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## Forgotten status of many: Kosovo's economy under the UN and the EU administration

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# Ordnungspolitische Diskurse

## Discourses in Social Market Economy



**Mulaj, Isa**

**Forgotten Status of Many:  
Kosovo's Economy under the  
UN and the EU Administration**

**Diskurs 2007 – 8**

**Mulaj, Isa**

# **Forgotten Status of Many: Kosovo's Economy under the UN and the EU Administration**

## **Abstract**

After eight years of the United Nations (UN) administration, Kosovo again is returned to the international centre of attention – this time about her future political status. The document presented by the UN Special Envoy for Kosovo, Martti Ahtisaari, proposed an ambiguous status settlement that is portrayed and understood as a “supervised independence”. Whatever expectations from political perspective will be, that is of secondary importance for this paper – the aim is in Kosovo's aggregate uncertainty about her economic sustainability, namely to investigate the relationship between fragile institutions, poor governance and weak economic performance. With a foreign aid since the second half of 1999 amounting to €22 billion, Kosovo still has massive unemployment and widespread poverty. How the UN's largest experiment ever undertaken, involving considerable resources and long time, left the economy in such a poor state?

**Keywords:** Kosovo, UNMIK, Provisional Institutions of Self-government, poverty, political status settlement.

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**Mulaj, Isa**

## **Forgotten Status of Many: Kosovo's Economy under the UN and the EU Administration**

### **Introduction**

Kosovo is a landlocked country in the Western Balkans with an estimated population of 2.1 million inhabitants in an area of 10,887 km<sup>2</sup>. Over 60% of the population lives in rural areas and around 1/3 is younger than 15 years old (Statistical Office of Kosovo, 2006). On 10 June, 1999 the UN Security Council (UNSC) passed the Resolution 1244 authorizing the establishment of the United Nations Mission in Kosovo (UNMIK).<sup>1</sup> The deployment of UNMIK marked the beginning of transition to democracy and market economy that was delayed for a decade. While most countries in transition reformed their institutions, Kosovo needed to build them from scratches. This task was taken in charge by UNMIK which, in its first regulation On the Authority of the Interim Administration in Kosovo (Regulation No. 1999/1, amended by Regulation No. 1999/25 and Regulation No. 2000/54) declared itself the administrator in almost all major governance positions.<sup>2</sup>

Provisional Institutions of Self-Government (PISGs) are democratically elected institutions in charge of managing Kosovo's affairs under the supervision of UNMIK. They include institutions such as the Assembly of 120 members that elects the President of Kosovo. The President then nominates the PM that has to be endorsed by the Assembly. Following the approval of the Constitutional Framework for Provisional Self-government in Kosovo marked the beginning of gradual transfer of powers from UNMIK to the PISGs. The transfer of power is

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<sup>1</sup> The full text of this resolution is available at:  
<http://daccessdds.un.org/doc/UNDOC/GEN/N99/172/89/PDF/N9917289.pdf?OpenElement>

<sup>2</sup> Official Gazette of UNMIK and all its regulations can be accessed at:  
<http://www.unmikonline.org/regulations/unmikgazette/02english/Econtents.htm>

not full and a number of key decision-making areas are earmarked as the “reserved power” for SRSG, whose authority is derived from the UN Resolution 1244. Beside unlimited power to overrule every political decision of the PISGs, a long list of competencies falling in the reserved power for SRSG as laid down in section 8 of the Framework includes the following economic areas: approval of the Kosovo budget; monetary policy; controlling the UNMIK’s customs service; administration of social, state, and public property; appointing of members in economic and fiscal council; appointing of tax inspectors, etc.<sup>3</sup>

UNMIK and the PISGs are a set of institutions whose behavior is very similar to the one observed in early capitalist development in Western Europe centuries ago. Group and individual interests within the PISGs do not differ from illegal, what Marxists would call, accumulation of capital at the expense of others. The only difference is that accumulation of capital does not occur through violent means but instruments such as power and position. History and the experience from transition in CEE suggests that the road to enrichment of a social class to the extent that they feel fed enough then began to share their wealth with the rest of the population, maybe costly and with problems.

The PISGs repeatedly maintain that pending political status was and is still the main barrier to economic development, assuming that once that is sorted out, the economy will prosper. This paper shows that an overemphasis by politicians on externalities such as the unresolved political status (which certainly is a roadblock) while underestimating their management inefficiency associated with corruption, is a pettifogger explanation that impoverished population has started (with a delay) to get rid of its consumption. Now that rotation in power has included all main political parties, the general public doubts if current political establishment will ever run Kosovo honestly and efficiently. To this vicious circle it has come as a result of clientelism between Kosovo’s politicians and some UN bureaucrats with the loyalty of the first towards the latter, both pursuing own interests that were and are not necessarily part of their work or mission.

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<sup>3</sup> Provisions of UNMIK Regulation No. 2001/9, amended by Regulation 2002/9.

By not having an exit strategy, the mission of UNMIK is only formally drawing at an end. Having realized that Kosovo's Provisional Institutions of Self-Government (PISG) that have a designated scope of operation, are not sufficiently capable of ruling independently, it is expected that an EU mission will support an outspoken "supervised independence". The EU was principally in charge of managing Kosovo's reconstruction and economic development under UNMIK, and now is drawing plans for a greater role in what is expected to be the EU's largest mission so far.

The interplay between UNMIK and the PISGs in economic development is an interesting case for research as an alternative in transition economics. To find this out, in section one of this paper I first consider a theory of the role of institutions in economic performance. It starts with a brief discussion on limited role of institutions from classical economics point of view, and then it expands to their greater importance in transition economies. Since major decisions in the economy are still made by UNMIK, section two will explore the magnitude of this power exercise and the mission of its EU Pillar IV is discussed in subsequent sub-section. The impact and constraints of pending political status in economic development is discussed in section three. Rhetoric towards political status has distracted the attention from miserable economic status – the indicators of which are presented in section four. Unemployment and poverty are not the only statuses that did not receive serious attention. There are other areas not related to political status at all and where performance is disappointing, especially in education and health. These are named and described in a sub-section as Kosovo's other forgotten statuses. Section five tries to answer the question if the UN's interim mission is turning permanent, or explaining the proposed resolution of political status. The last section draws conclusions and offers some lessons to be learned.

## **1. Theoretical background on the role of institutions in economic performance**

Classical economics, its main architect Adam Smith respectively, advocated for a role of the government outside the economy. Smith's arguments on laissez-faire or liberal economic policies that the government is better placed to collect taxes, provide peace and security, and protect private property rights rather than interfere in the markets that should be left to operate freely, dominated the economic thought in the 19<sup>th</sup> century. It was not until the Great Depression 1929-1933 in the capitalist world, the rise of the Soviet Union as a socialist country and foundation of Keynesian economics where, free market economics would fall out of popularity and superseded by the government control of economy in the former socialist countries and significant state intervention in capitalist countries after World War II. During the 1980s, a neoliberal doctrine that emerged in the U.S.A. and the U.K. as Reaganomics and Thatcherism witnessed a declining state intervention in economic affairs. It preceded by tax cuts to lower government expenditures at the benefits of businesses.

Under the influence of neo-liberalism the so-called the Washington Consensus has been built as a package of reforms to be transplanted in the former socialist countries upon transition from government controlled to market economy in the early 1990s. The implication of this reform package was that deteriorated performance of companies in former socialist economies exposed to competition of more experienced and technologically advanced Western companies.

Economic liberalization alongside institutional disorganization and reorganization process in Central and Eastern Europe (CEE) has led to the strengthening of individual and/or group interests and their opportunist behavior vis-à-vis weaker role of state in the economy. When individuals advance their interests, Adam Smith was convinced that they serve the interests of society, too. A coincidence of then individual behavior has been observed in the early transition in CEE with the rise of tycoons, though the difference is that tycoons mostly made themselves better off at the expense of society and aggregate economy in the short run.

In early transition and emerging democracies, patron-client relationships or clientelism between the rich and political establishment are often personalized. The rich first influence and then support those economic policies that help them further advance their private interests. Such a political reliance of the government and institutions on the few rich leads to underperformance of public goods supplied by the government to the rest of population (Keefer, 2005). The extent of clientelism is the factor contributing to the rise of sharp differences in economic welfare among the population in transition economies. In Russia, a group of powerful tycoons known as oligarchs came out with a large stake of resources to exercise sufficient control over politics and run institutions by proxy for their interests (Guriev and Rachinsky, 2005). Oligarchs who by definition mean the rule of few should be distinguished from tycoons. The tycoons may be very rich but may not necessarily exercise active and direct influence in politics.

It would be wrong to assume equality in economic terms between the people in similar as well as different circumstances; there were and always will be differences. But the gap that arose during transition from communism to a market economy through dishonest and controversial ways has become subject to much research and criticism. In the course of resource redeployment, profitable opportunities of the few taking the largesse from existing wealth along with increase in poverty for the majority, were later assessed when democratic elections of majority of the votes corrected “their failures” by putting into power the parties with social democracy orientation, and in some cases “reformed” Communists (Stiglitz, 2002).

The very diverse economic performance in transition economies encouraged the scholars to incorporate in their economic analyses non-economic factors such as cultural differences and institutions, by which it is aimed to explain economic growth or decline. In this respect, Roland (2004) refers to fast-moving institutions that are characterized by political changes, typical what happened after immediate collapse of the communist system and the multiparty political transition period in CEE, and slow-moving institutions related to the changes that are more gradual. An interaction between these two types of institutions affects economic performance and development differently. When institutional



transplantation or exporting the stock of knowledge and system of rules elsewhere failed to bring about economic prosperity (like in India under the British rule) Roland explained that as a cause of incompatible interaction between fast-moving and slow-moving institutions. The alternative to institutional transplantation that the economic reforms should be endogenously based or designed on local specific features in a globalizing world also cannot be supported. To some extent, the success of economic reforms depends on the level of accumulated knowledge, cultural factors and the peoples' mentality in shaping institutions.

Relative economic performance in transition has mostly been addressed to institutions that have managed it. A study by Brunetti, Kisunko and Weder (1997) that included twenty transition countries found that political stability was of primary importance for the performance of other institutions such as property rights security, reliable judicial system, and a lack of corruption, were all important for economic growth. A later study by Redek and Sušjan (2005) for twenty-four transition economies over the period 1995–2002, confirm that long-term growth was more stable in the countries with better legal system, protection of property rights, plus stable financial system. The variation in overall economic performance is explained by institutional transformations and aggregate uncertainty during which there was a decline of output (Roland, 2002). Another explanation was that institutional building and development for economic growth, which also varied across countries, depended on several factors, e.g. years under socialism, civil wars, availability of natural resources, EU accession, speed of liberalization, and privatization. According to Beck and Leaven (2005), civil wars in Armenia, Azerbaijan, Tajikistan, Georgia, Moldova, Croatia and FYR Macedonia were found to have had negatively affected economic performance (as measured by economic growth and GDP per capita) only in the short run, after which sustainable development followed. Bosnia and Herzegovina that Kosovo is often compared with, has reached a sort of economic consolidation and nearly half of her imports are covered by exports (European Commission, 2006). In Kosovo the opposite happened; the first two years after the 1999 war marked a significant rate of economic growth that was explained by foreign aid and the very low economic base. Now when the economy should have entered

the phase of sustainable development, it went to a slump. Instead of political economy and sound economic policies, politicization of the economy prevailed and is still at stake.

Kosovo had a low level of accumulated knowledge and experience for democracy and transition to a market economy. What had been achieved during self-management socialism was reversed in the '90s under Serbia's repressive rule by dismissing majority of Albanians from public administration and social sector. A decade lost in management of public administration would later result in inexperience and deficiencies of managing the transition. There was no longer any interest in self-management even from theoretical point of view and Kosovo Albanians perhaps wrongly associated that system with Serb domination.<sup>4</sup> The knowledge needed for democracy and economic transition was missing. Having this disadvantage into consideration, one would come to a conclusion that institutional transplantation would be more than welcomed to catch up with what was lost. It actually happened.

UNMIK and the PISGs are an example of fast-moving institutions. Their interaction between themselves and slow-moving institutions, i.e. Kosovo's historical, social and cultural factors, help to explain many outcomes that can be classified as moderate successes and in largest part as failures, especially in economic front. Aside from ineffective criticism by various stakeholders outside fast-moving institutions or any subjective assessment to undermine the mission, only now we are finding the books like "How the World Failed Kosovo", written by those who worked for UNMIK.<sup>5</sup> The authors of this book tried to partially show their honesty by reporting some of the failures in the mission they worked for. And they did so only after walking away with the sums of money that they would have not gotten in their home country for the entire working career.

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<sup>4</sup> The Serbs in turn have not shown any sympathy for self-management system on the eve of its collapse. When the Serb nationalism rose in the early 1990s, it used a propaganda to blackmail Slovenia for inventing self-management for the purpose of allegedly exploiting Serbia (Bennet, 1995: 107).

<sup>5</sup> The full title of this account is: King, Ian and Whit Mason, *Peace at Any Price: How the World Failed Kosovo?, Crisis in World Politics 2* (Ithaca: Cornell University Press, 2006). The first author has worked for UNMIK from April 2000 to December 2003 as head of planning. The second worked as public affairs officer for UNMIK from May 2002 to January 2004.

## **2. Kosovo's economy as a property of the UN**

When UNMIK moved in, Kosovo's economy was almost in ruins. The first challenging task for UNMIK was institution building in order to coordinate the postwar reconstruction through a massive international assistance. Legally, the UN is an organization that does not own anything in the countries in which it is deployed, except the facilities it rents for a certain time. As Kosovo in mid-June 1999 was in chaos, it was necessary to establish a control over major remaining assets of the economy. It is worth referring to Article 6 of the Regulation No. 1999/1 mentioned in previous section according to which UNMIK becomes a direct administrator of social and public property in Kosovo. UNMIK proceeded with the legal framework to establish the department of reconstruction, customs duties, central fiscal authority to collect taxes, banking and payment authority of Kosovo – BPK (a sort of central bank without the right to print money and regulate monetary policy), and department of trade and industry, or the basic institutions for functioning of the economy. Many of those institutions underwent significant changes and the powers were gradually transferred to the PISGs. For instance, department of reconstruction disappeared, central fiscal authority was transformed into the ministry of economy and finance, department of trade and industry was split into a ministry with the same name and the Kosovo Trust Agency (KTA).<sup>6</sup> Customs duties and BPK (recently this has been renamed as Central Banking Authority of Kosovo – CBAK) remained. Kosovo became the first country outside the EU zone to use Euro (€) as official currency.

The final say on economic issues still rests with UNMIK. In some institutions such as the KTA, UNMIK excludes any possible important decisions by the PISG's representatives. Having major assets in strategic sectors under control through the KTA that is established with a mandate to privatize socially-owned enterprises (SOEs) and restructure public companies, it can be argued that Kosovo's economy is still like a property of the UN, irrespective of its interim mission. But that is not the magnitude of control to call the UN as (provisional) owner. The following sub-section provides additional details that makes it more like the economy of an EU mission.

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<sup>6</sup> For more details about the KTA visit <http://kta-kosovo.org/html/>.

## **2.1 Pillar IV and its mission in emerging transition**

UNMIK is still the administrator of Kosovo, which the Resolution 1244 recognizes as technically province of Serbia. The head of UMMIK is the Special Representative of the Secretary General (SRSG), who is appointed by the UN's Secretary General. In a simpler language, SRSG means the Governor of Kosovo. UNMIK exercises its administration through 4 Pillars in the following areas: Pillar I – police and justice (led by the UN); Pillar II – civil administration (also led by the UN); Pillar III – democratization and institution building (under the direction of the Organization for Security and Cooperation in Europe – OSCE); and Pillar IV – in charge of reconstruction and economic development (directed by the European Union).<sup>7</sup> The last pillar is of special importance not only for this paper but also for the future of Kosovo's economy.

After some two years of the UNMIK's administration, the Constitutional Framework for Provisional Self-government in Kosovo outlining the beginning of gradual transfer of powers from UNMIK to the PISGs was approved. The transfer of power in economic affairs does not include key decision-making areas that are earmarked as the "reserved power" for SRSG, whose authority is derived from the UN Resolution 1244. A list of areas falling under the reserved power for SRSG that is provided in section 8 of the Framework includes: approval of the Kosovo budget; monetary policy; controlling the UNMIK's customs service; administration of social, state, and public property; appointing of members in economic and fiscal council; appointing of tax inspectors, etc.<sup>8</sup>

The mission of Pillar IV to support the reconstruction of key infrastructure is still underway. Major reconstruction has taken place ranging from impressive results at the Prishtina international airport which is made the busiest one in the Western Balkans, to electricity shortages in spite of huge investments through the European Agency for Reconstruction (EAR) worth hundreds of millions of Euros in the monopoly based Kosovo Electricity Company. Economic development is being supported through various programs financed by the EAR in the newly

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<sup>7</sup> UNMIK's website is available at: <http://www.unmikonline.org>

<sup>8</sup> Provisions of UNMIK Regulation No. 2001/9, amended by Regulation 2002/9, available at: [http://www.unmikonline.org/regulations/unmikgazette/02english/E2002regs/RE2002\\_09.pdf](http://www.unmikonline.org/regulations/unmikgazette/02english/E2002regs/RE2002_09.pdf)

established private enterprises and privatization of SOEs. The process of privatization as one of the aspects of transition begun in mid-2003 and was expected to be formally completed by mid-2005 when the mandate of the KTA should have been terminated.<sup>9</sup> As of nearly three years after that deadline, the process is miles away from meeting that target, the KTA is still alive and has got much work to do in the coming years.

### **3. How Kosovo's unresolved political status impeded economic development?**

Pending political status in many ways has restricted Kosovo's economic development. By not being politically independent and a recognized state, Kosovo still cannot access loans from international organizations such as the World Bank, International Monetary Fund (IMF), International Finance Corporation and many more, to finance large projects in infrastructure and facilitate economic development. Furthermore, it was constrained to reach and sign certain agreements with other countries until recently when UNMIK signed free trade agreements with Albania, Macedonia, Bosnia and Herzegovina, and Croatia.

Although Kosovo is technically still part of Serbia and trade is supposed to be free, Kosovo's exports (and also imports) are charged with transit charges of 3% in Serbia and 5% in Montenegro, whereas Kosovo's infrastructure is freely used by everyone (EU Pillar IV, 2004). These asymmetric trade relations are impeding greater economic cooperation and integration, which obviously is coming at Kosovo's expense. Trade is also restricted because foreign countries, except FYR Macedonia, Albania, and Montenegro do not recognize Kosovo's number plates.

Kosovo's economic underdevelopment in terms of unresolved political status may be attributed to three major constraints: i) initiatives of the European Stability Pact sidestep Kosovo in many projects of regional development; ii) the PISGs do not have the power to make major decisions regarding economic development;

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<sup>9</sup> On how the KTA underestimated the challenge of privatization, difficulties and uncertainties it faced in the process, see Mulaj (2005).

and iii) related to and within the previous constraint, there is a lack of transparency in the functioning of the PISGs (Perrit, 2004).<sup>10</sup>

Losses due to prolonged political status settlement are enormous. Entering into more details to explain them would be beyond the scope of this paper. However, when the Government was constantly confronted with poor economic conditions, it blamed the unresolved political status with generalized statements; that this political status quo is impeding us to do this and that, once independence is recognized many doors will be opened, and alike. As political status began to be dealt with, frustrations about poor economic conditions were caressed a little, and when it entered a more dynamic phase that resulted in the Proposal of Martti Ahtisaari, the attention to the economy again lost its importance. At the time when the Proposal became public and the media were massively focusing on it, Sweden's foreign minister, Carl Bildt, paid a visit to Kosovo. To my surprise, as he said in a short interview with Radio and Television of Kosovo (RTK) on 1 February, 2007 "the politicians here are underestimating the poor state of the economy. They are thinking that the economy will do fine after the political status is settled. It is not that easy as they are thinking. Tough challenges for the economy lie ahead".

### **3.1 Economic policies and management: too much blame on politics**

According to international methodology, Kosovo has got one of the most business friendly environments in South Eastern Europe (SEE). A study conducted by USAID (2005) on Business Conditions Index that uses the methodology of the World Bank's Doing Business,<sup>11</sup> found that an average period to settle up a business in Kosovo is 23 days after 5 procedures being completed. This is much faster than in any other SEE country. The costs of starting a

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<sup>10</sup> Perrit also argued that the U.S.A. should push for Kosovo's independence not only to facilitate Kosovo's economic development, but given that Kosovo's majority population is Muslim and secular with great sympathy towards the U.S.A., then it would help the U.S.A. to have more friendly relations with less friendly Muslim countries. He further added in favor of Kosovo's independence that Yugoslavia (now disintegrated) means the land of southern Slavs and Albanians are not Slavs.

<sup>11</sup> There are seven components that are part of Business Conditions Index: 1) Starting a Business; 2) Hire/Fire of Workers; 3) Registering Property; 4) Access to Credit; 5) Protecting investors; 6) Enforcement of Contracts; 7) Closing a Business. More details about the survey can be found at: <http://www.doingbusiness.org/MethodologySurveys>

business are very low (5.5% of income per capita), even by international standards. The procedure of hiring and firing workers are very flexible, costs to register property are the second lowest in the region and the average time to close the business is the lowest comparing to other countries in SEE region. Areas where business environment lagged behind the region are related to property rights and underdevelopment of the banking system to act as a creditor to a business community. The study on business environment concluded that Kosovo has the necessary regulations in place, therefore recommended to the Government to focus on their implementation rather than passing additional regulations or amendments. Despite appropriate legal and regulatory framework to do business, development continues to be undermined by insufficient law enforcement and unreliable courts to resolve disputes.

Trade regime consists of: i) 0% Value Added Tax (VAT) on exported goods (no customs duties); ii) a tariff rate of 10% charged at the border on imported goods (agriculture inputs are exempt; goods subject to excise taxes which have different higher rates or per value); iii) VAT of 15% as a border tax for imported goods. These tax rates do not apply to all countries that Kosovo has trade exchange with. Goods coming from Macedonia are not subject to customs duties at the border (only VAT is collected) except a charge of 1% of goods' value collected in the name of customs' fees. Border taxes in 2005 accounted for 68% of Kosovo's budget revenues (Ministry of Economy and Finance, 2006), or much higher than in any transition country. The implication of such a budget composition in the medium term will be the rising trend of liberalization such as the entry into force of the Central European Free Trade Agreement (CEFTA) that will inevitably force Kosovo to rely more on taxes collected within the country to maintain budget sustainability.

Agriculture is referred to as one the sectors that is in a more disadvantaged position than others and with potentials to development at the same time. The development of this sector is facing strong competition from countries in the region, where producers enjoy support from their government subsidies. Kosovo producers cannot afford this competition in an entirely open market. The price of local products is higher than of imported ones, often with dumping prices. The

budget of the Ministry of Agriculture Forestry and Rural Development is very small. In fact there is no budget for anything about agriculture – that is a budget for salaries and costs of the Ministry and not for any support or investment in agriculture. Limited and difficult access to finance features all businesses, but agribusinesses got only 2% of total loan portfolio from by the banks. Access to finance by agribusinesses could be improved through the loans from a commercial bank where the Government would subsidise the interest rate.

An undesirable impact on the economy has been frequent changes in the Government and the split between political parties. Just one month after the death of former Kosovo president Ibrahim Rugova who was also the chairman of the largest political party – the Democratic League of Kosovo (LDK), the Assembly Speaker Nexhat Daci (LDK), the Prime Minister (PM) Bajram Kosumi (from the Alliance for the Future of Kosovo – AAK) and his deputy Adem Salihaj (LDK) were dismissed overnight in the beginning of March 2006. The Assembly Speaker was dismissed by majority of votes in the Assembly of LDK-AAK coalition charges of misusing public funds, the PM who had inherited his position from the AAK leader Ramush Haradinaj was accused of being too inefficient and was forced to resign. Agim Ceku, who was the commander of Kosovo Protection Corps and politically unaffiliated, became PM as the member of AAK (UNDP, 2006a). In all this political turmoil that continues, economic issues are being neglected, whereas non-professionalism, inefficient and corrupted governance have associated the PISGs and local administration. The Office of the Auditor General found enormous irregularities in managing public finances, mismanagement of procurement policies, non-compliance with tender procedures, and use of money for other purpose than allocated.<sup>12</sup> The destination of some funds was found as money laundering and their use later discovered.<sup>13</sup>

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<sup>12</sup> All reports of the Auditor General are available at: [www.oag-ks.org](http://www.oag-ks.org).

<sup>13</sup> For example, the KTA in 2006 was forced to abolish the tender winner for an SOE (Jugoterm) in Gjilan city after it found that the deputy PM Lutfi Haziri and his political associates are behind the bid. Before becoming deputy PM, Mr. Haziri was mayor of Gjilan. The Auditor General found the Government had pledged €5.0 million of which €3.7 million were actually delivered to repair the damaged caused by an earthquake that struck the region in 2002. Only €1.25 million were spent for intended purpose whereas the destination of €2.45 million was unknown. See full report at:



The PISGs and UNMIK are an example of joint and dualist administration at the same time as there is no a clear cut line who is in charge to do what. The PISGs often complained that they do not have sufficient competencies to do more in certain economic areas. Their vociferous critique against UNMIK, Pillar IV respectively, is that the funds of privatization, Kosovo Pension and Savings Trust are frozen, then a part of Post and Telecommunication profit and banks' deposits is being used abroad, which the PISGs rightly complain against it as a cause of economic recession by withdrawing the money from circulation. The main problem in this governance system between UNMIK and the PISGs is perhaps that some foreign countries have interests in strategic sectors, therefore are selective towards some clientelist local politicians (Domadenik, Mulaj, and Redek, 2006). After all, some local and international stakeholders are interested to keep this system in operation for their benefits.

#### **4. Economic conditions and indicators**

Kosovo's economy today is one of the poorest in Europe (more on poverty in forthcoming sub-section). With an estimated GDP per capita of €1,120 in 2005 (International Monetary Fund – IMF, 2007) Kosovo ranked second lowest in Europe after Moldova where the related figure was \$862 (European Bank for Reconstruction and Development – EBRD, 2006). GDP per capita fell to €1,117 in 2006 and is estimated to fall to €1,114 in 2007 as a result of expected population growth from 2.033 million in 2006 to 2.067 million in 2007. GDP per capita is slightly more than 1/3 of that in the neighboring countries (Albania, FYR Macedonia, Montenegro, and Serbia).

As indicators in Appendix to this paper show, Kosovo's economy suffers from a considerable number of structural distortions and macroeconomic imbalances. Interesting enough, consumption as one of four components of GDP since 2001 to the present day is higher than the GDP itself. Imports are several times higher than exports causing a very large trade deficit which currently is running at around 55% of GDP. In principle, consumption generates production and

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[http://www.oag-ks.org/Reports\\_ENG/AR2004EngGJILAN%20P-AM.PDF](http://www.oag-ks.org/Reports_ENG/AR2004EngGJILAN%20P-AM.PDF). On involvement of Lutfi Haziri in the privatization of Jugoterm and scanned documents of financial transactions through Kasabank, see Një privatizim që korruptoi gjysmën e kabinetit Çeku (A privatization that corrupted half of [Agim] Ceku's cabinet) available at: <http://www.cohu.org/jugoterm.html>.

production investment, which is not so much the case in Kosovo. Most consumption goods are largely imported, thus making Kosovo's population as a consumption society, the money of which largely ends up abroad. The main source of financing this economic paradox is foreign assistance and remittances of Kosovar emigrants that encourage production and investment in the countries that export consumption goods to Kosovo (Mulaj, 2007). Workers' remittances in 2006 accounted for around 15% and donor assistance for over 17% of GDP. This implies that around 1/3 of Kosovo's economy directly depends on abroad.

The donor support, including UNMIK's expenditures, has been declining year by year having a significant impact in the economy. The EU Pillar IV estimated that UNMIK has spent around €2.6 billion since it was established in mid-1999 to 2006 (EU Pillar IV, 2006). The IMF (2007) assessed that UNMIK spent €280 million in 2006 should have and is spending €224 million in 2007. That makes a cumulative of well over €3 billion that would have been sufficient to establish sustainable and efficient institutions of a small market economy like Kosovo. Beside this direct amount within UNMIK only, Zaremba (2007) notes that after eight years, a total €22 billion euros have been spent in Kosovo by the UN and international organizations in all aspects. The fact that this enormous amount has not resulted in economic consolidation and sustainability but produced fragile conditions presented earlier, in the view of Zaremba has one core explanation; Kosovo became the UN's biggest money laundering mission in history where the UN's bureaucrats and some local political mafia filled up their pockets.<sup>14</sup>

A large business activity is going on in informal sector. Private small and medium enterprises (SMEs) which played an important role in economic growth and employment generation in other transition countries still cannot make any significant change in the economy of Kosovo. Their development is being disadvantaged by a number of barriers. It is worth referring to unfavorable loans

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<sup>14</sup> The journalist Maciej Zaremba of Sweden's largest newspaper Dagens Nyheter (30 June, 2007) who has referred to the UN administration as "UNMIKISTAN" and "a bizarre form of government", addresses much of this phenomenon to the European countries in the following way: "ONCE UPON A time the world was easier to understand. Italians were corrupt while Scandinavians stood for honesty. But in Kosovo, *the Viking mafia* is a concept that stands for Danish, Norwegian and Icelandic profiteers. And local Kosovans pray to Allah that some day the incorruptible Italians will catch them".

from commercial banks involving an average yearly interest rate between 12% and 15%, small volume of loans, and short repayment period.

Unemployment has been, is and will be the most pressing economic problem for Kosovo. Unemployment rate in 2006 stood at over 45% or up from around 35% in 2005. It is the highest one in Europe. The Government does not have any employment strategy for the large number of unemployed, mostly unskilled for the labor market demands. The legal framework on social policies such as health care and insurance created just in February 2007 is not yet implemented due to budget constraints (Commission of the European Communities, 2007).

#### **4.1 Widespread poverty, dissatisfaction and frustration are on the rise**

As a result of massive unemployment, poverty in Kosovo is widespread and deepening every year. Economic growth which in 2007 is expected to be very small or unobservable, cannot stop the poverty from rising. The World Bank (2005) study that uses the data of 2002/2003 showed that around 37% of the population was living in poverty line consuming less than €1.42 and over 15% living in extreme (food) poverty of €0.93 consumption per adult per day.<sup>15</sup> In later estimates up to 2006, the World Bank (2007a) maintains that poverty in Kosovo has not risen and the explanation provided in another report (World Bank, 2007b) was because of a problem in data comparability between different samples and large margins of error. The study on the other hand indicates that there were no any real changes in household welfares except a slight rise in income inequality. Certainly, the rise in food prices in 2007 has increased poverty. Group age over 65 enjoy old aged pensions of only €40 per month (see Appendix), which when measured by €1.42 consumption per day, all of them fall in the category of poverty line if they do not have any other incomes. Perhaps the biggest poverty in Kosovo is the lack of human and economic reliable data that would enable better research and decision makings. There has been no population census for over a quarter of the century, the last one being carried out in 1981. For more

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<sup>15</sup> The Living Standards Measurement Study (LSMS) household survey as a standard measure of poverty is usually expressed in USD, but at that time there was no any significant difference in exchange between USD and Euro, therefore the World Bank preferred to use Euro.

than two years, the Ministry of Public Services has been making preparations to register Kosovo's population.

UNDP's quarterly Early Warning Reports, a measure of risk indicators, show that Kosovo's general public is becoming more and more dissatisfied with the economic conditions. Over 76% of the respondents were "very dissatisfied" or "dissatisfied" with current economic trends compared to 73.3% sharing the same opinion in 2005. Confidence on UNMIK has dramatically dropped from over 60% in November 2002 to 31% in June 2007. Similarly, confidence for the PISGs dropped from over 75% to 36% over the same comparative period. More respondents are able to protest due to economic than political reasons (55% versus 31%).<sup>16</sup> All these indicators have alerted, if not alarmed, UNMIK, the PISGs and international players that a major unrest with far reaching consequences is just around the corner, especially after ambiguities that the political status may not be resolved by the end of 2007. A Berlin based think tank European Stability Initiative – ESI (2006), identified the hopes for better economic future of Kosovo through emigration. It recommended that the resolution of Kosovo's political status should be seen through enabling the unemployed youth to go to Western Europe and find temporary job like Romanians, Bulgarians and Poles. Bringing additional police from the EU to deal with frustrated and unemployed people will not improve anything; "migration may help", ESI maintained. The population does not have alternatives of political reaction like other transition countries had, i.e. to bring into power social democrats, "reformed" Communists or any other political party which in Kosovo ideologically are not so diversified. In practice, political parties are more of less the same that can be mostly addressed to the ideology of diversified opportunism. Democratic elections got an alternative choice anyway. The population largely boycotted the elections both at central and local level held on 17 November 2007, where the turnout recorded the lowest level at only 41%. The Government is established from the results of these minority votes.

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<sup>16</sup> Findings of the UNDP (2007) report are drawn from opinion poll of over 1,200 respondents over time.

## 4.2 Kosovo's other forgotten statuses

The media and their diversified profile play a very important role in a transition economy. Kosovo is not short of them but short of diversification. There are 10 daily newspapers, half of which mostly report political news, the other half (also news agencies) containing between 6-10 pages called VIP to report what Paris Hilton, Nicole Kidman and other famous celebrities are doing. Public TV – RTK regularly broadcasts matches of the English Premier League. Much of the unemployed youth and students have become so addicted that it would not be a surprise for someone to find that Kosovo has more fans per capita of the English Premier League than does England. It certainly shows that the youth is able to adapt to modern trends but the trend offered to them is not the one from which they can benefit anything. Poor Kosovar football also does not benefit much either. The UN's largest development agency and assistance provider – United Nations Development Programme (UNDP) – is playing football in Kosovo. It has appointed a Kosovo born footballer Lorik Cana who plays as midfielder for Olympique de Marseille and Albania's national team, as UNDP's ambassador to promote the battle against poverty in Kosovo.) UNDP and the U.S. Agency for International Development (USAID) which often fund projects jointly, apply discrimination against development and never deal with respective complaints.<sup>17</sup> Many funds of international organizations have gone through incompetent and bad research as a consequence of favoritism, clientelism, nepotism, outright discrimination, jalousie, and hostility against professionalism applied by local personnel. Neither UNDP's hotline nor USAID's Office of the Ombudsman and Inspector General have been committed to investigate complaints from Kosovo.<sup>18</sup>

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<sup>17</sup> The author of this paper has submitted a complaint against UNDP's mission in Kosovo to the UNDP's headquarters in New York in December 2006 for discrimination in the selection process of a joint project of UNDP and USAID on Kosovo Early Warning System. The author was informed in advance by local employees of UNDP that your (i.e. my) application will not be taken into consideration at all, for the reasons as they stated, that I was trying to build a monopoly in this sector of research (Koha Ditore, 13 November, 2006). The UNDP's hotline stated that there was no any intention to discriminate me except the desire to bring in new analysts, a desire that had no legal basis and was against the terms of reference. The investigation specialist of UNDP's hotline said that the report is ready, but was never made neither public nor available to me.

<sup>18</sup> After my first complaint, I only got an answer from UNDP's investigation specialist in New York stating that my complaint does not affect my future applications. I submitted two more applications for the same project, one as individual analyst and the other as project coordinator. Unlike in the first one where I was accused of trying to build a monopoly, local personnel at UNDP in Kosovo told me that I was not even short listed in the second application. I received no answer for the third application and submitted complaints for investigation to UNDP's and USAID's HQ in New York and Washington D.C. USAID's Office of the Ombudsman once told me

If one is to ask a citizen of the former Yugoslavia and Kosovo to remember something nostalgic about the system of self-management socialism, the most likely answer they will provide is: that was the system of education and health. These are the two sectors where UNMIK has fully transferred the power to the PISGs. The situation in the health sector has deteriorated so much that emergency centre in the hospital of Pristina often does not have basic medicines for the patients and sutures to hold the skin of open wounds.

Education that is seen as a way out of poverty has become a poverty in itself. There are currently not less than 30 private universities in Kosovo in Kosovo. They are to provide higher education in a country of over 2 million inhabitants, where about 50% of the population is under 25 years old, and where illiteracy rate is 6% (UNDP, 2006b). Now, compare it with the U.K. that has a population of 60 million and 120 universities, excluding the availability of hundreds of million students across the world. Slovenia with approximately the same number of inhabitants like Kosovo has got four universities, all of them public. Most private universities in Kosovo have got some education for business, which in reality is the business of education, i.e. to collect higher fees from poor students than in public university.

Internet cafes that spread like mushrooms in a forest after rainfall throughout Kosovo, manage to make profits largely by hosting the youth who play a violent game called “counter strike.” These and other examples of youth degeneration refute any claim of deeply corrupted institutions and academics that Kosovo’s best resource is her people, in particular the youth, which under present governance system it is not.

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that I should submit complaints for this project (that USAID finances the largest part) to UNDP. The U.S. is very much interested to investigate who finances whom in Middle East and elsewhere in the world, but constantly turns a blind eye and deaf ear to the misuse of its funds and discrimination in Kosovo. Moreover, USAID’s Ombudsman and Inspector General have left USAID’s employees in Kosovo to pursue the practice of misconduct which, apart from discrimination in their projects, influence discrimination elsewhere. That may fit into what Stiglitz (2004) would describe as “the ideas America pushes abroad are markedly different from what it practices at home.”

## **5. From the UN to an EU mission: is interim mission turning permanent?**

Perhaps the first mistake with Kosovo was made in the UN Resolution 1244 not only in the text it contained, but also because it did specify a timeframe of the mission and what will happen to Kosovo, or was the UN administration interim as it was said, or is likely to become permanent as it appears? One way out or an exit strategy could be understood by the functions and the powers that UNMIK was exercising to be transferred to the Government of Kosovo. After status talks in Vienna and presenting of Ahtisaari's Proposal, the UN wants to end that interim administration by transferring it to the EU. A question here arises: if Kosovo does not need an outside administration such as the UN or the EU, then can it go to independence on its own if it wants? The answer from what we observed in Kosovo's politics and economy is, No.

Ahtisaari was appointed as the UN's Special Envoy for Kosovo, to mediate the talks between Kosovo and Serbia over the future of Kosovo. The talks started in early 2006 in Vienna and coordinated through the UN Office of the Special Envoy for Kosovo (UNOSEK), that includes the staff from NATO, the EU, and the U.S.A. Serbia is represented by her government, Kosovo by the Unity Team involving all government and opposition high ranking officials. A total of seven rounds of talks were held in 2006 before Ahtisaari prepared the Proposal and made it public in February 2007.<sup>19</sup>

The Proposal came as a surprise with huge favors to the Kosovo Serbs and no mentioning of independence so much promised by Kosovo's government, except giving Kosovo a new political identity and independence from Serbia, but monitored by the EU. It appears that the core objective of this Proposal is to get rid of major roadblock – the UN's Resolution 1244 at any cost, by building other impediments. Even in its current content that offends the rights of the majority of population, is being opposed by Serbia and her traditional ally Russia, which threatened to use the veto in the UN's Security Council against the Proposal. The EU, however, is on the way to send its mission and replace UNMIK.

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<sup>19</sup> The Proposal is available at: <http://www.unosek.org/unosek/en/statusproposal.html>

For the relevance of this article, the discussion will mainly consider the Proposal's economic implications. It offers Kosovo the chance to have access and become member of international financial institutions. The International Civilian Representative (which is like SRSG but as a representative of the EU) will play a role in appointments in key economic positions. SOEs and public companies remain under the jurisdiction of the KTA and foreigners again will have major say. In the section on external debt, the Proposal says that Kosovo will assume its share of the external debt of the Republic of Serbia, but is silent about huge damages that Serbia caused Kosovo and the property stolen by Serbia's during the violent rule. These provisions of Ahtisaari's proposal do not guarantee any economic perspective, and in general is a continuation of existing mission with a different name and similar role.

An issue which in the Proposal is not directly related to the economy is decentralization on ethnic basis to create Serb municipalities and enclaves with direct ties to Belgrade. This may have serious implications in limiting the movement of goods and services. From political perspective, it may very easily lead to partition of Kosovo. The Unity Team has not explained this risk to the population and was largely not transparent during the entire process of negotiations. What the Unity appears to have been interested was fat salaries in the negotiation process paid by Kosovo's poor budget. The only Kosovo group opposing Ahtisaari's Proposal is the movement Vetvendosje (Albanian for Self-determination), an organization gathering mainly the youth. Vetvendosje's opposition to UNMIK rule, the PISGs and Ahtisaari's Proposal is only through peaceful protests, for which the Unity Team does not care. The rest of the population is passive, short-sighted, does neither know what went and is going on, nor what may happen in a distant future.

### **Conclusions and lessons learned**

Managing political and economic transition in Kosovo through the UN and institutional transplantation was obviously a better alternative than go it alone with enormous constraints, inexperience and limited resources. Arguments that what has already been accomplished in the economy is a bed of roses and must



be never compared to what might have happened without UNMIK presence, can be found days and nights. However, the alternatives within the existing mission for the resources spent would have had resulted in remarkably better socio-economic conditions. Since we are not in a position to rerun the experiment elsewhere due to specificity of slow-moving institutions and the impact of cultural factors, it is useful to learn some useful lessons from the experience that involved trial and error.

The UN mission in Kosovo did not have any carefully planned exit strategy in sight. That is why its mission is trapped. Transferring it to the EU does not mean that the mission is accomplished. Having into consideration the resources it involved, the mission failed to provide better and sustainable economic perspective for majority of the population. The drawbacks were and still are related to non-coordination, lack of transparency and accountability. Many UN and development agencies personnel would face punishment if they were to act in their home countries as they did in Kosovo. Such a behavior is not their born habit; it is generated in Kosovo. The UN and EU in future should ensure that their envoys are more accountable to the headquarters. Imposing modern legal framework and rules in the countries where the mission is deployed, is fine. Better enforcement of them is what future UN and the EU mission should consider seriously.

It should be reminded that UNMIK and the PISGs belong to different slow-moving institutions, therefore their work together was not easy, nor it will be easy under forthcoming EU mission. As fast-moving institutions, UNMIK and the PISGs are partially responsible for underdevelopment, unemployment, and poverty in Kosovo. The rest of responsibility may be addressed to certain segments of the population for not pushing the changes when they are necessary, in particular the change in peoples' mentality towards modern fast-moving institutions and their "excessive love and respect" for some countries that would be the first to recognize Kosovo's formal political independence. The population is missing a strategic thinking to gradually build the true independence at base in cooperation with international partners, after which it would have less foreign presence and better relation with them. A collective transformation in the way of thinking

should happen, regardless that it may take time. It is true that Kosovo Albanians learn from the past but do not learn lessons for the future. There is a growing consensus at home and among some foreign countries that political independence should have been declared and recognized immediately after the deployment of the UN for the purpose of having a better status today, and not delayed to become more uncertain for the future. By the same token, someone today may think that raising a loud voice against development agencies for the projects' mismanagement and discrimination even in individual recruitments, is of less importance and urgency compared to other major issues, therefore let it go and resolve later. After some time, when the problem evolves into a system of operation, it is very easy to find out the consequences in economic development for not reacting earlier, like in the case of political status. And this is what features many areas in Kosovo – non-reaction until the consequences are seriously felt.

In current conditions of widespread unemployment, deep poverty, the youth without perspective, many fear that tensions that may have far reaching consequences are just around the corner. Although the NATO-lead peacekeeping force (KFOR) is not allowing this to happen for a moment, social problems, disappointment, and Serb enclaves blessed by Ahtisaari's humiliating Proposal, will keep the situation fragile.

The status that is not yet forgotten is the final political status, though this too, has become uncertain. Other statuses explored in this paper are not receiving due attention. If the EU is planning to commit more resources than it has so far, then it should spend them differently, and that is, invest in changing the behavior of Kosovo's slow-moving institutions. Only this approach can make Kosovo more economically viable and sustainable in the long run. Continuing current attempts with similar management methodology may result in some economic development, but at the end of the day high costs are very hard to justify suboptimal results. The EU should remember that in Kosovo's economic development far more than economics is involved.

**Appendix: Kosovo's main economic indicators (in mil. of Euros unless otherwise indicated)**

	2001 <sup>a)</sup>	2002 <sup>a)*</sup>	2003 <sup>a)*</sup>	2004 <sup>a)*</sup>	2005 <sup>b)*</sup>	2006 <sup>b)*</sup>	2007 <sup>b)**</sup>
Population (in '000)	1,868	1,900	1,932	1,965	1,999	2,033	2,067
GDP	2,439	2,447	2,426	2,516	2,238	2,270	2,303
Consumption	2,680	2,623	2,600	2,699	2,792	2,862	2,772
Investment	661	603	572	591	583	666	793
Government expenditures	240	402	543	749	698	723	724
Net Export (Exports-Imports)	-901	-779	-746	-774	-1,136	-1,259	-1,262
➤ Exports	372	321	300	298	204	249	284
➤ Imports	1,273	1,100	1,046	1,072	1,340	1,508	1,546
GPD per capita (in €)	1,305	1,235	1,256	1,301	1,120	1,117	1,114
Workers' remittances	317	341	341	341	281	318	410
Total budget	232	500	590	601	628	713	693
Foreign assistance	1,170	887	688	573	491	465	376
Employment rate (%) <sup>c)</sup>	19.6	23.8	25.3	27.7	28.5	n.a.	n.a.
Unemployment rate (%) <sup>c)</sup>	57.1	55.0	49.7	39.7	41.4	n.a.	n.a.
Population in poverty line (%) <sup>c)</sup>	50.3	37.7	38.1	43.5	34.8	45.1	-
Population in extreme poverty (%) <sup>c)</sup>	11.9	15.4	13.9	12.4	12.7	16.7	-
Number of registered job-seekers	n/a	257,505 <sup>d)</sup>	280,923 <sup>d)</sup>	300,697 <sup>d)</sup>	319,72 <sup>e)</sup>	326,026 <sup>f)</sup>	332,013 <sup>g)</sup>
Basic pensions (in €, month)	-	-	-	40	40	40	40

\* Estimated;

\*\* Projected;

n.a. data not available or could not be obtained.

Note: GDP variables C+I+G+(NX-I) do not add up the numbers of aggregate GDP due to methodology used by the IMF. Amounts in the variable Government expenditures (G) are spread in Consumption and Investment. Following this, C+I+ (NX-I) adds total GDP as presented by the IMF and shown in the table.

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