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GRAY/16/104

January 13, 2016

Statement by Mr. Meyer and Mr. Hillebrand on Republic of Kosovo
(Preliminary)
Executive Board Meeting
January 15, 2016

We thank staff for the insightful report and Mr. Canakci and Mr. Mehmedi for their helpful Buff statement. **We agree with the completion of the first program review and acknowledge Kosovo's overall strong program performance.** The missed prior action, however, is unfortunate. While we can nevertheless go along with the completion of the review based on staff's arguments as presented in the Supplement and assurances of considerable efforts by the authorities also alluded to in the Buff statement, *we would welcome if staff could be more precise on when they expect this issue to be resolved (before the next review?) and confirm that based on currently available information the transfer of tax obligation from the PAK is indeed not needed to meet fiscal targets for end-December.*

A firm commitment to the full implementation of the envisaged reform agenda is needed to maintain macroeconomic stability in the unilaterally euroized economy which puts a premium on prudent fiscal policies and meaningful measures to improve domestic productivity. Overall, and despite satisfactory progress, the program remains subject to considerable risks not least in the political domain. We thus invite the authorities to stay in close dialogue with the staff to deal with any possible delays or slippages that might jeopardize program objectives.

We appreciate that fiscal targets under the program have been achieved so far and welcome the authorities' commitment to fiscal consolidation. We encourage the authorities to go ahead with the implementation of the proposed measures in the amount of ½ percentage point of GDP to reach the deficit target for next year. These measures should include savings that can be achieved through adjustments to the ill-targeted pension scheme adopted in 2014. Going forward, unfunded spending initiatives should be avoided in the first place through a careful budget planning process that controls the fiscal deficit and creates room for high priority capital spending. Looking ahead, completing the privatization agenda will be of utmost importance to mobilize non-tax revenues and restore cash buffers of the government up to the recommended level.

To improve the business environment and move away from the current remittance- and consumption-driven growth model, reforms should focus on boosting competitiveness and spurring the private sector activity. While we take positive note of Kosovo's efforts to improve the business climate, we would welcome further efforts to redirect remittances to more productive sectors; a step that would in turn also help to diversify the production and export base.

Staff appropriately emphasizes that the new public wage rule, once it becomes effective, could prove a competitiveness-enhancing reform. By gradually narrowing the gap between public and private sector wages, it could foster a more efficient allocation of talents towards the corporate sector. However, the wage moderation process in the public sector should be monitored carefully with a view to ensure a build-up in institutional capacity and corruption prevention.

In general, previous steps taken and the envisaged way ahead to preserve and strengthen Kosovo's financial sector stability appear reasonable. The regulatory agenda of rolling out risk-based supervision, adoption of ELA regulation, implementing a macroprudential policy framework and strengthened contingency planning and crisis management capacities could provide the authorities with essential tools to deal with and contain systemic stress.

Further steps in the financial sector reform agenda should focus on structural impediments to the sector's proper intermediation process. In this regard, it is essential to improve the conditions enabling creditors to reliably enforce claims against debtors. Bearing in mind that the enforcement of claims and contracts – and subsequently access to credit of households and corporates – crucially depends on well-defined and properly documented property titles, we consider the absence of a dependable register of land rights warrants more analysis and *would appreciate additional staff comments on this topic*.