RECENT POLITICAL, ECONOMIC, AND SECTORAL DEVELOPMENTS

Political Developments

Kosovo is a potential candidate for European Union (EU) membership. In October 2012, the EU confirmed in its Feasibility Study—an inventory of the country’s political, economic, and legal environment—that there was no legal obstacle and Kosovo was ready to open negotiations on a Stabilization and Association Agreement (once four short-term policy priorities were met). In parallel, the European Commission (EC) has opened a visa liberalization dialogue. The International Steering Group agreed to end Kosovo’s “supervised independence” on September 10, 2012, closing the International Civilian Office, which had acted in the role of final authority regarding the interpretation of the Ahtisaari Plan.

Kosovo’s unresolved status issue remains a key obstacle to its attaining the overarching objectives of political integration and socioeconomic development. By mid-September 2012, 90 UN member countries had recognized Kosovo’s independence, including 22 EU member states. However, Serbia continues to regard Kosovo’s territory as a UN-governed entity within its sovereign territory. At present, UN membership seems improbable over the near term, given that only three out of five permanent members of the UN Security Council, and less than the required two-thirds majority of the currently 193 UN member states represented in the General Assembly, have recognized Kosovo. Against the backdrop of smoldering tensions and periodic eruptions of violence in the Serb-majority municipalities north of the Ibar River, related status issues are being placed onto the (geo-)political agenda, albeit without a clear perspective for a political resolution anytime soon.

Economic Developments

Kosovo has weathered the euro crisis fairly well, with economic growth rates consistently above those in neighboring countries, relatively strong fiscal fundamentals, and a healthy banking sector. The government focuses its reform efforts on (i) reducing the high rates of unemployment and poverty; (ii) strengthening public institutions and infrastructure; and (iii) improving the business and investment climate.

Growth and External Performance

Kosovo’s economic growth has been steady and generally at rates above those in neighboring countries (figure 1). The average growth rate of 4 percent during 2009–12 has largely been attributable to public investments in post-conflict reconstruction, donor assistance, and remittances. The particular structure of Kosovo’s economy—with limited financial linkages and a small export base—has implied that, similar to the aftermath of the global crisis in 2008–09, spillovers even from the worsening Eurozone crisis have been less severe than in neighboring countries. In particular, remittances (recorded as “transfers” in the balance of payments), foreign direct investment (FDI), and other non-debt-creating flows from Kosovars living in Germany and Switzerland are expected to remain relatively stable. FDI inflows—covering close to 60 percent of the current account deficit (figure 2)—are expected to surge over the medium-term horizon, reflecting considerable investor interest in the telecommunications and energy sectors.

However, Kosovo’s current growth model is unsustainable over the longer term. Increasing private sector activities and investments will become more and more critical as engines to generate growth and, in turn, improve job and income perspectives. To date, the productive base in Kosovo’s economy has remained narrow, despite some progress in recent years. The buoyant increase in exports during 2010–11 could not be carried over into the first half of 2012, having declined by 19 percent compared to the same period in 2011. This development was mainly due to the falling prices of base metals, Kosovo’s main exports. However, because of the low degree of export reliance, the impact of this decline on economic growth will be limited. In any case, exports have not reached a level that would be required to transform the economy.

For the most part, companies in Kosovo are not yet in a position to compete successfully in local and international markets. Reflecting binding public infrastructure and business climate constraints, domestically produced goods,
including in the agricultural sector, have not yet been supplied at the quantity and quality required to compete successfully in either the domestic or foreign markets. Thus, imports have grown more rapidly than exports, resulting in a gradually widening current account deficit to a range of about 15–20 percent of GDP in 2011 (figure 3).

**Figure 1. Real GDP Growth Rates, 2009–12**

![Image](image1.png)

*Source: Country authorities; IMF; and World Bank staff estimates.*

**Figure 2. Current Account Deficits and FDI**

![Image](image2.png)

*Sources: Central Bank of the Republic of Kosovo (CBK); IMF; and World Bank staff estimates.*

**Fiscal Policies**

Kosovo has managed to maintain healthy public finances and protect the fiscal space for public investments. During the second half of 2011, the government reined in election-related fiscal slippages and succeeded in limiting its overall 2011 fiscal deficit to 1.9 percent of GDP. With a budgeted deficit of 2.7 percent of GDP for 2012, which would increase the stock of public debt to 8.9 percent, Kosovo’s euroized economy is better positioned than most countries in the region (figures 4 and 5). The government anchored these fiscal achievements in an agreement with the International Monetary Fund (IMF) on a 20-month, €107-million Stand-By Arrangement, approved by its Board in April 2012. Within the program context, the government has sought IMF assistance in preparing the potential adoption of a fiscal rule that would ensure Kosovo’s long-term fiscal sustainability.

**Figure 3. Balance of Payment, 2007–11**

![Image](image3.png)

*Source: CBK; IMF; and World Bank staff estimates.*

**Figure 4. Fiscal Performance, 2009–12**

![Image](image4.png)

*Source: Ministry of Finance; and IMF and World Bank staff estimates.*

**Figure 5. Western Balkans: Deficits and Debts**

![Image](image5.png)

*Source: National authorities; and World Bank staff estimates.*
Legislative and financing constraints have already defined limits to the extent that government can pursue expansionary fiscal policies. To prevent public debt from rising to unsustainable levels, Kosovo has (i) adopted a public debt law that sets the maximum public-debt-to-GDP ratio at 40 percent; and (ii) stipulated in its Constitution that external borrowing by government (including highly concessional International Development Association [IDA] credits) requires parliamentary ratification with a qualified majority. Until end-2011, the public debt stock was entirely external. In 2012, short-term domestic debt was introduced. As commercial banks are not allowed to hold government securities in lieu of reserve requirements, the Ministry of Finance managed to sell nine €10-million issues of 3-month, and one €20-million issue of 6-month, Treasury bills during the first eight months of 2012. Signaling increased confidence in the Government’s fiscal position (and reflecting banking sector liquidity), yields gradually came down from 3.5–4.0 percent in the first quarter of 2012 to 1.8 percent in September.

Nonperforming loans (NPLs), though having increased marginally, remain lower than in neighboring countries. Between December 2011 and July 2012, NPLs rose from 5.9 to 7.0 percent. With loan-loss provisions against adversely classified loans having remained adequate (at 117 percent at end-2011), NPLs have had a limited impact on the banks’ ability to provide credit, and have not led to a decline in bank profitability. As a result, banks have been able to increase their profits, according to the Central Bank of the Republic of Kosovo (CBK), by 12.8 percent to €37 million in 2011.

Monetary Policies and Financial Sector

The banking sector has proven astonishingly resilient to the deterioration of the external environment—principally in consequence of its conservative outlook and risk-averse lending decisions. The largely foreign-owned commercial banks have remained well capitalized, liquid, and profitable. During the first seven months of 2012, Kosovars entrusted the banks with an average of €2.1 billion in deposits, an increase of 8.9 percent relative to the same period in 2011, while borrowing €1.7 billion (+10.7 percent) from the local banks. The average loan-to-deposit ratio increased marginally from 79.7 percent during January–July 2011 to 81.6 percent during the same period one year later (Figure 4).
The CBK and Finance Ministry have maintained their focus on preserving and strengthening banking sector stability. Among other reforms, (i) €46 million from treasury deposits have been earmarked for the “emergency liquidity assistance” fund; (ii) a Deposit Insurance Fund established; and (iii) a new law on banking, microfinance, and non-bank financial institutions approved by parliament in April 2012.

**Rule of Law and Business Climate**

To improve its growth perspective, Kosovo will need to continue to focus its efforts on strengthening the rule of law. An inviting business and investment climate is particularly important for a euroized economy with limited or no access to fiscal and monetary policy instruments. Since mid-2011, Kosovo has made significant progress in strengthening the basic legal framework and institutional structures, with a view to reinforcing the necessary foundations for a functioning market economy. These reforms (partially supported by World Bank-financed projects and a multi-donor, World Bank-led budget support operation) should begin to help improve the—thus far still unimpressive—rule of law and business climate indicators (figure 9). Notwithstanding the fact that several features in the overall business environment compare favorably to those of Kosovo’s neighbors (such as flexible labor markets, an open trade regime, and a healthy banking sector), weak institutional capacity, unclear property rights, and a complicated and fragmented licensing regime continue to create disincentives for formal private sector activities.

The Government made reforms to enhance the business environment a policy priority, aimed at improving *inter alia* its disappointing ranking (117/183) in the World Bank Group’s *Doing Business* survey. Although in a number of areas, investment climate indicators are better than the averages for the Western Balkans and the EU10+1 countries (figure 10), other constraints constitute considerably higher hurdles for businesses. In response, a task force—established to coordinate corresponding reform efforts—has sponsored amendments to business organizations and internal trade laws to reduce registration costs, simplify procedures, eliminate work permits, and wave charter capital requirements for limited liability companies. The Government has also taken measures to speed up business registration through the establishment of one-stop shops that have, *inter alia*, integrated business registration, value added tax (VAT), and fiscal numbers into one document. All of these reforms were undertaken after the relevant cut-off date for the 2011 *Doing Business* survey and, as such, have not been reflected in the figures below.

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1 Getting credit, resolving insolvency, paying taxes, and registering property.
2 Protecting investors, construction permits, starting a business, enforcing contracts, cross-border trade, and getting electricity.

*Figure 9. Rule of Law and Business Climate*

*Figure 10. Subcategories of Doing Business*

*Poverty and Unemployment*

With per capita GDP estimates of around €2,600, Kosovo is one of the poorest countries in Europe. With almost 35 percent of its
population of 1.8 million living on less than €1.55 per day, and 12 percent of that population living on less than €1.00, poverty is widespread. However, Kosovo has a relatively low Gini index and flat consumption distribution. No significant differences exist between urban and rural poverty, but there are notable regional differences. Extreme poverty is disproportionately high among children, the elderly, households with disabled members, female-headed households, and certain ethnic-minority households (especially in the Roma, Ashkali, and Egyptian communities). As in many other countries, there is a strong negative correlation between education and poverty.

Widespread unemployment and a lack of quality jobs have contributed to poverty and income insecurity. With an estimated unemployment rate of above 40 percent and an employment rate of only 29 percent, Kosovo has the weakest employment record in Europe. Kosovo’s 53-percent labor force participation rate among the working-age population is substantially below the 65-percent average estimated for the countries represented in the World Bank’s Europe and Central Asia (ECA) region. The lack of jobs has direct consequences on income. Households with unemployed heads have the highest extreme poverty indices. In addition, many households with adult members in precarious or unsteady jobs are below the poverty line and depend on small, informal enterprises offering uncertain employment for the majority of their income.

Kosovo’s difficult labor market conditions have been especially severe for youth and women. Estimates suggest that unemployment among 15–25-year-olds exceeds 75 percent. The generally poor quality of the education system, coupled with limited employment opportunities, makes it difficult for young people to access and retain jobs; young people who do succeed in finding employment are typically hired into low-skilled, low-productivity positions, often in the informal sector. According to survey data, about 20 percent of employed youth did not have an employment contract, 37 percent were not entitled to paid leave, and 73 percent were not registered in the social security system. At 56 percent, unemployment is very high among Kosovo’s women. There are large differences in female/male employment rates, with 11 (68) percent of working-age women (men) being employed.

**Education**

Kosovo’s education system does not yet provide its nearly one-half million students with adequate curricula and instruction to produce the skills that the evolving labor market requires. It needs to improve quality and relevance throughout the system and address access issues at secondary and postsecondary levels, where students from the poorest households and women/girls from all income quintiles are underrepresented. About 45 percent of businesses surveyed reported difficulties in recruiting skilled workers, while more than 50 percent of unemployed men cited the lack of appropriate education and skills as a reason for their inability to find work. Kosovo’s school infrastructure is insufficient, with more than one-half of schools operating on double shifts and about 5 percent on triple shifts. School and university management is generally weak, particularly with respect to the monitoring of enrollment, performance, and institutional finances.

The government is placing a high priority on strengthening the education system. The Ministry of Education, Science and Technology (MEST) has developed the Kosovo Education Strategic Plan (KESP) and an associated Action Plan for 2011–16. The strategy tackles all levels of education and addresses issues of quality, access, management, and implementation. In 2011, key legislation was approved and enacted (Laws on Pre-University and Higher Education), and reforms in improving the monitoring and allocation of institutional finances were implemented. In addition, the National Curriculum Framework (NCF) was revised with the intention of redirecting teaching from subject-based to competency-based curricula to provide

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3 The census from April 2011 revealed that the population of Kosovo (even when adding the estimated number of residents in northern Kosovo) is smaller than previously estimated, resulting in higher than previously estimated per capita GDP figures.

4 These figures are based on 2009 data, the quality of which causes some observers to question the estimates of the (un)employment rates for not sufficiently taking into account underemployment or informal or seasonal employment.
students with transferable skills. A teacher career system is being developed to assess performance and improve career opportunities. Instruments for student assessment and examination are also being developed and improved. Finally, school infrastructure standards are being upgraded and school capacities increased. However, moving towards universal access to secondary education requires additional efforts to increase the access of girls and women to secondary and postsecondary education and significantly raise enrollment. Similarly, attention needs to be paid to ways of raising secondary school enrollments for children from the poorest households, of which only about two-thirds currently attend schools at that level.

Energy and Mining

Businesses regard the unreliable electricity supply as a major obstacle to their operations and a constraint to investment and business expansion. Demand for energy has been growing rapidly in Kosovo over the past decade, with considerable variances in hourly and seasonal peak demand (figures 11 and 12). Actual energy consumption and peak demand has grown by more than 90 percent during 2000–10, despite being constrained by supply limitations and consequent frequent load shedding. Most of Kosovo’s domestic electricity generation comes from two outdated, inefficient (and highly polluting) thermal power plants (TPPs). Additional supply—amounting to 5–17 percent of annual consumption over the past decade—has been derived from unreliable (and generally very expensive) electricity imports from an altogether energy-starved region.

As a signatory to the Energy Community Treaty, Kosovo is obliged to decommission one and rehabilitate the other TPP by 2017. To address the energy supply and corresponding environmental challenges, the Government—in close collaboration with the World Bank and other development partners—has developed a multipronged strategy aimed at (i) ensuring adequate and reliable energy supplies; (ii) reducing the need for public subsidies to energy; (iii) limiting the environmental externalities; and (iv) attracting the private sector for generation and distribution. In addition, Kosovo seeks to step up payment enforcement, adjust tariffs to levels consistent with full cost recovery, and invest in energy efficiency and energy alternatives.

Several studies of Kosovo’s energy options have been conducted over the last decade. Most recently, the World Bank conducted a study entitled Development and Evaluation of Power Supply Options for Kosovo to assess ways of meeting current and future energy needs and balance corresponding economic, financial, and environmental costs. The study found that the lowest-cost reliable energy supply that would meet Kosovo’s base load and peak demand was a mix of thermal and renewable sources of energy (figure 13).

Kosovo is very rich in mineral deposits, although their potential has been left largely untapped. Apart from 10.9 billion tons of exploitable lignite reserves, the country has abundant deposits of ferronickel, lead, zinc,
magnetite, and other ores that—if developed—could make a major contribution to employment and exports. Prior to ex-Yugoslavia’s dissolution, the mining sector had been an important growth engine for Kosovo’s economy, but the capacity suffered from neglect during the 1990s, damages caused by the war, and the unresolved political status of the four Serb-majority municipalities in northern Kosovo.

Figure 13. Simulated Energy Mix 2010–25


Public Infrastructure

The transport system is inadequate for business and trade needs and incompatible with European standards. As a landlocked country, Kosovo’s economy is dependent on adequate road transport and its integration with the networks of neighboring countries. At present, the costs for transporting goods from and to Kosovo are among the highest in the region and hence, a major deterrent to greater trade integration and the development of export-oriented businesses. In this context, the Government has embarked on major road investments, notably the ongoing construction of a €660-million motorway to Albania (and access to international ports) and plans for another route to FYR Macedonia, Kosovo’s largest trading partner. Within Kosovo, the road network density (3.3 kilometers per 1,000 people) lags behind the ECA average (8.6 kilometers per 1,000 people) and quality is poor due to shoddy construction and inadequate maintenance. The rail network is in slightly better condition, but only because the limited traffic meant that the inadequate maintenance led to a relatively slower rate of deterioration.

The urban transport network is showing considerable signs of strain. The population of Pristina has doubled over the last decade. There are an estimated 80,000 registered vehicles in the city, and some 200,000 vehicles operating within the municipal boundaries on any given weekday. There is a severe parking shortage in the city center. In addition, the urban public transport system offers an unreliable, low-quality service, and the physical condition of the buses—irrespective of whether they are operated by private or public companies—is poor. In addition, buses stop anywhere to pick up passengers, further exacerbating congestion and road safety conditions. There is also no coordination between the various companies, no route integration, and no common ticketing or information systems.

Not surprisingly, road safety remains a major economic and public health problem. During 2003–05, there was an average of 8,633 accidents (with an average of 152 fatalities) on an annual basis. However, this figure obscures the fact that the number of accidents showed a steady increase over this period from 5,416 in 2003 to 13,917 in 2005. This trend is expected to continue with further increases in car ownership and use. The fatality rate per 10,000 vehicles—at 9.5—is more than nine times higher than in the “safest” EU member countries. Moreover, the traffic accident figures in Kosovo are likely to be underestimated, reflecting generic underreporting problems. The economic cost of road traffic accidents has been estimated to amount to about 1.2 percent of GDP.

Environment and Water

Air pollution is a significant problem, especially in Kosovo’s urban areas. Principal sources of contaminants are sulfur dioxide (SO2), nitrogen oxide (NOx), ozone (O3), lead (Pb), carbon dioxide (CO2), suspended particles (dust), and dioxin. Urban ambient air quality is particularly poor in and around Pristina, Obiliq, Drenas, and Mitrovica. The principal sources of pollution include (i) energy and mining production activities; (ii) the burning of wood and lignite for household heating purposes; (iii) smoke and
emissions from large industrial complexes; (iv) landfills for urban and industrial waste; and (v) vehicular emissions. Estimates contained in the recent Country Environmental Analysis have sought to quantify the economic costs of pollution in Kosovo.

Table 1. Costs of Pollution

<table>
<thead>
<tr>
<th>Pollution/contamination</th>
<th>Annual cost (percent of GDP)</th>
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</thead>
<tbody>
<tr>
<td></td>
<td>low</td>
</tr>
<tr>
<td>Total estimate</td>
<td>2.9</td>
</tr>
<tr>
<td>Outdoor air</td>
<td>0.9</td>
</tr>
<tr>
<td>Lead, heavy metals</td>
<td>1.0</td>
</tr>
<tr>
<td>Solid waste</td>
<td>0.5</td>
</tr>
<tr>
<td>Other</td>
<td>0.6</td>
</tr>
</tbody>
</table>


Key health impacts from air pollution are related to the high levels of particulate matter (PM). During 2010–11, the monthly average PM concentration in Pristina fluctuated between 40 and 130 µg/m³—i.e., almost always above the 40 µg/m³ average concentration deemed acceptable by the EU and consistent with human health. The key sources of fine particle emissions in Pristina and neighboring communities are the antiquated power plants (picture 1) and household use of wood and coal heating during winter. High PM levels are responsible for increases in cardiopulmonary and lung cancer mortality (in cases of long-term exposure), chronic bronchitis, and respiratory diseases, particularly in children.

Picture 1. Visible Externalities

Kosovo has limited water resources, divided into four main water basins. Water resources in Kosovo are limited and insufficient and—in light of rising demand for water (reflecting urban, industrial, and agricultural development)—are expected to represent a limiting factor for socioeconomic development in the near future. Only about 70–75 percent of the population has access to a piped water supply and 50–55 percent is connected to the sewerage systems. Data from the Institute of Public Health show that bacterial (rather than chemical) contamination affects the quality of drinking water. Much of this bacterial (fecal) contamination occurs in the water supply systems of small cities and rural areas where a large proportion of wells and springs are thought to be contaminated. There are no wastewater treatment plants in operation in Kosovo, adding to the challenges of water contamination.

The lack of adequate environmental protection measures has resulted in serious environmental impacts from former mining and mineral processing activities. Historical and current industrial waste has remained, over long periods of time, within production sites, storage areas, and industrial hot spots. Mining and industry activities generate about 1.3 million tons of (commercial, hazardous, and nonhazardous) waste per year, with municipal solid waste adding another 0.4 million tons. At present, there is no proper waste management for any type of waste—whether domestic, industrial, or (bio-) hazardous. This applies to both current and historic waste. Current “waste management” practices, if left unchanged, will lead to high levels of air and groundwater pollution, including through methane or landfill gas, dioxins, and fine particles (when burned). In line with the municipal waste management policy, the International Finance Corporation (IFC) has been working toward concessioning the Pristina landfill, in which private investors have expressed interest.

The Ministry of Environment and Spatial Planning (MESP) is preparing an update of the Kosovo Environmental Strategy (KES) and an associated National Environment Action Plan (NEAP) for 2011–15. The NEAP will define environmental objectives so as to be able to meet EU requirements. In the short term, the focus will be on the implementation of existing legislation and continued efforts to modify legislation and institutions. In this context, the MESP aims to integrate acquis communautaire-related requirements into sectoral development policies in the relevant line ministries. In the
longer term, the KES/NEAP will define goals and/or strategies to (i) reduce pollution and mitigate environmental degradation; (ii) prohibit economic activities that would cause harm to human health or the environment; (iii) promote biodiversity protection and preserve the ecological balance; (iv) use rationally and sustainably natural resources, including agricultural land; and (v) protect valuable natural landscapes. In addition, the NEAP will identify, cost, and prioritize needed investments in water, air quality, waste (including chemical waste) management, biodiversity preservation, and environmental policy development.

Rural Development

Kosovo is endowed with high-quality agricultural land. Agriculture has always been a key sector in Kosovo’s economy, but it declined precipitously during and after the conflict. With the decline of the agriculture output, Kosovo’s agro-food trade deficit has been widening. Given Kosovo’s ample supply of agricultural labor, proximity and free market access to the EU, and relatively good climate, Kosovo should have a comparative advantage in the production of high-value horticultural and dairy products. Average agricultural land per person is around 0.15-0.18 hectares per resident, which is less than half of the EU average. The fragmentation and small size of agricultural parcels are a problem for sustaining adequate agricultural outputs and lead to lower agricultural outputs and subsequent economic losses. This is further aggravated by the constant conversion of designated agricultural land into residential or industrial plots. In 2006, Kosovo had an estimated 600,000 buildings of all types, of which 250,000 were in rural areas.

The agricultural sector currently contributes about 12 percent to GDP and accounts for approximately 35 percent of total employment. With its relatively abundant and underutilized labor, Kosovo has competitive potential in the horticulture sector, i.e., the production of fruits and vegetables, as well as in the livestock subsector. Domestic demand for horticulture and livestock products is expected to grow as purchasing power increases. Over the last decade, the demand for high-value horticulture products surged more than any other food category. However, while there is great potential for growth and the expansion of productivity in agriculture, the sector faces several challenges that are reducing the quantity and quality of agricultural production and hence, competitiveness in local and foreign markets. The difficulties are largely due to unfavorable farm structures, outdated farm technologies and farm management practices, the suboptimal use of inputs, weak rural infrastructure, a rudimentary rural advisory system, and the limited access to credit and investment capital. Agricultural imports from Kosovo’s trading partners, who receive production and export subsidies, place Kosovo’s farmers at a competitive disadvantage.

The World Bank supports the Government’s strategy to promote growth and competitiveness in the agriculture sector, with a view to overcoming identified bottlenecks that hold back sustainable rural development. Through the support provided by the World Bank and other development partners, the Government has sought to align Kosovo’s rural sector with the four axes of the Instrument for Pre-Accession for Rural Development (IPARD). The Government is undertaking several significant and strategic initiatives in this direction, including by establishing institutional structures consistent with EU accession requirements. In this context, the Government recently established a Paying Unit within the Ministry of Agriculture, which is expected to evolve into an IPARD Paying Agency.

WORLD BANK PROGRAM IN KOSOVO

Since 1999, the World Bank has provided and/or managed around US$400 million to Kosovo through more than 30 operations, including trust funds. As of September 1, 2012, there were six active lending operations with commitments totaling US$68.9 million and two trust funds with total commitments of US$8.9 million. These operations provide support in a wide array of sectors, including energy, education, public sector reform, cadastre, agriculture, social inclusion, and financial sector strengthening. As Kosovo joined the World Bank Group as a full member only in June 2009, all previous Bank-supported projects were financed through grants from a variety of sources, principally the Bank’s
net income, the Trust Fund for Kosovo, the Post-Conflict Fund, and the IDA.

The two Sustainable Employment Development Policy Operations (SEDPO) supported a stable macro-fiscal framework and improved the conditions for sustainable employment. Through the various SEDPO-inspired reforms, the Government has increased the transparency, accountability, and management of public expenditures and laid the institutional and legislative foundations for sustainable employment and growth. The first SEDPO tranche in the amount of US$34 million was disbursed in December 2011, while the second SEDPO disbursement, a US$49-million grant, was paid out in June 2012.

As such, the World Bank-financed projects have been designed to strengthen the business climate and improve competitiveness. These included the (i) Financial Sector Strengthening and Market Infrastructure Project; (ii) the Public Sector Modernization Project; (iii) the Real Estate Cadastre and Registration Project; (iv) the Agriculture and Rural Development Project; and (v) the Institutional Development for Education Project. A key obstacle toward meeting Kosovo’s socioeconomic development objectives is the energy sector, a central element of Bank assistance to Kosovo. The active portfolio includes the Energy Sector Clean-Up Project, which addresses the environmental legacy issues related to the open dumping of ashes from Kosovo’s oldest TPP.

The CPS envisages five new IDA operations, designed to support the government to meet its overarching objective of accelerating the EU integration process. These include (i) additional finance for the Energy Sector Clean-Up and Land Reclamation Project; (ii) the Energy Efficiency and Renewable Energy Project; (iii) the Partial Risk Guarantee supporting the Kosovo Power Project; (iv) the Water Supply Project; and (v) the Education Improvement Project. The Bank and IFC would support the development of other infrastructure services through studies and other advisory services. IFC would also seek to selectively provide financial support to private firms involved in infrastructure projects in Kosovo in areas such as water, transport, solid waste disposal, and energy.

The main focus of the new lending under the CPS program is the energy sector, aimed at addressing Kosovo’s energy crisis in a comprehensive way—seeking to balance energy security and energy affordability with efforts to minimize socio-environmental externalities and mitigating the adverse environmental, public health, and economic impacts on affected citizens. The CPS will support the business environment and good governance and address the issues of skills, while continuing to implement reforms in the agriculture sector, financial sector, and the cadastre.

The World Bank’s program in Kosovo is anchored in its four-year Country Partnership Strategy FY12–15 (CPS), following a series of Interim Strategy Notes. This document provides the World Bank Group and Kosovo with a framework of cooperation. In support of Kosovo’s EU integration objective, the CPS provides support to the authorities to (i) accelerate broad-based economic growth and employment generation; and (ii) improve environmental management.
KOSOVO: INSTITUTIONAL DEVELOPMENT FOR EDUCATION PROJECT

Key Dates:
Approved: December 13, 2007
Effective: December 14, 2007
Closing: June 30, 2013

Financing in million US Dollars*

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<th>Undisbursed</th>
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<td>IDA Grant</td>
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<td>4.9</td>
<td>4.0**</td>
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<tr>
<td>GoK</td>
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<tr>
<td>Total Project Cost</td>
<td>10.7</td>
<td>5.0</td>
<td>4.6</td>
</tr>
</tbody>
</table>

*Source Client Connection as of August 31, 2012.

**Withdrawal application in the total amount of US$0.98 million is being processed.

Note: Disbursements may differ from financing due to exchange rate fluctuations at the time of disbursement.

In Kosovo’s complex social, historical, geographical, and economic circumstances, improvements in the education sector can help to form the foundations of peace, poverty reduction, and economic growth. Education is one of the few sectors where these strategic ambitions have been articulated into detailed and credible sector development plans.

The Project Development Objective is to strengthen the systems, institutions, and management capacities needed for education quality improvements. The long-term overall goal is to support the Government in the implementation of the Strategy for the Development of Pre-University Education in Kosovo and the Strategy for the Development of Higher Education. The project addresses: (i) developing the organization and financing of the education system in Kosovo; (ii) building institutions and management capacities to promote quality improvements in primary and secondary education; (iii) creating conditions to introduce efficient and appropriate designs and reduce multiple shifts in Kosovo’s schools; and (iv) strengthening the management capacity at the system and institutional levels for higher education.

Results achieved:
- The Laws on Pre-University Education and Higher Education developed and approved.
- The Education Management and Information System (EMIS) software was finalized in February, and the school data collection process using the software for the first time was completed in July 2012.
- The school mapping database is finalized, providing an extremely rich database that should guide future investments in infrastructure. The Manual for School Standards and Design for Pre-University School Facilities was finalized and endorsed by the authorities, and the construction of the model basic education school showcasing the standards began in July 2012.
- A total of 180 schools received grants through the School Development Grant component to implement their priority activities related to quality improvements in education, including training on school management, planning, and procurement.
- Nation-wide implementation of school financing autonomy began this year, after three years of piloting in several municipalities.
- The National Council for Teacher Licensing is functional, and key documents establishing the framework for teacher professional development, performance evaluation, and licensing have been put in place or are in the piloting stage.
- Baseline of Grade 5 assessment established national assessment and examination capacities improved.

Key Partners: The Bank team worked closely with the Ministry of Education, Science, and Technology (MEST), responsible for the overall implementation, the Ministry of Finance, and municipalities. Key Development Partners included European Commission, German Society for International Cooperation (GIZ), Austrian Development Agency (ADA), Swedish International Development Cooperation Agency, (SIDA), and UNICEF.
The major constraints reported by firms in the 2003 Kosovo Business Environment Survey were unfair or informal competition, regulatory policy uncertainty, corruption, and the cost of and access to financing. These findings reflect, to varying degrees, (i) the weak enterprise regulatory regime, and (ii) the still rudimentary property rights system. The high degree of regulatory policy uncertainty, complexity, and non-transparency stems from the fact that municipalities in Kosovo are responsible for establishing the overall enterprise regulatory regime. As a result, there are essentially 30 different regulatory regimes throughout the municipalities. In many cases, regulations are vague and poorly enforced, do not define service delivery standards for enforcement bodies, and involve multiple offices or directorates within a given municipality. Further, enforcement of regulations such as licensing, construction permits, and health and trade inspections have been extremely erratic.

The **Project Development Objective** was to improve the business environment in Kosovo by reducing the uncertainty in key regulatory processes, improving the delivery of related services, strengthening property rights, and increasing the transparency and accountability of implementing institutions. The project was divided into two main components: (i) Business Service Integration to reduce regulatory uncertainty, reduce existing administrative barriers to starting and operating a business, improve the transparency and accountability of regulatory functions administered by municipalities, and facilitate investment; and (ii) Enhancement of Real Property Rights through registration improvement, a land policy and legal framework, an immovable property rights registration system, and cadastre reconstruction.

**Results achieved:**

- Equipment and technical assistance was provided to upgrade Business Registration hardware and software, to increase data security, and to pilot connectivity with municipalities in order to extend outreach and ensure decentralized service provision while preserving single principles of registration, single database, etc.
- Establishment of Municipal Business Centers serving as one-stop shops for citizens and providing advice on permits, taxes, customs, and business registration processes.
- Establishment of Project Coordination office within Cadastral Agency, staffing, and equipment.
- Renovation of three cadastral offices in three largest towns in Kosovo.

**Key Partners:**

The Bank team worked closely with (i) United States Agency for International Development (USAID) Local Government Initiative Program; (ii) Kosovo Cluster and Business Support Program (USAID/Chemonics); and (iii) the Business Enabling Environment Program (USAID).
Air pollution, particularly from the dust generated by the power stations and the ash dumps near the capital Pristina, is a critical problem. Soil and groundwater contamination from the ash dumps create negative environmental impacts, but pose less of a direct threat to public health than the direct exposure to airborne dust. The use of outdated mining practices, an industrial infrastructure that ignored environmental impacts, and a nonfunctioning environmental management system are the main factors behind the high exposure to environmental health risks. In addition, the sizeable overburden dumps from lignite mining occupy large areas near the mines, sterilizing land for other productive uses, while the former gasification plant consists of numerous structures containing hazardous chemicals in deteriorating and risky conditions.

The Project Development Objective is to: (i) address environmental legacy issues and problems related to the open dumping of ashes on land; (ii) enable the Kosovo Energy Corporation (KEK) to free land for community development purposes currently taken by overburden material, and enable the KEK to remediate Kosovo A ash dump; and (iii) initiate structural operations in the KEK for continued clean-up and environmentally good practice mining operations. The project aims to support the Kosovo Government and the KEK in promoting higher standards in environmental protection and social sustainability in the energy sector.

Results achieved:

- The depleted mine is being prepared to receive the sanitary disposal of ashes from power plant Kosovo A. The conversion of the current system of dry ash transportation to hydraulic transport is expected to be completed by the end of 2012 with a contribution of €1 million from the project. The disposal from Kosovo B plant is already directed through a hydraulic ash system to the Mirash mine.
- The project’s objective to remediate more than 55 percent of the projected remediation of the ash dumps was achieved in 2011 and work continued after this. Work has been initiated on the reclamation of 650 hectares of land available for community development, including agriculture, resettlement purposes, and/or natural habitats. In the course of 2012, 55 percent of the works will be completed. More than 120,000 seedlings have already been planted at the overburden dumps.
- The removal of the highest priority hazardous substances from the storage tanks and other containments at the gasification site (tars, benzene, phenols, methanol, oily compounds) is near completion, with all of the 14,000 tons of watery hazardous substances treated and neutralized. All storage tanks have been emptied and cleaned, with sludgy chemicals repackaged for transport. The shipment for the international disposal of these chemicals is ongoing and expected to be completed in October 2012. KEK staff is now fully responsible for clean up and land reclamation operations.

Key Partners: The Bank team worked closely with the Ministry of Energy and the Mining and Ministry of Environment and Spatial Planning. Kosovo Energy Corporation is the main project beneficiary and implementation agency. Key Development Partners included Dutch Government, USAID, EC, and Germany Development Bank (KfW), which are financially contributing to the energy sector in Kosovo, and with which the Bank team coordinated closely on policy issues.
KOSOVO: FINANCIAL SECTOR STRENGTHENING AND MARKET INFRASTRUCTURE PROJECT (FSSMIP)

Key Dates:
Original Project Approved: December 13 2007,
Additional Finance Approved: June 14, 2011
Closing: June 30, 2014

Financing in million US Dollars*:

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Total Project Cost 8.85

*Source Client Connection as of August 31, 2012.
Note: Disbursements may differ from financing due to exchange rate fluctuations at the time of disbursement.

Background: A Financial Sector Fiduciary Assessment (FSFA) conducted in May 2006 highlighted substantial institutional weaknesses in the Central Bank of Kosovo (CBK), which is responsible for the regulation and supervision of banks and other financial institutions. The weaknesses pertained to its institutional and financial sustainability; the banking and non-bank financial institutions (NBFIs); a prudential regulation, supervision, and resolution framework; and the financial sector infrastructure. The original project aimed to: (i) strengthen the CBK’s institutional capacity and the regulatory and supervisory framework for banks and non-banks; (ii) strengthen the microfinance industry to achieve sustainability and expand outreach; and (iii) strengthen the capacity of the Kosovo Banker’s Association to provide adequate training to local banks.

Additional Finance: Following the work under the original project, further weaknesses were identified and an additional finance project was approved by the Board of the World Bank to expand the mandate of the original project. As a result of the additional finance, the original project (called Financial Sector Technical Assistance) was combined with the additional finance and renamed the FSSMIP.

The Project Development Objectives are to: (i) enhance the stability and development of the financial sector; and (ii) strengthen the financial sector’s underlying market infrastructure. The additional components are: (i) establishment of a Real Time Gross Settlement System; (ii) establishment of a Business Continuity Center; and (iii) provision of seed funding to the Deposit Insurance Fund of Kosovo (a first for a World Bank investment project).

Results achieved: The CBK’s institutional strengthening and sustainability have substantially improved, thanks to the preparation of a development strategy based on market development trends and a review of the CBK’s sources of funding options, including (i) assistance for a functional assessment, and (ii) the development of a medium-term staffing plan and the revision of staff incentives.

The project has helped the CBK (i) to revise the banking sector and regulatory framework and (ii) to provide assistance to the insurance sector on preparing a legal framework to third-party liability and on providing detailed functional supervision and technical assessment of compulsory third-party liability tariff liberalization. The additional finance became effective in February 2012 and will contribute to further strengthen the infrastructure of the financial sector.

Key Partners: The Bank team works closely with the U.S. Treasury, the International Monetary Fund (IMF), and the Government of Germany through the Kreditanstalt für Wiederaufbau (KfW).
KOSOVO: PUBLIC SECTOR MODERNIZATION PROJECT

Key Dates:
Approved: February 4, 2010
Effective: June 17, 2011
Closing: June 30, 2013

Financing in million US Dollars:

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*Source Client Connection as of March 13, 2011.
*Note: Disbursements may differ from financing due to exchange rate fluctuations at the time of disbursement.

Despite the considerable progress achieved in the past few years, Kosovo still needs to improve public financial management and further utilize information technology to make efficient use of scarce public resources. The capacity of the civil service to attract, motivate, and retain qualified staff is also a pressing constraint to the effectiveness of Government institutions.

The Project Development Objective is to (i) strengthen the performance of key budget organizations in budget formulation, budget execution, and public procurement; (ii) establish the foundations for fiscally sustainable payroll management and effective human resource management in the core civil service; and (iii) create conditions for the further automation of government work processes and for the development of e-government applications.

Expected results:

- Improved quality of budget formulation and execution in participating budget organizations (Ministry of Agriculture, Ministry of Education, Ministry of Health, Ministry of Justice, and Judicial Council), as measured by specific indicators.
- Increased bidder participation in public procurement tenders and cost savings through Quick Gains actions and e-procurement modules.
- A transparent and coherent pay and grading structure introduced in the civil service, supported by improved information and communications technology (ICT) systems that enable effective fiscal and management controls in payroll administration.
- Enhanced security, efficiency, and interoperability of government information systems (through centralized data storage and systems maintenance, security standards, and interoperability frameworks).

Key Partners:
The project was prepared in close cooperation with the Ministry of Economy and Finance (public financial management reform) and the Ministry of Public Administration (civil service reform, ICT infrastructure), which will be the key institutions responsible for the project’s implementation.

Key Development Partners include UK Department for International Development (DfID), which has contributed to some of the activities related to project preparation (e.g. support for drafting the civil service legislation and financial impact assessment of civil service pay reform). DfID, the European Commission, and USAID have also supported the development of the Public Financial Management Reform Action Plan and public procurement reform.
In Kosovo, the real estate property market is constrained by its legacy. As a result of the 1999 conflict, thousands of homes were damaged or destroyed, up to 75,000 properties were abandoned, and land records were either destroyed or moved to Serbia, where they remain. Many citizens lost access to their properties; ownership records remain incomplete or unreliable; and vacated properties were occupied illegally (about 20,000 claims on properties that were illegally occupied as a result of the conflict, are still being processed by the Kosovo Property Agency). Real property is now private, socially owned, state-owned, or owned by publicly owned enterprises, primarily public utilities that are also being privatized. In 2006, there were an estimated 600,000 buildings of all types, of which 250,000 were in rural areas. There are about 2 million land parcels and an estimated 350,000 property owners. Government institutions are weak, and property rights transactions often go unregistered until there is a need for documentation for a procedure or loan, at which time the registered owner may not be available.

The Project Development Objective is to help develop Kosovo’s land and property markets and to improve tenure security. The project addresses a range of issues by: (i) supporting the improvement of the capacity of Municipal Cadastre Offices (MCOs) to deliver services by rehabilitating the MCOs and carrying out systematic registration in the Kosovo Cadastre Land Information System (KCLIS); (ii) financing the establishment and maintenance of a Continuous Operating Reference Network (CORN) to provide a single source of reference points to surveyors; (iii) supporting institutional reform by upgrading the legal and normative framework and promoting the greater financial self-sufficiency of the Kosovo Cadastre Agency (KCA); and (iv) training for Kosovo Cadastral Agency (KCA) and MCO managers and staff, the project coordination office, private surveyors, and other key stakeholders in management, planning, legal, technical, and administrative subjects.

Expected Results:
The project was declared effective on June 17, 2011 and has had a good start. The KCA and project coordination unit are fully operational and working effectively. The working group for the institutional reform of the KCA meets regularly and the strategy for ensuring the long-term sustainability of the KCA has been agreed upon. The Inter-Ministerial Committee for Land Administration has been established and is functional. Donor coordination meetings are taking place, aiming to reap synergy among donor projects in the land administration area. Important procurement packages are under implementation, including major contracts to undertake cadastral survey work and to develop information systems. Customer surveys and other project activities to improve legislation and provide training and public awareness are well under way.

Key Partners: The Bank team works closely with the Ministry of Environment and Spatial Planning, MCO, other municipal structures, and the KCA. The Governments of Norway, Sweden, and Switzerland have been involved in Kosovo’s land administration since 2000, and RECAP substantially builds on shared experience. GIZ began providing support in 2007 and has plans to work directly with four pilot MCOs for the 2011–13 period. The EC is funding a unit within KCA to implement the address registry.
**KOSOVO: FIRST SUSTAINABLE EMPLOYMENT DEVELOPMENT POLICY OPERATION I**

**Key Dates:**
- **Approved:** September 30, 2010
- **Effective:** December 15, 2011
- **Closed:** January 31, 2012

**Financing in million US Dollars:**

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*Source Client Connection as of March 13, 2012.*

*Note: Disbursements may differ from financing due to exchange rate fluctuations at the time of disbursement.*

The Project Development Objective was to support the Government of Kosovo in (i) maintaining a stable macroeconomic framework while increasing the transparency, accountability, and management of public expenditures, and (ii) laying the institutional and legislative foundations that Kosovo needs for sustainable employment and growth.

The Program was the first of two annual operations providing budget support to the Government of Kosovo under World Bank procedures since its membership in the World Bank Group on June 29, 2009. The support went directly to the budget of Kosovo to finance overall budget needs.

**Results achieved:**
- Public Expenditure and Financial Accountability (PEFA) self-assessment completed in 2009;
- An action plan to improve Kosovo’s Public Financial Management (PFM) system adopted;
- A new Civil Service Law that creates uniform pay and grading structures for public services enacted;
- A cross-sector Employment Strategy, a first for Kosovo, completed and adopted;
- The financeable elements of the strategy translated into the 2010 budget;
- A new leasing law that will allow credit-constrained firms to gain access to machinery and equipment enacted;
- An accreditation review of the higher education institutions made by the Kosovo Accreditation Agency, which will contribute to improve the quality of education and skills much needed for future private sector growth; and
- An increase in the budgeted funds for social assistance and pensions as a crisis mitigation measure.

**Key Partners:**

The Bank team worked closely with the Deputy Prime Minister’s Office, Ministry of Economy and Finance, Ministry of Education, Science and Technology, Ministry of Labor and Social Welfare, and Ministry of Trade and Industry. The program was cofinanced by 10 international donors, viz., the Czech Republic, Denmark, the European Community (EC), Estonia, Finland, Italy, Norway, Sweden, Switzerland, and the United States.
KOSOVO: SECOND SUSTAINABLE EMPLOYMENT DEVELOPMENT POLICY OPERATION

Key Dates:
Approved: May 3, 2012
Effective: May 15, 2012
Closed: May 31, 2012

Financing in million US Dollars:

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*Source Client Connection as of August 31, 2012.

Note: Disbursements may differ from financing due to exchange rate fluctuations at the time of disbursement.

The Project Development Objective was to support the Government of Kosovo in (i) maintaining a stable macroeconomic framework while increasing the transparency, accountability, and management of public expenditures, and (ii) laying the institutional and legislative foundations that Kosovo needs for sustainable employment and growth. The program was the second of two annual operations providing budget support to the Government of Kosovo under World Bank procedures since its membership in the World Bank Group on June 29, 2009. The support went directly to the budget of Kosovo to finance overall budget needs.

Results achieved:

- Secondary legislation to implement the Public Procurement Law and the Rules of Procedure for the Central Procurement Agency to conduct consolidated procurement on behalf of the Government for selected procurement categories were approved.
- A monitoring and review system for monitoring and reviewing the financial and physical progress of capital expenditure was introduced.
- All major capital projects (i.e., those to be financed with public funds and exceeding €1 million in cost) approved in the 2012 budget, and incorporated in the Public Investment Program database for 2012.
- A mechanism requiring all ministries to prepare program performance indicators with their budget submissions was introduced, and program performance indicators have been included in all ministries’ 2012 budget submissions.
- The Regulation on Classification of Jobs in Civil Service specifying the coefficients in the recipient’s new civil salary grid was approved.
- A total of 22 “one-stop-shops” for business registration were established in 22 municipalities.
- The amended Law on Business Organizations and the Law on Internal Trade were adopted
- The Regulation on Credit Registry was approved.
- The Law on Labor, which regulates employment and labor relations, was approved.
- The Public Works Program was introduced in 2010 and expanded in 2011 and 2012 to promote labor market activation for Category II social assistance beneficiaries and the long-term unemployed. In addition, all social assistance registries were digitized.
- The Kosovo National Qualifications Framework was approved and the accreditation of vocational training providers initiated.

Key Partners: The Bank team worked closely with the Deputy Prime Minister’s and Minister of Trade and Industry Office, Ministry of Economy and Finance, Ministry of Education, Science and Technology, Ministry of Labor and Social Welfare, Ministry of Public Administration and the Central Bank of Kosovo. The program was cofinanced by 10 international donors, viz., the Czech Republic, Denmark, the European Community (EC), Estonia, Finland, Italy, Norway, Sweden, Switzerland, and the United States.
KOSOVO: AGRICULTURE AND RURAL DEVELOPMENT PROJECT

Key Dates:
Approved: June 14, 2011
Effective:
Closing: July 31, 2017

Financing in million US Dollars:

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*Source Client Connection as of October 10, 2012.
Note: Disbursements may differ from financing due to exchange rate fluctuations at the time of disbursement.

The Project Development Objective is to help the Government of Kosovo to promote competitiveness and growth in the livestock and horticulture subsectors over the next decade through the implementation of selected measures of its agricultural strategy and institutional development. Towards this, the project will support the Transfer of Knowledge to the Rural Sector and Investments to Promote Sustainable Rural Development through rural development grants and the capacity building of the Ministry of Agriculture Forestry and Rural Development.

Expected Results:

• Strengthened rural advisory services, enabling commercial and semi-commercial farmers and agro-processors to take sound investment decisions to improve productivity and growth;
• Improved growth and competitiveness in the agricultural sector through the provision of rural development grants in the horticulture and livestock subsectors to commercial and semi-commercial farmers and agro-processors; and
• Improved institutional capacity of the Ministry of Agriculture and Rural Development to implement the National Agriculture and Rural Development Plan.

Key partners:
The project builds on past and ongoing support provided by the Government and several donors, including inter alia the European Commission, United States Agency for International Development (USAID), and Inter-Cooperation (Swiss and Danish support) to promote growth and competitiveness in the agricultural sector, and help put in place the institutional structures for managing funds that will become available under the Instrument for Pre-Accession Assistance for Rural Development (IPARD) program.
How to contact us:

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