Facility for Approximation with the EU Acquis

Further support to the development of trade in Kosovo

Project Identification No.
EuropeAid/138565/DH/SER/XK
Service Contract No. 2018/395-320

KOSOVO'S CHALLENGES AND PRIORITIES IN INTERNATIONAL TRADE

December, 2019

European Union 4 Kosovo

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Kosovo

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Report
Act. no. 2.3.3 - Kosovo's Challenges and Priorities in International Trade

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Abbreviations

AmCham	American Chamber of Commerce
BMO	Business Membership Organisation
CEFTA	Central European Free Trade Agreement
CN	Combined Nomenclature
EFTA	European Free Trade Association
EBRD	European Bank for Reconstruction and Development
EIU	Economist Intelligence Unit
EU	European Union
ERO	Energy Regulatory Office
FTA	Free Trade Agreement
GSP	Generalized System of Preferences
KCC	Kosovo Chamber of Commerce
KCGF	Kosovo Credit Guarantee Fund
KEDS	Kosovo Energy Distribution Services
KAA	Kosovo Accreditation Agency
KMA	Kosovo Metrology Agency
KSA	Kosovo Standardisation Agency
KTA	Kosovo Tax Administration
IPA	Industrial Property Agency
JDC	Joint Declaration on Cooperation
MAFRD	Ministry of Agriculture, Forestry and Rural Development
MFN	Most Favoured Nation
MoF	Ministry of Finance
MTI	Ministry of Trade and Industry
NGO	Non-Governmental Organisation
NTFC	National Trade Facilitation Committee
NCED	National Council for Economic Development
ROW	Rest of the World
SAA	Stabilisation and Association Agreement
SPS	Sanitary and Phytosanitary Measures
SEZ	Special Economic Zone
TBT	Technical Barriers to Trade
VAT	Value Added Tax
VET	Vocational Schools
WB	World Bank
WTO	World Trade Organization

1. Introduction

Trade deficit in goods constitutes one of Kosovo's most challenging economic issues. In 2018, imports amounted to EUR 3.3 billion, while exports stood at just over EUR 360 million,[1] marking the largest trade deficit in absolute terms since the end of the war. This alarming level of import dependence (in goods) has been persisting for a long time. Indeed, the gap has been widening continuously. If Kosovo follows the pattern of the last ten years (a 'business as usual' scenario), the trade deficit will keep on growing for the next 25 years, reaching very high levels and therefore seriously threatening the stability of the whole economy.[2] Whereas Kosovo imports pretty much everything from raw material to finished products, the export base, on the other hand, is rather undiversified and fragile, with base metals and minerals comprising more than 70 percent of total goods exports in 2018.[3] The underdeveloped industrial base with limited value addition explains, to a great extent, Kosovo's dismal trade performance in goods.

Contrary to the case of trade in goods, Kosovo is faring better in regard to trade in services, noting a surplus of around EUR 0.78 billion in 2018.[4] This surplus, coupled with remittances from Kosovo's diaspora, which are estimated to be around EUR 745 million in 2018,[5] have largely contributed to offset the sustained trade deficit in goods. Although at first glance the general figures on services trade look very promising, a detailed analysis unveils that the composition of exports in this sector is not well diversified. Travel, which is mostly driven by Kosovo's diaspora, makes up the lion's share of services exports with around 82 percent.[6] An export structure with diaspora tourism being the main driver is hardly sustainable, mainly because diaspora ties with the motherland are likely to wear off as generations change, resulting in less visits and less remittances. One additional concern is that the services sector is generally dominated by low productivity activities.

A cross-country assessment with CEFTA countries conducted by the Economist Intelligence Unit (EIU) reveals that Kosovo utilizes only 37.9 percent of its export potential in goods and services based on the main drivers of trade potential: that is, Kosovo's level of development, its size and distance with key markets.[7] In this respect, Kosovo is the worst performer among the Western Balkan countries and far away from the EU 11 where actual exports are only 2 percentage points short of the estimated potential. A World Bank study, which also relies on the fundamental determinants of predicting exports, shows that Kosovo can increase its goods exports by 80 percent from its current base, suggesting that it performs well below its estimated potential. This overall picture depicts that prospects for developing a strong export sector remain rather dim if Kosovo follows the path it has been following thus far.

[1] Kosovo Customs (2019). Trade Data. *[Database]*
[2] The EU Trade Project – MTI (2018). Factors Affecting Trade in Kosovo: A Gravity Model Approach
[3] Kosovo Customs (2019). Trade Data. *[Database]*
[4] CBK (2019). External Sector Statistics. Services. *[Database]*
[5] CBK (2019). External Sector Statistics. Remittances inflows. *[Database]*
[6] CBK (2019). External Sector Statistics. Services. *[Database]*
[7] EIU (2018). Western Balkans to 2025 A brighter future or permanent marginalization.

Given this context, the Ministry of Trade and Industry (MTI) has committed itself to drafting a national trade policy that articulates the government's aspiration towards trade development. The MTI is cognizant of the poor and deteriorating trend in the trade sector and as such seeks to propose concrete and comprehensive solutions in line with Kosovo's development objectives. This new document will build on the existing trade policy, which was commissioned in 2009. A good trade policy is a precondition for a better and inclusive trade performance, which is critical to creating new jobs, tackling poverty and improving the overall economic wellbeing of Kosovo citizens.

To support the MTI in formulating the most appropriate trade policy, a consolidated assessment and consideration of the key trade and trade-related challenges of the private sector along with the main priorities in the area has been performed. The findings and recommendations from this document are expected to serve as initial inputs for the further elaboration of the trade policy and other related policy documents. This undertaking is drafted as part of the project, "Further support to the development of trade in Kosovo", which is funded by the European Union (EU), managed by the EU Office in Kosovo, and implemented by GFA Consulting Group, the Danish Patent and Trademark Office, the European Institute for Public Policy and WTI Advisors.

In order to obtain relevant information on the topic, the following two data-collection instruments have been used. First, a thorough review of relevant trade and trade-related studies and strategic documents was conducted. Second, open semi-structured interviews with business membership organisations (BMOs),[8] both general and sectoral, have been carried out. This actually constitutes the main data collection instrument of this report. A list of all the interviewed BMOs and the guide used for interviews are included in Annex A and Annex. In the meantime, a draft report was also circulated for comments.

The findings presented in this report combine an aggregate overview of opinions from BMOs with information obtained from desk research. While defining the challenges of the private sector, no subjective opinion has been incorporated besides the information collected in the interviews. Some of the opinions provided would certainly need further validation grounded on more detailed evidence, if available. It should be noted that, in some instances, BMOs were not able to comment in detail on all the questions included in the interview guide. Overall, this report is not intended to be exhaustive. Further work is needed to identify additional challenges and to further analyse the current ones.

The rest of this report is organised as follows. *Section 2* provides an overview of the private sector involvement in policy making concerning trade, mainly focusing on the knowledge of the private sector with regard to decision-making and the institutional setting for trade policy formulation; current inclusion of the private sector in drafting new legislation and strategic documents; and level of effectiveness of the consultation process. *Section 3* summarizes Kosovo's current trade arrangements and points to key trade challenges concerning trade liberalisation and market access. *Section 4* lists and elaborates supply side constraints. *Section 5* briefly highlights some challenges in trade in services. *Section 6* touches upon some key institutional constraints. *Sector 7* concludes and highlights the main recommendations.

[8] *Note:* In addition to BMOs, two economic think tanks have been interviewed.

2. Public-Private Sector Dialogue in Relation to Trade

Engaging in public–private sector dialogue is one of the best ways for a government to learn more about the concerns of the private sector. A policy that undergoes a collective process ensures that policymakers do not have monopoly on perspective, knowledge and wisdom. In order to create a level playing field for businesses, policymakers need to have a better understanding on the potential effects of their actions. The involvement of the private sector in policy making is also critical to improving transparency, accountability and good governance in general, thereby consolidating institutional legitimacy and performance.

Moreover, a proper dialogue and consultation process is crucial, since it:

- Facilitates the identification of problems and contribute to effective solutions;
- Helps determine the best alternative in terms of applicability when different alternatives are proposed by public-policy makers;
- Leads policymakers to new ideas, as well as feeds them with a wide spectrum of effective options/solutions;
- Serves as a low-cost source of data;
- Helps public authorities to find the most appropriate means for implementing a decision/policy; and
- Helps public authorities to highlight potential consequences of potential decisions at very early stages.

2.1 Kosovo's Legal Framework on Stakeholder Involvement in Policy Making

Kosovo's regulatory framework is relatively advanced in regard to involving stakeholders in the process of policy making. In addition to legal and sub-legal acts which regulate this matter, there are also guidelines that show how concept documents should be developed.[9] Key legislative documents along with relevant regulatory provisions are summarized below.

Regulation of Rules and Procedure of the Government of Kosovo.[10] This document contains three feature elements that regulate the involvement of the public in policy making. *Article 32* obliges the originating body to publish the substance of its proposal to seek comments from the public. It also specifies that the originating body should give sufficient time and digestible information to the public to understand the nature and consequences of the proposal. In addition, this article stipulates that the consultation results should be reported to the Government meeting or Ministerial Committee as part of the concept document or explanatory memorandum. Moreover, *Article 39* states that the proposing body is responsible for conducting public consultations. Finally, *Article 69* obliges the

[9] Office of the Prime Minister (2018). Guidelines and Manual for Developing Concept Documents.
[10] Government of Kosovo (2011) http://www.kryeministri-ks.net/repository/docs/Rregullore_e_punes_se_Qeverise_09.2011_(anglisht).pdf

Government to cooperate with the Chamber of Commerce and other chambers, associations, professional associations, NGOs, unions and communities by taking their opinion into consideration.

Regulation on Government Legal Service.[11] This regulation entails three provisions associated with public involvement in drafting legal documents. *Article 8* obliges the government to incorporate public consultations in the legislative cycle. *Article 10*, amongst others, stipulates that the consultation process should take place before and during the formulation of legal documents. The text of this article, however, is rather vague in regards to defining the methods of the consultation process. It is left to the discretion of the originating body to decide on the most effective way of stakeholder involvement. *Article 12* specifies that following preliminary consultation and eventual incorporation of comments, the proposing body shall publish on the website the content of the draft normative act for public comments and specifically to seek comments by the interest groups that are affected by the proposal.

Administrative Instruction on the procedures, criteria and methodology for the preparation and approval of strategy documents and plans for their implementation.[12] This document contains one relevant article linked to the consultation process, namely *Article 8*. According to this article, both formal and informal consultations should be used to obtain the views of the stakeholders within or outside the government, particularly putting an emphasis on experts of the respective field.

Regulation on minimum standards for public consultation process.[13] This is the most detailed and comprehensive regulation on the public consultation process. The document aims to promote and ensure a public consultation process between public authorities, interested parties and the public, for an inclusive participation process of policy making and decision making of public interest. This *Regulation* defines the minimum standards, principles and procedures of the public consultation process between public authorities, interested parties and the public in the process of drafting the policy and legislation.

2.2 Kosovo's Institutional Mechanisms for Public Private Dialogue

There are currently two main long-term operational institutional mechanisms (including respective working groups) under the MTI responsible for the coordination of government institutions and the private sector on trade or issues related to trade. In addition, there are working groups, which can be established for drafting new legislation and policies, as well as for other ad-hoc issues.

National Council for Economic Development (NCED). Established in 2015, the NCED is a platform within the MTI responsible for coordinating activities of state institutions in order to eradicate

[11] Government of Kosovo (2013). http://www.kryeministri-ks.net/repository/docs/Rregullore_Nr132013_per_sherbimin_ligjor_qeveritar.pdf

[12] Government of Kosovo (2012). http://www.kryeministri-ks.net/repository/docs/Draft_Udhezimi_Administrativ_Per_Strategjite_FINAL_2012__2_.pdf

[13] Office of the Prime Minister (2016). https://konsultimet.rks-gov.net/Storage/Docs/Doc-58b819f98ec60.pdf

obstacles and address the challenges faced by the private sector and investors in Kosovo. The NCED assembles the most important representatives of the private sector (mainly business associations), relevant government ministries and state agencies. The NCED can also establish working groups focused on defined priorities with representatives of the government/ministries, private sector, business associations, civil society and other relevant experts. With the decision issued in 2015, the NECD established four working groups:

- Working group on legislative matters and handling investors complaints towards institutions;
- Working group on trade issues and addressing trade barriers;
- Working group on improving the doing business climate, public investments and quality infrastructure investments; and
- Working group for attracting and facilitating diaspora investments in Kosovo.

To enhance the NCED's effectiveness and strengthen its impact, the European Bank for Reconstruction and Development (EBRD) in the end of 2018 decided to provide a professional secretariat. The specific role of this body is to provide robust analytical underpinnings to the council's work as well as to monitor the implementation of the council's conclusions and recommendations. The whole team foreseen for this secretariat has been assembled only recently. Despite this, according to the head of the secretariat, they have managed to conduct several individual meetings with private sector stakeholders; organise two round tables; and gather the working group on trade issues.[14]

National Trade Facilitation Committee (NTFC). Established in 2016, the NTFC is a body under the MTI responsible for coordinating activities during the negotiation and implementation of the Agreement on Trade Facilitation on the national and regional level. In particular, this body seeks to deal with issues related to the simplification and harmonization of procedures among CEFTA members. This committee consists of representatives from the MTI, Kosovo Customs, and other state institutions. The business community is represented by the Kosovo Chamber of Commerce (KCC) and American Chamber of Commerce (AmCham). Under this committee, there are three sub-working groups (see below) that are created as consultative mechanisms for including stakeholders from the private sector in the formulation of trade policy in Kosovo.

- Sub-working group on agriculture;
- Sub-working group on industry; and
- Sub-working group on services.

2.3 Main Public-Private Dialogue Challenges

BMOs generally share the view that compared to, say, five years ago, the public-private dialogue in areas related to trade has marked a considerable improvement. Besides being represented in at least one of the aforementioned consultation mechanisms, the MTI, Trade Department in particular, unlike in other neighbouring countries, has been willing and open to hosting BMOs or businesses directly to discuss and address (where possible) trade issues. Nonetheless, there are still some challenges that

[14] Daija, L. (2019). [Email]. Message to: Nixha, A. 11 Dec. 2019

hinder the proper involvement of the private sector in policy making and the overall effectiveness of the public-private sector dialogue.

a) Limited effectiveness of NCED

BMOs that are members of the NCED are not very much satisfied with the dynamics of this council. For more than two years, this council was gathered only twice and, what is worse, those meetings, according to BMOs, have not produced any tangible results. The majority of BMOs see NCED as largely ineffective in addressing challenges faced by businesses. As indicated previously, the NCED has four working groups, which are designated to serve as platforms for dialogue at technical level. Although the NCED's 2015 decision stipulates that these working groups shall meet at least every two months,[15] this has not been the case. In 2019, for instance, the working group on trade issues has had only one meeting, while the other working groups none. It is worth noting that the absence of meetings in the second part of 2019 is linked with the fact the country has been with a caretaker government. BMOs, especially the sectoral ones, are very interested in having regular meetings on a technical level.

b) Involvement of BMOs and other stakeholders only at final stages of policy making

Some BMOs complain that the MTI involves them at some later stages of the policy making process. The most common practice, they say, is to engage with the private sector only after a decent draft of the document is produced. Given that with the initial draft the general structure of the document is already in place, the private sector remains with very limited space to provide substantial contribution other than "validating" the content of the draft. One BMO representative claimed that even when they make comments only the superficial ones are taken into consideration, while the rest are generally disregarded without explanation.

c) Technical language of documents for public consultation

Some BMOs, especially the smaller ones, share the view that MTI documents subject to public consultation are usually disseminated to BMOs and other stakeholders in a technical format, often overloaded with legal terminology. This makes it hard for non-technical stakeholders to unambiguously understand these documents; as a result, it affects their participation and the quality of input. Note that the *Regulation on minimum standards for public consultation processes* specifies that institutions are obliged to provide all the necessary information in a comprehensible form so that the public and interested parties understand the content and the expected impact of the draft proposal.[16]

[15] NCED (2015). Decision. https://mti.rks-gov.net/desk/inc/media/CE8ED083-0716-4086-A99A-DF849E696ECF.docx

[16] Office of the Prime Minister (2016). https://konsultimet.rks-gov.net/Storage/Docs/Doc-58b819f98ec60.pdf

d) Lack of cooperation between NECD and NTFC including sub-working groups

Some BMOs claim that there is limited cooperation between the NECD and NTFC including sub-working groups. This, on some occasions, has produced overlapping in the work done. One likely cause is attributed to the fact that the competences of these bodies are not very clearly defined.

e) Misalignment of interests between traditional BMOs and new BMOs

A number of new BMOs with a very specific membership base have emerged over the past years in Kosovo. They represent very specific interests, which at times diverge from the interests of the overall private sector in Kosovo. As a result, these new BMOs quite often end up in rivalry positions with traditional BMOs. Although new BMOs have been generally more dynamic in comparison to the traditional ones, they have been too small to be considered as representatives of a majority of businesses and therefore have remained to a great extent underrepresented. This has created the need for some coalition building to align interests and improve the bargaining power of underrepresented categories of businesses.

f) Lack of trust in institutions

Some BMOs indicate that in the past, the private sector community was more willing to participate in policy initiatives. However, their requests seem to have fallen on deaf ears. This has caused some disappointment among the business community, which is also reflected in low trust in institutions. In the recent years, according to a BMO, the situation has been reversed: the MTI is more open to the private sector, but the latter is not very much willing to participate.

3. Trade Liberalisation and Market Access

Kosovo is characterized by a fairly open trade regime. Preferential trade arrangements that shape Kosovo's international trade policy include the Stabilisation and Association Agreement (SAA), the Central European Free Trade Area (CEFTA), and Kosovo-Turkey Free Trade Agreement. Recently, a "continuity" trade agreement has been signed with the UK, which is expected to come into effect when the EU-Kosovo Agreement ceases to apply to the UK. Also, some initial steps have been undertaken to have an FTA with EFTA states. In addition to these, Kosovo benefits from Generalized System of Preferences (GSP) schemes with the US, Norway, Switzerland and Japan. Under these schemes, the aforementioned countries offer one-sided preferential treatment (better than MFN) to products originating in Kosovo. In the following two sub-sections, the main (potential) preferential agreements and key challenges on liberalisation and market access are discussed and elaborated.

3.1 An Overview of Preferential Trade Agreements

The Stabilisation and Association Agreement (SAA)[17]

Following a series of negotiations that took place during 2013 and 2014, Kosovo and the EU signed the SAA on October 22, 2015, in Strasbourg. This agreement was subsequently adopted by the Government of Kosovo and entered into force on April 1, 2016. Through this agreement, Kosovo and the EU established a bilateral free trade area supporting the free movement of goods, services and capital. The SAA allows greater and guaranteed access to the European market consisting of around 500 million customers, as well as technical expertise and financial support in enabling the improvement of quality, safety and standards of products originating in Kosovo. In addition, the Agreement regulates and facilitates a range of issues, such as: political dialogue; regional cooperation; approximation to EU law; cooperation on security and justice; and financial assistance instruments.

As far as tariff concessions are concerned, the SAA is considered rather asymmetric in favour of Kosovo. On the one hand, all Kosovo products have been immediately exempted from customs charges or equivalent measures, except baby beef, sugar, and wine, and some other products, which are still subject to quantitative restrictions. On the other hand, Kosovo committed to applying successive tariff reductions to a number of products (especially agricultural ones) for a period between five to 10 years. A small number of products (14), notably milk, potatoes, wine and some others, are subject to a fixed duty of 10 percent and are not subject to future tariff reductions.

In 2018, the EU was the most important trade partner for Kosovo, accounting for 42.2 percent of Kosovo's total trade (sum of exports and imports). Exports to the EU amounted to around EUR 111 million, accounting for 30.2 percent of total exports; while imports stood at EUR 1.45 billion, making

[17] Stabilisation and Association Agreement (2015). https://ec.europa.eu/neighbourhoodenlargement/sites/near/files/news_corner/news/news-files/20150430_saa.pdf

up 43.5 percent of total imports. This resulted in a coverage ratio (exports/imports) of only 7.6 percent. Historically considered (2008-2018), Kosovo's goods exports to the EU have been almost stagnant, with an average annual growth rate of only 1.4 percent. Imports from the EU, on the other hand, grew at an average annual growth rate of 6.2 percent. As a result, Kosovo's trade deficit with the EU has grown in a sustained manner. This suggests that Kosovo still has not been able to reap all the potential benefits of the Agreement with the EU.[18] Compared to ten years ago, the EU contribution in Kosovo's total exports has dropped by 10.5 percentage points, from 40.7 percent in 2008 to 30.2 percent in 2018.

The Central European Free Trade Area (CEFTA)[19]

In 2006, UNMIK on behalf of Kosovo signed the Central European Free Trade Agreement (CEFTA), which came into effect between July and November 2007. CEFTA is a modern and ambitious free trade agreement with six members from the South Eastern Europe (SEE). At the time when CEFTA was formed, the main objective was to consolidate the matrix of existing bilateral free trade agreements between countries in the region into a single regional agreement. CEFTA now seeks to further expand trade in goods and services in the region, eliminate trade barriers and distortions, offer fair conditions for competition, attract investments and promote diagonal cumulation of origin. Overall, regional cooperation is seen an essential aspect towards economic development and EU integration.

Under CEFTA, UNIMK on behalf of Kosovo, unlike other members which initially and for a limited period of time maintained some level of protection for some strategic products, committed to eradicating all tariff charges or other quantitative measures for products originating in CEFTA, thereby offering full market access. Even agricultural products, which are often protected (at least for some period) in many trade agreements worldwide, have been granted full duty-free treatment.

As a CEFTA member, Kosovo is exposed to a market representing approximately 28 million consumers. Trade data reveal that CEFTA is Kosovo's second biggest trade partner after the EU, participating with around 28 percent in 2018. Kosovo's exports to CEFTA in this year reached a value of EUR 173.5 million, comprising 47.2 percent of its total exports; while imports amounted to EUR 853.5 million, accounting for 25.5 percent of all imports. Although Kosovo's trade deficit with CEFTA is still high, exports to this region have seen a higher average annual growth (10 percent) than imports (2.2 percent) in the past ten years. This has led to an improved export coverage ratio from 9.1 percent in 2008 to 20.3 percent in 2018.[20]

[18] Kosovo Customs (2019). External Trade. *[Database]*
[19] CEFTA (2006). https://cefta.int/legal-documents/#1463498231136-8f9d234f-15f9
[20] Kosovo Customs (2019). External Trade. *[Database]*

Free Trade Agreement with Turkey[21]

In September 2013, Kosovo signed a Free Trade Agreement (FTA) with Turkey. This agreement, however, did not come into force until September 2019. The objective of this agreement is to enhance trade and overall economic cooperation between Kosovo and Turkey; gradually eradicate restrictions on trade in goods; promote reciprocal trade; remove barriers to trade; and create conditions for investments.

This Agreement grants to Kosovo's exporters duty-free access to the Turkish market for 8,336 industrial products. In return, Kosovo agreed to immediately remove customs tariffs on 2,292 industrial products, which at the time of negotiations were not produced in Kosovo. Tariffs for other industrial products are to be progressively dismantled within a timeframe of 10 years. As per agricultural products, Kosovo's exporters will have duty-free access for 2,442 products. This does not apply to meat products. In return, Kosovo committed to immediately removing the customs duties on 493 agricultural imports from Turkey. Some 52 other agricultural products, which are considered to be strategic for Kosovo, such as dairy products, fruits and vegetables, flour products, water and beer will be protected for 10 years. According to the Agreement, the average nominal tariff rate for Turkey, including both agricultural and industrial products, is expected to drop from 8.0 to 1.7 in the next ten years.

Trade data reveal that Turkey is one of the most important individual trade partners, comprising 9.2 percent of Kosovo's total trade in 2018. Kosovo's exports to Turkey in this year amounted to EUR 8.3 million, constituting only 2.3 percent of total exports; while imports amounted to EUR 853.5 million, accounting for 25.5 percent of all imports. As these figures indicate, the trade deficit with Turkey is tremendously high, with exports covering only 2.5 percent of imports. While exports to Turkey fluctuated in the last ten years with annual values not exceeding EUR 12 million, imports from Turkey increased at an average rate of 10.6 percent.[22]

Free Trade Agreement with the United Kingdom[23]

The UK has started negotiating and signing "continuity" trade deals with a number of trading partners with whom the EU has free trade agreements, mainly with the objective of maintaining the reciprocal trade preferences after the UK is no longer bound by the EU's FTAs. In December 2019, Kosovo signed an agreement of this type with the UK. Under the new agreement, both parties agree to preserve the preferential conditions concerning trade which resulted from the EU-Kosovo Agreement (the SAA), as well as to provide a platform for further trade liberalisation of goods and services. This agreement will enter into force the day on which the EU-Kosovo Agreement ceases to apply to the UK.

[21] FTA Kosovo and Turkey (2013). Available at MTI.
[22] Kosovo Customs (2019). External Trade. *[Database]*
[23] FTA between UK and Kosovo (2019). Available at MTI.

Potential Free Trade Agreement with the European Free Trade Association (EFTA)[24]

In November 2018, Kosovo and European Free Trade Association (EFTA) states, notably Iceland, Liechtenstein, Norway and Switzerland signed a Joint Declaration on Cooperation (JDC). Through this document, the parties agreed to strengthen their economic cooperation; facilitate private sector involvement in trade; ensure compliance with labour and environmental standards; examine the possibility of further developing trade relations – all of these in the view of reaching a potential FTA. The JDC usually constitutes the first step towards opening of FTA negotiations with EFTA. Since last year, however, this process has been stalled because EFTA countries officially stated that given the imposition of a 100 percent tariff by Kosovo against Bosnia and Herzegovina and Serbia, it would be premature to hold the first meeting of the Joint Committee established by the JDC, as requested by Kosovo.

Under typical FTAs, EFTA states abolish customs duties on industrial goods, including fish and other marine products and offer tariff concessions on processed agricultural products and selected basic agricultural products. Because there is no common agricultural policy within EFTA, trade in basic agricultural products is covered by separate bilateral agreements concluded with trading partners.

Despite not having an FTA with EFTA yet, Kosovo is still among the most important EFTA partners in the region with a total trade volume of EUR 78.5 million in 2018, leaving behind Albania, Moldova, and Montenegro. Exports to EFTA in 2018 reached EUR 32.4 million (8.8 percent of Kosovo's total exports), while imports stood at EUR 46.1 million (1.4 percent of Kosovo's total imports). It is worth noting that amongst all its trading partners, Kosovo has seen the highest increase in exports to EFTA compared to five years ago – around 368 percent. This is reflected in a much lower trade deficit compared to CEFTA and the EU. Within EFTA, around 99 percent of Kosovo's trade is generated with Switzerland in 2018. This to a large part due to Switzerland accommodating the majority of Kosovo's diaspora.[25]

3.2 Main Trade Liberalisation and Market Access Challenges

In general, BMOs have a negative perception regarding the impact of the trade agreements in which Kosovo is participating. The predominant view is that Kosovo has not been able to reap significant trade benefits from these agreements. On the contrary, BMOs view Kosovo's trading partners as having benefited most, as reflected in the growing trade deficits with these partners. A publication by the KCC, for example, states that, "The CEFTA agreement does not seem to have brought much benefits to Kosovo, not because of substantial stagnation as a country, but more as a result of obstacles in achieving quality and applying international trade standards. The problem seems to be

[24] EU Project MTI (2019). EFTA's Trade and Tariff Concessions: A Comparative Perspective with Reference to Kosovo

[25] Kosovo Customs (2019). External Trade. *[Database]*

greater after the entry into force of the Stabilization and Association Agreement where Kosovo producers are facing the ‘European aggressive’ market.”[26]

A negative view concerning the benefits of the trade liberalisations under the current agreements is also found in a number of other analysis assessing the impact of trade liberalisation. A prior EU-funded trade project, for instance, found that, “[…] the liberal trade policies of recent years have largely fallen short of delivering the expected results – that is, a creation of a strong manufacturing base and a well-performing private sector emerging from increased levels of competition. On the contrary, the liberalisation of international trade has further aggravated Kosovo’s import dependency, widening the trade deficit.”[27] Another study by a BMO notes the limited benefits of the SAA and highlights that “many challenges still remain which impede Kosovo’s potential to increase the level of its exports towards the EU.”[28]

Similarly, concerns have also been raised about the potential impact of the recently ratified FTA with Turkey on domestic producers. The private sector has requested the Government to take some action to delay the tariff dismantling as provided by the Agreement.

In the interviews conducted with BMOs, the following specific issues were raised regarding trade liberalisation and market access.

a) Lack of visa-free travel

Conducting trade requires more often than not personal contacts between exporters and importers. Visa requirements and the difficulties in obtaining visas affect trade between Kosovo and a number of countries with whom Kosovo has not reached a visa waiver agreement yet. According to a survey with Kosovo businesses conducted by the KCC, visa requirement is the single biggest obstacle in doing business in export markets.[29] In the context of CEFTA, Bosnia and Herzegovina and Moldova are the two countries that maintain visas to Kosovo. Lack of visa-free travel with Moldova is less of an issue, probably because Kosovo historically did not have any notable trade links with this country. Bosnia and Herzegovina, on the other hand, is perceived as a serious potential trading partner and the inability of people to move freely, in addition to other issues stemming from non-recognition, plays a negative role in the trade prospects with this country. During the interviews, BMOs highlighted the issue of visas as being of special significance in Kosovo’s trade relations with the EU. They commonly believe that the inability of Kosovo businesses to move freely to the EU comprises one key impediment to creating and advancing business connections with partners in this block.[30]

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[26] KCC (2018). Paving the Way for Better Business in Kosovo: What are the growth obstacles for business in Kosovo. 4th Edition.

[27] MTI (2015) Annual Report No 1. 15 Years of Transition in Kosovo: Implications for Trade. EU Trade Project.

[28] American Chamber Of Commerce in Kosovo (2018) Private Sector Pulse on SAA. August.

[29] KCC (2019). Paving the way for a better business in Kosovo. https://www.oek-kcc.org/uploads/files/2019/June/28/Bottleneck_study_ENG_2018_r1561708255.pdf

[30] Kosovo citizens remain the only citizens from the Western Balkans (WB) that are obliged to apply for and obtain a visa to travel to the Schengen Area.

b) Difficulties in satisfying sanitary and phytosanitary requirements

The EU, exercising its legitimate right to protect human and animal life and the possible transmission of diseases, has laid down a wide range of health requirements in its Directives that need to be satisfied by exporters of animal products in order to enter the single market. Some additional requirements of this kind are also set out in specific Commission Decisions. The general rule is that products of animal origin must come from an EU approved establishment in the country of origin, and be accompanied by a health certificate to enter the single market.

Although the SAA foresees zero tariffs for the vast majority of animal products, because Kosovo has not been able to meet all the aforementioned requirements yet, there has been no exports of such products to the EU. This, to a great extent, has been the case with Kosovo's exports to other countries as well. BMOs are also aware of Kosovo's inability to comply with EU requirements in relation to animal products. One BMO specifically stated that "Kosovo fails to guarantee proper traceability of animal products and to provide internationally recognised health documents or certificates." That said, the onus is on Kosovo to undertake all the necessary measures that would allow its exporters to satisfy the EU sanitary and phytosanitary requirements, as the current situation is yielding non-reciprocal results for Kosovo. A significant amount of animal products is being imported from the EU.

c) Low EU quota on wine classified as "other wine"

The EU applies a quota of 4 million litres (40 thousand hl) to wine classified as "other wine" originating in Kosovo. In 2018, Kosovo's exports of this category of wine to the EU stood at 2.3 million litres (2.3 thousand hl), utilising only 55 percent of the quota. Main wine producers in Kosovo unanimously claim that their plan is to invest in expanding the exports of wine classified as "other wines" to the EU and therefore the quota might be reached soon.[31] Article 33 of the SAA provides for the possibility of further concessions between the EU and Kosovo, with a view to implementing greater liberalisation of the trade in agricultural and fishery products. If a larger quota for Kosovo wine producers would be needed in the future, Kosovo could legitimately activate the above-mentioned review Article.

d) Additional trade costs when transiting goods through Serbia

The majority of BMOs indicate that a number of exporting businesses encounter transit problems when shipping their goods to the EU through Serbia. This has had an effect by increasing trade costs, which are then reflected in the price of final products, making them less competitive vis-à-vis other comparator countries. There are products, such as metals, that cannot pass through Serbia at all, under the justification that Kosovo is not a member of the *Basel Convention on the Control of Transboundary Movements of Hazardous Wastes and Their Disposal*.

[31] EU Trade Project – MTI (2019). Trade in Agricultural and Fishery Products with the EU: A Review of the SAA Concessions.

e) Regulatory reform issues

Some issues have been raised concerning the direct transposition of international regulatory frameworks, which according to some BMOs, could be premature taking into account the situation of Kosovo and/or the constrained policy options available to support the private sector. In the realm of trade, the rights and obligations under the SAA are predominantly derived from the World Trade Organization (WTO) framework. In effect, Kosovo has taken bound commitments, both through international agreements or direct incorporation of provisions into domestic legislation, without having recourse to the instruments provided by some of the multilateral agreements, because it is not a member of the WTO. According to some BMOs, Kosovo's institutions and the private sector are not yet in a position to fully comply with the undertaken obligations. It is believed that Kosovo should have some autonomous policy space before it internalizes major provisions from the WTO or from other international fora. This was particularly stressed by one BMO with respect to the constraint imposed by the regulation limiting the capacity of the state to protect domestic producers.[32]

f) Possible specific tariffs from the EU on fruit and vegetable products

A close review of the SAA reveals that Chapter 7 and Chapter 8 of the Combined Nomenclature (CN), which consist of fruit and vegetable products, is exempted from the *ad valorem* tariff only. The *EU regulation (EC) No 1215/2009*, however, provides additional trade preferences for this category of products originating in Kosovo, namely elimination of quantitative restrictions and custom duties. The measure which originally applied until 31 December 2010 was extended until 31 December 2020 by *Regulation (EU) 2015/2423*. If this Regulation is not extended any further, the EU reserves the right to apply specific tariffs on products under Chapter 7 and 8. This could have an effect on the predictability of Kosovo exporters and their propensity to export as a result. It is worth noting, however, that EU's SAAs with other CEFTA members are not any different in this regard.

g) Non-recognition-related barriers in CEFTA

BMOs claim that non-tariff barriers of political nature, mainly stemming from non-recognition, constitute a hurdle that is hard to overcome. In many cases, these barriers are believed to be translated into pure import prohibition. They derive mainly from the fact that three CEFTA member states, namely Serbia, Bosnia and Hercegovina and Moldova, do not recognise Kosovo as an independent state. Non-recognition of documents or products that carry official Kosovar symbols is the most common form of politically inspired barriers applied by these countries. Such barriers are most pronounced in the case of Serbia. To illustrate, wine producers are not allowed to export wine on glass bottles to Serbia, because "Made in Kosovo" appears on the label.[33] Certificates issued by Kosovar authorities carrying the official Kosovar symbol are not recognized either. Almost every

[32] This was the case when domestic producers requested that 40% of the shelf space of retailers should be reserved for domestic products.

[33] EU Trade Project (2019). Report on Non-Tariff Barriers affecting Exports from Kosovo. https://mti.rks-gov.net/desk/inc/media/F280502A-D0BD-4ED4-ACA3-AAD0042AB950.pdf

exporting company is confronted with obstacles of this kind. A study by Bardigi (2017) concluded that, "Kosovo export products are facing the biggest challenge from the Serbian authorities, mostly related to trade barriers against export-import of agricultural and some non-agricultural products from Kosovo, but also when Kosovo products are in transit through the territory of Serbia since they don't recognize Kosovo exporters and importers."[34] This issue has been raised numerous times by the Government of Kosovo to the appropriate CEFTA instances in search for a solution. Progress on the issue is currently further complicated due to the 100 percent tariff imposed by Kosovo on imports from Serbia and Bosnia and Herzegovina.

h) Sanitary and Phytosanitary Measures (SPS) and Technical Barriers to Trade (TBT) in the context of CEFTA

Most of the non-tariff barriers imposed on Kosovo within CEFTA are of the SPS and TBT kind. Parties are expected to cooperate and share information in the field of SPS and TBT, with the aim of applying regulations in a non-discriminatory manner. Under normal circumstances, SPS measures and TBTs are thought to provide quality and safety assurance and enhance consumer trust as a result. However, BMOs claim that Kosovo's trade is hampered, because other CEFTA parties frequently use these measures in a non-appropriate manner, generating unnecessary obstacles to trade. However, BMOs also acknowledge the fact that in many cases Kosovo does not have the capacity to satisfy legitimate SPS measurers and TBTs due to its underdeveloped sanitary and quality assurance systems.

i) Additional charges and taxes when exporting to CEFTA

Some BMOs complain that the majority of CEFTA members apply price control measures (including additional taxes and charges) to Kosovar exporters, mainly to support domestic producers in cases when prices of products from Kosovo are lower. For instance, Albania applies a higher excise rate on imported plastics products, although under CEFTA the rate must be the same for both domestic and imported products.[35] A similar case is encountered with wine and beer as well. A higher excise tax is charged by Albania if the production capacity exceeds 1 million litres. An estimation reveals that, on average, a Kosovar firm needs to pay USD 264 to export. The average cost in other WB countries is USD 72.[36]

[34] Bardigi Olivera (2017) "Economic Relations between Serbia and Kosovo" in Overcoming Barriers to Business and Normalization' Heinrich Boell Stiftung. Belgrade.
[35] Bardigi Olivera (2017) "Economic Relations between Serbia and Kosovo" in Overcoming Barriers to Business and Normalization' Heinrich Boell Stiftung. Belgrade.
[36] Agon Nixha (2017). Foreign Direct Investments and Exports: Kosovo and the Western Balkans. https://d4d-ks.org/en/papers/policy-brief-foreign-direct-investments-exports-kosovo-western-balkans/

j) Burdensome customs procedures

Delays and other burdensome customs procedures constitute a great hindrance to the free flow of goods in the region. According to the World Bank (2017), firms in Kosovo face the highest exporting costs among the Western Balkans. The study notes that, a Kosovar exporter, on average, needs to wait 42 hours for border compliance and another 38 hours for documentary compliance.[37] The same study reveals that the average border and documentary compliance in other Western Balkan countries is 7 hours and 3.8 hours, respectively. Delays take place in different forms. For example, on the border between Kosovo and Serbia, the Serbian phytosanitary officials work on reduced working hours. There is no presence of inspectors at the border after 2:00 pm; therefore, Kosovo companies that arrive to the border after this hour have to wait until the next day.[38]

k) Limited integration into regional value chains

BMOs share the view that the integration of local suppliers into regional supply chains is limited. There is a number of rather big multinational companies located in SEZs in some CEFTA countries (mostly in Serbia and North Macedonia), which source the majority of intermediate products from the country of origin or from countries beyond CEFTA. Although these SEZ-based companies actively look for local suppliers, the lack of cooperation between local and regional suppliers prevent the development of linkages with these international companies. An eventual integration of Kosovo input suppliers into regional supply chains would create backward spill-over effects.

l) Aggressive competition coming from China

Historically, Kosovo has not used tariffs as an instrument of trade policy. Under the current preferential agreements, over 80 percent of Kosovo's imports will have duty-free access by 2025. On the other hand, imports from all other non-preferential countries are subject to a flat rate of 10 percent, except for some imports that are universally exempted from this tariff. Kosovo's tariff regime towards these countries is not bound and therefore can be adjusted to provide for an adequate level of protection. According to some BMOs, a 10 percent uniform rate is no longer appropriate for countries like China and as such it should be re-examined. Trade data show that Kosovo's imports from China in 2018 stood at EUR 311.9 million, accounting for 9.2 percent of total imports.[39] Textiles, plastics and some other manufacturing sectors seem to have been damaged form subsidized products originating in China. Nonetheless, a possible change in policy towards China or any other country should take into consideration all economic and political factors.

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[37] World Bank (2017) Western Balkans: Regional Economic Integration Issues Notes. June

[38] EU Trade Project (2019). Report on Non-Tariff Barriers affecting Exports from Kosovo. https://mti.rks-gov.net/desk/inc/media/F280502A-D0BD-4ED4-ACA3-AAD0042AB950.pdf

[39] Kosovo Customs (2019). External Trade. *[Database]*

m) Aggressive competition coming from Turkey

BMOs are generally afraid that the tariff concessions granted to Turkey as part of the recently ratified agreement will negatively affect the private sector in Kosovo. Even with the current level of tariffs, Kosovo has been flooded by Turkish imports. Some industries, food processing for instance, are expected to suffer most, provided that imports from Turkey will be in direct competition with what Kosovar companies produce. In addition, some sector-specific BMOs also claim that new sub-sectors, which had not been considered at all when negotiations took place, have emerged in Kosovo. For example, many new successful companies in the apparel sub-sector were established after the FTA with Turkey was signed.

n) Lack of market data and limited export promotion

BMOs complain that Kosovo lacks institutionalized sources that provide systematic market intelligence on potential export markets. Rather than being able to proactively search for opportunities in export markets based on reliable and accessible data, most of the time Kosovo companies depend on one-time hints from personal Kosovo Albanian diaspora contacts and some ad hoc orders to generate exports, which occur on a sporadic basis mostly. In its efforts to promote Kosovo’s exports, in recent years KIESA has been mainly focused on sending exporting companies to trade fairs. Although the majority of BMOs declare not to be against these fairs, they also mention that a better monitoring and evaluation of these fairs is needed because there is room for improvement. Lack of export financing is another issue brought up by BMOs.

4. Inside-the-Border Aspects

Trade liberalisation per se, if not accompanied by policies that support the development of the private sector, does not necessarily produce better outcomes for a developing economy. Liberalisation is not a "magic wand". Kosovo is a perfect case that supports this assertion. Despite entering into preferential arrangements with the main surrounding markets, Kosovo has not seen improvements in the trade balance. Many reports concerning trade in Kosovo highlight that supply-side (inside-the-border) constraints actually constitute the main factors for the dismal export performance. A weak and comparatively less competitive private sector has put Kosovo in a disadvantageous position vis-à-vis countries with which it has preferential deals. It should be noted that policies that deal with competitiveness and other border-in issues do not fall under the scope of international trade per se; however, in the case of Kosovo, they seem to have very important implications and such should be dealt with seriously in the context of trade policy. Main inside-the-border challenges are discussed below.

4.1 Main Inside-the-Border Challenges

a) High cost of electricity and other related electricity issues

Electricity is perceived to be one of the most serious barriers by BMOs. The first issue in this area is the high cost of electricity. Electricity tariffs for industrial consumers in Kosovo are the highest in the region.[40] This increases operational costs for businesses, thereby making them less competitive both in the domestic market and in the region. The second issue has to do with the costs to obtain a permanent electricity connection for a newly constructed business facility. BMOs claim that a new business has to invest in building the entire necessary infrastructure in order to be connected to the grid. What is worse, in the end the business is obliged to hand over all these assets to the Kosovo Energy Distribution Services (KEDS), which is the only electricity distribution company in Kosovo. This huge initial cost has become an entry barrier to many new businesses, in the manufacturing sector in particular. The final issue is related to the reliability of supply. Although the duration and frequency of power outages have been generally reduced, they are still deemed problematic for businesses. Unreliable supply of electricity gives raise to significant costs for business and constitutes a huge obstacle to attracting export-oriented FDI. In the latest Work Bank Doing Business Report, Kosovo is ranked 113th in the world for ease of getting electricity.[41] The latest business survey carried out by KCC also reveals that the manufacturing sector faces problems with the high cost of electricity (71%) and lack of regular supply with energy (65%).[42]

[40] World Bank (2018). Western Balkans: Directions for the Energy Sector.
[41] World Bank (2019). Doing Business 2020. Economy Profile Kosovo. https://www.doingbusiness.org/content/dam/doingBusiness/country/k/kosovo/KSV.pdf
[42] KCC (2019). Paving the way for a better business in Kosovo. https://www.oek-kcc.org/uploads/files/2019/June/28/Bottleneck_study_ENG_2018_r1561708255.pdf

b) Mismatch in the labour market

BMOs commonly claim that businesses face the challenge of getting a workforce with relevant skills. This challenge is highlighted in multiple other sources as well. A recent report by AmCham reveals that finding skilled labour is one of the most significant challenges faced by Kosovo businesses.[43] Moreover, a survey conducted by the World Bank (WB) shows that 75 percent of businesses that attempted to fill a higher skill vacancy, and 60 percent of those that sought to fill a medium to lower skill vacancy, were confronted with challenges because of applicants' skills deficiencies and/or inexperience.[44] Businesses in general suffer when it comes to finding various sector-specific technicians. The export-oriented ones, in addition, face difficulties in finding a workforce with relevant skills for export. This mismatch in the labour market is caused by several factors. First, the education system is poor and not able to produce graduates with skills demanded by the market. Second, programmes delivered by vocational schools (VET) or training centres are not based on surveys that measure the market demand, as well as lack quality assurance mechanisms. An interesting finding is that more than 50 percent of VET schools do not offer opportunities for practical work.[45] Third, a limited number of businesses provide work-based training to upskill their workers; the majority are afraid of inter-business migration.

c) Lack of incentives for export-oriented FDI

Kosovo is underperforming compared to countries in the region in terms of attracting export-oriented Foreign Direct Investments (FDI). This, to some extent, stems from the fact that Kosovo's FDI incentive program is predominantly based on investment protection agreements and some fiscal relief measures; the latter are even less attractive vis-à-vis those provided by the majority of regional countries. It is worth noting that competition over FDI is getting tough. While financial incentives are not available in Kosovo, countries in the region such as Macedonia, Serbia and to some extent Bosnia and Herzegovina have developed financial incentive regimes including various employment-related subsides, subsidies to cover total investment costs, R&D incentives, and some other similar incentives. This has led to the development of new manufacturing centres, which have attracted the bulk of FDI in the region, leaving Kosovo behind. Serbia's robust growth in exports, for instance, has been attributed to the strong growth of export-oriented FDI, which came as a result of Special Economic Zones (SEZ) supported by an attractive incentive regime. Serbia, indeed, has the largest network of active SEZ (14), forming close to 15 percent of the country's total exports and contributing with around 22,000 jobs in 2017.[46]

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[43] AmCham (2018). Private Sector Pulse on SAA.
http://www.amchamksv.org/wpcontent/uploads/2018/09/Private-Sector-Pulse-on-SAA.pdf
[44] World Bank (2019). Kosovo Country Report: Findings from the Skills towards Employment and Productivity Survey.
[45] World Bank (2019). Kosovo Country Report: Findings from the Skills towards Employment and Productivity Survey.
[46] OECD (2017). Tracking Special Economic Zones in the Western Balkans. http://www.oecd.org/south-east-europe/SEZ_WB_2017.pdf

d) High level of informality

One of the main business environment obstacles continues to be the high level of informality. According to some recent estimations, general informality accounts for around 31 percent of Kosovo's GDP.[47] Likewise, labour informality ranges between 30 percent to 40 percent.[48] This endemic level of informality produces unfair competition, which is often perceived among the most severe barriers to doing business. Unfair competition, according to BMOs, brings about detrimental effects on new, honest, and innovative businesses, as well as sends negative signals to potential foreign investors.

e) Discriminatory treatment of local producers on VAT

Many BMOs, especially those in the agriculture sector, claim that domestic suppliers of raw material are treated disadvantageously when it comes to VAT. According to the new law, imported raw material used for the production process is exempted from VAT, whereas raw material produced domestically is subject to VAT.[49] This has created an unprecedented case where rather than having foreign companies ask for national treatment – which is normally the case, it is the domestic ones that ask for foreign treatment. Moreover, what is considered a raw material is not well-defined by the legislation in place. A new administrative order foresees that exemptions are determined by a committee in the Tax Administration on a case-by-case basis. Some BMOs claim that the criteria for import VAT exemption is not transparent, leaving too much discretion to the committee and as such creating grounds for unfair treatment.

f) Fragmented land and ownership problems

Kosovo's agriculture sector is unable to realize its potential as a dynamic economic sector mainly due to the fragmented land structure. Close to 60 percent of all farms in Kosovo have less than 5 ha of utilized agricultural area.[50] This land structure constraints farmers to grow and profit from economies of scale. In addition, unresolved issues of land administration and ownership negatively affect farmers' ability to invest, expand, and access credit.

g) Unfair Trade Practices

Within the agricultural and food supply chain in Kosovo, there are significant imbalances in bargaining power between local producers/processors and retailers. Retailers are thought to have established some sort of a dominant position in the market and are constantly imposing unfair trade practices

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[47]European Commission (2019). Economic Reform Programme of Kosovo (2019-2021). https://data.consilium.europa.eu/doc/document/ST-8546-2019-INIT/en/pdf
[48] Ibid.
[49] Ministry of Finance (2015). Law on VAT. https://mf.rks-gov.net/desk/inc/media/F8871713-07D4-43B5-B11A-C8618626BB27.pdf
[50] European Commission (2019). Economic Reform Programme of Kosovo (2019-2021). https://data.consilium.europa.eu/doc/document/ST-8546-2019-INIT/en/pdf

(UTP) on local producers/processors. Such practices seem to occur at any stage of transaction. First, due to the economic dependence of the local producers/processors on the retail chains, the former group are “forced” to accept contracts, which are less favourable to them. One local producer, for instance, declared that his company pays an additional 10 percent on top of the value of the merchandise just for the retail chain to accept the product. Second, UTPs such as delays in payments, pricing below the costs of production, fees for services not contracted, unilateral changes of contracts occur during the execution of the contract. BMOs in the agriculture sector share the view that one cannot talk about international trade without solving these unfair practices that occur internally.

h) Poor quality infrastructure

BMOs commonly believe that Kosovo has a poor-quality infrastructure. A number of exporters claim that it has become increasingly difficult to export products to well-regulated markets due to the inability to satisfy internationally recognised quality standards and systems. Currently, the internationally recognised third-party standards certification usually required for trade is also not available in Kosovo. Exporters do not have reasonable access to simple laboratory tests. Consequently, Kosovar exports have no other option but to do the testing and certification outside of Kosovo, thus incurring extra costs which have an effect on their competitiveness. Conversely, quality standards imposed on imported products and the overall control by public authorities seem to be very limited, creating room for poor quality products, thus leaving consumer interests with a minimum level of protection.

i) Poor adherence to corporate governance principles

The overwhelming majority of exporting businesses in Kosovo are family-owned. BMOs claim that such businesses face a particular set of challenges that are, to a great extent, intrinsic to their organizational structures. While family involvement is proven to be beneficial in the early stages of business development, at some later stages the tendency to retain all the power within family members makes companies vulnerable to adverse effects. This is a problem faced by many bigger exporting companies in Kosovo. Despite the need for professional staff in managerial positions, family members usually want to retain the ultimate control over the company. Generally, Kosovar companies are often characterized by weak and ineffective corporate governance systems.

j) Low productivity and limited linkages

BMOs claim that lack of investments in modernizing production is another obstacle affecting the performance of businesses. This appears to be somewhat more pronounced in the agriculture sector. Moreover, they consider that investments in innovation are generally minimal. This limits the abilities of businesses to catch up with market changes, as well as to differentiate their products from their competitors. Another issue identified is the generally low level of production capacities. Most of the Kosovar businesses are unable to produce the quantity of goods requested by importers in international markets. In a recent survey, around 34 percent of non-exporting firms declared that "production capabilities" is the main problem for not exporting.[51]

k) Limited access to finance

Limited access to finance is another barrier Kosovo businesses face. The KCC survey report with businesses ranks it amongst the first two barriers, with 49 intensity points.[52] BMOs, moreover, declared that their members often complain regarding their inability to meet working capital requirements due to financial reasons. In many instances, businesses forego opportunities because they cannot handle transaction-specific liquidity issues and non-payment risks. Moreover, equity finance is practically unavailable in Kosovo, creating a gap in the market for financing riskier investments. In addition, Kosovar banks do not offer export financing products.

l) Limited participation of women in trade

Women own only 10 percent of businesses in Kosovo, compared to a world average of around 37 percent.[53] They predominantly operate in low-value added services sectors, which are by their very nature non-tradable. Of all women-owned businesses, only about 10 percent have managed to successfully penetrate international markets. The participation of exports in total turnover for women-owned businesses stands at 30 percent, on average. Limited access to finance is perceived to be one of the most pressing issues.[54] They find documentary and collateral requirements difficult to fulfil, mainly due to cultural norms, which are reflected for instance in property owned by women often being registered in men's name.

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[51] Gazmend Qorraj, Gezim Jusufi (2018). The EU Stabilisation and Association Agreement for the Western Balkans: Between Challenges and Opportunities.
[52] KCC (2019). Paving the way for a better business in Kosovo. https://www.oek-kcc.org/uploads/files/2019/June/28/Bottleneck_study_ENG_2018_r1561708255.pdf
[53] MCC (2017). Kosovo Constraints Analysis. https://assets.mcc.gov/content/uploads/Constraints-Analysis-Kosovo-1.pdf
[54] Riinvest Institute (2017). Women's Entrepreneurship An Analysis on Doing Business in Kosovo. https://www.riinvestinstitute.org/uploads/files/2017/November/10/Womens_Entrepreneurship1510307815.pdf

5. Trade in Services

Over the last decades the services sector has become increasingly important in the world economy. In 2018, it is estimated to have accounted for 75 percent of GDP in developed countries, up from 50 percent in 1950. Consistent with its key role in domestic economies, trade in services has also become the most dynamic component of international trade, participating with around 20 percent in the overall world trade. On average, trade in services increased by 5.4 percent annually from 2005 to 2018, faster than trade in goods. [55] It is becoming increasingly easy to trade in services thanks in large parts to technological advancements.

In Kosovo, likewise, the services sector is an important segment of the economy. Kosovo's economic structure is predominantly based on services. The services sector has emerged as the largest sector, contributing with around 73 per cent to GDP. Moreover, it is responsible for over 80 percent of total formal employment in Kosovo.[56] It also plays an important role in Kosovo's overall trade (both goods and services), contributing with around 35 percent. As indicated in the very beginning, unlike trade in goods, which is characterized by a huge trade deficit, the balance of trade in services is in surplus. Exports of services are almost four times higher than exports of goods. Although this topic was brought to the attention of BMOs, little information could be gathered in regard to challenges, reflecting the overall low level of awareness in the private sector about this sector. A few challenges have been identified, nonetheless, mainly relying on desk research. Some more specific attention should be given to this sector provided its growing importance.

5.1 Main Challenges in Trade in Services

a) Lack of proper data on trade in services

Generally, the collection of statistics on services activities and the way they are disseminated is not satisfactory. There is no sufficient data on the sub-sectoral level. For example, there is no information on the exact amount of IT services outsourced to foreign markets.

b) Limited focus on high productivity services activities

In spite of the fact that trade in services has been growing in the recent years, its contribution to economic growth and development in general is not at a desirable level. Kosovo is expanding towards low productivity services activities. The bulk of the services sector is mainly comprised of non-tradable activities. Public administration and defence, real estate and wholesale and retail services account for almost half the valued added generated by services activities in the Kosovo economy.

[55] World Trade Report 2019: The future of services trade. https://www.wto.org/english/res_e/booksp_e/executive_summary_world_trade_report19_e.pdf
[56] EU Trade Project – MTI (2018). Brief on Trade in Services. https://mti.rks-gov.net/desk/inc/media/7593CC1B-475F-4E0E-B130-B3A58AED5ECB.pdf

c) Lack of proper infrastructure for e-commerce

International electronic payments cannot be made effectively because of SMEs' limited access to third-party e-payment service providers linked to Kosovar banks. Kosovo doesn't have a proper legal and regulatory infrastructure in place that regulates e-commerce, neither domestically nor internationally.

d) Lack of a strategic framework on services

Kosovo lacks a coherent overarching strategic framework for promotion of trade in services tying opportunities to education, training programs and budgeting.

6. Institutional Aspects

The quality of institutions is very important for creating the necessary pre-conditions for trade development. Alongside physical capital, human capital and technology, good institutions constitute the main differentiating factors in an economy. Administrative organizations underpin the creation of what economists call an "enabling environment". On the flip side, low institutional infrastructure has detrimental effects by limiting market access for exports and impeding the overall economic growth.

In Kosovo, the main institution responsible for designing and implementing trade policies is MTI. The ministry has a number of trade-related institutional mechanisms under its umbrella that deal with trade. The key body is the Trade Department. This department is mainly responsible for designing trade policies. Other relevant implementing bodies within MTI include: Kosovo Investment and Enterprise Support Agency (KIESA), which supports the private sector as well as promotes exports and investments; Kosovo Standardization Agency (KSA), Kosovo Metrology Agency (KMA) and Kosovo Accreditation Agency (KAA), which are responsible for quality infrastructure; and the Industrial Property Agency (IPA), which deals with intellectual property rights. Beyond MTI, other public institutions, such as the Ministry of Finance (MoF), the Ministry of Agriculture (MAFRD), the Ministry of Economic Development (MED), Kosovo Customs, the Kosovo Tax Administration (KTA), the Central Bank of Kosovo (CBK) are also directly and indirectly tied to trade. Below are summarised some key institutional problems identified during the research.

6.1 Main Institutional Challenges

a) Weak institutional capacities for trade negotiations

The effective participation in trade negotiations requires a robust negotiation mechanism in the form of an institutional structure and staff with requisite skills. Currently, the MTI lacks a proper standing committee to undertake trade negotiations. MTI staff also does not have sufficient expertise to perform underpinning analytical work before and during trade negotiations. In addition, the MTI lacks a mechanism for ensuring that representatives from line ministries who are seconded to undertake specific negotiations remain as permanent members and to ensure institutional memory and consistency.

b) Insufficient capacities to impose trade remedies

As every country, Kosovo is allowed policy space to take measures against unfair trade practices. Exploiting this policy space, Kosovo has built a legal framework that foresees counterbalancing measures on imports that cause or threat to cause injury to the domestic economy. Some BMOs have voiced concerns that some trade partners, within and beyond CEFTA, often engage in unfair trade practices, exposing Kosovar producers to threats of dumping and sale of imported goods benefiting from subsidies. According to BMOs, the MTI lacks institutional capacities to undertake proper surveillance for cases of dumping, subsidies and other unfair practices of this kind.

c) Inadequate level of inter-institutional cooperation and coordination

There is room for better cooperation and coordination among institutions that are involved in trade development. Several issues have been identified in this regard. First, there is no effective inter-institutional mechanism that coordinates activities in the services sector. This omission has led to conflicting policies and weak policy implementation in the sector. Second, cooperation between the Trade Department and KIESA does not seem to take place in a systematic manner. This has created a gap between policy design and implementation. Third, there is some overlapping of competences between Kosovo Customs and Kosovo Tax Administration. This has been manifested in delays and arbitrary decisions at the border. Finally, the Trade Department does not have instant access to trade data collected by Kosovo Customs. Delays in obtaining trade databases from Kosovo Customs have played a negative role in the efficiency of the Trade Department.

7. Conclusion and Main Recommendations

This assessment report attempts to identify and elaborate Kosovo's main challenges concerning international trade. The generated findings are intended to feed into the trade policy document to be formulated by the MTI, as well as into other policy documents if relevant. The report draws on three data-collection instruments: desk research (literature review); open semi-structured interviews with BMOs; and on a final validation meeting with MTI representatives, businesses and other stakeholders.

This assessment initially looks into the involvement of the private sector in trade policy making. It finds that Kosovo's regulatory and institutional framework on public-private dialogue is relatively advanced. BMOs commonly believe that compared to five years ago, the public-private dialogue on trade issues has seen some notable improvements. The openness of the Trade Department in particular is widely appreciated. Despite the overall improved trend, there are still some challenges that need to be dealt with. Some of the challenges identified include the involvement of BMOs and other stakeholders being often only pro forma; limited effectiveness of NCED; technical language of documents subject to public consultation; misalignment of interests between traditional BMOs and new BMOs; and low trust in public institutions.

The report, further, summarizes Kosovo's current trade arrangements and discusses key trade liberalisation and market access challenges. The two main preferential trade agreements, notably CEFTA and the SAA, according to BMOs, do not appear to have produced the expected outcomes for Kosovo, indicating that trade liberalisation alone is not very effective. Among the challenges identified under the current preferential agreements and beyond are the following: lack of visa-free travel; difficulties in satisfying sanitary and phytosanitary requirements in export markets; potentially limiting effect in the future of the quota on "other wine" by the EU (if the possibility of further concessions between the EU and Kosovo provided by the SAA is not realized); additional unnecessary trade costs when transiting through Serbia; limited policy space resulting from (premature) incorporation of international commitments into domestic legislation; possible specific tariffs from the EU on fruit and vegetable products (if additional preferences granted by EU regulation (EC) No 1215/2009 are not extended beyond 2020); trade obstacles due to non-recognition of Kosovo by some CEFTA countries; unfair SPS measures and TBT imposed by some CEFTA countries; additional charges and taxes when exporting to CEFTA; burdensome customs procedures; aggressive competition coming from China and Turkey; and lack of market data and limited export promotion.

The dismal export performance is also largely attributable to the challenges occurring in Kosovo's backyard. Although such challenges are not linked to international trade per se, they have very serious implications in the performance of Kosovo, putting Kosovo in a disadvantageous position in the international arena. The report identifies the following inside-the-border challenges: high cost of electricity and other related electricity issues; mismatch in the labour market; lack of incentives for export-oriented FDI; high level of informality; discriminatory treatment of local producers on VAT; fragmented land and ownership problems; unfair trade practices in the domestic market; poor quality infrastructure; poor adherence to corporate governance principles; low productivity; limited access to finance; and limited participation of women in trade.

In spite of the growing trend of the services sector in Kosovo and its overall trade potential, the report reveals that BMOs have little information on the sector. A few challenges identified from the desk research have been included in the report, however, in the hope of provoking some further thought and work in the area. Lack of proper data on trade in services; limited focus on high productivity service activities; lack of proper legal and regulatory infrastructure on e-commerce; and lack of a strategic framework on services, constitute some of the problems requiring immediate and specific attention in this sector.

The report finally sheds light on some institutional challenges, highlighting weak institutional capacities for trade negotiations; insufficient capacities to impose trade remedies; and an inadequate level of inter-institutional cooperation and coordination.

Despite the great efforts to include as many challenges as possible, this report is not intended to be exhaustive. Some further work is required to identify additional trade challenges and to individually scrutinize the challenges identified in this report.

In view of the constraints and challenges found in this report, the following recommendations have been proposed. The recommendations draw on the priorities identified from interviews with BMOs, relevant strategic documents, and on the author's experience.

Public-private sector dialogue

- Enhance the effectiveness of NCED and ensure that its working groups are gathered every two months;
- Engage with the private sector and other stakeholders in early stages of trade policy and decision-making processes;
- Develop a system that ensures that the private sector receives proper justifications in cases when their inputs are not addressed in policy and legal documents;
- Undertake campaigns to showcase the effectiveness of public consultation processes and to build trust between private sector stakeholders and MTI;
- Develop "open door" policies or take affirmative measures to ensure broad-based involvement of the private sector;
- Provide necessary information in a comprehensible and digestible form to the private sector during the trade policy process so that private sector stakeholders are better able to unambiguously understand the content and therefore become more involved;
- Facilitate the coalition building efforts between traditional well-established BMOs and newer BMOs to align their interests and improve the bargaining power of underrepresented categories of businesses; and

- Improve cooperation between public-private sector institutional mechanisms within MTI and ensure that their competencies are clearly defined.

Trade liberalisation and market access

- Review all the existing trade agreements (CEFTA, SAA, Kosovo-Turkey FTA) to ensure parties' compliance with commitments;
- Intensify efforts to speed-up the visa liberalisation process with countries with which Kosovo has trading interests;
- Undertake all the necessary steps that would allow Kosovo exporters to satisfy the EU sanitary and phytosanitary requirements;
- Consider negotiations under SAA Article 33 with the EU to increase the quota on wine classified as "other wine" from 4 million litres to 6 or 8 million litres;
- Negotiate with Serbia to eradicate additional and unnecessary costs imposed on Kosovo exporters when transiting goods to the EU;
- Undertake an assessment of all WTO rules and regulations established in Kosovo's legislation to measure their impact on trade development;
- Explore the possibility of an extension of the additional preferences for fruits and vegetables currently granted by the EU.
- Negotiate constructively with CEFTA countries that have not recognised Kosovo to eliminate non-recognition-related barriers;
- Support regional negotiations to fast track the removal of SPS and TBT barriers against Kosovo's exports;
- Negotiate with CEFTA countries to remove additional charges, taxes and other burdensome procedures on Kosovo's exports;
- Change the tariff regime towards China to provide for an adequate level of protection for strategic products in the manufacturing sector;
- Renegotiate tariff concessions with Turkey and prepare for negotiations on trade in services;
- Negotiate and finalise an FTA with EFTA States;
- Develop an Export Market Information Centre to provide (potential) Kosovar exporters more information on international markets;
- Analyse possibilities for partial scope agreements with African countries and Middle East countries.
- Monitor and evaluate the effectiveness of export promotion activities and design new activities according to the generated findings;
- Develop a subsidy scheme for sectors that have better prospects to export; and
- Cooperate with banks to develop export financing products.

Internal/domestic

- Cooperate with the Energy Regulatory Office (ERO) and other relevant institutions to adjust the tariff regime for industrial consumers and to avoid all the unnecessary costs and cumbersome procedures which a business faces to get connected to the grid;
- Facilitate capacity building of VET schools and training centres and help them to develop connections with the private sector;
- Encourage export-oriented FDI through developing financial investment incentives, streamlining procedures and providing additional fiscal relieves;
- Develop a scheme where the government supports with diaspora investments;
- Build a regulatory and institutional framework that deals with unfair trade practices in the domestic market;
- Work with tax authorities to eliminate VAT on raw material produced domestically and develop concrete criteria to determine what is considered a raw material;
- Cooperate with relevant authorities to initiate land consolidation reforms;
- Undertake soft law approaches to promote and incentivize voluntary compliance with corporate governance principles by businesses;
- Facilitate the development of linkages within and across sectors and help businesses to integrate in regional and global value chains;
- Support businesses to advance technology, improve innovation and improve management and overall work processes;
- Facilitate the creation of a window under the Kosovo Credit Guarantee Fund (KCGF) to promote export diversification and value addition;
- Establish a government-funded instrument to assist in quality standards certification for Kosovar enterprises;
- Design and implement ‘green box’ policies, especially to support poor farmers in remote rural areas;
- Promote quality infrastructure to the private sector and other involved stakeholders;
- Design and accredit certification bodies and testing labs for sectors with export potential;
- Promote gender equality in trade development;
- Enhance capacities of national and regional associations of women in business; and
- Develop education programmes to eliminate prejudices against women and promote gender equality.

Trade in Services

- Cooperate with CBK to develop a better system for the collection and dissemination of data on services trade;
- Establish an inter-institutional mechanism responsible for trade in services to ensure that Kosovo exploits opportunities in a coordinated manner;
- Develop an adequate legal and regulatory infrastructure for e-commerce;

- Profile all high productivity service activities with trade potential in international markets and develop incentives for these activities; and
- Develop a strategic framework for trade in services.

Institutional Aspects

- Establish a proper standing committee as a robust negotiation mechanism to undertake trade negotiations;
- Enhance capacities to perform underpinning analytical work before, during and after trade negotiations;
- Build institutional capacities to undertake proper surveillance for cases of dumping, subsidies and other unfair practices of this kind;
- Improve cooperation and coordination between Trade Department, KIESA, Kosovo Customs and KTA.

8. Annexes

8.1 Annex A

List of Interviews		
Interviewees	**Sector**	**# of interviews**
Main Business Membership Organizations (BMOs)		
Kosovo Chamber of Commerce	All Sectors	1
American Chamber of Commerce	All Sectors	1
European Investors Council	All Sectors	1
Chamber of Doing Business of Kosovo	All Sectors	1
Kosovo Manufacturing Club	All Sectors	1
Kosovo Banking Association	All Sectors	1
Association of Craftsmen and Entrepreneurs of Prizren	All Sectors	1
Total General BMOs		**7**
Sectoral BMOs		
The Association of Wood Processors of Kosovo (AWPK)	Wood Sector	1
The Kosovo Apparel Marketing Association (KAMA)	Textile (Apparel) Sector	1
The Association of Plastics Processors (APP)	Plastics Sector	1
The Association of Metal Processors (AMP)	Metal Sector	1
The Kosovo Association of Information and Communication Technology (STIKK)	ICT Sector	1
Association of Builders and Manufacturers of Construction Material	Construction	1
Kosovo Fruits and Vegetable Processors Association - Pepeko	Agriculture Sector	1
Kosovo Dairy Processors Association	Agriculture Sector	1
Kosovo Milk Producers Association	Agriculture Sector	1
Total Sectoral BMOs		**9**
Relevant Research Institutes		
Riinvest Institute	Economic	1
GAP Institute	Economic	1
Total Research Institutes		**2**

8.2 Annex B

Interview Guide - Inputs for Trade Policy Document

Introduction 10 min.

I am currently performing a consolidated assessment and consideration of the key trade-related challenges faced by the main private sector actors, while at the same time trying to define their main priorities in the area. This work will feed into the new Trade Policy document to be drafted by the Trade Department (TD) of the Ministry of Trade and Industry (MTI). In order to obtain relevant information on the topic, the following three data-collection instruments will be used: desk research (literature review), **open semi-structured interviews with BMOs**, and thematic meetings with sub-working groups.

- Explaining that the information collected will be used for report purposes;
- Explaining that interviewees should feel free to express their opinion;
- Elaborating the scope of the process.

The interview will be structured around the following three topics:

1. Involvement of the private sector in policy making;
2. Trade-related challenges faced by the private sector;
3. Priorities of the private sector on trade development.

Theme 1: Involvement of the private sector in policy making

- How do you assess the dialogue between the private sector and public institutions on trade-related issues?
- Are you aware of the decision-making institutional setting for trade policy formulation?
- To what extent is the private sector included in the drafting of new legislation and strategic documents?
- Is the process of national consultations effective?
- How would you judge the responsiveness of relevant public institutions towards concerns of the private sector?

Theme 2: Trade-related challenges faced by the private sector

Market access/trade liberalisation:

- Could you please highlight the main challenges faced by the private sector under the current trade preferential agreements (SAA, CEFTA, FTA with Turkey etc.)?
- Is there any country or a trade block of specific interest with whom Kosovo needs to have a free trade agreement?
- How does the current tariff regime affect the private sector in Kosovo?

Trade-related development policies:

- What are the main challenges affecting the level of competitiveness of Kosovo companies? Please elaborate.

- [To sector-specific associations only!] To what extent the supply-side constraints (quality and quantity of products) explain the poor/dismal export performance?
- How would you assess the export promotion measures undertaken by Kosovo institutions?
- What are the main issues for the comparatively low level of export-oriented FDI?

Cross-cutting:
- What are the main challenges that hinder the participation of gender and youth in trade?
- What are the challenges affecting trade and the environment?

Institutions:
- Is the current institutional setup adequate to create a favourable environment for trade development?
- Is the current legal framework advanced and tailored enough for realization of foreign trade?

Theme 3: Priorities of the private sector on trade development

- What steps need to be undertaken to strengthen the dialogue between the private sector and public sector on trade-related issues?
- What needs to be done from the viewpoint of accessing other country markets?
- What measures need to be undertaken to increase the level of competitiveness and to address other “border in” issues?
- Could you please list and elaborate some actions that need to be undertaken on export promotion?
- How can Kosovo (MTI) increase the participation of women and youth in trade?
- How can Kosovo (MTI) accommodate environmental concerns in its trade policy?
- What changes need to take place in the institutional and legal framework to accommodate the interests of the private sector?

Recapitulation of main points *10 min.*

Thank you for your participation!