

FOREIGN TRADE AND ECONOMIC GROWTH IN KOSOVO: TRENDS AND SOME FEATURES

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ABSTRACT

The paper presents an analytical overview on some aspects of Kosovo's economic growth, with particular emphasis on the issues concerning Kosovo's Foreign Trade. The purpose of the paper is to analyze trends in Kosovo's foreign trade through various statistical data published by the relevant institutions in Kosovo, in order to see directions and trends of development of exports and imports and trade balance of Kosovo, the obstacles that foreign trade activities are facing, especially those relating to export of goods and services. The data analyzed leads to the conclusion that Kosovo is facing a huge challenge such as large negative trade balance for the entire period observed. Having into consideration that disproportion between export and import is huge and given the fact that exports growth is vital for the economy of developing countries such as Kosovo, the natural and human potential available in Kosovo, which may be mobilized for the economic and export growth, are also analyzed.

Keywords: Kosovo, economic growth, foreign trade, export, import, trade balance

1. INTRODUCTION

The effect of foreign trade on economic growth has been an important subject of debate for several decades. Many prior studies have found a positive relationship between the growth rate of trade and the growth rate of output. It can be said that the positive effects of International Trade on Economic Growth were first pointed out by Smith (1776) and David Ricardo, who argued that international trade plays an important role in economic growth, and that there are economic gains from specialization. It was also recognized that exports provide the economy with foreign exchange needed for imports that cannot be produced domestically.

Exports of goods and services represent one of the most important sources of foreign exchange income that ease the pressure on the balance of payments and create employment opportunities. An export led growth strategy aims to provide producers with incentives to export their goods through various economic and governmental policies. It also aims to increase the capability of producing goods and services that are able to compete in the world market, to use advanced technology, and to provide foreign exchange needed to import capital goods. Exports can increase intra-industry trade, help the country to integrate in the world economy and reduce the impact of external shocks on the domestic economy. Experiences of Asian and Latin American economies provide good examples of the importance of the export sector to economic growth and development, which led economists to stress the vital role of exports as the engine of economic growth.

Kosovo is committed to trade liberalization. Participation in regional and wider trade facilitating mechanisms has been one of the main policy objectives of Kosovo institutions. Enhancing trade in Kosovo through liberalized trade requires three aspects to be in place: import rationalization and replacement, trade facilitation, and export promotion. This is actually the UNCTAD (United Nations Conference on Trade and Development) integrated export strategy which gives equal importance to competitiveness in the domestic market and competitiveness in the foreign market.

However, trade liberalization, in and of itself, is not sufficient to enhance the exporting activity. There are a number of reasons for this; firstly, trade policies should be formulated, implemented, and assessed in a manner,

which prioritizes development rather than international trade outcomes themselves. Secondly, in order for the benefits from trade liberalization to be the highest and most sustainable, not only trade policies, but also trade-related development policies should be understood and well managed. Finally, trade is a cross-cutting concept affecting almost all areas of economic and social life. Therefore, there is an urgent need for improvement in the institutional quality, including the collaboration and coherence among all of the relevant actors that form the trade system in Kosovo.

Kosovo has a liberal trade regime characterized by simplicity and neutrality, key features considered to be important for stimulating private sector led growth as well as creating the conditions for healthy exports. But as trade liberalization has not been accompanied by an improvement in the competitiveness of the emerging domestic production sectors, Kosovo is facing a huge trade deficit. The continuation of this trend will hamper macroeconomic stability and economic growth.

International experience in export development in other countries suggests that measures designed to improve the competitiveness of the economy improve trade performance.

The collapse of the socially owned sector during the 1990s, as a consequence of the forcefully installed administration, as well as the delay in ownership transformation of socially owned enterprises (SOE), resulted in a drastic fall of exports and a loss of foreign markets. In this situation trade was dominated by imports taking into consideration the destruction of key exporting sectors. After 1999, the Kosovo economy was faced with the consequences of war, and achieved a very low level of exports compared to the volume of imports, being continuously and heavily dependent upon imports.

2. SOME FEATURES OF KOSOVO'S ECONOMIC GROWTH

Kosovo's economic growth has been solid since the end of the war in 1999. Kosovo economy has been damaged by the post-conflict uncertainties, broken external trade links, and a long period of insufficient investment in infrastructure and other areas of economic and social life.

Driven by the massive donor-funded reconstruction effort, GDP growth was initially in double digits in 2000–2001, but moderate thereafter, despite continued donor financing and remittances.

The sustainability of this economic performance remains an issue, and as foreign assistance and remittances decline, Kosovo clearly needs to replace these flows with export earnings and foreign investment.

Following the post-war economic boom, economic growth has been both moderate. Between 2005 and 2007, growth averaged around 4 percent and was driven by strong increases in public investments and private consumption, mainly financed through bank loans, remittances, foreign assistance and significant increase of budget expenses. Exports also rose rapidly, but from a very low starting base, so their contribution was more modest. Growth peaked at 5.4 percent in 2008, mainly due to an expansionary fiscal policy, and slowed slightly to 4 percent in 2009. (Table 1)

Table 1. Key Economic Indicators

	2005	2006	2007	2008	2009
Percent change					
GDP real growth	3.8	3.8	4.0	5.4	4.0
GDP per capita	2.4	2.3	2.7	3.8	2.5
Consumption	5.8	2.2	6.1	3.7	2.6
Investments	-6.1	1.3	3.9	15.5	12.6
Exports	8.8	31.9	11.7	4.2	-1.2
Imports	4.1	5.7	11.8	6.0	3.5
CPI, period average	-1.4	0.6	4.4	9.4	-2.4

Source: SOK and IMF

In course of the adoption of the EURO, foreign trade became easier and Kosovo has achieved great progress in terms of maintaining the inflation close to EURO area levels being mainly an import base economy, inflation closely reflects the imports price developments.

The global financial and economic crisis has had relatively little impact on the economy, reflecting Kosovo's limited international integration.

The negative effects of the crisis were transmitted through three channels: exports, FDI, and remittances. Kosovo's exports suffered a sharp decline (about 18 percent) in 2009, also, according to preliminary data, FDI fell by 22 percent and remittances by some 8 percent. The fall in remittance receipts has been lower than anticipated, mostly because Kosovo's migration has been long term in nature: 70 percent of migrants have a foreign citizenship. The banking sector has remained stable, with deposits as well as credit to the private sector continuing to grow in 2009 and 2010. The negative effects of the global financial crisis were offset by the continued expansionary fiscal policy of the government, which has maintained moderate growth rates (World Bank, 2010).

Unlike the region, Kosovo's performance remained solid and its economy outperformed the entire region, growing at 4 percent. As a matter of fact, Kosovo and Albania were the only two economies to record GDP growth in 2009. However, Kosovo needs to significantly accelerate its growth if it is to reach regional income levels. For example, Kosovo's economy would need to grow at 10 percent per annum for a decade to reach Albania's income level (assuming Albania's economy continues to grow by 5.5 percent annually during this period). And to reach Montenegro's current GDP per capita level of €5,700, Kosovo's economy would have to grow at 12 percent per annum for an entire decade (World Bank, 2010).

Macroeconomic stability in Kosovo continues to be challenged by the main problem for the local economy, which is the high unemployment rate (45%) (SOK, 2010c), and which is not being reduced through the current economic growth rate. As a result of the high dependence of Kosovo's economy on the import of goods from abroad, Kosovo continues to be characterized by a high trade deficit, which represents the main cause for the high rate of current account deficit in the country. Despite the growth of exports, the continuous growth of imports caused an increase of the current account deficit during 2011. Kosovo's economy during this year is also facing inflationary pressures, which are more pronounced, compared to the previous year. Inflation in Kosovo was quite volatile in the recent years, reflecting to a large extent the developments of prices in foreign markets, which correlation results from the high dependence of country's economy on imported goods. (CBK, 2011).

Economic developments in the first six months of 2011 suggest that the economic activity in Kosovo is expanding continuously, and as a result, the real economic growth in 2011 is forecasted to be around 5.0 percent (3.9 percent in 2010). In nominal terms, the Gross Domestic Product (GDP) during 2011 is expected to be over euro 4.7 billion. Consumption represents the main GDP component, with a share of around 107 percent of GDP. However, the consumption-to-GDP ratio continues to decrease as a result of the growth of investments in the country, which represent around 35 percent of GDP. The structure of consumption is dominated by the private sector, whereas the public sector consumption recorded a decline. (CBK, 2011).

Trade balance represents the component with a continuous negative impact on Kosovo's GDP, is constantly characterized by a high rate of deficit. During the first half of 2011, the trade deficit in Kosovo amounted at euro 925.4 million which represents a growth of 16.1 percent compared to the same period of the previous year. The deficit increase is mostly attributed the rapid growth of imports in this period, which amounted at euro 1.1 billion euro which presents a growth of 16.5 percent. The growth of imports was also affected by the increase of prices of goods with higher share in total imports. (CBK, 2011).

3. KOSOVO'S FOREIGN TRADE

3.1 Features of Kosovo's foreign trade

Kosovo is an open economy; the share of exports and imports to the GDP (or the market openness, i.e. export + import/GDP) was almost 0.6 in the year 2010 (for previous years the situation does not change significantly). The foreign trade is dominated by imports; the level of export is small resulting in high trade deficit, which represents one of the main characteristics of the Kosovo's foreign trade and one of the biggest challenges for the Kosovo.

Kosovo's foreign trade during the post-war period has had some increasing trends of both export and import. Despite rapid growth of export comparing to import, the low base of exports makes this growth have a relatively small impact on the trade deficit reduction in Kosovo.

Table 2. Flow of goods on foreign trade (000 €)

Period	Export		Import		Trade Balance	Per cent cover
	1	2	3	Chain base index	4=2-3	5=2/3
2001	10 559	-	684 500	-	-673 941	1.54
2002	27 599	261.38	854 758	124.87	-827 159	3.23
2003	35 621	129.07	973 265	113.86	-937 644	3.66
2004	56 567	158.80	1 063 347	109.26	-1 006 780	5.32
2005	56 283	99.50	1 157 492	108.85	-1 101 209	4.86
2006	110 774	196.82	1 305 879	112.82	-1 195 105	8.48
2007	165 112	149.05	1 576 186	120.70	-1 411 074	10.48
2008	198 463	120.20	1 928 236	122.34	-1 729 773	10.29
2009	165 328	83.30	1 935 541	100.38	-1 770 213	8.54
2010	295 957	179.01	2 157 725	111.48	-1 861 768	13.72

Source: SOK, External trade 2010, July 2011, and author's calculations

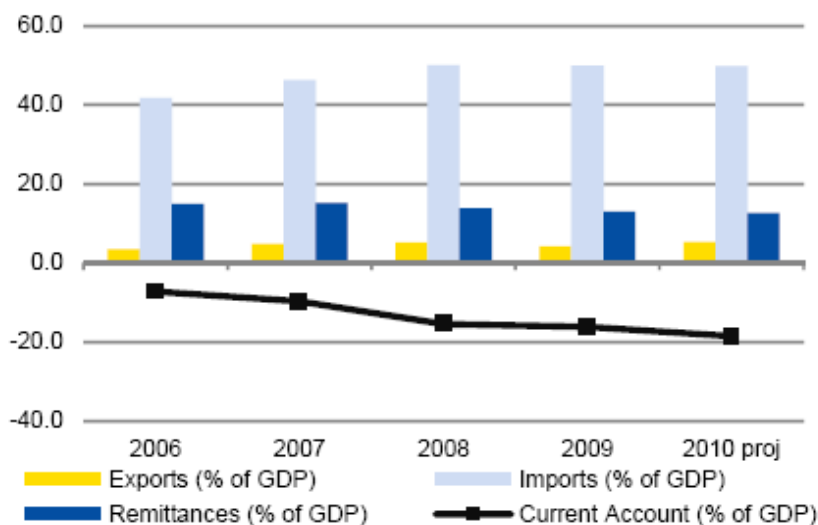
Over a period of ten years exports have marked an increase of 44, 82% on average per annum, whereas in 2009, due to the impact of global financial crisis and fall of prices in the international markets, exports declined by approximately 18% while imports marked an increase of 13,6% on average per annum. The imports growth was slower comparing to the exports growth, the large weight of imports in the general structure of Kosovo's trade continues to neutralize the effect of exports growth. (Table 2)

The annual increase of fuel prices in the international market for about 25.0 percent reflected to a large extent in the amount of total imports, given the fact that mineral products represent one of the main categories of import in the country. (CBK, 2010a).

Even though the import coverage is still very low, it has increased steadily since 2001, reaching double figures in 2007, 2008 and 2010, 10.5; 10.2 and 13.72 % percent respectively (SOK 2010a). A more promising picture would occur if the so-called 'virtual' export is taken into consideration - which includes the consumption of International presence in Kosovo - according to which export covers 20 percent of imports (in the national accounts this part of export is considered as 'export in services'. (MTI, 2009).

Nevertheless, the coverage of imports with exports improved, reaching at 15.4 percent in June 2011 compared to 15.1 percent in the same period of the previous year. Marking an increase of 1.86 billion euro, the trade deficit in Kosovo in 2010 was higher for about 4.6 compared to 2009. As a proportion of GDP, the trade deficit in 2010 marked a slight decline compared to the same period of the previous year, respectively from 45.8 percent of GDP in December 2009 to 45.0 percent of GDP in December 2010. The high level of trade deficit makes the Kosovo's economy be characterized with a high current account deficit rate. In June 2011, the current account deficit amounted at euro 287.1 million.

Fig.1 Current account in percentage of GDP

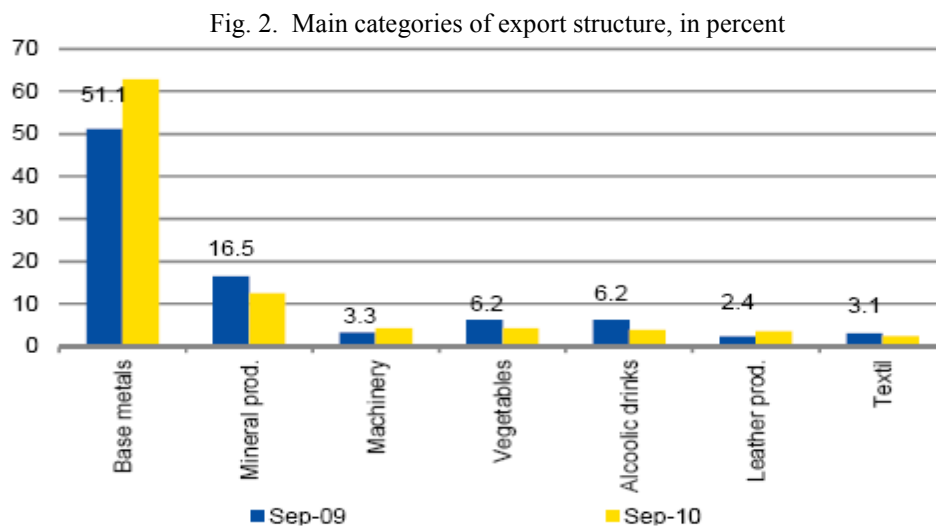


Source: CBK (2010)

The largest component in the current account continues to be represented by goods and services, which is characterized with a relatively large disproportion between imports and exports value. On the other hand, another category with a relatively large share in the current account consists of current transfers, which are dominated by migrants' remittances. This category is characterized with a positive balance and it significantly contributed to the narrowing the current account deficit. (CBK 2011),

3.2 The export and import structure

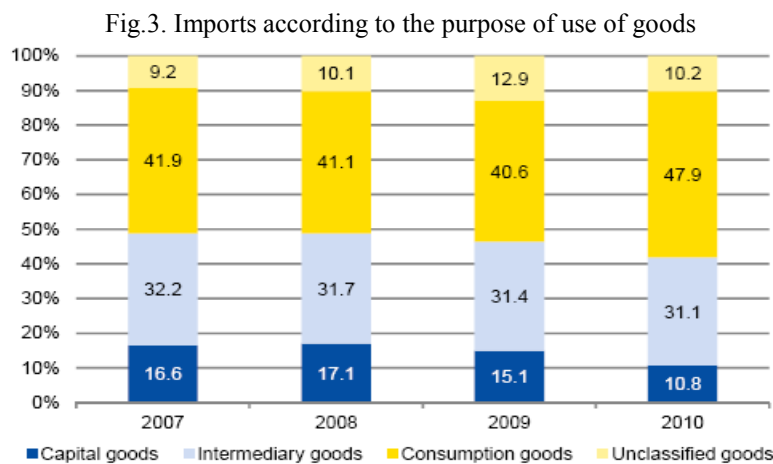
In 2009, Kosovo exports were characterized by a sharp decline mainly due to the global crises contributing to a large extent to industrial metal sale, respectively the nickel ores. Recuperation of the world economy in 2010 contributed to strengthening of the demand for these metals. As a result, the increase in metal prices in 2010 led to the increase in the production and reflected in the sales volume and value. Given that around 90 percent of metals exported from Kosovo are nickel ores, Kosovo exports have marked an annual growth of 77.8 percent in December 2010, reaching at 296.0 million euro.



Source: CBK, 2010

Kosovo **mainly exports** over 60% of base metals, 15% of mineral products, 6% of fruits and vegetables. If data of exported goods are analyzed carefully, one may see a tendency of consistent increase of the export of manufactured goods classified chiefly by material, which share 56.1 % in the total export in 2010 and 11.9% in 2005, whereas crude materials have a tendency to decline by 47,5% in 2005 in 25% in 2010. (SOK, 2010)

The import structure in Kosovo over years has not changed significantly. Usually there are imported consumption goods, machinery and transport equipment.



Source: CBK, 2010

Over years, the import structure was dominated by the share of wide consumption products, where in 2010 there was a significant increase of around 47.9%. The share of intermediary goods is also quite large with over 31% during 2007-2008.

The relatively high share of intermediate goods in the overall imports indicates that the production activity in the Kosovo's economy considerably depends on the import of raw materials from abroad. Also, the increase of the share of consumption goods to total imports continuously indicates a low level of domestic production. The share of capital goods to total imports decreased to 10.8 percent in 2010 compared to 15.1 percent in 2009, in spite of the faster growth of investments in the country during 2010. (CBK 2010b),

In all categories of exported and imported goods a high trade deficit is created reflecting the overall trade deficit. The agro-food trade in Kosovo has also had a very high negative trade balance, reaching the amount of 453 million euro in 2008.

Table 3. Kosovo Agro-food Trade (€ million)

	2005	2006	2007	2008
Imports	285.5	319.4	384.1	473.7
Eksports	7.9	11.6	18.1	20.7
Neto eksports (Eksports minus imports)	-277.6	-307.8	-366.0	-453.0

Source: SOK and Kosovo Customs (2009).

With the decline of agriculture output, Kosovo's agro-food trade deficit has been widening, reflecting a diluted competitive basis. Agro-food imports are large and growing, from €280 million in 2005 to €470 million in 2008, an increase of 68 percent. The value of agro-food exports grew even more rapidly over the same period, from €8 million to €20 million, an increase of 156 percent. But exports are dwarfed by imports, resulting in an agro-food trade deficit that grew to €453 million in 2008.

3.3 Main partners of Kosovo in foreign trade

The main destinations for Kosovo's exports are the European Union and the SEE region. Half of Kosovo's exports go to the EU, and these exports have been rising as a share of the total exports.

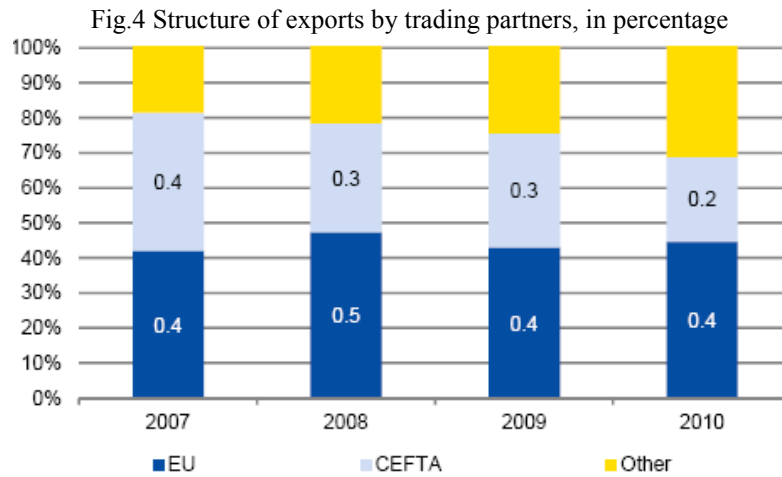
Until 2007, Kosovo products were exported mainly in the region; but since 2007, due to the Autonomous Trade Measurement Agreement between Kosovo and the EU, the main exporting destination became EU. However, the Autonomous Trade Measurement Agreement expired in December 2010 and until now it was not renegotiated. The table below presents the export and import of Kosovo with the region and EU.

Table 4. Export and import with the Region and EU (in 000 €)

Years	EXPORT				IMPORT			
	Region	EU	Total	% EU	Region	BE	Total	% EU
2004	23 510	16 248	39 758	40.87	368 701	378 144	746 845	50.63
2005	26 027	17 285	43 312	39.91	440 334	431 977	872 311	49.52
2006	51 745	28 602	80 347	35.60	536 254	391 335	927 589	42.19
2007	67 500	69 370	136 870	50.68	579 574	572 904	1 152 478	49.71
2008	61 534	93 974	155 508	60.43	717 640	701 982	1 419 622	49.45
2009	53 382	71 275	124 657	57.18	692 465	755 004	1 447 469	52.16
2010	70 933	131 460	202 393	64.95	799 015	821 233	1 620 248	50.69

Source: SOK, External trade 2010, July 2011, and author's calculations

Around 74 % of the trade of Kosovo is realized with EU and CEFTA countries. From EU countries, Kosovo mostly exports in Italy (around 30 %) and Germany (around (4 %), while imports from Germany (around 13 %) and Greece (around 5 %). See the figure below:



Source: CBK, 2011

The recovery of the demand in EU countries, especially in the second half of 2010, made Kosovo exports to these countries record a higher growth compared to export to the region countries.

The noncompliance with CEFTA agreement, for political reasons, by Serbia and Bosnia and Herzegovina continued to obstruct Kosovo's exports to these countries also during 2010. In addition to the problems related to the implementation of the CEFTA agreement, as of end 2010, also Kosovo's status as a favored country for trade with EU has expired, thus presenting another obstacle for Kosovo's firms to penetrate the external markets.

3.4 Barriers on foreign trade development

Reasons for the poor performance of the export sector in Kosovo are many and of all natures; **political, historic and economic**, as presented below:

- The unresolved political status of Kosovo has been a hindrance to Kosovo economic development.
- The post-war Kosovo has inherited industries and companies in almost a total collapse as a result of destruction and theft; Delays and many complications in the privatization process have made even more difficult for them to recover.
- For many years Kosovo was not part of regional initiatives aiming liberalization of trade, mainly due to unresolved political status.
- The level of Foreign Direct Investments (FDI) has not been satisfactorily (insignificant early after the 1999, however, relatively high since 2005), a factor very important in many transition countries in boosting their economies and particularly their export sector.
- Informal economy is also a dimension that should be mentioned which is estimated to comprise about 30-40% of Gross Domestic Product.
- Irregular power supply and limited road infrastructure as part of Kosovo reality.

These problems, which are basically related to the specific reality of the post-war Kosovo, in constellation with the emerging institutions and policies, have hampered the development of the private sector, a sector which should be able to bear the main burden for export.

Currently, the private sector is almost entirely comprised of not very efficient microenterprises, with about 98,7% , small and medium enterprises participate with 1.57% , while only 0.06% of firms are large scale enterprises. (GRK 2011). Inexistence of large scale enterprises in the structure of enterprises in Kosovo has had a direct impact on the low level of export since those are the enterprises that are very active in exporting activities in most countries, as a result of their potential and resources. On the other hand, specifically the absence of large enterprises had an impact on the development of SMEs because the former as they usually comprise a significant share of the demand for SMEs products and services.

In the context of impediments related to economic policies and institutions, one should discuss the tax policy. The latter has continuously caused dissatisfaction among the business community, although facts have often not been argued.

The financial system has also attracted the attention as a hindrance for business development in Kosovo. In the context of enterprise development and in relation with the financial system, is law enforcement (particularly contract enforcement) which serves as a major impediment.

Then, in the context of export sector, it should be noted inexperienced customs service, the complexity of reimbursement procedures of the value added tax (VAT), underdeveloped institutions for quality assurance, and other impediments.

In addition, the flow of Kosovo's export has been hampered by the measures and instruments applied in the trade policies of other countries; Kosovar exporters were forced to face the tariffs charges (for example, transit taxes) as well as nontariff charges (such as subsidies). Particularly, the latter were prevalent and have taken different forms and have contributed to the decline of exports with regard to agricultural products.

4. KOSOVO'S POTENTIAL FOR ECONOMIC DEVELOPMENT AND EXPORT GROWTH

Kosovo's economy is small, even at the regional level, and long-term development prospect will depend highly on **development of its export potential**.

Much more is needed to set Kosovo on a sustainable path. Increased export competitiveness, however, cannot come about through exchange rate policy because Kosovo uses the euro as its currency.

Kosovo will thus need to use its assets for higher and sustainable growth: its considerable supply of physical and human capital, much of which is sitting idle, as well as its favorable geographical position.

The richness in natural resources, the abundant labor force, as well as the access to the regional and European market, offer great potential for economic growth.

Kosovo is very rich with mineral deposits, however, their potential has been left untapped for various reasons. Kosovo's soil has abundant deposits of lignite, ferronickel, lead, zinc, magnetite, and other ores. Developing these industries could make a major contribution to economic development through employment and exports. Prior to the dissolution of the former Yugoslavia, the mining sector was an important growth engine for Kosovo's economy. However, the mining capacities suffered from neglect during the 1990s, as well as from war damage. (ASAK 2002),

The abundant lignite resources, estimated to exceed 10 billion tons, have the potential to make the energy sector a key contributor to growth stimulating employment and its accompanying economic activity, as well as possibly exports (if the capacity of the new power plant is higher than the domestic demand).

Other untapped resources include lead, zinc, and magnesite. Kosovo is also well endowed with lead and zinc deposits which is estimated to be about 38 million tones and its utilization may last for more than 20 years. The lead-zinc company Trepça was the largest mine in the former Yugoslavia and included integrated mining and manufacturing operations. The mine continued to operate as a state-owned company in the 1990s, but operations were halted in 2000, mostly for political reasons, but also for environmental reasons. Despite donor efforts to rehabilitate the mines with the intention of resuming operations, the mines remain idle. (ASAK 2002). Reviving the mining sector will require substantial investment and can only be accomplished by relying on foreign investors, and possibly some domestic private investors.

Agriculture land has also been underutilized, despite the favorable soil and weather conditions. Agriculture has traditionally been an important economic activity in Kosovo, accounting for as much as a quarter of total output. The transition process, underinvestment, and war led to a sharp decline in the sector. Its share in total output has fallen to about 12 percent in recent years.

Though some progress has been made in land privatization, land use remains low, and the dissolution of the large state-owned agriculture enterprises has created new obstacles to developing the agriculture sector.

Farmland use has also been hampered by poor property rights and inadequate or nonexistent land-zoning rules. (MAFRD 2010).

Kosovo's labor force could be another important potential source of growth. Kosovo has the youngest population in Europe: one-third is estimated to be under the age of 15, about half is under the age of 24, and

only 6 percent of the population is older than 65 years (SOK 2011b). Unfortunately, much of this human capital has been idle for a long period.

One key asset for Kosovo is that its wages are competitive in comparison to most countries in the region. By mid-2009, the average monthly wage in Kosovo's private sector reached €300, about half of the average salary in the high-wage countries of the region. (SOK 2010c).

Relatively low wages in Kosovo are partly explained by the difference between net wages and gross wages, which is smaller compared to other countries in the region.

This competitive advantage should play an important role in promoting export in Kosovo and attracting export-oriented foreign investments. But productivity is the second and equally important element of the labor competitiveness equation.

Kosovo's wage competitiveness comparing to countries in the region is very strong in low-skill sectors, but much less in high-skill sectors due to the high skill premium. So, in the short to medium and short term plan, Kosovo's focus should be on attracting more foreign investment into low-skill, labor-intensive, export-oriented sectors. The low wages of low-skilled labor give a competitive edge also to domestic exports, which could enable higher export growth once other constraints are addressed. However, basing competitiveness on low costs and unskilled labor-intensive activities will not be a viable strategy for the long term and for achieving EU convergence. Improved education attainment and workforce skills, hence productivity, are fundamental for achieving high and sustainable growth. (World Bank 2010).

Kosovo has the advantage of free and relatively easy access **to its two most important markets: the regional (CEFTA) economies and the European Union.** Kosovo is part of the regional CEFTA market, which enables it to access customs free a market of over 20 million consumers and a GDP of about €120 billion. The CEFTA market offers free trade in manufactured goods and most agriculture products. It also envisages full liberalization of agriculture trade as well as liberalization in services. To fully utilize the potential of the regional market, Kosovo, as well as the other CEFTA countries, needs to address the remaining non-tariff constraints to greater regional trade integration.

The free trade access to the EU market opens up even larger possibilities for Kosovo's products. For almost a decade now, the European Union has been granting duty-free access for all of Kosovo's products, with some limited exceptions (for example, beef and sugar). The trade relationship between Kosovo and the European Union is asymmetrical, and EU products enter the Kosovo market under its most favored nation (MFN) tariff regime. It would be useful for Kosovo to have a free trade agreement with the European Union because the current agreement prevents Kosovo from entering into diagonal arrangements with other CEFTA countries.

The free trade access to the EU and SEE markets is complemented by Kosovo's geographical proximity to these countries. Kosovo's central position in the Balkans and its relatively close proximity to the main European markets (for example, Germany and Italy) and the port of Thessaloniki are important to its competitive advantage for sectors that outsource production and require just-in-time delivery. The importance of the regional market for Kosovo is special for the fact that factors related to language, culture and common history will remain important for trade exchanges between some countries of the region of Balkans. Then, low transport costs, joint participation in the integration initiatives, and the common goal of joining the EU, are the factors that should be taken into consideration in the future trade relations of Kosovo with the countries of the region.

5. FOREIGN TRADE POLICIES OF KOSOVO

Reducing trade imbalances is necessary for long-term economic growth in Kosovo. An export-lead growth strategy should be considered as a key factor in building up an open and free market economy and in reducing the huge imbalances of Kosovo.

On the basis of the East Asian experience and the experiences of advanced transition countries it was argued that the essential requirement for export promotion is an integrated export strategy that emphasizes that competitiveness in the domestic market is of equal importance to competitiveness in international markets.

The UNCTAD approach to export policy identifies three elements in an integrated export policy. The first element is a range of so-called “border-in issues” that emphasize measures that can be adopted to increase the competitiveness of companies in the domestic market.

The second element is a range of so-called “border issues” – measures designed to improve the procedures at borders and to reduce the transaction costs facing businesses when they cross borders. These are sometimes referred to as “trade facilitation” measures”.

The third element encompasses the so-called “border-out issues”. These are the traditional export promotion policies that focus on improving the performance of domestic enterprises in foreign markets through the provision of market information, partner-search measures such as trade fairs and trade missions, marketing and publicity for exporting enterprises, the creation of export websites and exporter databases, training in export techniques and procedures, and other similar export promotion measures. (Rinvest, 2003).

An essential part of creating a competitive export-led economy is the creation of a strong domestic base of competitive enterprises.

The first step in an effective export strategy should be to improve the competitiveness of the economy’s enterprises in the domestic economy. The reason for this is simple enough. *Firstly*, by successfully competing against foreign and local competitors in the local domestic market, enterprises can develop their competitive capabilities.

Secondly, by operating successfully in the domestic market and increasing their market share, Kosovar enterprises will increase their scale of production, reduce unit costs and hence become yet more competitive as a result.

Thirdly, the policy instruments which need to be developed to support competitive domestic producers on the home market will also be needed to support successful businesses when they decide to enlarge their market share by competing in export markets. Therefore focus on developing the small-scale private sector needs to be given priority.

The advantages of an integrated export promotion policy should be apparent through an acceleration of the processes toward substantial progress in the areas of: Small and Medium Enterprise development; Foreign Direct Investment promotion; Privatization of Social and Public Enterprises.

In addition to the turning point in advancing economic policies in favor of the export industry in Kosova, a number other measures are needed to coordinate the activities of the different stakeholders involved in export development, such as: the Government, the business community and its associations, banks, donors and different international organizations that operate in Kosova.

The Government of Kosovo has officially endorsed Kosovo Trade Policy document in August 2009, which gave the main orientations of the trade policy of Kosovo and of the foreign trade policy particularly. Based on this strategic document Kosovo is committed to trade liberalization and foreign trade policy integration, which requires three aspects to be in place: import rationalization, trade facilitation, and export promotion. (MTI, 2009).

6. CONCLUSIONS

Imbalances in foreign trade generate macroeconomic disproportions with long-term implications for economic growth and macroeconomic sustainability in Kosovo. Therefore, alleviating such disproportions should be a long-term priority.

Kosovo has a very low export base – 10 times less than import – and export is very concentrated. In the regional market and European Union market, Kosovo is competing with other Eastern Europe countries, which not only have the strong exporting sector, but also a better climate of investments, an essential element to attract export oriented FDIs.

Furthermore, authorities cannot use the currency exchange policy to put Kosovo exports in a better competitive position.

Improvement of the competitive position of Kosovo export will require **investments in infrastructure, improvement of the legislation and institutional capacity building**, including:

- Investment in transport infrastructure to cope with increasing demands;
- Increase of the efficiency of trade related institutional infrastructure;
- Development of “**quality infrastructure**”(standardization, accreditation and meteorology) to ensure the product meets the requirements of international and European Union standards.

In an increasingly globalized world, the success in export markets is increasingly affected by the ability of governments to support an environment which promotes efficient and low cost trade services and logistics. Economic policies aimed at overcoming this situation should focus on increasing the manufacturing of goods and services, competitiveness and export promotion.

The design and implementation of an integrated export promotion strategy requires the coordination of activities by the Government, business associations and other stakeholders in several important areas.

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