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January 23, 2023

**Statement by Mr. Jennings, Mr. O'Brolchain, and Mr. Day on Republic of Kosovo
(Preliminary)
Executive Board Meeting
January 25, 2023**

We thank staff for their comprehensive report and complementary Selected Issues Paper, and Mr. Palotai for his helpful Buff statement. While growth is projected to moderately pick up, and inflation to decline, spillover effects of Russia's invasion of Ukraine have resulted in high energy and food prices and contributed to a negative terms-of-trade shock, estimated at 5 percent of GDP. It has also meant a shift in policy focus to the short term. Uncertainty remains high, with risks to the downside for growth and to the upside for inflation. We therefore welcome in the Buff statement that the authorities have expressed interest in a precautionary Stand-By Arrangement. **We agree with the thrust of the report** and add the following remarks for emphasis.

We welcome that the 2023 budget appropriately envisages a return to the fiscal rule deficit ceiling. We note staff's view that the authorities appropriately cushioned the impact of the terms-of-trade shock on households and firms in 2022, though some measures, including transfers to workers and energy subsidies, could have been better targeted. We note the underspend in 2022 and agree with staff that increasing allocations for health, education and green energy remains essential. Faster public investment program (PIP) implementation could lead to stronger growth, but we note that challenges remain to increase absorption. We would encourage the authorities to continue implementing the 2018 IMF's Public Investment Management Assessment's (PIMA) recommendations. Large blanket allocations for contingencies, at 2.7 percent of GDP, should be further outlined and detailed. We positively note the authorities continued progress in strengthening tax administration and tackling informality.

While we note the resilience of the financial sector, we agree with staff that further monitoring and surveillance is warranted. In particular, strengthened housing sector surveillance is warranted, given the high levels of construction and real estate activities in

terms of FDI and GDP. We positively note staff's assessment that the Central Bank of Kosovo's (CBK) ability to provide liquidity has strengthened, its financial position has improved and that it has continued improving its policy toolkit. However, we agree with staff that continued implementation of the 2019 Financial Sector Stability Review (FSSR) and of the 2021 Safeguard Assessments (SA) recommendations remains essential and we welcome the authorities' commitment to continued implementation. We welcome staff's clear annexes on implementation status for past Article IV and FSSR recommendations, noting with concern limited or partial progress over a range of areas.

We note staff's view that the reform program needs to be revitalized, including strengthening coordination across all levels of government. We agree with staff that efforts to close governance gaps and further reduce corruption should continue, particularly in the areas of AML/CFT, the rule of law and tackling conflicts of interest in public procurement. We positively note that the authorities recognize the urgency of increasing green energy generation to boost energy security and decrease greenhouse gas emissions. A gradual implementation of carbon pricing would also promote a more efficient use of energy. This is particularly important given Kosovo's dependence on coal-based electricity generation, the drop in domestic energy production due to outdated capacities as outlined in the Buff statement, and that the EU's carbon border adjustment mechanism (CBAM) may limit Kosovo's attractiveness as an FDI destination. We welcome that the authorities are considering IMF Resilience and Sustainability Trust financing. We agree with staff that early withdrawals from Kosovo's Pension Savings Trust (KPST) should be avoided, noting staff's view that these would undermine the pension system, create contingent fiscal liabilities and compromise domestic financial market development. Finally, we note that nominal wage growth has lagged inflation, especially for females. *Can staff comment further on the potential reasons for the recent widening in the gender pay gap and any other labor market gaps?*