Analysis on Public Debt

Kosovo

CSOs as equal partners in monitoring public finances

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This document has been produced as a part of the project "CSOs as equal partners in the monitoring of public finance" which started beginning of 2016 and is implemented by a consortium of 10 organizations from 7 countries and will last for four years.

The aim of the project is to improve the transparency and accountability of policy and decision making in the area of public finances through strengthening the role and voice of NGOs in monitoring the institutions that operate in the area of public finances. In this way, the project will strengthen CSO knowledge of public finance and IFIs and improve CSO capacities for monitoring. Additionally, it will help advocate for transparency, accountability and effectiveness from public institutions in public finance. Moreover, this project will build know-how in advocating for sustainability, transparency and accountability of public finance and IFIs. This project will also increase networking and cooperation of CSOs on monitoring of public finance at regional and EU level. Lastly, it will increase the understanding of the media and wider public of the challenges in public finance and the impacts of IFIs.

Key project activities are research and monitoring, advocacy, capacity building and transfer of knowledge/practices and networking in the field of the 4 specific topics: public debt, public-private partnerships, tax justice and public infrastructure.

More information about the project can be found on http://wings-of-hope.ba/balkan-monitoring-public-finance/ and on the Facebook Page Balkan Monitoring Public Finances

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CONTENT

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INTRODUCTION

The study was intended to present the foundation for understanding the recent crisis from 2008 on, to acquire an insight into the impacts on Slovenia's recent reforms, and to determine …

The analysis has an attempt to summarize the consequences of the financial crisis in Slovenia, while it also presents some new results…

The research process is a discovery and one of the most fulfilling parts of the process involves uncovering new facts and adding new insights into unresolved debates about debt economy, debt state and its related public debt...[1]

Generally, **borrowing** is understood as an instrument allows the State to bridge the discrepancies in budget revenues and expenditure. Recently Slovenia has been quite active in the field of borrowing, mostly on account of restructuring of banks with the aim to create stability in the banking sector. Furthermore, Wolfgang **Streeck's** (2014) conceptualization of the **debt state** is illustrated as "a state which covers a large, possibly rising part of its expenditure through borrowing rather than taxation, thereby accumulating a debt mountain that it has to finance with an ever-greater share of its revenue." When are we talking about the debt state, how can we determine that Slovenia is or is not the debt state? The **influence** that finance holds over politics and society is therefore a product of its position in the economy. This tendency towards concentration and centralization in the **debt** system makes everyone else in society — states, firms and households alike — increasingly dependent on an ever-smaller number of private banks and financial institutions for their own reproduction.[2]

[1] This 1st para will include the short presentation of the paper, its chapters, and methodology... in the making...
[2] Defeating the Global Bankocracy, Jerome Ross, ROAR 3, 2016, https://roarmag.org/magazine/defeating-the-global-bankocracy/

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1. PUBLIC DEBT

Kosovo has introduced and adopted numerous constitutional and legal stipulations on preventing public debt from reaching unsustainable growth. Such stipulations include (i) the Law on Public Debt that sets the maximum public debt-to GDP ratio at 40 percent (a recent amendment of the fiscal rule reduced it to 30 percent of GDP); (ii) a constitutional stipulation, according to which a parliamentary ratification with a qualified majority is required when the Government makes external borrowing (including for highly concessional International Development Association (IDA) credits), (iii) a law on public financial management and accountability that requires any additional budget to be "deficit neutral"; and (iv) a specific fiscal rule which would, with few exceptions, limit overall budgetary deficits, to 2 percent of GDP (as agreed with the International Monetary Fund [IMF]).[3] According to the Law on Public Debt,[4] Kosovo is granted the authority to "borrow funds, make loan guarantees, and to pay the principal and interest on its debt". In the current setting, public debt is estimated to only 12.5% of GDP, according to the Central Bank, at about 749 million euros in 2015, with an annual increase of 28.5%, is deemed as a rate of no real concern for the time being. However, public expenditure continues to show its Achilles' heel in some particular areas. The public sector employs 83,000 citizens or ¼ of the total work force, and 34% of the total public expenditure – 540 million euros – is funneled to support wages and related expenses in the public sector. Kosovo's relatively low public debt has not been a matter of concern, considering recent reports from both the IMF and the World Bank. Moreover, to avoid public debt from rising to unsustainable levels, Kosovo has established a constitutional fiscal rule, and has adopted competitively low corporate tax rates.[5] However, no relevant debates on the matter have occurred, mainly because currently there is little to debate. The only issue to be monitored for the near future is whether the rapid yearly pace of debt growth will persist in similarly remarkable rates, which would then become an issue for public debate.

In June 2016, a reform strategy named public financial management (PFM) entered into force in Kosovo's financial structure. Along with this strategy, there are four other ones that altogether form a so-called strategic package as part of the public administration reform package. Part of this newly adopted strategy suggests improving revenue forecasting and the aspect of macroeconomics as well as

[3] "The World Bank in Kosovo, Country Snapshot", The World Bank, April 2016
http://pubdocs.worldbank.org/en/419461462386476530/World-Bank-Kosovo-Program-Snapshot-April-2016.pdf
[4] The Law on Public Debt, No. 03/L – 175, The Republic of Kosovo
http://www.kuvendikosoves.org/common/docs/ligjet/2009-175-alb.pdf
[5] The Heritage Foundation, Kosovo
http://www.heritage.org/index/pdf/2017/countries/kosovo.pdf

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collecting the fiscal discipline. Even though Kosovo receives loans from domestically as well as from international actors, public debt is not as high as forecasted; however, the suggestion is for budget commitments to be under control. Also, there are a few challenges that the PFM reform might face, such as the combination of tax and customs administrations. Another priority of this reform is to contribute to making the budget credible. That is, making improvements to the quality of medium-term budgeting, preparing budget, and providing information regarding investments in capital.[6]

Kosovo's debt has been historically relatively low. During 2010 and 2011, the vast majority of Kosovo's debt consisted of World Bank – IBRD CLC loan, which was inherited in the aftermath of Kosovo's country's independence. The remaining part of debt, moreover, was borrowed from the International Monetary Fund (IMF) and World Bank – IDA. In September 2016, Kosovo's public debt reached the value of EUR 842.1 million, which amounts for 17 percent higher, when compared to the previous year's. Public debt, as a percentage to GDP, experienced an increased level percentage from 12.5 percent in September 2015, to around 14.3 percent in September, 2016. As such, the accelerated public debt increase, is mainly a result of the growth of domestic debt of 34.5 percent (which reached EUR 473.6 million), whereas the external debt increased slightly by 0.3 percent, reaching EUR 368.4 million. Also, in September 2017, there was a documented decreased level of the share of the external public debt to the total domestic debt, from 51 to 43.8 percent.[7] For the period of 2016-2018, according to the Central Bank of Kosovo, the Kosovar government has initially foreseen to carry out numerous capital projects, premeditated to be financed by international borrowings.

Most of the projects approved for funding, are aforethought to be engaged in the improvement of infrastructure, social development, and welfare promotion. Moreover, numerous other projects have been tabled for funding approval from the government, which are initially intended to rehabilitate, among others, agriculture, irrigation, hospital infrastructure, energy efficiency, welfare, social housing, etc. As such, the Ministry of Finance, according to the Central Bank of Kosovo,[8] has already started securing contacts with several international financial institutions (IFIs), and it will further process it in the following months. Based on the Central Bank's estimates, potential creditors all have an interest in common: financially supporting projects. Adding more to that, it remains under the responsibility of the

[6] "Public Finance Management Reform Strategy", Ministry of Finance, June 2016.
http://www.kryeministri-ks.net/repository/docs/Public_Finance_Management_Reform_Strategy2016-2020.pdf
[7] "Quarterly Assessment of the Economy", Central Bank of Kosovo, 2016
http://bqk-kos.org/repository/docs/2015/01.%20CBK_Q3%202016.engl.pdf
[8] "Macroeconomic Developments Report" Central Bank of Kosovo, 2016.
http://bqk-kos.org/repository/docs/2015/CBK_Macroeconomic%20developments%204.%20doc.pdf

line Ministries, to carry on with projects designing, and thus pushing forward the negotiation process with the potential creditors, in order to particularize and exemplify it.

In September 2014, public debt accounted for 10.2% of the country's total GDP, however, in the following year, it has reached 12.5 percent, representing a slightly low level of public debt. Although Kosovo has witnessed an increased debt level, the country is classified, compared to the region, as the country with the lowest public debt levels. Bearing that in mind, Kosovo remains relatively far from exceeding its value of public debt in relation to GDP, considering that the established fiscal regulation, regulating the public debt, stipulates that the highest levels of general public debt, shall not exceed 40 percent of the total GDP. The average of the public debt in SEE in 2015, according to the IMF, has accounted for 60.5 percent of GDP. While the ratio of public debt to GDP during 2015, among regional countries, witnessed an increase of an average of 2.9 percent, Kosovo's public debt ratio to GDP, in September, was 2.3 percentage.[9]

The vast majority of public debt, during the previous years, was composed of external debt. Mainly due to the accelerated growth of domestic public debt, however, the share of the external debt and domestic debt in the structure of the general public debt remained almost the same. On a similar vein, around 51 percent of the total public debt, in September, 2015, stood as international debt, largely owned by the *International Bank for Reconstruction and Developments*, *IBRD*, (49.3 percent of total international public debt) and *International Monetary Fund*, *IMF*, (36.1 percent of total international debt).[10] The remaining part, 49 percent of public debt, which is mostly constituted from government debt to commercial banks (71 percent of total domestic debt) and pension funds (22 percent of total public domestic debt), is domestic debt.

As previously mentioned, under the Law on Public Debt, the Republic of Kosovo remains authorized "to borrow money; to make loan guarantees, to pay expenses for debt issuance and to pay the principal and interest on its State Debt". The given law, additionally, provides The Ministry of Finance the stated authority, according to which, the Minister is vested as the sole entity to incur State Debt for the designated purposes (The Law on Public Debt, article 3).[11] As such, the given Ministry, under the given law, is delegated as the only institutional body to enter into State Debt. Moreover, if the state desires to

[9] "Macroeconomic Developments Report" Central Bank of Kosovo, 2016.
http://bqk-kos.org/repository/docs/2015/CBK_Macroeconomic%20developments%204.%20doc.pdf
[10] Macroeconomic Developments Report" Central Bank of Kosovo, 2016.
http://bqk-kos.org/repository/docs/2015/CBK_Macroeconomic%20developments%204.%20doc.pdf
[11] The Law on Public Debt, No. 03/L - 175
http://www.kuvendikosoves.org/common/docs/ligjet/2009-175-alb.pdf

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ensure compliance with the given law to the fullest, the total amount of debt should not exceed the 40% of GDP. When calculating this limitation, in accordance with this law, the State Guarantees shall be treated as State Debt. As such, the Ministry of Finance has the legal responsibility to compile the State Debt Program, through which, is both ensured and maintained a sustainable debt, in accordance with the fiscal and macroeconomic framework.

Although Kosovo, based on estimated data, is fairly stable in terms of public debt, the country is nevertheless challenged with debt sustainability. According to the World Bank, Kosovo possesses limited, but growing state guarantees and negligible municipal debt. In terms of borrowings, the government completely relied on foreign borrowings, secured from the international financial institutions. Whereas in 2014, the structure of government borrowing tipped to the government's complete dependence on domestic borrowing, although in 2015, the newly compiled IMF programme triggered the government's return to foreign borrowing. Despite its inexpensiveness and its sensitiveness towards political uncertainty, the domestic market in Kosovo remains shallow.[12]

In regards with *public debt*, Kosovo, the landlocked economy, is fairly stable when comparing with other countries in the region. Although Kosovo's public debt, in 2016, accounted for only 14.3 percent of the GDP, the past two years has witnessed visible increase of public debt levels, and this growth is expected to continue. Although countries like Kosovo, characterized with a low development, are stimulated to increase their public debt levels, it should carefully manage the debt received from international financial institutions. As such, rather than spending it for salaries or social transfers Kosovo should invest in projects that yield financial benefits.[13] On a similar vein, Kosovo has increased its spending on salaries and social transfers for the past two years, and thus impairing the capital investments. To illustrate it, in 2013, public investments reached 10.1 percent of the GDP, while in 2017, such percentage decreased to 7.7. Yet, while public spending on salaries, in 2013, accounted for 7.9 percent of the GDP, and that of social subsidies reached 4.2 percent of the GDP, Kosovo has increased the spending on the two, to 9.2 percent and 7.4 respectively. As such, according to Demi, being of the opinion that Kosovo has the highest economic growth hasn't done any good to its citizens, defining such perspective as an "only a desperate attempt to grab on to a positive indicator, which at the end of the day has not brought any improvements to the life of citizens in any way." He notes, additionally, that the fastest-growing economies are not typically among the largest, most developed

[13] "Insufficient Growth", Agron Demi, Prishtina Insight, May 2017
http://prishtinainsight.com/insufficient-growth/

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countries, but instead, they are usually the poorest. Certain countries, with a GDP per capita lower than 4,470 euros per year, which are undergoing any sort of economic growth under 5 percent, are experiencing economic regression, "or in the best case – stagnation."

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CONCLUSIONS AND RECOMMENDATIONS

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