over one year and to involve the commitment of IDA credits as well as grants.** Since Kosovo had not been a member of the WBG until end-FY09, all World Bank–Kosovo operations prior to that time were financed through grants from a variety of sources, principally the Bank's net income, the Trust Fund for Kosovo, the Post-Conflict Fund, and IDA grants. Some of these projects are still active (though nearing completion) and are included in the portfolio table shown below. Newer projects committed under the last ISN were financed either partially or wholly through IDA credits.

40. **The World Bank supported portfolio currently consists of seven operations totaling US$76.9 million in commitments and 11 trust funds totaling US$66 million, including two State and Peace-Building Fund (SPF) grants.** The Business Environment TA Project and four trust funds are expected to close by June 2012. The remaining six operations and seven trust funds are either midway through execution or just starting up and are expected to be in active status through most or all of the CPS period (FY12–15). The objectives, content, and expected results of these operations have been reviewed in discussions with the Government in the context of preparing this CPS to ensure that they are fully consistent with the main objectives/directions of the FY12–15 strategy.

Table 3: Kosovo Active Portfolio

Project name	Board	Revised Closing	Age in years	Orig. commitment $	% Project disb. ratio	Latest IP	Latest DO
Education Project	12/13/2007	6/30/2013	4.4	10.00	44.8	MU	MS
Public Sector Modernization	2/4/2010	6/30/2013	2.2	8.00	0.2	MS	MS
Business Env. TA Project	6/14/2005	5/31/2012	6.9	7.00	97.3	MS	MS
Kosovo, Financial Sector TA	12/13/2007	6/30/2014	4.4	8.90	12.3	MS	MS
Agriculture and Rural Dev	6/14/2011	7/31/2017	0.9	20.20	0	MU	MS
Real Estate Cadastre	2/4/2010	7/31/2015	2.2	12.30	1.4	MS	MS
Energy Sector Clean-Up and Land Reclamation	6/13/2006	06/30/2012*	5.9	10.50	65.7	MS	MS
			3.7	**76.9**	**25.4**		

*to be extended to 12/31/2013 to allow for additional activities under a proposed AF (see para 79)

41. **For the three-year period from FY08-10, disbursements for Bank-supported projects averaged close to 20 percent of total commitments per year but declined in FY11 to 13 percent, and have remained slow in FY12.** The decline in disbursements can be attributed, in part, to a slowdown in implementation associated with the municipal and national elections that diverted the attention of key officials. Disbursements were also affected by long effectiveness delays for some newly approved operations. The Public Sector Management Project and the Real Estate and Cadastre Project—both approved by the Board under the last ISN—were the first Bank operations in Kosovo to be financed wholly or in part by credits rather than grants and, as such, were subject to approval by a two-thirds majority in Parliament. Unfamiliarity with the processes for obtaining this approval and inadequate consultation with opposition parliamentarians led to considerable delays in securing the approval needed to make them effective. Eventually, both operations were approved by large parliamentary majorities (well in excess of the two-thirds requirement).

42. **The Government of Kosovo and the Bank are working to strengthen portfolio implementation.** The capacity of implementing agencies is being strengthened through a series of procurement and contract management training courses delivered quarterly to all employees and consultants involved in World Bank financed projects. In addition, the Bank's own capacity for supervision support and provision of just-in-time training to Government staff has been strengthened through the recruitment to the Country Office of a Country Operations Officer. Moreover, a Senior Operations Officer, who is based in Skopje, is providing part-time support. Jointly with the Ministry of Finance the World Bank team has started producing a Quarterly Portfolio Monitoring Tool, which outlines the main implementation milestones for all operations, and lays out the principal tasks of respective Government institutions and World Bank teams for the upcoming quarter. The Monitoring Tool, which will serve as benchmark to monitor implementation of the program, has been developed in close collaboration with the Ministry of Finance and is shared with all Ministers benefiting from Bank support.

43. **The CPS Kosovo program also benefits from substantial Trust Fund resources, currently amounting to about US$66 million** (Table 4). As the table shows, the trust funds are fully aligned with the Bank's country strategy, focusing in key areas such as employment, infrastructure, inclusion, and the financial sector.

Table 4: Country Specific Trust Funds

Trust Fund Name	Net Grant Amount US$000	Grant Closing Date	Donor	Exec. By
TA Service to Central Bank of Kosovo	498	FY12	MDTF	BE
Carbon Capture and Storage Capacity Building	400	FY12	MDTF	BE
Kosovo Second Sustainable Employment Development Policy Operation	17,000	FY12	MDTF	RE
Kosovo Second Sustainable Employment Development Policy Operation	30,000	FY12	IBRD	RE
Building Stakeholder Support for Public Private Partnership in the Energy Sector	150	FY13	MDTF	BE
Health results based financing Knowledge and Learning Grant	125	FY13	MDTF	BE
Youth Grant for Youth Employment	846	FY13	ITALY	RE
Energy Sector Clean up	1,165	FY14	Netherlands	RE
Second Youth Development Project - State and Peace Building Trust Fund	2,000	FY14	MDTF	RE
Social Inclusion and Local Development - State and Peace Building Trust Fund	4,900	FY14	MDTF	RE
Agriculture Rural Development Grant	9,200	FY15	Denmark	RE

44. **IFC's committed portfolio for Kosovo comprises three investments totaling US$15.5 million as well as focused advisory services in key sectors.** Two of the IFC's investments are allocated in the financial sector to strengthen the capacity of a foreign bank to provide credit and financial services to SMEs, while one is in the real sector to support a medium-sized manufacturing foreign company. IFC's advisory services will support public-private partnerships in the infrastructure sectors including the privatization of the distribution arm of the public electricity company (KEK), and solid waste management concession for Pristina municipality. Furthermore, through its Balkans Renewable Energy Advisory Program (BREP), IFC will aim to improve the renewable energy regulatory framework, help renewable energy sponsors to improve their project designs and business plans, and support financial institutions to improve their internal capacities and knowledge on renewable energy. In addition, the Trade Logistics Advisory Services program will provide assistance to improve administrative procedures to simplify trade logistics, aiming to reduce the time and cost of trade and to increase exports. Also, IFC plans to continue its corporate governance program and expand its regional Investment Climate Advisory program to Kosovo. IFC will explore options to deepen its advisory work in the agribusiness sector in the Western Balkans, including Kosovo.

45. **The current net exposure of the Multilateral Investment Guarantee Agency (MIGA), as of October 31, 2011, amounted to US$53.2 million**. The MIGA exposure is the result of a guarantee that MIGA issued in December of 2010 to ProCredit Holding (PCH) covering its investment in its subsidiary in the Republic of Kosovo. The coverage is for a period of up to 10 years against the risk of expropriation of funds for mandatory reserves held by the subsidiary in the central bank of its jurisdiction. This project is part of a master contract that MIGA has issued to PCH. PCH is headquartered in Germany and is the

parent company of 21 network banks (ProCredit group). In Kosovo, ProCredit Bank is a development-oriented full service bank and focuses in its credit operations on lending to micro, small, and medium size enterprises (MSMEs), thus contributing significantly to job creation and economic development in Kosovo. In 2010, ProCredit Bank continued to be the largest commercial bank in Kosovo (by asset size) and had the largest branch network with 62 offices in 27 different towns and cities across the country. MIGA's continuing support to this project signals the Agency's ability to underwrite projects in the country and support inward FDI in the energy, financial, infrastructure and agriculture sectors, and thus add to the World Bank Group's strategy of encouraging private sector development by addressing real and perceived bottlenecks in the country's operating environment.

Lessons Learned

46. **The Bank's decade-long operational experience, analytical work, and dialogue with national and external stakeholders offer important lessons for future WBG engagement in Kosovo.** On content, three priorities stand out as follows:

- Given Kosovo's extremely high unemployment rates, it is critical to continue to focus on accelerating growth and increasing employment opportunities, especially for youth and women;
- Related to the above, sustained efforts are needed to address weaknesses in Kosovo's business environment as a principal means of fostering private-sector activities and attracting greater volumes of private investment;
- The pattern of growth needs to be consistent with environmental sustainability, including ensuring that natural resources are used in a manner that minimizes damage to human health.

47. **In addition, there is growing concern that the implementation of projects supported by the Bank has been slow.** Addressing these concerns will involve the following:

- Focused outreach to the parliamentarians and civil society during project preparation to ensure full understanding of the objectives and design, thereby facilitating parliamentary approvals of projects.
- Greater selectivity in new operations, focusing on sustaining momentum in key areas where we are already engaged, such as energy, education, employment, and the environment;
- Instituting regular joint portfolio reviews with the Ministry of Finance to resolve bottlenecks and strengthening the Country Office in Kosovo to help to provide continuous implementation support, and capacity building, particularly on modern procurement and financial management.

48. **A recent portfolio review identified opportunities to enhance the gender dimension of selected projects.** The review, conducted by gender and sector specialists, focused on the following projects: (i) Agriculture and Rural Development; (ii) Real Estate Cadastre and Registration; and (iii) the Institutional Development for Education Project. The main goal of the review was to identify opportunities in the projects to incorporate gender in the analysis, design and monitoring and evaluation framework. In addition, it provided knowledge on some good practices in gender mainstreaming, which will contribute to a more systematic inclusion of gender issues in future projects. The review identified the following:

- The *Agriculture and Rural Development* project will increase women's access to training and advisory services to enable them to prepare quality grant proposals and business plans. This would enhance their access to grants to foster competitiveness and growth of their businesses. A detailed report on female beneficiaries in the agricultural and rural development sector was

recently prepared and will serve as the basis for the development of a communication and outreach campaign targeting women farmers and entrepreneurs. An important goal of the campaign is to raise female participation in training to at least one third of the total. In addition, five points have been added to the scoring criteria for rural grant applications submitted by female applicants to encourage women to participate in the grant competition. It is expected that the number of grants awarded to women would double (albeit from a low level of about 4.5%) by 2017. Progress in reaching women beneficiaries will be monitored throughout the project.

- The *Real Estate Cadastre and Registration* project will promote women's property registration by: (i) increasing outreach targeting women to register their land; (ii) ensuring protection of women's property rights on first registration through inter alia redesign of forms to encourage registration of all owners (not just head of household); (iii) modification of municipal cadastre office (MCO) practices to ensure full compliance with the Law on Gender Equity and Family Law in areas of inheritance and land transactions; (iv) specific training for MCOs on women's property rights and sensitivity to the special challenges faced by women in property issues; and (v) ensuring that the project's planned social survey provides a baseline to monitor progress of gender indicators in annual follow up surveys. Based on existing data it is estimated that about 20 percent of land is either individually owned by women or jointly titled (2011). The project will support Government's efforts to achieve an increase in women's land ownership of about an additional 10 percent by 2015.

- In the *Institutional Development for Education* project, school development grants (SDGs) will support selected schools to prepare and implement multiple-year school development plans which focus on the enhancement of the quality of teaching and learning activities. Recipient schools will be selected according to a set of criteria including retention and attendance rates among girls. Specifically, the six criteria for allocating the SDGs (of up to 15,000 Euro per school) will now include the Gender Parity Index which receives 10 out of 100 points. The index is calculated as the number of boys enrolled divided by the number of girls enrolled. In addition, the project will strengthen the capacity of municipalities to track the status of dropout and retention disaggregated by gender. The goal is to ensure that about two thirds of municipalities are able to report these gender statistics through a modern education management information system. This indicator is tracked through the project ISR.

Role of Other External Partners

49. **Kosovo has many multilateral and bilateral donors that provide support to a range of sectors at central and local levels, sometimes in concert with Bank operations.** The EU and USAID are the most important donors, with over 300 projects at national and local levels. For 2011–12, the EU has allocated €140 million for Kosovo from the Instrument for Pre-Accession (IPA) which funds preparatory activities for investment projects. Kosovo is also eligible to receive funds from the EU's Western Balkan Investment Facility (WBIF) for project preparation. Other important partners include Austria, the Czech Republic, Denmark, Germany, Italy, Netherlands, Norway, Sweden, Switzerland, and Turkey as well as the Bretton Woods institutions and the UN system.

50. **Substantial external donor support has been an important input to Kosovo's development efforts, but the Government has only recently put in place a formal mechanism to enhance coordination.** In early 2011, the Government of Kosovo adopted a Regulation on Donor Coordination, increasing the role of the Government in the coordination of development assistance. The Regulation creates the High Level Forum, established as a permanent mechanism for the purpose of analyzing and assessing progress in social and economic development and the efficacy of external aid. The Forum is chaired by the Prime Minister and comprises the highest officials of the Kosovo Government, donor

representatives and other relevant agencies. Decisions of the Forum are transferred to sectoral and sub-sectoral working groups, which coordinate development assistance in their respective technical areas. The Forum monitors the general effectiveness of the system of aid based on indicators defined by the Paris Declaration and defines ways to improve its impact. While still uneven in their effectiveness and impact, the High Level Forum and the sectoral working groups represent an important step forward in bringing more order to external assistance efforts, helping to ensure national ownership of development initiatives and reducing pressures on limited Government capacity.

Table 5: a&b: WBG Portfolio, New Lending FY12–15, CPS AAAs and Trust Funds

Table 5a: WBG Portfolio, New Lending FY12–15, Country Specific CPS AAAs and TFs

Accelerating Growth and Employment Generation		***Improving Environment Management***	
Ongoing Operations FY12-15 (closing dates)			
Business Environment TA	FY12	Energy Sector Clean-up	FY12*
Education Project	FY13		
Public Sector Modernization	FY13		
Fin. Sector Strength. Market Infrastructure	FY14		
Real Estate and Cadastre	FY16	*to be extended to 12/31/2013 to allow for additional activities under a proposed AF (see para 79)	
Agriculture and Rural Development	FY18		
New Operations FY12-15 (delivery date)			
Sust. Employment Dev.Policy Operation 2 (TF)	FY12	Energy Efficiency and Renewable Energy	FY13
PRG FOR KRPP	FY14	AF for Energy Sector Clean up and Land Reclam	FY13
Education Improvement Project	FY14	Water Supply	FY15
Country Specific non-lending AAA FY12-15 (delivery date)			
ROSCs*	FY12	Country Environmental Analysis	FY12
Privatization of Energy Distribution (KEDS) IFC	FY12	Water Strategy Follow-up/Round Table	FY12
Country Fiduciary Assessment and GAC support	FY12-15	Solid Waste Management Concession IFC	FY13
IFC PPPs in Infrastructure	FY12-15		
Financial Sector Assessment	FY13		
Statistical and Analytical Capacity TA	FY12-13		
Program. Public Expenditure Review	FY13-15		
Employment and Social Protection TA	FY13-15		
Country Economic Memorandum	FY15		

* ROSCs on Insolvency and Creditor/ Debtor Regimes; Review of Accounting & Auditing Practices in Kosovo; and Bank and Microfinance Governance Assessment

Table 5b: Regional Western Balkans Non-lending (AAA) and Trust Funds FY12-15(delivery date)

Monit. & Evaluation (EC TF)	FY12-13	Smart Safety Nets	FY13
TA Scienc., R&D/Innov. (EC TF)	FY12-14	Health Finance	FY14
Program. Financial Sector Dev	FY12-14	Employment and Jobs	FY14
Trade Logistics IFC	FY12-15	Energy Strategy	FY14
Renewable Energy Advisory IFC	FY12-15	Investment Climate IFC	FY13-15
Programmatic Gender Monit	FY12-15	Public Fin Mgt/PEFA (EC TF)	FY13-15
Programmatic Poverty Monit.	FY12-15	Climate Change	FY15
Corporate Governance IFC	FY12-17		

51. **The WBG works closely with many of these external agencies, including through joint analytical work and co- or parallel-financing of operations**. For example, the Bank is partnering with the IMF and USAID to provide TA to Kosovo's financial sector, with the Netherlands, US and EC in the energy and environment sectors, with Austria in public financial management and with DFID and SIDA to build capacity for statistical analysis. The Bank and other partners worked towards developing a

Sector-Wide Approach (SWAP) for the education sector, partly through conduct of a joint feasibility study under the leadership of the Ministry of Education, Science and Technology. A group of nine external partners have been closely involved in the design and implementation of the Sustainable Employment Development Policy Program (SEDPP) and have contributed substantial grant resources for its two budget support operations. Finally, given the importance of the EU perspective for Kosovo, all World Bank operations are aligned with the criteria for EU accession.

52. **Further possibilities for cooperation between the EC, European IFIs, and the Bank in the Western Balkans have been opened by the agreement in June 2011 to grant the Bank associate membership in the WBIF.** The WBIF is a financing mechanism designed to pool grants, loans, and expertise from the EC, IFIs, and bilateral donors to prepare a common pipeline of priority investment projects that could be financed by any of the WBIF donors. While in other Western Balkan countries, the Bank cannot act as the lead IFI for WBIF-financed project preparation activities, an exception to this rule has been agreed for Kosovo, where the Bank—as the only IFI that is fully operational in the country—has been encouraged to play a leading role in several areas. The Kosovo Government has already submitted a number of grant proposals to the WBIF Project Financiers Group including for studies on energy efficiency in public buildings, feasibility and environmental impact analyses for strengthening waste management (covering municipal and hazardous waste) and feasibility studies for protection of the 50-km long Ibër Canal. In addition, Kosovo will benefit from a number of regional proposals submitted by SEE Governments including for a study to examine development options (including financing options) for implementation of an Energy Community Gas Ring through public-private partnership consortia. These proposals will be reviewed by the WBIF Project Financiers Group in April 2012 and those which are positively assessed will be forwarded to the Project Steering Committee for final decisions in June.

B. WBG Country Partnership Activities for FY12-15

53. **The main objectives of the CPS are to support Kosovo to (i) accelerate broad-based economic growth and employment generation; and (ii) improve environmental management.** The goal of accelerating broad-based growth and employment creation is essentially a continuation of the priorities established in previous country strategies. The second objective—promoting better care of the environment—was less prominent in previous assistance strategies. It is being given higher priority now because of wider recognition within Government and its development partners that sustainable, environmentally-sensitive use of Kosovo's major natural resources and better management/clean-up of environmental hazards are critical elements of the effort to improve the population's living standards and create sustainable employment. Moreover, in light of the findings of the EC's Progress Report on Kosovo, it has become clear that significant progress will be needed in environment if the country is to achieve its longer-run objective of closer integration with the EU.

54. **The CPS has been shaped in important ways by consultations with a wide range of relevant stakeholders.** Apart from its ongoing discussions with the Government, the Bank held several discussions on the CPS with the President of the Republic, Parliament, the private sector, civil society and international development partners. All the groups consulted stressed the importance of addressing medium-term energy security and many were fully supportive of the balanced strategy included in the CPS. Some civil society groups, however, were critical of any support for the development of a new lignite-fuelled power plant to replace the existing (highly-polluting) Kosovo A but nonetheless welcomed other aspects of the CPS energy program aimed at reducing energy losses, promoting energy efficiency and developing renewable energy sources to the extent feasible. A detailed summary of a full-day consultation with civil society representatives in early April is given in Annex 2. In addition to energy, a number of other areas were emphasized during consultations and have been included in the CPS program. For example, the President viewed the economic empowerment of women as a particularly important challenge for Kosovo, various parliamentary leaders suggested the need for a clear focus on agriculture

and water supply and the private sector suggested the need for continued emphasis on improving the business climate.

55. **Taking into account the lessons learned from past experience in Kosovo and the limited lending envelope, the proposed new lending under the CPS program is selective.** New lending will support fewer, larger operations in sectors/sub-sectors where the WBG has a comparative advantage by virtue of (i) previous experience in Kosovo or relevant work elsewhere in the region; (ii) having undertaken analytical work that can inform lending; and (iii) synergies between IDA, IFC, and MIGA. Program design is also influenced by the potential for close cooperation with other external partners, particularly with a view to supporting Kosovo's aspirations for EU integration.

Expected Outcomes

Pillar I: Accelerating Broad-Based Growth and Employment Generation

56. **The first pillar of the CPS strategy aims at accelerating broad-based and sustainable growth through actions in six main areas:** (i) strengthening infrastructure, especially energy, including through promoting private sector participation in large projects via PPPs; (ii) improving the business climate, supporting the private sector and the financial sector; (iii) strengthening agriculture development; (iv) continuing to invest in education and skills; (v) promoting sustainable employment and inclusion; and (vi) strengthening public financial management and anti-corruption efforts.

(i) Strengthening infrastructure, with a focus on energy

57. As discussed in Section III, achieving an accelerated growth path in Kosovo will involve substantial investment in infrastructure and the adoption of PPP approaches for the implementation of large-scale projects. While Kosovo's needs with respect to infrastructure are vast, resource limitations dictate that the Bank supports the sectors selectively, with financial support focused largely on the energy sector. In addition, the Bank and IFC would support the development of other infrastructure services through studies and other advisory services. IFC would also seek to selectively provide financial support to private firms involved in infrastructure projects in Kosovo in areas such as water, transport, solid waste disposal and energy.

58. **The Government has developed a comprehensive strategy for the energy sector.** There is an urgent need to address problems in Kosovo's energy sector because (i) frequent power cuts constrain socioeconomic development (by impeding investment/job creation, disrupting social service provision and affecting heating availability in winter with consequences for health conditions); (ii) mismanagement of the sector results in a drain on Kosovo's scarce budgetary resources; and (iii) the outdated technologies employed in power generation have a severely negative impact on the environment (both in terms of air pollution and carbon emissions). To address these issues and, taking into account the limited opportunities to cost-effectively import electricity from the SEE region, the Government—working closely with the WBG, EC, and USAID —has identified a strategy to provide more reliable energy supplies to households and businesses. The strategy is based on development of Kosovo's domestic lignite, hydro and other renewable resources, and reducing consumption through demand-side management and end-use efficiency improvement. The **key elements of the Government's strategy**, are the following:

- ***Phased closure of the 5 inefficient outdated and highly polluting Kosovo A power generation units*** by the end of 2017. Since the 40-year old generation units cannot economically be brought into compliance with the EU Directive for Large Combustion Plants, they need to be closed by

2017 at the latest, as required under the Energy Community Treaty. Decommissioning of Kosovo A will be initiated as soon as feasible with possible support from the EC and other donors.

- ***Development, through private participation, of a state-of-the-art power plant—the New Kosovo Power Plant (KRPP) and the associated Sibovc SW lignite mine to replace Kosovo A.*** The KRPP would comprise two units of 300 MW each, the minimum necessary to enable retirement of Kosovo A, serve still-unmet domestic demand and barely meet demand growth, even under an aggressive loss reduction, tariff adjustments, and demand management regime.
- ***Rehabilitating Kosovo B to comply with EU environmental standards through privatization of that plant***.
- ***Establishing cost recovery tariffs (with appropriate life-line pricing provisions and strengthened social protection programs to protect the poor)*** as an important element of the effort to reduce the drain on scarce budget resources and encourage energy savings by users.
- ***Privatizing KEK Distribution as a means of improving its efficiency*** and gaining better control over the rampant losses of electricity due to technical losses and theft.
- ***Improving end-use energy efficiency*** through investments in energy efficiency in public buildings and household incentives for energy saving measures.
- ***Developing the country's limited hydropower and other renewable resources***.

The European Commission and the Bank plan to co-host a donor conference in September 2012 to raise financing for the closure of Kosovo A and for energy efficiency and renewables projects.

59. **When fully implemented, the Government Strategy would yield significant environmental benefits.** Compared to business as usual, the proposed strategy would put Kosovo on a lower carbon path. Demand-side management and efficiency improvements through privatization of electricity distribution are expected to reduce technical and commercial losses from the current level of about 40 percent to around 13 percent by 2025. Improvement in end-use energy efficiency will be supported through an IDA project. The new 600-MW KRPP—together with a rehabilitated Kosovo B and development of the full hydropower potential available—would, by end-2017, replace (i) Kosovo A; (ii) imports of about 500 GW from the regional grid; and (iii) about 150 MW in small diesel generation back-up supply. This change is expected to yield significant environmental benefits by reducing the annual emission of dust by more than 90 percent (from a current level of 20,000 tons), and nitrogen and sulfur oxides by about two thirds from their current very high levels (nitrogen oxide about 12,000 tons and sulfur oxide about 14,000 tons) resulting in significant improvements in air quality in Pristina, with concomitant reductions in adverse health impacts on the population.

60. **The Government has requested the WBG to provide support for several elements of the above strategy, including provision of a Partial Risk Guarantee (PRG) to bidders on the development of KRPP/Sibovc and rehabilitation of Kosovo B.** To determine its response to the Government request, the Bank appointed a ***panel of external experts*** to assess whether potential Bank support for KRPP under the aforementioned Government strategy would be consistent with the Bank's "Strategic Framework for Development and Climate Change" (SFDCC). The expert panel report, issued in January 2012, concluded that the proposed KRPP/Sibovc project complies with the six criteria of the SFDCC. It also recommended several complementary actions, all of which are fully consistent with Government's overall energy strategy. The Panel's main recommendations involve: (i) improving energy efficiency, including through regulation to promote energy efficiency in new building construction; (ii) reducing technical and commercial losses, partly through privatization of electricity distribution; (iii) further emphasizing renewables, including assessment of wind potential, increased use of solar power for water heating, and the adoption of regional strategies for renewables and natural gas; (iv) including

externalities in future analysis of energy projects and preparing an environmental baseline; (v) considering the use of lignite drying to increase the efficiency of the power plant; and (vi) ensuring openness and transparency on energy projects through a well-developed consultation process.

61. **In light of the conclusions of the Expert Panel, the Bank will proceed with preparation of support for the KRPP/Sibovc investment through offering an IDA PRG and possible complementary support from IFC and MIGA.** WBG credit-enhancement support (including the PRG) would be offered on a "non-binding, in principle" basis, in conjunction with issuance of Government's Request for Proposals (RfP) to pre-qualified bidders on the proposed project. A final decision on WBG support would be subject, inter alia, to compliance with all applicable WBG requirements, including those related to social and environmental issues, review and acceptance of the ownership, management, financing structure and transaction documents and approval by the management and Executive Directors of the World Bank Group. The PRG offered by IDA for the KRPP/Sibovc project would amount to approximately US$58 million (of which, only US$14.5 million or 25 percentage would be counted against Kosovo's IDA-16 allocation). This would help to mitigate investor perception of the high risks of investing in Kosovo and enable bidders to raise commercial financing at lower cost and with longer maturities. IFC would be prepared, in principle, to consider providing financing for its own account to the Operator, as well as assist in mobilizing additional funds from other international financial institutions and from commercial banks where possible, subject to its investment criteria and approvals. IFC will continue to work with the Kosovo Government as the lead ***transaction adviser for the privatization of KEK Distribution***, coordinating closely with USAID, which has been supporting management improvements at the enterprise. In addition to serving as transaction advisor for KEK distribution, IFC would also coordinate closely with the Bank and MIGA to seek additional ways of supporting the Government's energy sector strategy in particular by bringing to bear its global expertise to attract serious strategic investors to the sector. A Poverty and Social Impact Assessment (PSIA) would be conducted to determine ways of mitigating the impact of higher tariffs on poor households—including through life-line pricing and strengthened social assistance programs.

62. **The Bank will also support several other elements of the Government's energy strategy, including energy efficiency and development of renewable energy, reduction of environmental hazards, monitoring of air, soil and water quality associated with the power plants and strengthening capacity to regulate the energy and environment sectors in a manner consistent with EU standards.** Support in these areas—including an Energy Efficiency and Renewables Project and Additional Financing for the Energy Sector Clean-Up and Land Reclamation Project—is described in detail in Pillar II.

63. **CPS outcome for energy: WBG support for Government's energy strategy will significantly strengthen sectoral production capacity, efficiency and financial and environmental sustainability.** Given the time frame necessary for implementation of the projects, this outcome is likely to be realized in the next CPS. The PRG for KRPP/Sibovc would have an important impact on electricity availability and successful conclusion of the privatization of KEK Distribution would result in increased efficiency as a result of reduced technical and commercial losses (including theft). These two operations together would also significantly lessen the need for budgetary support to the energy sector, thus freeing up scarce budgetary resources for other key uses. The Energy Efficiency and Renewables Project would help to achieve significant reductions in the need for thermal power generation.

(ii) Promoting private sector development and financial sector strengthening

64. **The second main element of the growth pillar helps Kosovo to increase its** attractiveness to both domestic and foreign business investors by supporting a number of actions to improve the regulatory and institutional frameworks for business entry and operations and to strengthen the financial sector.

65. **CPS outcome: The environment for business operations has improved as a result of simplified regulations and processes and rules for business entries/exits and external trade has been simplified:** The on-going *Business Environment TA* project is successfully helping to reduce regulatory compliance costs for businesses, harmonize business regulations and the licensing framework at the central and municipal level, and secure immovable property rights. Building on a component of the ongoing Business Environment TA project, the *Real Estate and Cadastre Project (*RECAP) supports, inter alia, (i) the Municipal Cadastre Offices (MCOs) by financing physical upgrades to facilities and completing and updating real estate cadastre and registration records in the Immovable Property Rights Register; (ii) the transformation of the Kosovo Cadastre Agency (KCA) into an autonomous and self-financing body with capacity to work with municipal offices and ensure uniformity in property transactions; and (iii) the KCA to manage the project, monitor/evaluate the project's progress, organize public information events, and coordinate donor support. In addition to the annual analysis of Kosovo's business climate within the framework of the joint Bank/IFC Doing Business Reports, IFC advisory assistance could include: (i) regulatory simplification on the national and sub-national levels to help to reduce the cost and risk of doing business; and (ii) addressing the regulatory impediments for business start up and operation as well as for the efficient flow of goods into and out of Kosovo.

66. **CPS outcome: Local corporations in productive sectors are already growing at an accelerated pace**: IFC would support continued growth of competitive companies in agribusiness, manufacturing and services sectors. In particular, IFC will help local corporations overcome financing constraints through long-term financing combined with related advisory services. In this regard, IFC expects to support 1–2 projects in these sectors per year. MIGA could also provide guarantees to SMEs and small-scale agricultural and services projects through its Small Investment Program.

67. **CPS outcome: The regulatory and institutional frameworks for the financial system have been substantially strengthened and a modern deposit insurance scheme is in place.** The WBG, working with key partners such as the IMF and USAID, has been heavily involved in supporting the regulatory and institutional reform of Kosovo's financial system over the past few years and will continue its support during this CPS through the ongoing IDA-financed *Financial Sector Strengthening Market Infrastructure Project* (FSSMIP), approved by the Board in mid-2011. Among other activities, the project has already helped to establish a Deposit Insurance Fund, is reforming the payments system, supporting the implementation of an RTGS and developing a business continuity center. A corporate governance review of financial institutions undertaken last year will be followed up by two **ROSCs** on accounting and auditing and insolvency and creditor rights, both of which will be completed in FY12. AAA will also be provided during FY12–13 through a FIRST grant to harmonize existing regulations and procedures with Kosovo's new Banking Law, and to ensure conformity with EU practices. In addition, at Government's request, the Bank and IMF will conduct a *Financial Sector Assessment Program* (FSAP) review in FY12–13, which will assess strengths and potential vulnerabilities and means of risk reduction. While the Bank has focused on strengthening the legal, regulatory and institutional framework for the financial sector, IFC will explore the possibility of working with the banks with a focus on agribusiness, gender finance, climate change and SMEs. IFC will also consider supporting the microfinance institutions.

68. **CPS outcome: SME's have gained increased access to credit**. With respect to financing for SMEs as well, the Bank and IFC will work closely together, with the Bank concentrating on the regulatory framework and IFC providing financing and advisory services to support SME-oriented private financing institutions, as well as competitive SMEs. One key Bank input during the CPS period will be a Corporate Governance Review of Banking and Micro Finance Sector, using a methodology that was developed by the Bank, based on inputs from other supervisory and rating agencies, but substantially leveraging off of the newly issued Basel Committee's Principles for Corporate Governance. In addition, the Bank, utilizing resources from the Balkan TA facility will provide technical support to regulatory

framework for microfinance. This work, which will be undertaken in FY12, will involve working with the Central Bank to develop the best structures for micro-finance from a regulatory viewpoint. For its part, IFC will seek to strengthen Kosovo's micro-finance institutions, in conjunction with a suitable strategic partner.

(iii) Strengthening agriculture development

69. **CPS outcome: Agricultural growth and competitiveness have been boosted through provision of new technologies and rural development grants to agricultural producers.** The ongoing *Agriculture and Rural Development* project seeks to increase agricultural production and competitiveness in Kosovo through two main sets of activities: (i) establishment of a program of rural grants to encourage investment in agriculture and promote the use of improved agricultural technologies; and (ii) strengthen the knowledge of farm operators, agro-processing enterprise managers and municipal advisors to effectively plan investments and utilize the financial support available under the rural grant program. During the FY12–15 CPS period, the project's grant program will be expanded through a *Danish grant* of 50 million kroner (about US$9 million equivalent), thus nearly doubling the resources available for rural investment. Additionally, the project will be reviewed during this CPS period to ensure that it reaches out adequately to women as well as men, with adjustments made to its outreach and capacity building components to increase gender sensitivity as appropriate. As with the original project, Danish grant funds will be managed through a Managing Authority (MA) and Paying Unit (PU) established with the Ministry of Agriculture, Forestry and Rural Development. The MA and PU have been designed to be fully in line with the requirements for Paying Agencies under the EU's Instrument for Pre-Accession Assistance for Rural Development (IPARD) so that they will be competent to satisfactorily manage IPARD funds once Kosovo becomes eligible to receive them. In addition, through its regional agribusiness advisory project, IFC will contribute to increased Kosovo's agribusiness sector competitiveness and exports.

(iv) Investing in education and skills

70. **CPS outcome: The relevance and quality of education has been strengthened.** Kosovo's education system currently falls short in terms of quality and relevance. The Bank-supported ongoing *Institutional Development for Education Project* (IDEP) for Kosovo—developed in partnership with the Ministry of Education and a number of donors—is already helping Government in the implementation of the strategy for the development of pre-university education in Kosovo and the strategy for the development of higher education. Its main focus is on strengthening the systems, institutions and management capacities needed for education quality improvements. It also encompasses infrastructure planning and investment improvements and institutes a school grants program to support demand-driven initiatives throughout the school system. When designed in FY08, the project did not specifically target issues of girls' access to secondary and post-secondary education, but a gender assessment will be undertaken to capture the extent of and identify the factors exacerbating gender disparities to inform future projects. In addition, one of the criteria for the allocation of school development grants is the extent of gender disparities (enrollment and retention rates), and the project will document the impact of these school grants. The Education Improvement Project planned for this CPS period will continue broader efforts in improving education quality and efficiency but also include a clear focus on means of improving girls' access to secondary and post-secondary education. The new project, currently programmed for FY14, will be financed through an IDA credit of about US$10 million.

(v) **Promoting Sustainable Employment and Inclusion**

71. **CPS objective: Policies and institutions increasingly promote sustainable employment.** The Bank is preparing a second and final operation in support of the *Sustainable Employment Development Policy Program*. The program's multi-pronged approach expands on efforts in other CPS areas and

supports actions to strengthen policies and institutions governing (i) macro-economic and public financial management; (ii) the investment climate; (iii) labor markets; (iv) education, training and skills; and, (v) social protection. In its final phase, the program will strengthen procurement processes, salary systems for civil servants and the monitoring of expenditures. It will reduce barriers to register businesses, improve the access of customers to credit data, and establish a comprehensive regulatory framework for Banks and other financial institutions. In addition, the final phase of the program will expand public works programs, strengthen other labor market programs, and establish a comprehensive regulatory framework for the labor market. It will provide for a national qualifications framework and support the accreditation of vocational training institutions; furthermore, it will improve the targeting and management of social assistance programs. Following the second Sustainable Employment Development Policy Operation, a **programmatic analytical advisory activity** will provide technical assistance throughout the CPS period to further strengthen the policies and institutions governing the labor market, training and skills development, and social protection, including health financing.

72. **CPS Outcome: Social inclusion in poor communities and marginalized population groups is supported.** Two grants from the peace and state building fund are supporting social cohesion through: (i) rehabilitation of small-scale social and economic infrastructure in the poorest villages and in mixed/minority communities as well as promoting MSMEs in a socially inclusive manner; and (ii) youth services, youth employment and inter-ethnic collaboration among youth, especially from marginalized and vulnerable groups.

(vi) Strengthening Public Financial Management, Procurement and Anti-corruption Efforts

73. **CPS outcome: Public financial management has been modernized particularly with respect to public investments monitoring, efficient payroll management, transparent procurement and anti-corruption actions**. Complementing the public sector management improvements included in the SEDPP (i.e., strengthening public investment management, consolidated procurement and transparency in payroll management), the Government is also seeking to further improve public sector governance by (i) implementing a public financial management reform action plan; (ii) increasing the efficiency of procurement through e-procurement and consolidated procurement (Quick Gains reform); and (iii) reforming the civil service (see Box 3 below). The Bank is supporting these reform efforts through the ongoing *Public Sector Modernization Project* (PSMP). In addition, the Bank has recently completed a *Country Fiduciary Assessment* (CFA) FY12 report and shared a draft with the Government.

74. **In order to follow up on the key recommendations stated in the CFA, the World Bank—in cooperation with other development partners—would support the Kosovo Government with technical assistance** to assist the Government in (i) monitoring enforcement of the PPL, improving procurement implementation and contract management, and building capacity within the procuring authorities and private sector; (ii) establishing a system for the performance evaluation of procurement officers and professional growth of procurement officers; (iii) conducting a PEFA assessment and using its findings to refine the PFM reform action plan; and (iv) strengthening the capacity of the Central Procurement Agency (CPA) to conduct procurement of "common use" goods. In addition, the project would work with the Anti-Corruption Agency to follow-up on the integrity related recommendations and issues emanating from the CFA, working in partnership with other accountability institutions and donors. Throughout the CPS period, the Bank will track the Government progress in implementing the CFA recommendations and will maintain high level of vigilance in ongoing and planned operations through thorough fraud and corruption assessments of each operation, implementation of smart controls and accountability measures, and enhanced fiduciary reviews during project implementation.

Box 3: Public Procurement Laws, Country Fiduciary Assessment, Corruption and Governance

In the area of public procurement, the Government's main goal is to align its legislation with the EU Procurement Directives. To that end, the Public Procurement Law (PPL) in Kosovo has undergone frequent changes in the recent years aiming increased alignment and improvement of the overall institutional framework in public procurement. The World Bank conducted a Country Fiduciary Assessment (CFA) in Kosovo in 2010 which went through 2011. The assessment report is expected to be finalized in December 2011. Amid the assessment, a new PPL was approved by the Assembly on September 30, 2010 and was further amended on September 19, 2011. The CFA team reviewed both versions of the PPL and provided the Government with comprehensive comments, majority of which were addressed by the Government in the final version. Generally, the current PPL reflects adequately the main principles of a sound procurement system and is consistent with international good practices.

The EU Commission refers in its 2011 progress report as "this version of the PPL addresses most of the deficiencies of the previous law and significantly increases the compatibility with EU standards". The main institutional changes brought by the current amendment include inter alia: transformation of the Public Procurement Agency ("PPA") from an independent agency with mixed roles and responsibilities to a Centralized Purchasing Agency (CPA) within the Ministry of Finance (MoF) to be in charge of conducting centralized procurement; and the contract signing was further clarified to involve senior staff of the contracting authority in signing high value contracts in addition to the procurement officer.

However, Kosovo public procurement system is still in need of improving its performance. The legislative framework needs further refinements as it needs to be supplemented by the necessary implementing regulations, procurement manuals and tender documents including general conditions of contracts which have not been updated in parallel with the PPL. Monitoring enforcement of the PPL, improving procurement implementation and contract management, building capacity within the procuring authorities and private sector based on training needs assessment are areas of need of improvement. The Government also needs to establish a system for the performance evaluation of procurement officers and to include in the civil administration a clear path for growth of procurement officers.

The public financial management system in Kosovo, in general, has shown steady improvements since independence was declared. The key strengths of the system are the sound legal framework, integrated central treasury system and an increasingly effective external audit office. The strengths are offset by limited professional and technical capacities and gaps in implementation. There is considerable scope for improving the quality of budget planning and preparation, internal financial control and audit, debt management and capital investment management. Kosovo authorities are aware of their limitations and progress is occurring, with support from international bodies, including the World Bank.

The Government recognizes that corruption is still widespread with several high profile Cases currently under investigation. The key areas affected include procurement, civil works, transport, energy, health and land administration. Progress has been made on Procurement Code of Ethics, launch of an Internet website carrying full details of public procurement, and commencement of a procurement training program. Further work is still needed to develop a debarment mechanism, institute due diligence on bids reviews, scale-up compliance reviews, and build capacity to successfully prosecute high-profile Cases.

75. **CPS outcome: The capacity for statistical data collection and relevant analysis has been reinforced and data are being used more systematically by policymakers.** Poverty monitoring would be supported by collection of data from a number of sources, including a donor-financed AAA activity to support GOK to collect and analyze household level data. Under this AAA activity, the Bank will provide TA in three focal areas: monitoring poverty, inequality, gender differences and exclusion; strengthening capacity for data collection and analysis; and addressing emerging knowledge gaps. There will be a strong focus on expanding the use of data collected by the Statistical Office of Kosovo (SOK), and other data sources by a wider group of analysts and, ultimately, decision-makers in Kosovo, including through the creation of a data users' network comprising analysts from SOK, various Government departments, academic institutions and think-tanks. A series of training events and knowledge-sharing workshops are planned to help to establish and nurture this network, drawing in large part from experiences in neighboring countries, with appropriate adaptation to the Kosovo context. The activity will be

complemented by and coordinated with Bank-financed AAA to monitor gender, which will be ongoing throughout the CPS period.

Pillar II: Improving Environmental Management

76. **The second pillar of the CPS strategy seeks to improve environmental management,** particularly by supporting the Government to increase energy efficiency and the use of renewables, reducing environmental hazards, enhancing water supply and moving towards harmonization with EU environmental standards. The main activities envisaged for the CPS period, are described below:

(i) Improving energy efficiency and increasing energy production from renewable sources

77. **CPS Objective: Efficiency in energy use and generation from renewable resources has been increased, thus reducing carbon emissions.** The Government and the Bank are developing a proposed US$32.5 million *Energy Efficiency and Renewables Project* (FY13), modeled on similar Bank-supported projects in the region. GTZ has trained about 50 energy auditors and USAID has completed some demonstration projects retrofitting schools in Kosovo. In addition, the Government has submitted an application to the WBIF for grant funding for an energy audit and preparation of feasibility studies for energy efficiency investments in public service buildings (Government offices, schools, hospitals, or old-age homes). Building on these activities, the project would aim to retrofit public buildings to substantially reduce their energy consumption and strengthen the supply-chain through training of energy auditors, contractors, vendors and equipment suppliers. The project would also seek to reduce pollution and emissions caused by widespread use of liquid-fuel generators and firewood for household heating inter alia by providing households with incentives to improve energy efficiency and adopt cleaner heating methods. In this regard, the World Bank Institute is helping with assessment of market potential for energy efficiency investments, cost estimates and financing options, institutional capacity strengthening, and preparation of an energy-efficiency diagnostic for the Municipality of Pristina. In addition to efficiency investments, the proposed project will support development of renewable energy sources through exploration of geothermal and wind potential, preparation of feasibility studies for projects to be offered to the private sector, developing model concession agreements, and potentially provision of a credit enhancement to the local banks to finance mini-hydro and solar power plants, as well as renewable projects for households (e.g., solar water heating and small biogas for heating).

78. **In designing the renewable energy component of the Energy Efficiency and Renewables Project, the Bank will coordinate closely with the IFC's Balkans Renewable Energy Advisory Program (BREP), launched in 2010.** BREP is already operational in Albania, Bosnia and Herzegovina and FYR Macedonia. IFC intends to expand BREP to Kosovo, Serbia, and Montenegro. BREP objectives are to improve the renewable energy regulatory framework, help renewable energy sponsors to improve their project designs and business plans, and support financial institutions to improve their internal capacities and knowledge on renewable energy. BREP's Advisory Services in Kosovo will be focused on the following areas: (i) at the regulatory level, the program will help with the creation of a standardized PPA, grid connection agreement and concession contract for small hydro power projects, improvements in primary and/or secondary legislation, and better alignment of regulation from different sectors related to small hydro project development (water management, forestry, environmental regulation); (ii) at the firm level, the program will help with better design of small hydro projects, wind farms (if there is any investors' interest), and biomass plants (with proper incentive support); (iii) in terms of financing, since there is limited interest from local Kosovo banks in developing renewable energy products, the program will closely coordinate with IFC's investment services in both the financial market and infrastructure sectors to explore investment opportunities in renewable energy projects.

(ii) Reducing environmental hazards improving environmental monitoring and management and improving priority-setting

79. **CPS Objective: Environmental hazards around the site of the Kosovo A and B power plants have been significantly reduced and there is substantially strengthened capacity for environmental monitoring.** The Bank and donor-financed *Energy Sector Cleanup and Land Reclamation Project* (CLRP) has been under implementation for several years and was planned to close in FY12, having met all its development objectives. These original expected outcomes were partial in some cases (due largely to funding limitations) implying that a part of the work on ash dump remediation and land reclamation would remain for completion by Government after the project's original closing date (June 2012). However, given the importance of the clean up to the quality of life of the communities surrounding the power plant site and feedback from consultations with civil society representatives, this CPS includes a proposed Additional Financing for the Energy Sector Clean up and Land Reclamation Project (US$3.2 million), which, inter alia, will finance: (i) extension of the coverage of the clean-up and land reclamation efforts at the site of the Kosovo A and B power plants; (ii) environmental monitoring of air, soil and water associated with power generation; (iii) strengthening the capacity of Kosovo's environmental and energy regulatory authorities; (iv) environmental and social assessments for energy projects; and (v) preparation of a low carbon growth strategy and a greenhouse gas (GHG) inventory. The AF will be complemented by a Netherlands Government grant of about US$1,165,000.

80. **CPS outcome: Broader appreciation of environmental issues and of strategies for addressing them throughout Government and among stakeholders**. At Government's request, the Bank is undertaking a *Country Environmental Analysis* (FY12), with the objective of establishing environmental development priorities based on an analysis of the state of the environment and estimates of the economic costs of environmental degradation. The study will be based on internationally derived epidemiological research regarding the relationship between the affected population exposed to environmental issues and the increased risks of health impacts in order to estimate the disease burden in Kosovo caused by environmental neglect and its associated economic impacts thereof. While the figures derived from these analyses will be indicative rather than precise, they will provide a reasonably good picture of the costs of environmental neglect and propose practical approaches for reversing past practices to more environmentally sustainable ones. Following discussion of the draft report with the Government (late FY12), there will be an intensive dissemination effort within Kosovo—involving a wide range of stakeholders at national and local levels—to both discuss the study's findings and begin to develop effective, nationally-owned strategies for prioritizing among issues and developing practical action plans to address them through legislative, regulatory and institutional changes.

(iii) Increasing access to water

81. **CPS Objective: Better and more equitable access to water of appropriate quality according to use.** In FY11, the Bank undertook a comprehensive water sector assessment at Government's request to serve as a key input to the country's national water resources strategy. Inter alia, the water assessment reviewed the potential for using water resources to foster productive investments and analyze current and projected water uses in different sectors—water supply, sanitation, irrigation, hydropower and industrial—from a spatial planning perspective. Taking into account the study's recommendations, the Government has requested that the Bank finance a *Water Supply Project*. This project has been included in the proposed CPS program for FY15, for an amount of US$18 million. The project would help ensure the security (in terms of adequacy of supply and quality) of water in the Pristina region (including energy sector, business and domestic water consumption needs). At this stage, it is expected that the Water Supply project will include some of the following activities: (i) securing of uninterrupted water supply of good quality from the Ibër-Lepenc canal through repair of the canal, protection against physical damage, short-term storage along the canal, and improved canal management; (ii) protection measures for drinking

water reservoirs; and (iii) investments to improve the quality of water supply to communities living in the vicinity of the power plants.

C. The CPS Financing Program

82. **Although the program of Bank supported operations amounts to over US$180 million, a significant proportion of these resources are derived from special grants and TFs.** The overall size of the IDA envelope for the first three years of the CPS period is about SDR 36.8 million (US$58 million). An additional SDR 11.3 million or US$18 million equivalent is included for FY15, but since these funds will depend on IDA 17 they are only notional at this stage. Actual IDA allocations beyond FY12 will depend on: (i) total IDA resources available, (ii) the country's performance rating; (iii) the performance and assistance terms of other IDA borrowers; (iv) the terms of IDA's assistance to Kosovo (grants or credits); and (v) the number of IDA-eligible countries. IDA allocations are made in SDRs based on performance, and the US dollar equivalent is dependent upon the prevailing exchange rate.

83. **The allocation of the IDA-16 resources of SDR 36.8 million (US$58 million) and the notional amount of SDR11.3 million (US$18 million) is distributed as shown in table 6**. At this stage, we expect that the IDA contribution for energy sector PRGs will amount to approximately US$14.5 million, allowing for IDA partial risk guarantees up to US$58 million. This amount will likely be supplemented by IFC and MIGA as previously discussed.

Table 6: Proposed Lending Program by Fiscal Year (in US$m)

	IDA	Grant-funded operations	TOTAL
FY12			
SEDPO2	0	47	
Agriculture and Rural Development AF		9.2	
FY12 Total	**0**	**56.2**	**56.2**
FY13			
Energy Efficiency and Renewable Energy	32.5	0	
AF for Energy Sector Clean-up and Land Reclam	3.2**	0	
		0	
FY13 Total	**35.7**	**0**	**35.7**
FY14			
Education Improvement Project	10		
PRG for KRPP and Kosovo B	14.5(58.0)*	0	
FY14 Total	**24.5**	**0**	**24.5**
FY15			
Water Supply	18	0	
FY15 Total	**18**	**0**	**18**
Overall Total	**78.2**	**56.2**	**134.4**

*Only 25 percent of total PRG amount is counted. **includes US$2.2 m re-allocated from cancelled LPTAP funds.

V. Risks

84. ***The implementation of the FY12-15 CPS entails four main risks as follows:***

- **Kosovo's uneven track record in fiscal management raises questions about medium-term macroeconomic stability, and an economic downturn in Europe would exacerbate this risk.** The Government's growing experience in macro-economic management has been supported by several external partners, notably the IMF, the EC, USAid, and the Bank. Continued financial and advisory support—together with the difficulties in obtaining financing from abroad— should convince policymakers to maintain a prudent fiscal stance. Moreover, an IMF SBA is expected to be in place for a 20 month period beginning in April 2012. The SBA should help to reduce fiscal risks, especially in the event that Kosovo's economy is impacted by an economic downturn in Europe (which could result in lower revenue and remittances). It should be noted, too, that Bank support through the PSMP and SEDPP actions will help to improve priority-setting for public expenditures and improve budget discipline over time.

- **The WBG planned support for the KRPP has generated opposition from some civil society groups and hence involvement in the project entails reputational risk.** While investment in Kosovo's energy sector is critical to growth, job creation and poverty reduction, the Bank's involvement in the new lignite-fuelled power generation plant has already generated controversy among some civil society groups and this opposition is likely to continue throughout the CPS period. This risk is being addressed through ensuring transparent processes and regular dialogue/outreach throughout project development.

- **An additional risk is that, given continued turmoil in financial markets (especially in Europe), power project financing may not be easy to obtain.** The availability of WBG guarantees should to mitigate this risk. Credit enhancement from other multilateral lenders would also help catalyze needed funds from the private sector.

- **Kosovo's governance and political structures are fragile and could destabilize under certain shocks.** Kosovo's young and relatively untested institutions render it vulnerable to domestic unrest and political pressures. The tense situation in Northern Kosovo, though currently contained to about 4 municipalities, demonstrates this risk. Moreover, Kosovo's governance systems still lack full transparency, accountability, and viability. Governance and political developments will need to be closely followed as related problems could undermine external development support activities. Actions to support improved public financial management included in the CPS and in the ongoing PSMP project should help to reduce this risk. The Bank will also carry out programmatic AAA to follow on the recommendations of the Country Fiduciary Assessment, including support for anti-corruption initiatives.

Annex 1: Kosovo CPS: Results Matrix FY12-15

Country Dev. Goals	Issues and Obstacles	Outcomes the Bank Program is Expected to Influence	Milestones	WBG Program
Pillar I: Accelerating Broad-Based Growth and Employment Generation				
Strengthening infrastructure, with a focus on energy	Unreliable electricity supply system hampers the economic development and private sector investments.	Move towards increased the production, efficiency and financial and environmental sustainability of the energy sector.	Kosovo B is being rehabilitated to comply with EU environmental standards (completion by 2018) The Sibovc South lignite mine and the New Kosovo Power Plant (KRPP) are being developed, through private participation.	**World Bank** FY13 Energy Efficiency and Renewable Resources Project FY14 PRG for KRPP **IFC** FY13-FY15 Balkans Renewable Energy Advisory Program (BREP) PPP advisory in the power distribution sector **MIGA** FY13 possible political risk guarantee for Kosovo Power Project
	Unreliable electricity distribution systems and high level of technical and commercial losses.	Improved quality of service, with secure supply to all paying customers; elimination of the need for subsidies from Government and donors to pay for electricity purchases and investment in the Distribution Company.	Electricity distribution has been privatized and technical and non-technical losses have been reduced by 3-5 percent.	
	Inefficiency in end-use of electricity and heating, and low use of renewable resources.	Improvement in energy efficiency in the building sector; institutional strengthening of a to-be-created Energy Efficiency Agency to promote energy efficiency.	At least 15-20 public buildings (schools, hospitals, community buildings) are being retrofitted; revised building codes have been established, and households have access to finance to retrofit their houses.	
		Move towards increased use of renewable resources for electricity generation.	At least 3 bankable projects have been prepared for private sector investment in renewable resources; and a financing mechanism for private sector renewable energy projects is in place.	

Promote private sector development and financial strengthening	Substantial regulatory burden on businesses, deficiencies in the rule of law, shortage of skilled labor and limited access to finance impair economic productivity and Kosovo's business climate.	Provision of knowledge inputs to Government's efforts to promote private sector led growth through simplified processes for business licensing, inspection, and regulation.	Reduction in percentage of firms indicating problems with business licensing and regulation from 47 to 37%;	**World Bank** FY08 BETA, FY10 SEDPP, FY10 RECAP, FY10 PSMP, FY11 SILED FY11 KYDP2 FY11 FSSMIP, FY12 TA Central Bank
	Kosovo's property and land administration system is inadequate: high shares of properties are unregistered, Municipal Cadastre Offices (MCOs) are weak, and property records are inconsistent and incomplete.	Property and cadastral services have improved as indicated by increase in registered real estate transactions and decrease in the average days to register a standard sale or purchase of a residential property.	Average number of days to register a standard transaction of residential property decreased from 30 to 20 days; 11 out of 23 MCO facilities are reengineered.	**AAA and ESW** FY15 CEM FY12 ROSC FY12-13 FSAP FY13-15 PER
	Improve gender equity and property ownership.	Strengthen capacity of cadastre agency to promote greater gender equity in land ownership.	Percent of property individually owned by women or jointly titled to increase from 20% (baseline: 2011) to 30% by 2015.	**IFC Advisory:** FY12-14 Trade Logistics FY13-15 Investment Climate FY12-15 Corporate Governance FY12-15 Doing Business Report Analysis /Advisory Services
	Lack of capacity for establishing and strengthening of small and micro enterprises.	Direct support to development of small and micro enterprises through grants, training and TA.	300 small and micro enterprises created or strengthened.	
		Increased access to credit for SMEs	Support development of SMEs in key areas such as agribusiness and construction through helping to overcome financial constraints.	**IFC financing:** Create new jobs by supporting competitive local corporations. Support microfinance institution Support banks with a focus on SME sectors
	Financial sector suffers from structural weaknesses.	Stronger financial system through support of the regulatory and institutional reform of Kosovo's financial system.	Reform of the payment system, and implementation of Real Time Gross Settlement; harmonization of existing regulations and procedures with Kosovo's new Banking Law, and assurance of conformity with EU practices, particularly in the area of financial reporting and auditing.	
	The Central Bank of Kosovo has insufficient institutional, financial, and supervisory	The sustainability of CBK and its capacity to supervise banks and non-	CBK has developed plans to ensure access to long-term	

	capacity, and the financial system lacks an adequate payment settlement system.	bank financial institutions have been strengthened.	resources and supervises Kosovo's main banks and pension funds on a regular schedule.	
Strengthening agriculture development	Agriculture sector is underdeveloped, with low capacity and knowledge among agri-producers. Limited targeted support for women engaged in agri-business.	Promote competitiveness and growth in the livestock and horticulture sub-sectors through implementation of selected measures of its agricultural strategy and institutional development. Women farmers targeted through the awareness raising campaign. More women farmers engaged in agriculture and agri-business in Kosovo. Strengthen capacity of Ministry of Agriculture to include and support women farmers.	At least 80 agricultural enterprises have adopted improved products and/or processes. Number of women farmers awarded grants is doubled (Baseline 2011: 4.4%) At least one third of all participants trained in grant preparation are women. At least 20 new agricultural micro and small enterprises have been established.	**World Bank** FY11 KARDP + Danish TF FY11 SILED **IFC** Financing competitive local companies in the agribusiness sector. Western Balkans Agribusiness Advisory Services
Investing in education and skills	Efforts to improve the quality of Kosovo's education system are undermined by insufficient capacity to monitor the performance of the system, including its financing, and to plan and implement sound policies at the central and local levels. The vocational and higher education systems have substandard instruction and are of limited relevance to the evolving demand for labor.	The central and local capacities to monitor financial and quality trends and plan and carry out investment is strengthened as indicated by: The transfer of budget autonomy to municipalities; the adoption of a per capita funding formula that directs resources to areas of need; the monitoring and publication of annual current expenditures for key parameters Improved opportunities for relevant training and life-long learning as indicated by the establishment of a National Qualification Framework and continued accreditation of vocational training institutions.	Financial decentralization and transfer of autonomy to schools has occurred (baseline: 13 municipalities in 2011, target 37 municipalities in 2013). Percentage of municipalities that use EMIS data to report on the status of drop-outs and retention disaggregated by gender and community. (baseline; 0% in 2011; 60% in 2013). National Qualification Framework document and administrative instruction of accreditation criteria developed and approved. Decisions about the accreditation of training providers made publicly	**World Bank** FY07 IDEP FY10 SEDPP FY12 SEDPP

	Lack of reliable data on drop out and retention for girls and boys.	Better quality school data are collected regularly by a higher proportion of schools.	available. At least 60% of municipalities are reporting drop out and retention data disaggregated by gender.	
Promoting sustainable employment and social inclusion	Kosovo's unemployment rates are high – 46% among the general population and 76% among youth; yet, labor market programs are weak, and non-compliance with existing labor protections and regulations is widespread. The design and implementation of effective policies and programs is hampered by the limited capacity to monitor the labor market. Sub-par health outcomes, including for financial protection, call for a system reform with pressures to increase labor taxes and possibly adverse consequences for labor demand. Access to basic infrastructure and labor and enterprise development services is low in poor communities, particularly among poor and multiethnic communities (including youth).	Labor programs strengthened and employment opportunities enhanced, as indicated by increase in number of annual job placements made by Public Employment Services and decrease in the informal employment rate. The capacity for monitoring is strengthened as indicated by improved statistical data collection and analysis. Health outcomes are improved as indicated by the passing of a health insurance law that transforms the financing of health care to improve the financial protection of the poor without threatening the fiscal sustainability and increasing labor taxes. Support social cohesion through rehabilitation of small-scale social and economic infrastructure in the poorest villages and in mixed/minority communities as well as promoting MSMEs in a socially inclusive manner; and through youth centers, promoting inter-ethnic collaboration among youth, especially from marginalized and vulnerable groups.	Pilots of labor market programs with increased participation of regional and local employment offices have been carried out. Public works program expanded. The development of a Labor Market Information System has been initiated. Health insurance law passed. At least 20 basic community infrastructure objects have been rehabilitated or built through a socially inclusive approach and at least 300 small and micro enterprises have been created or expanded with a socially inclusive approach. At least 16 Youth Centers have fully developed sustainable strategies.	**<u>World Bank</u>** FY10 SEDPP FY11 SILED FY11 KYDP2 FY12 SEDPP **<u>AAA and ESW</u>** FY12-FY13 Kosovo Statistical and Analytical Capacity Development FY12-15 Programmatic Poverty and Gender monitoring
Strengthening public financial management, procurement and anti-corruption efforts	Kosovo's PFM system is impaired by unreliable multi-annual planning systems and weaknesses budget execution, particularly in payroll management and procurement. Lack of a pay and grading structure in the civil	Long-term focus on public financial management with strengthened internal controls and audit, strengthened external audit, as measured by improved performance in the PEFA indicators.	In no more than one out of last 3 years has the actual expenditure deviated from budgeted expenditure by more than 10% of budgeted expenditure (PEFA ind. PI-1).	**<u>World Bank</u>** FY10 PSMP FY11SEDPP **<u>AAA and ESW</u>** FY12 CFA

	service results in wide pay differentials for comparable positions in different civil service organizations, and erodes planning and controls in wage bill management.	Increased bidder participation in public procurement tenders and cost savings achieved through Quick Gaines actions and e-procurement modules. Transparent and coherent pay and grading structure introduced in the core civil service.	Bidder participation in public procurement tenders increases by 15% (baseline: 8,270 bidders). Grading system is fully introduced and there is an equal base pay for posts of equal grade and salary step across civil service bodies.	
Pillar II: Improving Environmental Management				
Reduce the environmental footprint of development activities, reducing environmental hazards to human welfare, and moving towards harmonization with EU environmental standards.	Lack of analysis of environmental issues and priorities Kosovo's mining operations have polluted land potentially viable for development, while institutional capacity to undertake environmentally sound mining operations is inadequate. Kosovo has high carbon emissions, along with an underutilized energy efficiency	Broader appreciation of environmental issues and of strategies for addressing them throughout Government and among stakeholders. Pollution in mining operations has been reduced and environmentally sound mining operations have been strengthened through elimination of dumping on open land of ash from the Kosovo A power plant. Initiate and enable KEK to achieve land reclamation for natural habitats, agriculture, resettlement or other land use purposes. Removal of highest priority hazardous substances from storage tanks at the gasification site. The KRPP program adheres to good environmental practices and options for deriving energy from renewable sources.	Completion of Government's Kosovo Environmental Action Plan (2011 draft) and the State of the Environment Report. Mirash open pit mine has been prepared for Kosovo A ash management, and the wet ash handling system has been installed. At least 55% of the total overburden area has been reclaimed. 4300 tons of tars, benzene, phenols, methanol, and oily compounds have been removed. Regular environmental monitoring of air, soil, and groundwater in the KRPP area is established; A low-carbon growth strategy for Kosovo is prepared.	**World Bank** FY06 Energy Sector Cleanup and Land Reclamation Project FY13 AF for Energy Sector Cleanup and Land Reclamation Project **AAA and ESW** FY12 Country Environmental Assessment **IFC** FY12-13 Solid Waste Management Concession

Annex 2: Summary of the Consultation on the Proposed World Bank Country Partnership Strategy for Kosovo for FY12-15 with Civil Society Organizations

World Bank Office in Kosovo, Wednesday, April 4, 2012

The World Bank office in Pristina sent invitations to a large number of CSOs, to discuss the proposed CPS for Kosovo for FYs12-15. The invitation included a detailed powerpoint presentation on the proposed CPS and an Agenda for the consultation meeting comprising six guiding questions as well as links to key reports available on the Bank's website (Country Economic Memorandum, Public Expenditure Review, Development and Evaluation of Power Supply Options for Kosovo, Report of the SFDCC External Expert Panel, and South East Europe Regular Economic Report). All the reports, as well as the PPT and Agenda, were translated into Albanian and made available well in advance of the meeting. The consultation meeting took place on April 4, 2012 in the new premises of the World Bank Office in Kosovo and lasted for a full day with lunch provided. The World Bank Vice President for Europe and Central Asia, Philippe Le Houérou opened the meeting with introductory remarks on the proposed CPS for Kosovo. The meeting was moderated by the World Bank's Senior Advisor, Theodore Ahlers. The Bank's Country Director for the Western Balkans, Jane Armitage, was also present. The Country Manager for Kosovo, Jan-Peter Olters, delivered a presentation on the key messages of the proposed CPS to kick-off the discussion.

Mr. Philippe Le Houérou's opening remarks:

As the World Bank moved from an Interim Strategy Note for Kosovo to a Country Partnership Strategy (CPS), it was an important moment in the partnership between the Bank and Kosovo. The Bank fully supported Kosovo's goal of joining the European Union and recognized that the EU could help Kosovo to lift its people out of poverty. Given the importance of diagnosis for shaping this first CPS for Kosovo, it was essential to discuss the Bank's diagnosis underlying the CPS. Bank staff believed that jobs and growth were critical and so the Bank focused the first CPS pillar on jobs. In the second pillar, the Bank had a clear focus on environmental management, reflecting the Bank's assessment that this was critical for the well-being of Kosovars. In so doing, the Bank wanted to help to balance environmental management with growth and job creation. Energy straddled both pillars of the proposed CPS – electricity shortages remained a key constraint to private investment and jobs, and inefficiencies in the sector were a key contributing factor to environmental pollution.

Mr. Ted Ahlers' opening remarks:

Mr. Ahlers noted that this was one of many consultations held in Kosovo over the past four years. The purposes of the full-day consultation were to get the CSOs' views on the proposed CPS, to answer their questions, and have a discussion on areas of concern. The Bank was preparing to go to the Board in late May or June with this CPS, leaving plenty of time to give due consideration to CSO concerns. To ensure that all issues were addressed, the Bank had previously distributed a detailed, powerpoint presentation on the CPS and an agenda for the

consultations including six guiding questions for the discussion. The powerpoint presentation and agenda are available on line at www.worldbank.org/kosovo.

Mr. Ahlers noted that many things in the proposed CPS have changed over the past year, based on the Bank's ongoing consideration of Kosovo's development challenges and inputs from civil society and the private sector.

Short presentation on the proposed CPS by Mr. Jan-Peter Olters:

Mr. Olters told participants that the CPS is dynamic and could be modified when warranted through the CPS Progress Report. The Bank would continue listening to the ongoing dialogue in Kosovo even after the World Bank document goes to the Board. The overarching objective of the strategy was to increase growth and domestic productivity. Mr. Olters noted that civil society has had positive influence on the CPS, as reflected in the scope of projects being proposed.

Agenda Item 1: Is the World Bank's diagnosis of the challenges facing Kosovo correct?

Questions were focused on the economic and social development priorities in the proposed CPS, specifically whether the only strategy for growth in Kosovo was EU integration. A question was raised about whether the Bank's consideration of support for a new power plant could actually be an obstacle to EU integration. There were also questions about the expected outcomes of the CPS and how success would be measured and why the Bank put the energy project in the category of growth when it is unclear how it will specifically help to create jobs. The moderator asked the participants to focus on the diagnosis question for this first agenda point, noting that, if one started with an agreed diagnosis, one could more easily move to how to address Kosovo's development challenges. Comments were made about perceived contradictions in the strategy, the identification of risks in the CPS, and if jobs and environment were the diagnosed challenges, then what specifically would the World Bank be doing about it? One member of civil society noted that the Bank should be implementing "job-building projects."

A representative of KEK employees asked whether there was a specific approach to handling the employees who currently worked at the power plants once Kosovo A was closed. If the first priority was the creation of jobs, why would the Bank include a project that would limit them at the power plants? The representative noted that Kosovo A, while unsustainable, employed about 1500 workers, with an average age of 50 years. Kosovars were concerned about giving the local capacity of Kosovo B to a private company. He noted that this did not have the support of the employees of the union of workers.

In terms of the challenges and constraints, there was general agreement that jobs and the environment were the main issues in Kosovo. A question was raised about why the World Bank was considering support to a new power plant if the environment was a problem.

Mr. Le Houérou asked about other ideas on how to create a thriving private sector that could create jobs because not everyone could be a civil servant. What would be the driver of the economy going forward – remittances? How did one build a thriving private sector? He asked for the views of the participants on where they saw the growth coming from, underlining that the diagnosis on this was critical. How could Kosovo go from the current GDP per capita to that of

Slovenia and then to that of a country such as England? What were the economic and social impediments to that? Mr. Le Houérou noted that if there was no agreement on the diagnosis then it was very hard to have an agreement on solutions.

A representative of the Community Development Fund, which is implementing the World Bank-funded Social Inclusion and Local Development Project, asked whether there would be other projects of this type financed by the Bank in Kosovo, commenting that the direct link between building a new power plant and jobs was not clear. She agreed that unemployment was a big problem but pointed out that she did not see how the proposed CPS addressed that.

A representative of Development 4 Democracy listed as a challenge the low productivity and Kosovo's competition in the jobs market. The Labor Union noted that thousands of workers would be sent home but what was the productivity currently? Other questions were raised about the Bank's strategy for addressing women's unemployment, the government policy of borrowing funds for highways, and how the World Bank felt Kosovars should be addressing their indebtedness and the future.

One participant pointed out that industry competitiveness should be listed specifically in the development strategy. A representative of KIPRED highlighted the rule of law as a challenge for curbing unemployment. Claiming that 40 percent of Kosovo's economy was in the black market, he recommended that the World Bank built mechanisms to shift the black economy into a formal economy so there was actual data and policies in order for the issues to be addressed more easily. He expressed the view that rule of law and education should be the main pillars.

One participant suggested investing in local products and encouraging local farmers, noting that the World Bank was enriching the government and creating oligarchs rather than supporting entrepreneurs. The CDF representative mentioned that the World Bank was indeed supporting small and micro enterprises through SILED project, but that she hoped that the Bank would have more money for this type of support in the future.

World Bank Country Director, Ms. Jane Armitage, acknowledged that the Bank's consideration of supporting the new power plant was controversial. She noted that preparation of the project was still at a very early stage and that there would be many opportunities for in-depth discussions with CSOs as preparation proceeded. She indicated that the proposed CPS had changed to reflect previous discussions with CSOs, namely by adding a Water project to improve water supply and quality for households, businesses and agriculture and a Renewable Energy and Energy Efficiency project which would be the largest project over the next four years in Kosovo. She also informed the participants that there were plans to hold a Donor Conference in September on supporting the closure of Kosovo A and enabling further investments in renewable energy and energy efficiency. Ms. Armitage noted that the Bank is supporting and will continue to support employment under the new CPS and urged the group to look at the current portfolio and the pipeline of future projects, emphasizing that the World Bank was already financing important projects in agriculture, education, business climate improvement, cadastre and the financial sector which all help support job creation. In addition, the Bank has provided €33 million in budget support for a Sustainable Employment Development Policy Operation to strengthen the institutional and regulatory environment for employment creation. Ms. Armitage noted that the European Commission supports development of the new power plant project (which would be

fully consistent with EU environmental requirements) and that a priority for many of Kosovo's partners (including the EU) was to close the old, highly polluting Kosovo A Power Plant.

A representative of the education unions highlighted the importance of reforms in the education sector, concluding that not much had changed in the Kosovo schools as they lacked the tools to become modern. He questioned the results of the promised strategies in the education sector and underlined that children should not fail for lack of education.

The Director of Kosovo's Center for Gender Studies considered that the proposed CPS lacked a gender focus. She suggested that gender issues should be included in all the projects. As an example, she wanted to see in the CPS the unemployment figures for women. The improvements in gender aspects proposed in the CPS were deemed by her as insufficient.

A World Bank consultant working on the agriculture and cadastre sector provided information on the gender aspects of some Bank-funded projects. He mentioned that both the ongoing agriculture and cadastre projects include design features that promote women's legitimate rights through, for example, special outreach efforts, training for business development and secure title to land.

A representative of GAP institute claimed it was difficult to see Government's development strategy. In her view, the priorities put forward in the proposed CPS were contrary to the country's real priorities. Her objection was that the challenge of rule of law was dealt with only through the strategy of EU integration. She also suggested that there were other alternatives to promote development besides building a new power plant.

Agenda Item 2: Is the proposed package (of ongoing operations, new lending, analytical work, and technical assistance) appropriate to address the challenges?

The moderator noted that governance, gender, and education were some of the issues discussed in the previous session and invited participants to discuss those further. His view was that, while governance and rule of law was clearly a very big issue for Kosovo, the EU and many other partners might play a bigger role than the World Bank in that regard. He agreed that gender should not be just a box in the CPS document and welcomed additional ideas on addressing this issue.

Mr. Olters highlighted the importance of consultations with all stakeholders in Kosovo, not least with a view to identifying development priorities with broad-based support. He explained that every Bank-funded project would need to be ratified by Parliament with a 2/3-majority because they would be funded with IDA credits and not grants. He also explained the links between the different Bank-funded projects. For example, the Cadastre and Real Estate project, provided farmers with titles documenting their land ownership, which, in turn, could enable them to use land as collateral. The Agriculture project was helping farmers and small agri-businesses with applications for loans from commercial banks.
One participant questioned the results of several Bank-funded projects such as the Institutional Development in Education, the Business Environment Technical Assistance, and the Cleanup and Land Reclamation Projects. He noted that students did not study agriculture, that last year Kosovo ranked lower in the Doing Business ranking, and that there were protests of area residents dissatisfied with the Cleanup Project. He praised the Real Estate and Cadastre

Registration Project, but expressed concerns that unemployment might not be addressed sufficiently in the new CPS. The moderator highlighted that creating jobs was a huge challenge and required a multi-pronged approach to growth and business development.

One participant asked why all World Bank funding needed to be channeled through the Government and not through CSOs, especially since disbursement was an issue on the side of government agencies. The moderator noted that the World Bank was owned by the countries of the world and that it provided financing to the member governments. The lending contracts had to be between the World Bank and the government, as required by the Bank's founding charter.

One participant suggested that the education piece in the strategy should be bigger in order to address fundamental issues and expressed reservations about indebting future generations. Specifically, she suggested a future education project should aim at making education in Kosovo aligned with EU standards.

A representative of the Group for Legal and Political Studies suggested that the World Bank could monitor Government's budget planning and help competition in the markets, such as the telecom sector. One participant expressed the opinion that the World Bank would suppress the market for renewable energy in Kosovo with its proposed support for a new power plant. She noted that an external expert claimed that 80,000 jobs could be created if the Bank invested in renewable energy in Kosovo. The moderator suggested that the crux of the discussion on energy was about how much electricity Kosovo needs and where to get that electricity from. The moderator explained that Bank officials had reviewed all of the analyses very carefully and published all of its own analysis in English and Albanian.

One participant disagreed with the Bank's analysis and noted that the Bank should be held to its own standards for supporting renewable energy in the future and for making accurate assessments of the various energy alternatives. The moderator confirmed that the World Bank would provide many more opportunities to discuss the proposed Kosovo Power Project as it moved forward with considering the project and conducting all the necessary environmental, technical, and social assessments.

A representative of KEK workers' union suggested that the World Bank should focus on improving energy efficiency and expanding the existing irrigation system in Kosovo.

A representative of IFC informed the participants about the areas where IFC wanted to increase its program in Kosovo, explaining that IFC had been working on strengthening the competitiveness of Kosovo's goods by improving adherence to international standards and technical cooperation. He noted that IFC was active also in supporting improvements in corporate governance and trade logistics. He highlighted that IFC's investment in one leading commercial bank was very important, as it was the first bank in Kosovo and that IFC is also working with SMEs. The IFC representative also noted that Kosovo would be included in IFC's Balkan Energy Renewable Program which aimed at helping firms to design projects and financial institutions to develop new products for renewable energy projects.

One participant asked whether the World Bank supported the blockade of Serbian goods to Kosovo. The moderator responded that the Bank did not support blockades anywhere in the world because open markets, when managed well, were considered contributors to growth. When

a follow-up question was asked about subsidies for Kosovo's products in relation to Serbian and Bosnian subsidies, the moderator noted that issues of protection warranted great care.

One participant noted that the figures for GNI coefficient and the birthrate were not recorded in Kosovo so it was difficult to assess whether improvements had been achieved in the well-being of the population. He asked if the Bank did any analysis on these figures and if it were to finance a project supporting improvement of statistics in Kosovo. The Country Manager agreed that more accurate and more timely statistics were crucial to understanding changes in poverty levels and agreed that having EU standards in education was very important because it could help with employment. He underlined that it took a lot of time to achieve these improvements.

Staff from the Bank office in Pristina explained the outcomes of the ongoing education project, including the decentralization of fiscal management of schools. School development grants support selected schools to prepare and implement quality enhancement plans. Selection criteria include retention and attendance rates among girls. There was also support for a training mechanism for teachers linked to salary increases, which was likely to continue. The project also strengthened the capacity in the Ministry of Education to improve the assessment of the *matura* exam. Links between education and the labor market had been supported through the budget support operation SEDPO. The Bank official also explained that the project provided international training on the design of test questions, that the Ministry of Education was building mechanisms to ensure misconduct was not repeated, and that education institutions would receive further capacity building. Responding to a comment on politicization of schools in Kosovo, the Bank official encouraged civil society to devote more attention to the education sector.

Following the lunch break, staff from the Bank office provided clarifications on the results of the Environmental Clean-Up Project. The project was ongoing, with the objectives for the ash dump and overburden dump stabilization having already been achieved. The highest point of the ash dump had been lowered by 14 meters and its slide towards the village of Dardhishte had been stopped. Some 100,000 plants have been planted on top of the overburden dumps and, by the end of May, the current open-air transport of ash should be replaced with a hydraulic transport of ash. At the end of April, the process of cleaning up tons of phenolic waste water should be completed. The Government of Kosovo had signed bilateral agreements with countries such as Sweden and Germany to remove some of the waste.

Agenda Item 3: Is the proposed comprehensive approach to supporting the energy sector sufficient to address concerns about the Kosovo lignite power plant?

The moderator provided a framework for the discussion by posing a few key questions: how much electricity did Kosovo need and from where should it get it? How much energy could Kosovo get from energy efficiency, from renewable energy, and where could it get the rest of the power needed?

To frame the discussion, Bank staff gave a short presentation and responded to some questions raised earlier in the day.

The importance of affordable and reliable power supply for small businesses was underlined. The Bank official explained that the Bank's analysis assumed higher carbon prices than were demanded in the market and that the forecasted demand used in the Bank's analysis of Kosovo's energy demand was very optimistic. He noted that, even if a smaller supply-demand gap was used, Kosovo still needed to determine how it was going to secure its energy in the coming years, particularly as the country was legally obligated to decommission the highly polluting Kosovo A Power Plant by 2017. The Bank's analysis was also optimistic about the potential for renewable sources of energy, such as biogas and wind power. The Bank had been encouraging the Government to make better use of solar power for water heating. The Bank noted that a detailed analysis of externalities had not yet been conducted because the project was still in the earliest stages of consideration. However, this analysis would be done at the stage of Project Appraisal and consultations would be conducted on its findings .

The Bank also clarified that it would not support the New Kosovo Power Plant if it did not meet EU standards. The Bank official provided clarifications on the issue of water supply, sharing data from a technical study on the Iber-Lepenc Canal which concluded that there was sufficient water for power generation and that the Bank's water project would help with the conveyance system and reduction of losses.

The Bank official also responded to an earlier comment about the inclusion of the rehabilitation of the Kosovo B power plant in the project package, noting that Kosovo's Parliament had approved the strategy to combine the closure of Kosovo A, the rehabilitation of Kosovo B, and the opening of the New Kosovo Power Plant. For as long as the Parliamentary decision allowed for an economically viable investment and took into consideration all the environmental and social safeguards, the World Bank would not argue against the current Parliamentary decision.

The Bank official explained that his team and Mr. Daniel Kammen's team at Berkeley have had numerous discussions about their respective analyses and that discussions were ongoing. He noted that running a model on an energy basis versus a capacity basis did not take storage into account and that a model needed to plan for meeting the peak demand during winter.

A participant disagreed with the findings of the Options Study, mainly because, in his view, peak consumption was treated in the study as base-load. Another participant warned that the proposed project would create an energy monopoly which would lobby the government to use more of its energy rather than promote energy efficiency. The moderator reiterated that, if the project was not in conformity with EU Directives, the Bank would not finance it, noting that the EU had confirmed its support for the proposed project and that, as currently planned, it considered the project to be in conformity with the relevant EU Directives.
Bank officials repeated that the Partial Risk Guarantee for the proposed project had not yet been approved and that a variety of studies needed to be conducted prior to the Bank's final consideration of the project. The moderator noted that it would take at least a year before the proposed project could be presented to the World Bank's Board of Executive Directors for further consideration – and then only if the project met all the Bank's environmental and social requirements.

Bank officials explained that the location of the new power plant would be next to Kosovo B and would thus not be a green field project, as suggested by representatives from the Municipality of Obiliq.

A discussion followed about the EU's rules on monopoly and the right of consumers to choose their energy supply. A participant objected to the proposed project saying that it breached the principles of the EU rules on monopoly. Bank officials agreed that Kosovo should have a fully liberalized, deregulated market but noted that, in other countries, "switch" rates by energy consumers were very low whereas the investments required to offer the switch were very expensive. Generally, only the large commercial consumers switched energy providers.

One Bank official noted that new capacity for coal power would not likely crowd out other renewable investments because Kosovo had a feed-in tariff which meant the operator was obliged to dispatch renewable energy as a priority. He also noted that the Bank was in favor of the 400kV transmission line with Albania and that he worked on the proposal for the feasibility study for this transmission line in 2002/03.

The point was raised by one participant that support from the EU for the proposed power project was not ensured and that CSOs had sent a letter to the EC asking them to confirm whether they supported the proposed new Kosovo power plant. He also remarked that the letter of support from the US Government was signed by a low-ranking Treasury official and not by the State Secretary. The moderator remarked that EC had told the Bank they supported the project and that the Bank's usual interlocutor in the US Government is the Treasury Department.

Questions were raised about the Bank's Options Study compared with the Berkeley RAEL alternatives study, as well as about the costs of the proposed power project. Specifically, one participant asked why the Bank had not modified its numbers on the cost of externalities since its last presentation and why the Bank was not conducting another externalities study. Bank officials repeated that the proposed project would not be going to the Board for at least a year. During that time, the Bank would undertake more detailed analyses about all aspects of the project. For example, the baseline Environment Social Impact Assessment (ESIA) and the Air Quality Monitoring had not been done but the Government and Bank would prepare these over the next year. Bank officials noted that the Board will not review the project until all of the ESIAs were drafted, discussed, and disseminated.

It was also noted that the studies had to be site-specific and could not rely on data from other countries.

The moderator clarified that the Bank had not *approved* the project, but rather agreed to consider "in-principle" the Partial Risk Guarantee by launching all the necessary preparatory studies. Ms. Armitage clarified the purpose of the CPS is to present the broader, long-range vision over the next four years and that the projects proposed within the CPS would require separate, individual approval by the Bank's Board. She explained that when the Board discussed the CPS at the end of May or early June, it would be looking principally at whether the Bank was proposing the right kinds of projects in Kosovo in relation to the country's overarching development challenges.

One participant suggested three points for further discussion: not treating the peak demand as base-load; working together on decoupling the proposed new power plant and the existing Kosovo B power plant; and working together on energy efficiency and renewable energy projects. He agreed that the targets for reduction of losses in the Options Study were ambitious.

The Bank's energy sector coordinator for Southeast Europe explained that increasing end-use energy efficiency was difficult because it required awareness and economic support. The introduction of price signals should be combined with support for the poor. Energy efficiency required sustained efforts over long periods of time, but very quick results were achievable in the public sector and by retrofitting public buildings. He noted that this would likely form an important part of the proposed US$32-million energy efficiency and renewables project to be supported by the Bank in coming years. Ms. Armitage added that the proposed project would have subsidies for poor households for insulation, windows, and solar panels. The proposed project would also have a renewable energy component and the Bank would co-host a donor conference on energy in the fall of 2012. She underlined that renewable energy and energy efficiency represented a large part of proposed new lending in the CPS for Kosovo and that the decisions to include these initiatives in the strategy had been the direct result of feedback received from the CSOs in attendance. She noted that the proposed water project in the new CPS also resulted from productive, ongoing discussions with civil society groups and community members in Kosovo. Ms. Armitage noted that, as the Bank moved forward with these projects, all of the necessary studies would be shared and consulted with civil society and the community.

The representative of the KEK workers' union suggested that power plants could provide heating for the bigger cities in Kosovo and asked again about the Bank's position on the 8,000 employees of KEK if Kosovo A were closed and Kosovo B and the distribution were "given away" to private companies. He asked how workers could get involved in the decommissioning of Kosovo A and what would happen with their property once construction and resettlement took place. He wanted to know what guarantees would workers have that their livelihoods would not be risked. A Bank official noted that, based on data from 2009, 50 percent of the KEK employees were older than the age of 55-58 so they were close to retirement. In Government documents, investors were required to keep the workers employed for three years on the same or better terms. After 3 years, they would have to follow the local laws. New construction would generate direct and indirect employment for the next four years (for 600MW, there would be a need for 1,000 people for four years). Local skilled workers would be preferred for construction by the investor. There would be another 300-400 skilled workers in operation and employment from decommissioning Kosovo A for at least 2-3 years. A combination of age profile, security from the new investor, and the new jobs that would be needed should compensate well for the loss of jobs by closing Kosovo A. A more detailed analysis would be done as part of a Poverty and Social Impact Assessment. The Bank official also explained that cogeneration for district heating of Pristina would be implemented in the next two years and that it would be connected with Kosovo B. Ms. Armitage noted that any resettlement needed for the new project would be handled according to the Bank's policies.

Agenda Item 4: Are there other areas of emphasis for the Country Partnership Strategy that have been overlooked? What risks are to be expected and how should the strategy address these risks?

The moderator asked the participants to provide any input they have on the last two guiding questions – was there anything left out of the CPS and if there was some other risk for the strategy as a whole besides the risks already identified in the proposed CPS?

One representative asked to see the link between the strategy and the rule of law and suggested that maybe something on improving the judiciary could be added to the CPS. Another participant said the Bank was doing more harm than good with the CPS by worsening the health perspective for the people of Kosovo with the new power plant, by encouraging a monopoly on energy generation, and spending US$32 million on Technical Assistance and studies. She suggested that the power plant would be very expensive and Obiliq would lose its village because its citizens' compensation would happen in such a way that they would be removed from their villages into apartment blocks. She added that the Bank would fail to compensate the community properly on resettlement and that, although the Bank would improve water quality, there simply would not be enough water in Kosovo. She mentioned the risk of the new power project hindering Kosovo's EU integration. The moderator remarked that the Bank agreed on the importance of EU integration for Kosovo. He reiterated that Bank officials did not know yet whether the Partial Risk Guarantee for the power plant project would be approved by the World Bank Board. However, he underlined that identifying the country-wide risks was important and that many of the issues raised regarding the power plant would be discussed in greater detail once some of the studies were under way.

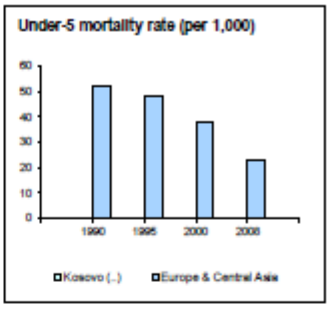
One participant asked whether the Bank could share details about the US$32 million Energy Efficiency and Renewable Energy Project. Ms. Armitage noted that the project's initial concept documents would be available publically later in the year when and preparation of the project started. She noted that all project information would be published on the website according to Bank policies and that she was happy to share with them information on other energy efficiency projects in the region.

Ms. Armitage noted that the draft CPS document would be shared with the CSOs when it was sent to the Bank's Board of Directors because the Government had agreed for simultaneous disclosure of the CPS. Comments could be sent to Bank staff present in the meeting and to the Board. Ms. Armitage emphasized that the CPS was a living strategy document, not one set in stone. This draft document was the Bank's best assessment at the moment of how it could help Kosovo to address its development challenges. It was the beginning of a process and the CPS could be adjusted over the next four years as implementation began through the CPS Progress Report. The final version of the CPS would incorporate possible comments/changes made by the Board and be posted on the Bank's Kosovo website.

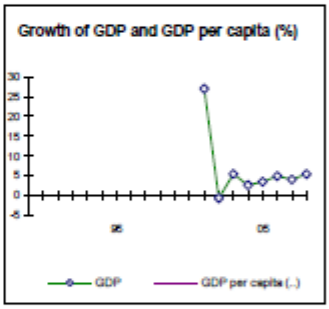
The moderator thanked the participants for a very useful discussion. The Country Manager noted there would be more discussions as preparations on all the projects proposed in the CPS move forward.

Annex 3: At-a-Glance

Key Development Indicators	Kosovo	Europe & Central Asia	Lower middle income
(2009)			
Population, mid-year (millions)	1.8	403	3,767
Surface area (thousand sq. km)	11	23,549	31,923
Population growth (%)	0.6	0.3	1.2
Urban population (% of total population)	..	64	40
GNI (Atlas method, US$ billions)	5.9	2,772	7,682
GNI per capita (Atlas method, US$)	3,240	6,880	2,039
GNI per capita (PPP, international $)	..	13,297	4,502
GDP growth (%)	4.0	4.0	7.5
GDP per capita growth (%)	3.4	3.6	6.3
(most recent estimate, 2003–2008)			
Poverty headcount ratio at $1.25 a day (PPP, %)	..	4	..
Poverty headcount ratio at $2.00 a day (PPP, %)	..	9	..
Life expectancy at birth (years)	69	69	68
Infant mortality (per 1,000 live births)	..	20	44
Child malnutrition (% of children under 5)	..	..	25
Adult literacy, male (% of ages 15 and older)	..	99	87
Adult literacy, female (% of ages 15 and older)	..	97	73
Gross primary enrollment, male (% of age group)	..	100	109
Gross primary enrollment, female (% of age group)	..	98	105
Access to an improved water source (% of population)	..	95	86
Access to improved sanitation facilities (% of population)	..	89	50



Net Aid Flows	1980	1990	2000	2009
(US$ millions)				
Net ODA and official aid	..	..	..	..
Top 3 donors (in 2007):				
n.a.	..	..	..	..
n.a.	..	..	..	..
n.a.	..	..	..	..
Aid (% of GNI)	..	..	..	..
Aid per capita (US$)	..	..	..	..



Long-Term Economic Trends	1980	1990	2000	2009	1980–90	1990–2000	2000–09
					(average annual growth %)		
Consumer prices (annual % change)	..	..	..	-2.4			
GDP implicit deflator (annual % change)	..	..	*11.4*	-3.4			
Exchange rate (annual average, local per US$)	..	..	1.1	0.7			
Terms of trade index (2000 = 100)	..	..	..	..			
Population, mid-year (millions)	..	..	..	..	..	..	..
GDP (US$ millions)	..	..	1,849	5,367	..	..	4.8
		(% of GDP)					
Agriculture	..	..	..	12.0	..	..	..
Industry	..	..	..	20.0	..	..	..
Manufacturing	..	..	..	17.3	..	..	..
Services	..	..	..	68.0	..	..	..
Household final consumption expenditure	..	..	..	..	..	..	..
General gov't final consumption expenditure	..	..	..	18.2	..	..	..
Gross capital formation	..	..	..	27.7	..	..	..
Exports of goods and services	..	..	..	14.1	..	..	..
Imports of goods and services	..	..	..	54.4	..	..	..
Gross savings	..	..	..	..			

Note: Figures in italics are for years other than those specified. 2009 data are preliminary. .. indicates data are not available.

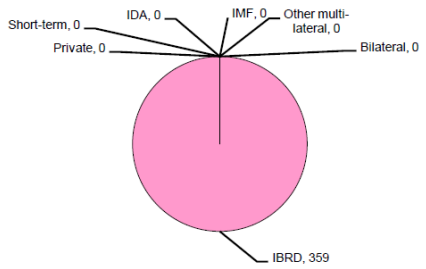
Development Economics, Development Data Group (DECDG).

Balance of Payments and Trade	2000	2009
(US$ millions)		
Total merchandise exports (fob)	..	..
Total merchandise imports (cif)	..	..
Net trade in goods and services	..	-2,171
Current account balance	..	-1,002
as a % of GDP	..	-18.6
Workers' remittances and compensation of employees (receipts)	..	..
Reserves, including gold	..	..

Central Government Finance		
(% of GDP)		
Current revenue (including grants)	..	29.7
Tax revenue	..	21.1
Current expenditure	..	18.6
Overall surplus/deficit	..	-0.6
Highest marginal tax rate (%)		
Individual	..	..
Corporate	..	..

External Debt and Resource Flows		
(US$ millions)		
Total debt outstanding and disbursed	..	359
Total debt service	..	230
Debt relief (HIPC, MDRI)	–	–
Total debt (% of GDP)	..	6.7
Total debt service (% of exports)	..	14.5
Foreign direct investment (net inflows)	..	426
Portfolio equity (net inflows)	..	0

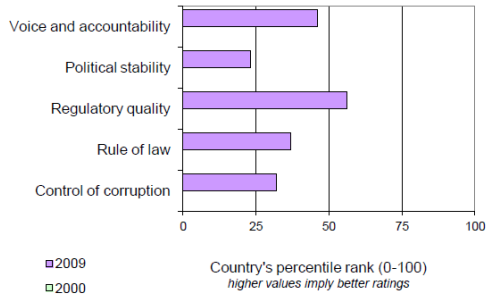
Composition of total external debt, 2009



US$ millions

Private Sector Development	2000	2009
Time required to start a business (days)	–	52
Cost to start a business (% of GNI per capita)	–	26.4
Time required to register property (days)	–	33
Ranked as a major constraint to business (% of managers surveyed who agreed)	2000	2009
n.a.	..	..
n.a.	..	..
Stock market capitalization (% of GDP)	..	..
Bank capital to asset ratio (%)	..	..

Governance indicators, 2000 and 2009



Source: Kaufmann-Kraay-Mastruzzi, World Bank

Technology and Infrastructure	2000	2008
Paved roads (% of total)	..	..
Fixed line and mobile phone subscribers (per 100 people)	..	..
High technology exports (% of manufactured exports)	..	..

Environment		
Agricultural land (% of land area)	..	*52*
Forest area (% of land area)	..	..
Terrestrial protected areas (% of surface area)	..	..
Freshwater resources per capita (cu. meters)	..	..
Freshwater withdrawal (billion cubic meters)	..	..
CO2 emissions per capita (mt)	..	..
GDP per unit of energy use (2005 PPP $ per kg of oil equivalent)	..	..
Energy use per capita (kg of oil equivalent)	..	..

World Bank Group portfolio	2000	2009
(US$ millions)		
IBRD		
Total debt outstanding and disbursed	–	359
Disbursements	–	0
Principal repayments	–	208
Interest payments	–	23
IDA		
Total debt outstanding and disbursed	–	0
Disbursements	–	0
Total debt service	–	0
IFC *(fiscal year)*		
Total disbursed and outstanding portfolio	–	–
of which IFC own account	–	–
Disbursements for IFC own account	–	–
Portfolio sales, prepayments and repayments for IFC own account	–	–
MIGA		
Gross exposure	–	–
New guarantees	–	–

Note: Figures in italics are for years other than those specified. 2009 data are preliminary. 2/25/11
.. indicates data are not available. – indicates observation is not applicable.

Development Economics, Development Data Group (DECDG).

Annex 4: Selected Indicators* of Bank Portfolio Performance and Management

As Of Date 1/30/2012

Indicator	2009	2010	2011	2012
Portfolio Assessment				
Number of Projects Under Implementation [a]	6	8	9	7
Average Implementation Period (years) [b]	2.6	2.8	2.9	3.6
Percent of Problem Projects by Number [a, c]	33.3	12.5	55.6	14.3
Percent of Problem Projects by Amount [a, c]	30.2	15.8	50.3	13.0
Percent of Projects at Risk by Number [a, d]	33.3	25.0	55.6	14.3
Percent of Projects at Risk by Amount [a, d]	30.2	20.6	50.3	13.0
Disbursement Ratio (%) [e]	13.8	24.4	13.0	7.8
Portfolio Management				
CPPR during the year (yes/no)				
Supervision Resources (total US$)				
Average Supervision (US$/project)				

Memorandum Item	Since FY 80	Last Five FYs
Proj Eval by OED by Number	18	2
Proj Eval by OED by Amt (US$ millions)	22.4	6.4
% of OED Projects Rated U or HU by Number	5.6	0.0
% of OED Projects Rated U or HU by Amt	0.0	0.0

a. As shown in the Annual Report on Portfolio Performance (except for current FY).
b. Average age of projects in the Bank's country portfolio.
c. Percent of projects rated U or HU on development objectives (DO) and/or implementation progress (IP).
d. As defined under the Portfolio Improvement Program.
e. Ratio of disbursements during the year to the undisbursed balance of the Bank's portfolio at the beginning of the year: Investment projects only.
* All indicators are for projects active in the Portfolio, with the exception of Disbursement Ratio, which includes all active projects as well as projects which exited during the fiscal year.

Annex 5: Summary of Non-Lending Services

Product	*Completion FY*	*Audience* [a]	*Objective* [b]
Recent completions			
Country Economic Memorandum	2010	G,B,PD,D	KG, PD, PS
Public Expenditure Review	2011	G,B,PD,D	KG, PD, PS
Public Works	2011	G,B,D	KG, PS
Comprehensive Water Sector Assessment	2011	G,B,D	KG, PS
Migration and Economic Development	2011	G,B,D	KG, PS
Underway			
Country Fiduciary Assessment Report	2012	G,B,D	KG, PS
Environmental Analysis	2012	G,B,D	KG, PS
Planned			
Transport Sector TA	2013	G,B,D	KG, PS
Financial Sector Assesment	2012-2013	G,B,D	KG, PS
Road Maintenance	2012-2014	G,B,D	KG, PS

a. Government, donor, Bank, public dissemination.
b. Knowledge generation, public debate, problem-solving.

Annex 6: Social Indicators

	Latest single year			Same region/income group	
	1980-85	1990-95	2003-09	Europe & Central Asia	Lower-middle-income
POPULATION					
Total population, mid-year (millions)	1.7	2.0	1.8	404.2	3,810.8
Growth rate (% annual average for period)	2.0	1.7	0.5	0.2	1.2
Urban population (% of population)	..	..	..	64.0	40.9
Total fertility rate (births per woman)	4.6	2.7	2.3	1.8	2.5
POVERTY					
(% of population)					
National headcount index	..	..	45.0	..	..
Urban headcount index	..	..	37.4	..	..
Rural headcount index	..	..	49.2	..	..
INCOME					
GNI per capita (US$)	..	..	3,240	6,793	2,321
Consumer price index (2000=100)	..	..	112	141	130
Food price index (2000=100)	..	..	..	..	..
INCOME/CONSUMPTION DISTRIBUTION					
Gini index	..	..	..	..	..
Lowest quintile (% of income or consumption)	..	..	..	..	..
Highest quintile (% of income or consumption)	..	..	..	..	..
SOCIAL INDICATORS					
Public expenditure					
Health (% of GDP)	..	..	2.5	3.9	2.1
Education (% of GDP)	..	..	3.7	4.1	4.1
Net primary school enrollment rate					
(% of age group)					
Total	..	..	97	92	87
Male	..	..	97	93	88
Female	..	..	96	92	86
Access to an improved water source					
(% of population)					
Total	..	..	..	95	86
Urban	..	..	..	98	94
Rural	..	..	..	89	81
Immunization rate					
(% of children ages 12-23 months)			98.0		
Measles	..	..	95	96	79
DPT	..	..	97	95	79
Child malnutrition (% under 5 years)	..	..	..	..	24
Life expectancy at birth					
(years)					
Total	67	69	70	70	68
Male	65	67	68	66	66
Female	69	71	72	75	70
Mortality					
Infant (per 1,000 live births) (2004-09)	..	..	35	19	43
Under 5 (per 1,000)	..	..	..	21	57
Adult (15-59)					
Male (per 1,000 population)		..	..	286	201
Female (per 1,000 population)	..	..	..	123	136
Maternal (modeled, per 100,000 live births)	..	..	..	32	230
Births attended by skilled health staff (%)	..	..	98	97	66

Note: 0 or 0.0 means zero or less than half the unit shown. Net enrollment rate: break in series between 1997 and 1998 due to change from ISCED76 to ISCED97. Immunization: refers to children ages 12-23 months who received vaccinations before one year of age or at any time before the survey.

World Development Indicators database, World Bank - 15 April 2011.

Annex 7: Key Economic Indicators

Indicator	Actual			Estimate		Projected		
	2007	2008	2009	2010	2011	2012	2013	2014
National accounts (as % of GDP)								
Gross domestic product[a]	100	100	100	100	100	100	100	100
Agriculture	12	12	12	12	12	13	13	14
Industry	20	20	20	20	20	20	19	20
Services	68	68	68	68	68	68	68	66
Total Consumption	113	113	111	108	101	98	95	94
Gross domestic fixed investment	26	29	27	30	31	31	32	31
Government investment	4	8	10	12	13	13	14	15
Private investment	22	20	17	18	19	18	18	16
Exports (GNFS)[b]	15	14	15	19	20	21	21	22
Imports (GNFS)	54	56	54	60	61	59	57	56
Gross domestic savings	-13	-13	-11	-8	-1	2	5	6
Gross national savings[c]	17	13	13	15	20	21	23	24
Memorandum items								
Gross domestic product (US$ million at current prices)	4661	5668	5449	5594	6453	6300	6709	7034
GNI per capita (US$, Atlas method)	..	3070	3280	3410	3530	3660	3870	3930
Real annual growth rates (%, calculated from .. prices)								
Gross domestic product at market prices	6.3	6.9	2.9	3.9	5.0	4.0	4.1	3.2
Gross Domestic Income	..	..	..	..	..	..	..	..
Real annual per capita growth rates (%, calculated from .. prices)								
Gross domestic product at market prices	5.4	6.0	2.1	3.1	4.2	3.1	3.0	2.2
Total consumption	..	..	..	..	..	..	..	..
Private consumption	..	..	..	..	..	..	..	..
Balance of Payments (US$ millions)								
Exports (GNFS)[b]	690	817	838	1036	1294	1295	1397	1514
Merchandise FOB	226	292	240	405	448	455	501	559
Imports (GNFS)[b]	2510	3195	2929	3366	3942	3689	3842	3917
Merchandise FOB	2118	2776	2516	2822	3355	3133	3279	3362
Resource balance	-1820	-2378	-2091	-2330	-2648	-2394	-2445	-2403
Net current transfers	1105	1221	1206	1179	1167	1088	1049	1094
Current account balance	-415	-924	-770	-1032	-1312	-1154	-1229	-1130
Net private foreign direct investment	591	503	386	475	516	542	806	511
Long-term loans (net)	0	0	0	0	0	0	0	0
Official	..	..	..	..	..	..	..	..
Private	..	..	..	..	..	..	..	..
Other capital (net, incl. errors & omissions)	222	455	253	618	..	..	..	..
Change in reserves[d]	-397	-34	131	-62	..	..	..	..
Memorandum items								
Resource balance (% of GDP)	-39.0	-41.9	-38.4	-41.7	-41.0	-38.0	-36.4	..
Real annual growth rates (.. prices)								
Merchandise exports (FOB)	..	..	..	..	..	..	..	..
Primary	..	..	..	..	..	..	..	..
Manufactures	..	..	..	..	..	..	..	..
Merchandise imports (CIF)	..	..	..	..	..	..	..	..

Continued

Indicator	Actual			Estimate		Projected		
	2007	2008	2009	2010	2011	2012	2013	2014
Public finance (as % of GDP at market prices)[e]								
Current revenues	26.4	24.4	29.3	27.6	28.1	28.2	27.1	27.8
Current expenditures	14.9	15.5	16.2	16.5	17.9	18.4	18.5	18.7
Current account surplus (+) or deficit (-)	11.5	9.0	13.1	10.6	10.2	9.7	8.5	9.1
Capital expenditure	2.8	7.4	10.8	12.2	11.9	12.0	11.7	10.7
Foreign financing	..	..	..	..	..	..	..	..
Monetary indicators								
M2/GDP	34.7	38.1	42.1	41.7	41.0	43.7	46.4	..
Growth of M2 (%)	23.8	24.4	12.2	6.7	8.2	13.0	13.0	..
Private sector credit growth /	40.1	32.7	8.9	12.6	15.0	9.4	9.3	..
total credit growth (%)	40.1	32.7	8.9	12.6	15.0	9.4	9.3	
Price indices(.. =100)								
Merchandise export price index	..	..	..	..	..	..	..	..
Merchandise import price index	92.1	100.0	95.2	100.9	110.0	..	..	..
Merchandise terms of trade index	..	..	..	..	..	..	..	..
Real exchange rate (US$/LCU)[f]	..	..	..	..	..	..	..	..
Real interest rates								
Consumer price index (% change)	4.4	9.4	-2.4	3.5	7.3	1.6	0.7	0.7
GDP deflator (% change)	6.2	-1.3	3.7	5.8	5.1	2.7	2.0	2.0

a. GDP at factor cost

b. "GNFS" denotes "goods and nonfactor services."

c. Includes net unrequited transfers excluding official capital grants.

d. Includes use of IMF resources.

e. Consolidated central government.

f. "LCU" denotes "local currency units." An increase in US$/LCU denotes appreciation.

Annex 8: Key Exposure Indicators

Indicator	2008	2009	2010	Estimated 2011	2012	Projected 2013	2014
Total debt outstanding and disbursed (TDO) (US$m)[a]	0	364	382	400	490	491	520
Net disbursements (US$m)[a]	..	-234	46	36	187	46	38
Total debt service (TDS) (US$m)[a]	..	259	19	21	28	29	28
Debt and debt service indicators (%)							
TDO/XGS[b]	0.0	21.9	20.7	17.9	22.5	21.3	19.1
TDO/GDP	0.0	6.7	6.8	6.6	8.0	9.7	11.0
TDS/XGS	..	..	..	..	..	..	..
Concessional/TDO	..	0.0	7.7	14.8	42.8	46.0	46.1
IBRD exposure indicators (%)							
IBRD DS/public DS	..	..	..	..	..	..	..
Preferred creditor DS/public DS (%)[c]	..	..	..	..	..	..	..
IBRD DS/XGS	0.0	11.3	1.4	1.2	1.2	1.1	1.0
IBRD TDO (US$m)[d]	0	346	331	315	300	286	271
Of which present value of guarantees (US$m)	0	0	0	0	0	0	0
Share of IBRD portfolio (%)	0	0	0	0	0	0	0
IDA TDO (US$m)[d]	0	0	0	12	17	25	33
IFC (US$m)							
Loans	0.0	0.0	8.4	11.3	5.0	5.0	5.0
Equity and quasi-equity /c	0	0	0	0	0	0	0
MIGA							
MIGA guarantees (US$m)	0	0	0	0	0	..	..

a. Includes public and publicly guaranteed debt, private nonguaranteed, use of IMF credits and net short-term capital.

b. "XGS" denotes exports of goods and services, including workers' remittances.

c. Preferred creditors are defined as IBRD, IDA, the regional multilateral development banks, the IMF, and the Bank for International Settlements.

d. Includes present value of guarantees.

e. Includes equity and quasi-equity types of both loan and equity instruments.

Annex 9: IDA Program Summary

(in US million)

Fiscal year	*Proj ID*	*US$(M)*	*Strategic Rewards b (H/M/L)*	*Implementation b Risks (H/M/L)*
2012	SEDPO2	47.0	H	M
	Result	***47.0***		
2013	AF for Energy Sector Clean up and Land Reclam	3.2**	H	M
	Energy Efficiency and Renewable Energy	32.5		
	Result	***35.7***	H	M
2014	Education Improvement Project	10.0	H	M
	PRG for KRPP and Kosovo B	14.5 (58)*		
	Result	***24.5***		
2015	Water Supply	18.0	H	M
	Result	***18.0***		
Overall Result		**78.2**		

*Only 25 percent of total PRG amount is counted. Preparation of PRG is subject to the findings of an external expert panel that is currently reviewing the proposed project to ensure that it complies fully with Bank policies regarding investments in fossil-fuel fired power generation plants. The panel is expected to complete and disseminate by December 2011

**includes US$2.2m re-allocated from cancelled LPTAP funds.

Annex 10: IFC Investment Operations Program

	2009	2010	2011	2012*
Original Commitments (US$m)				
IFC and Participants		6.45	8.25	0.33
IFC's Own Accounts only		6.45	8.25	0.33
Original Commitments by Sector (%)- IFC Accounts only				
FINANCE & INSURANCE			100	100
INDUSTRIAL & CONSUMER PRODUCTS		100		
Total	0	100	100	100
Original Commitments by Investment Instrument (%) - IFC Accounts only				
Guarantee				100
Loan		100		
Quasi loan			100	
Total	0	100	100	100

* Data as of January 01,2012

Annex 11: Operations Portfolio (IDA)

as of January 30, 2012

Closed Projects 21

IBRD/IDA *

Total Disbursed (Active)	17.10
of which has been repaid	0.00
Total Disbursed (Closed)	42.34
of which has been repaid	0.00
Total Disbursed (Active + Closed)	59.44
of which has been repaid	0.00
Total Undisbursed (Active)	60.81
Total Undisbursed (Closed)	2.28
Total Undisbursed (Active + Closed)	63.09

Active Projects

		Last PSR Supervision Rating			Original Amount in US$ Millions
Project ID	Project Name	Development Objectives	Implementation Progress	Fiscal Year	IDA
P112526	Agriculture and Rural Devpt	S	S	2011	20.15
P096181	CLEAN UP & LAND RECLAM	MS	MS	2006	10.5
P102174	Inst. Devt. for Education	MU	MS	2008	10
P101614	Public Sector Modernization	MS	MS	2010	8
P101214	REAL ESTATE CADASTRE	S	S	2010	12.25
P088045	XK Business Env TA	MS	MS	2005	7
P108080	XK Fin. Sect. Strengthen.&Market Infrast	MS	MS	2008	8.85
Overall Result					76.75

Annex 12: IFC Committed and Disbursed Outstanding Investment Portfolio

as of January 30, 2012

		Committed					Disbursed Outstanding				
FY Approval	**Company**	**Loan**	**Equity**	****Quasi Equity**	***GT/RM**	**Partici pant**	**Loan**	**Equity**	****Quasi Equity**	***GT/RM**	**Partici pant**
2010	Newko Balkan	6.73	0	0	0	0	6.73	0	0	0	0
2011	TEB Kosovo	0	0	8.41	0	0	0	0	8.41	0	0
Total Portfolio:		**6.73**	**0**	**8.41**	**0**	**0**	**6.73**	**0**	**8.41**	**0**	**0**

* Denotes Guarantee and Risk Management Products.

** Quasi Equity includes both loan and equity types.

KOSOVO

- *KOMUNA*/OPŠTINA CAPITALS*
- *RRETH*/OKRUG CAPITALS**
- NATIONAL CAPITAL
- RIVERS
- MAIN ROADS
- RAILROADS
- *KOMUNA*/OPŠTINA BOUNDARIES
- *RRETH*/OKRUG BOUNDARIES
- INTERNATIONAL BOUNDARIES

* *The first name is in Albanian and the second one is in Serbian.*

** *Names of the Rreth/Okrug are the same as their capitals.*