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July 27, 2015

**Statement by Mr. Beblawi and Mr. Faras on Republic of Kosovo
(Preliminary)
Executive Board Meeting
July 29, 2015**

Kosovo's program aims at supporting macrofinancial stability and increasing the country's growth prospects. We support the proposed decision, and highlight the following issues:

Fiscal Policy

A prudent fiscal adjustment is an essential component of the program. The sharp increase in current spending in the run-up to the 2014 elections threatened the credibility of the fiscal rule, and pushed the fiscal deficit to 3.9 percent of GDP in 2015. We welcome the measures already taken, along with those to be incorporated in the revised 2015 budget, to raise tax revenues and lower current spending which are aimed at reducing the deficit to 2.4 percent of GDP. We also look forward to the modification of the fiscal rule to accommodate higher capital spending without undermining debt sustainability. We welcome the inclusion of safeguards to limit the scope for pre-electoral excesses ahead of the 2018 elections, as noted by staff.

Financial Sector

We welcome the authorities' steps to enhance the regulatory and supervisory framework. The planned adoption of a new legal framework for Emergency Liquidity Assistance is particularly important for a euroized economy. The low credit penetration rate, despite ample liquidity, suggests that there is significant scope for the financial sector to support growth. This will be facilitated by improvements in the business environment and creating more investment opportunities. In this regard, we look forward to the work that staff intends to undertake in the coming months to assess the legal and structural impediments to credit provision and identify possible solutions.

Competitiveness and Structural Reforms

We note that the program includes a nominal wage freeze, to be followed by a public wage rule. We concur with staff that restoring Kosovo's competitiveness requires, among others,

deflating labor costs and linking the growth of public sector wages to well-defined macroeconomic indicators. *We would be grateful for staff elaboration on the criteria that will be used to lift the wage freeze, and whether future increases in wages will be contingent on the adoption of a wage rule.* Reforming the public procurement process, as planned under the program, would help to improve transparency and curb corruption. Implementing safeguards to enhance the efficiency of using public funds to upgrade infrastructure in areas of high priority is also encouraging. Nevertheless, restoring competitiveness may require structural reforms beyond the areas of public wages and procurement. *Does staff believe that the measures listed in the report are sufficient to restore competitiveness and, if not, what else should be considered?*

With these remarks, we wish the authorities success in implementing their economic and reform program.