

WESTERN BALKANS

Regular Economic Report No. 14 (Fall 2018)



Higher But Fragile Growth

Prishtina, 11th October, 2018

Regional Messages

- Growth in the region strengthened primarily due to higher public spending.
- Limited private sector dynamism reflected in the slow response of employment.
- High and rising public debt is coupled with fiscal and external imbalances.
- Positive outlook, but vulnerable to tightening in financial markets and domestic politics defining the speed of structural reforms.

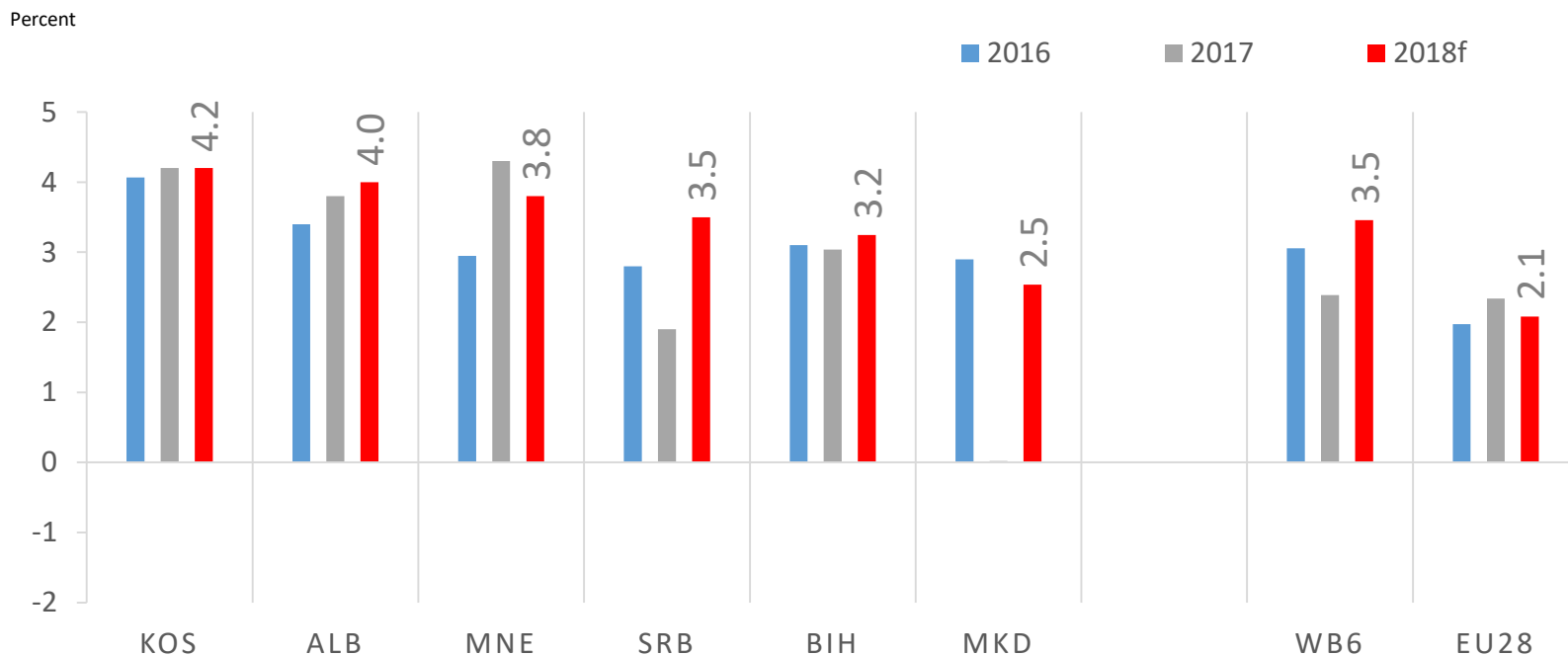
Main Messages for Kosovo

- *Kosovo is the fastest growing country in the region, and strong growth is expected to stabilize at about 4.2 percent in 2018.*
- *Fiscal deficit is projected to increase due to higher public investment, mainly infrastructure, and untargeted social protection spending, will remain within the fiscal rule.*
- *Growth is projected to reach 4.5 percent in 2019-2020, but the outlook is vulnerable to external and domestic (including political) risks.*
- *While the headline fiscal policy has been in line with the fiscal rules, improving the allocation of spending to invest in human and physical capital is essential for faster and sustainable growth.*

Growth in the region strengthened in 2018, driven by public investment

Kosovo: Good growth performance is expected to continue through 2018 with a projected 4.2 percent, supported by public investment, service exports and consumption

Real GDP growth, percent

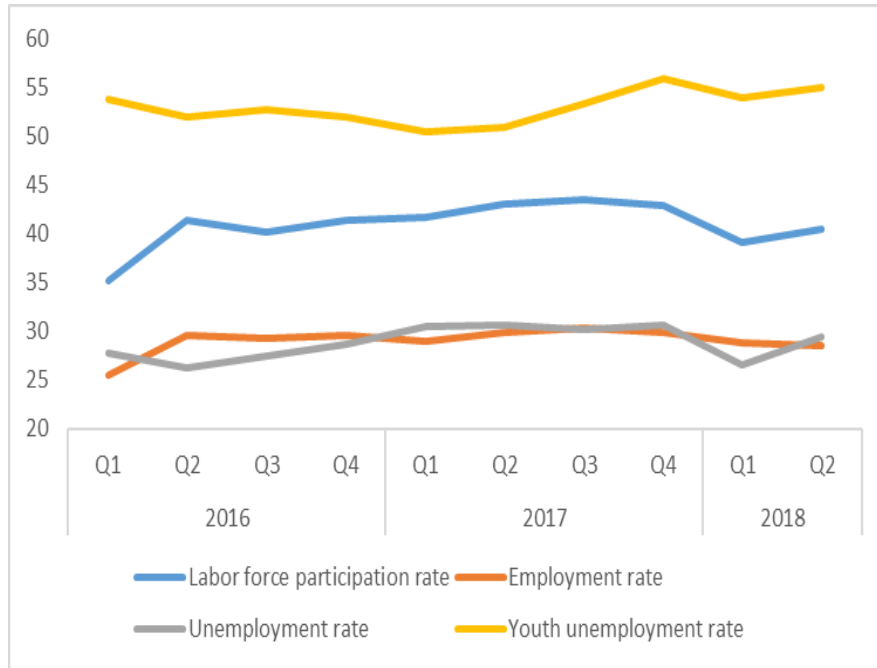


Source: World Bank staff calculations based on data from national statistical offices.
Note Kosovo 2018 data based on SAK recent revision.

Employment recovered to pre-2008 levels across Western Balkans

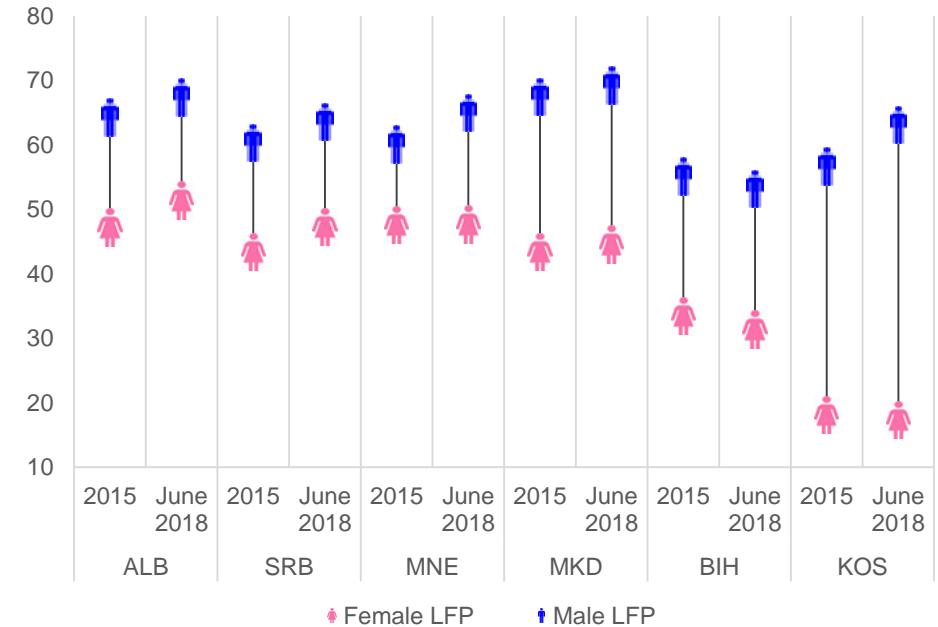
Kosovo: Labor market performance weakens in the first half of 2018.

Labor market dynamics (2016-2018)



Source: National statistical offices and World Bank staff estimates.

Labor force participation, 2015 and June 2018

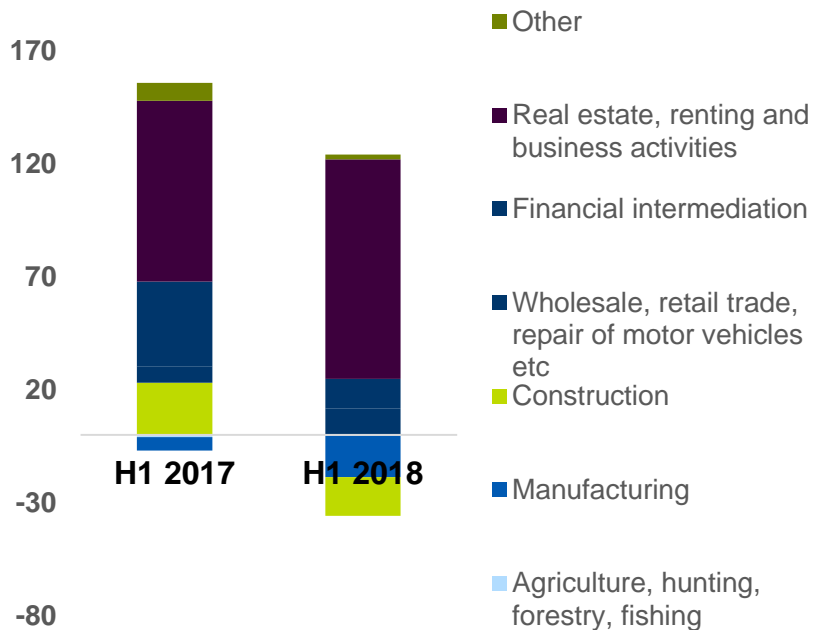


Source: Kosovo Statistics Agency and World Bank staff estimates.

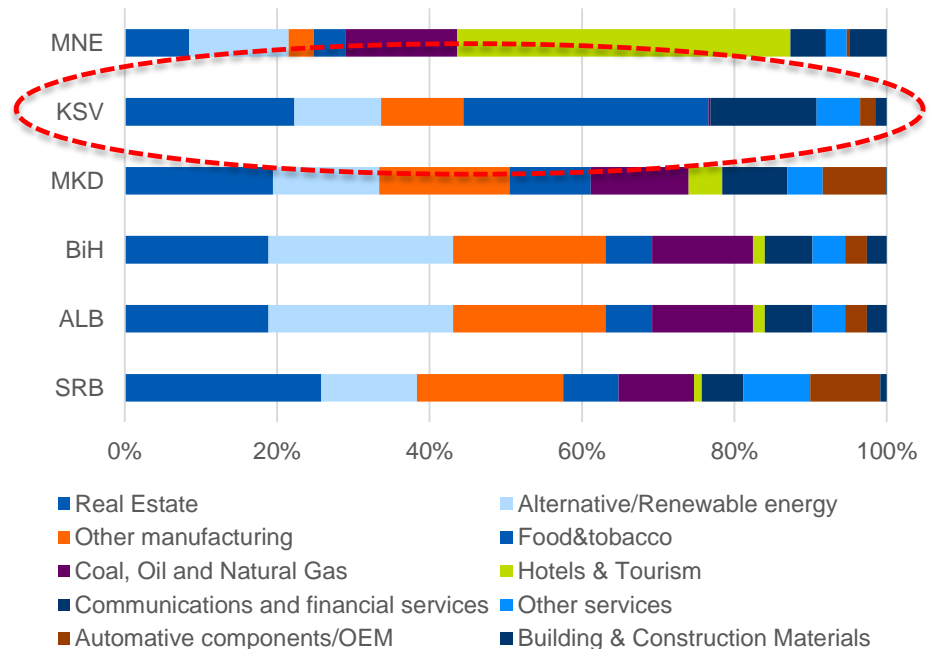
FDI flows continue to finance external imbalances, but FDI is not necessarily growth enhancing

Kosovo: Net FDI inflows fell by 40 percent y-o-y in the first half of 2018 due to weaker firm performance and higher repatriation of profits.

FDI outflows in construction and manufacturing led to a decline in net FDI (million euros)



Greenfield FDI flows in the region are mainly in non-tradable sectors (million euros)

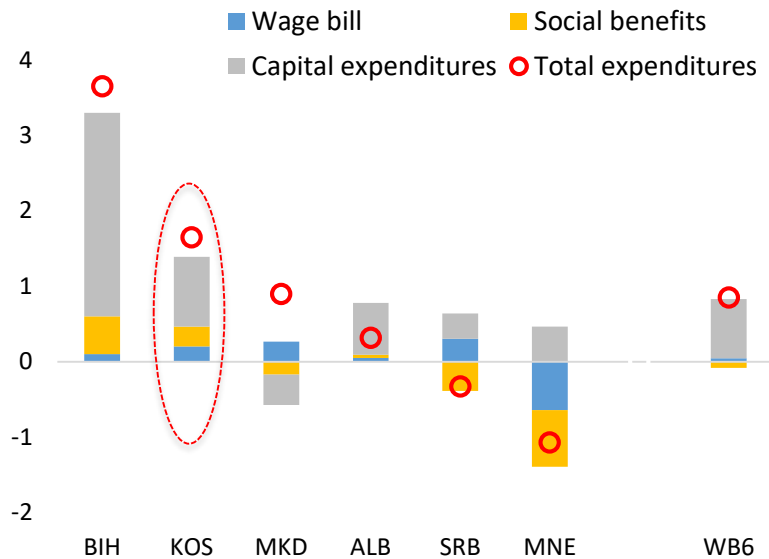


Source: Central Bank of the Republic of Kosovo and Statistics Agency of Kosovo; World Bank staff estimates, FDImarkets data

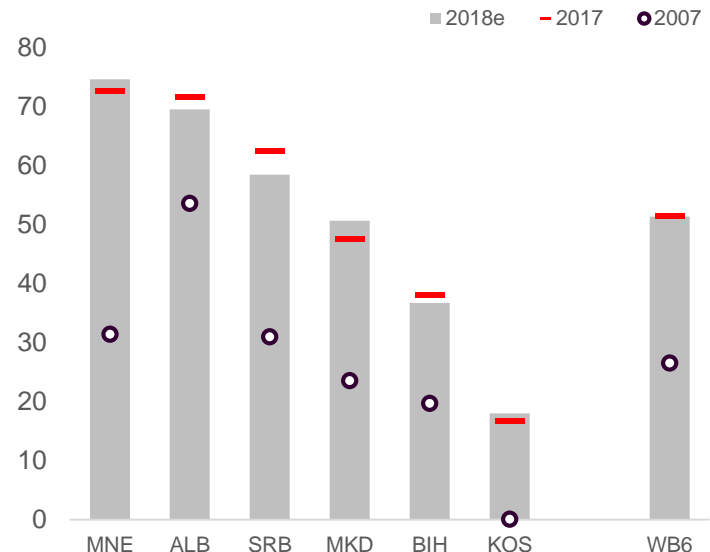
Revenue increases did not contribute to growth-enhancing spending

Kosovo: Higher investment, particularly on roads, and spending on untargeted social benefits and transfers (veterans and pensions) will widen the fiscal deficit. The deficit is expected to be within the fiscal rule.

Contribution to change in public spending 2018, percent of GDP



Public and publicly guaranteed debt, percent of GDP

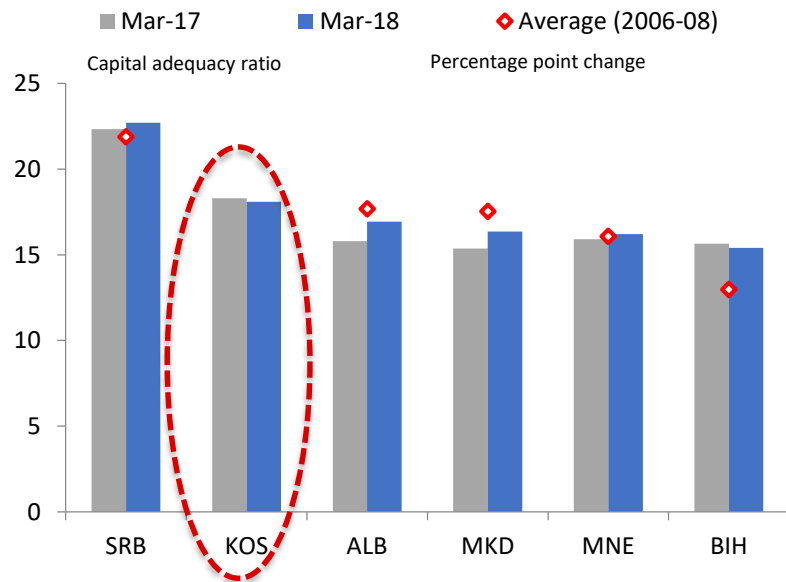


Sources: National statistical offices, Ministries of Finance, World Bank staff projections.

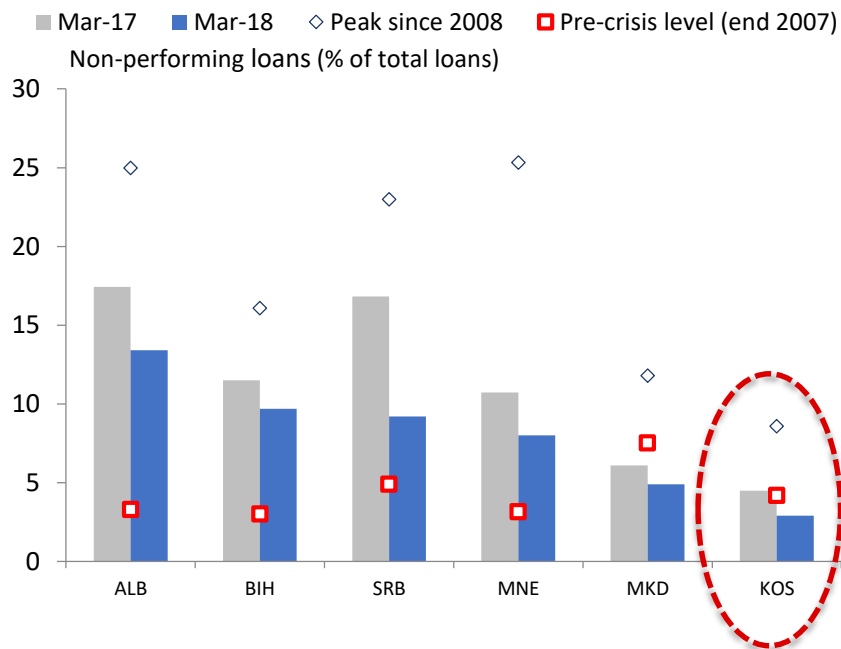
NPLs are declining in WB, while banks remain well-capitalized and liquid

Kosovo: Banks are well capitalized; NPLs are the lowest in the region and continue to decline

Capital adequacy ratio, percent and percentage point



Non-performing loans (% of total loans)



Source: National Central Banks

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POSITIVE NEAR-TERM OUTLOOK

Positive growth prospects, but vulnerable to risks

Real GDP Growth, percent, 2017-20

	2017	2018e	2019f	2020f
Albania	3.8	4.0	3.6	3.5
Bosnia and Herzegovina	3.0	3.2	3.4	3.9
Kosovo	4.2	4.2	4.5	4.5
Macedonia, FYR	0.0	2.5	2.9	3.2
Montenegro	4.3	3.8	2.8	2.5
Serbia	1.9	3.5	3.5	4.0

Source: Data from Central Banks and National Statistical Offices, World Bank staff projections.

Note: *Western Balkans is a weighted average.

Upside risks:

- Better absorption capacity of IFI investments.
- Better performance of exports, due to higher than expected growth in the EU and higher-than-expected base metal prices

Downside risks:

- Political instability.
- Further increases in unproductive spending (untargeted benefits).
- Global decline in trade and capital inflows



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Thank you!