Republika e Kosovës

Republika Kosova - Republic of Kosovo

Qeveria –Vlada–Government

ECONOMIC REFORM PROGRAMME (ERP) [1]

2025-2027

[1] For any difference between ERP versions, the English language prevails

Contents

LIST OF ABBREVIATIONS

ADR	Alternative Dispute Resolution	**MAFRD**	Ministry of Agriculture, Forestry and Rural Development
ALM	Active Labour Market	**MCC**	Millennium Challenge Corporation
ARDP	Agriculture and Rural Development Programme	**MCYS**	Ministry of Culture, Youth and Sport
BCI	Business Climate Indicator	**MED**	Ministry of Economic Development
BEEPS	Business Environment and Enterprise Performance Survey	**MESP**	Ministry of Environment and Spatial Planning
CBK	Central Bank of Kosovo	**MEST**	Ministry of Education, Science and Technology
CEFTA	Central European Free Trade Agreement	**MLSW**	Ministry of Labour and Social Welfare
CMIS	Case Management Information System	**MoF**	Ministry of Finance
CPI	Consumer Price Index	**MOJ**	Ministry of Justice
EARK	Employment Agency of the Republic of Kosovo	**MSME**	Micro, Small and Medium Enterprises
EC	European Commission	**MTEF**	Medium Term Expenditure Framework
EE	Energy Efficiency	**MTI**	Ministry of Trade and Industry
EED	Energy Efficiency Directive	**NDS**	National Development Strategy
EFTA	European Free Trade Association	**NEET**	Not in Education, Employment, or Training
EMIS	Education Management Information System	**NGO**	Nongovernmental Organizations
EPC	Engineering, Procurement and Construction	**NPISAA**	National Programme for Implementation of the SAA
ERA	European Reform Agenda	**OECD**	Organisation for Economic Cooperation and Development
ERP	Economic Reforms Program	**OPEC**	Organization of the Petroleum Exporting Countries
EU	European Union	**OPM**	The Office of the Prime Minister
FDI	Foreign Direct Investment	**PFM**	Public Finance Management
GDP	Gross Domestic Product	**PISA**	Programme for International Student Assessment
GoK	Government of Kosovo	**PPRC**	Public Procurement Regulatory Commission
HBS	Household Budget Survey	**REER**	Real Effective Exchange Rate
HE	Higher Education	**RES**	Renewable Energy Sources
HEI	Higher Education Institutions	**RDI**	Research, Development and Innovation
HEMIS	Higher Education Management Information System	**SEED**	The South East Europe harmonised qualification of professional Drivers
HHI	Herfindahl- Hirschman Index	**SEETO**	South East Europe Transport Observatory
IFI	International Financial Institutions	**SIDA**	Swedish International Development Agency
IMF	International Monetary Fund	**SME**	Small and Medium Businesses
IPA	The Instrument for Pre-Accession Assistance	**SPO**	Strategic Planning Office
KAA	Kosovo Accreditation Agency	**STIKK**	The Kosovo Association of Information and Communication Technology
KB	Kosovo's Budget	**TPD**	Tourism Product Development
KCA	Kosova Cadastral Agency	**TPP**	Thermo Power Plant
KEDS	Kosovo Electricity Distribution and Supply	**ULC**	Unit Labour Costs
KESP	Kosovo Education Strategic Plan	**UNDP**	United Nations Development Programme
KFCG	Kosovo Fund for Credit Guarantees	**USAID**	United States Agency for International Development
KIESA	Kosovo Investment and Enterprise Support Agency	**VET**	Vocational Education Training
LFPR	Labour Force Participation Rate	**WB**	World Bank
LFS	Labour Force Survey	**WTO**	World Trade Organization
LMIS	Labour Management Information System		

1. OVERALL POLICY FRAMEWORK AND OBJECTIVES

The ERP 2025- 2027 process was led by Ministry of Finance, Labour and Transfers as the National Coordinator. This preparation process of the ERP is to assure that short-term activities from the draft ERP were included in the National Development Plan 2024-2026 and are consistent with activities planned in the draft SAA National Implementation Plan (SAANIP) and the European Reform Agenda (ERA), as well as with the 2025 Budget.

Considering the current economic structure of Kosovo and the obstacles to economic growth, it is necessary to orient the reforms aimed at a functioning market economy and boosting competitiveness, which are also reflected as the main fundamentals in the Government Program 2021- 2025.

In this line, the Government remains committed to supporting economic growth and improving employment prospects. The overall ERP policy framework is a combination of: (1) economic program aiming to strengthen resilience against adverse shocks; (2) a rule-based fiscal policy oriented towards stability of public finances and, within the available fiscal space, supporting economic growth through capital investments and increased funding for priority development areas.

2. IMPLEMENTATION OF POLICY GUIDANCE

[1A]. Implement the foreseen shift in the 2024 budget spending structure from current to capital expenditure while ensuring compliance with the fiscal rules. [1B]. Increase budgetary transparency by further reducing blanket allocations. [1C]. Enhance the revenue side by reducing loopholes and exemptions through amendments to tax legislation, including personal income tax (PIT), corporate income tax (CIT) and value added tax (VAT).

[1A]. The budget spending structure in 2024 compared to 2023 had a slight positive change from current to capital expenditures. The share of current expenditures in total budget declined from 72.7 % in 2023 to 72.3 % in 2024. The share of capital investments in total budget experienced a slight improvement from 25.4% in 2023 to 25.9% in 2024. The fiscal rules were also implemented as foreseen by law.

[1B]. Compared to 2023 the share of contingencies in the total budget of 2024 experienced a substantial reduction from 10% to 3.1%. Related to transparency increase, it is worth noting that the textual part of the budget law provides reasonable explanations of purposes for the contingencies and procedures for their allocation.

[1C]. Based on the legislative plan for 2025, the Corporate Income Tax (CIT) law will be amended, while new laws will be drafted for Personal Income Tax (PIT) and Value Added Tax (VAT). Through these changes in tax legislations, the aim is to improve revenue collection and review of all tax exemptions in order to minimize tax loopholes.

[2A]. Undertake and publish a review of tax expenditure quantifying the size of the revenue forgone from all exemptions, preferential rates and special regimes. [2B]. Improve the execution rate of capital spending including by establishing the linkages between the e-procurement and Kosovo Financial Management Information System (KFMIS) systems, following the recommendations made under the IMF's updated Public Investment Management Assessment. [2C]. Improve financial oversight and accountability of Publicly Owned Enterprises (POEs) by approving and publishing their annual performance report; adopt amendments to the POEs' Law to improve their corporate governance.

[2A]. The Tax Policy division within the Economic Policy Department (MFLT) with the support of World Bank completed the assessment of tax expenditure, which assessment has not yet been published. However, these assessments are being updated for the year 2023. At the same time, WB continue to provide trainings for the assessment of tax expenditure for the staff, in order to use this model in the future as well.

[2B]. Many new processes have been developed and are now being integrated with the existing components. This development is expected to bring noticeable improvements in the functionality and performance of the product. After its completion, we will move on to the finalization and integration of the last changes. The product is expected to be ready for launch in the short term, specifically by the end of February 2025 (the project's completion date), after the final testing and its closure.

[2C]. The POE Monitoring Unit within Ministry of Economy, continue to reporting on quarterly basis the POE debt data and quarterly financial reports to the MFLT. This enables MFLT to conduct the POE-related fiscal risk analysis. These quarterly financial reports are being published on the website of the MFLT, as stipulated by the EU Macro Financial Assistance and World Bank Development Policy Loan. The Annual POE Performance Report for year 2022 is approved by the Parliament.

The Concept Document of the Law on POEs is planned to be drafted during 2025, while the Law on POEs in 2026. Through this law, the government aims to create the framework for the functioning of the POE sector, and align the corporate governance of PEs with recognized international standards, improving the performance of POEs, increasing the value of their assets and providing quality services to the public.

Furthermore, the government is continuing its efforts regarding the stabilization of the boards and management of the POEs through a transparent and meritocratic process of restructuring.

[3A]. Continue to thoroughly assess price developments and possible second-round effects and stand ready to use the limited tools available under the chosen monetary framework to ensure price stability. [3B]. Continue efforts to ensure that core areas of the central bank are adequately staffed, particularly by finding ways to attract and retain skilled staff. [3C]. Enhance risk-based supervision in line with best international and European practices,

including by further strengthening the monitoring toolkit and the reporting framework across the banking system and improving data collection to enable a comprehensive assessment of financial sector risks.

[3A]. CBK publishes monthly time series from inflation expectations survey (conducted with commercial banks). Additionally, CBK publishes **time series of core inflation data** monthly. Forecasting and analytical capacities are expected to improve throughout our medium-term work plan and objectives.

[3B]. In line with this recommendation, and following consultations with relevant international institutions, the CBK has made significant changes to its organisational structure by creating a new resolution department and ensuring the segregation of duties within the core areas through the creation of new units. Recruitment continued actively throughout the year and some transfers were made to support the core areas. Efforts are focused on attracting and retaining skilled professionals by improving working conditions and incentives. This approach ensures that key positions are effectively covered and that the process is on a positive trajectory.

[3C]. CBK is dedicated to continuously enhance risk-based supervision in line with the highest international and European standards. This is achieved by improving risk-based supervision mechanisms, techniques, and systems to enable the continuous monitoring, assessment, and management of risks within the financial sector. CBK advocates a proactive approach to risk identification and timely intervention, with the objective of maintaining the stability and soundness of financial institutions.

To further strengthening the reporting framework, in January of 2023 CBK has adopted new regulation and reporting forms regarding Liquidity Coverage Ratio and Net Stable Funding Ratio. While, this year CBK has implemented new reporting forms regarding credit exposures of companies exposed to transition costs related to the implementation of the carbon border adjustment mechanism. Currently, CBK is working in implementing Supervisory Review and Evaluation Process (SREP) and harmonizing existing reporting forms with Finrep and Corep framework. On the other hand, to be in line with best international and European practices, CBK ensures capacity building and trainings by providing ongoing trainings to supervisory staff on advanced risk management techniques and engaging in knowledge-sharing initiatives with international bodies.

3. MACROECONOMIC FRAMEWORK

3.1. External Economic Environment

Although the ongoing challenges posed by geopolitical tensions and the lasting impact of high inflation, the global economy showed notable resilience, where the global growth is project to be in line with the April 2024 World Economic Outlook (WEO) forecast, at 3.2% in 2024. As a projection for economic growth remain the same, notable upward revisions taken place to the forecast for the United States, offsetting downward revision for other advanced economies in particular, the largest European countries. Despite the growth being projected to be 0.2pp less than the year before, consumptions remain robust, and labor markets are resilient, especially in advanced economies. This positive momentum is complemented by steady growth in global services trade, with sectors like tourism and digital services continuing to expand. However, growth remains uneven across regions, with some advanced economies, particularly in Europe, experiencing slower recoveries compared to their emerging counterparts.

According to the latest projections from the International Monetary Fund (IMF) in October 2024[2], global economic growth is expected to remain stable in the medium term. Global growth forecast showing no significant change from 2024 in 2025 and 2026. Advanced economies are estimated to have a modest growth, where it is projected to increase from 1.7% in 2023 to 1.8% in 2024, while 2025 remains unaltered. Moreover, emerging market and developing economies are expected to experience a more considerable growth, moving from 4.4% in 2023 and projected to register a modest decline 4.2% in 2024. This more tempered decline in emerging markets highlights their relatively stronger economic resilience despite the global challenges.

On the other hand, according to the WEO October 2024, global headline inflation is expected to decline, from 6.7% in 2024 to 4.3% in 2025 due to cyclical imbalances being eased. This disinflation process to reach inflation targets is expected to progress more rapidly in the advanced economies rather than the emerging and developing markets. However, there are several obstacles that could disrupt the process such as sudden eruptions in financial market volatility, new spikes in commodity prices and persistent geopolitical tensions which could result in tighter monetary policies and tighter financial conditions. Global disinflation continues to progress, broadly in line with the baseline. Goods prices have stabilized, but services price inflation remains elevated in many regions, pointing to the importance of understanding sectoral dynamics and the calibrating monetary policy.

[2] World Economic Outlook, November 2024: https://www.imf.org/en/Publications/WEO/Issues/2024/10/22/world-economic-outlook-october-2024

According to the European Commission Autumn Forecast, in 2024[3], the economic growth in EU is revised downwards by 0.1 p.p compared to the previous round of projections, reaching a growth rate of 0.9% in 2024. Overall within January-September 2024 we account for a positive real growth of 0.6% primarily driven by growth of net exports and public consumption.

Figure 1. Forecast for economic growth

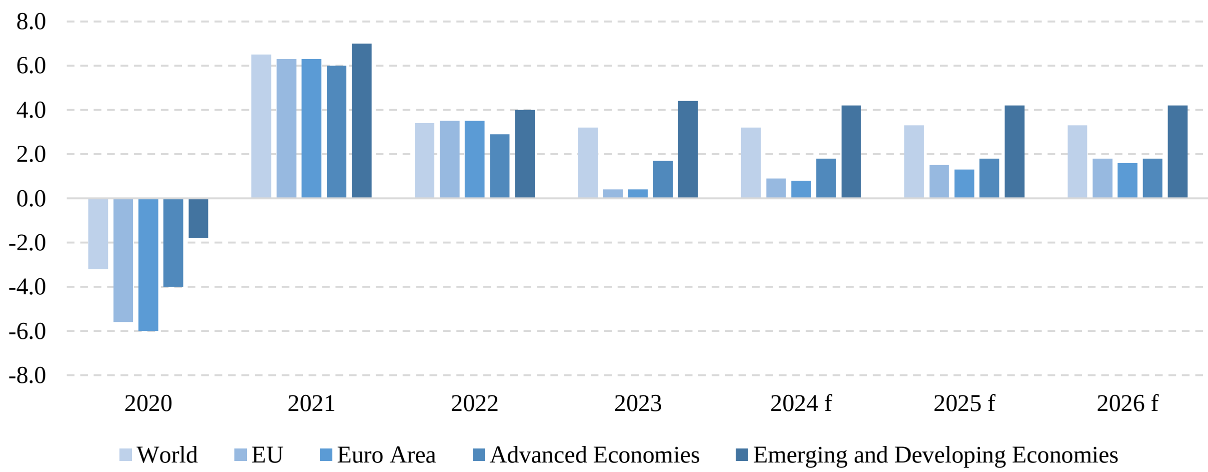


Table 1 provides information about the performance of several commodities prices during the period 2019-2026.[4] The World Bank's Commodity Markets Outlook (October 2024) highlights the ongoing normalization of commodity markets after sharp spikes in 2021-2022, driven by supply chain disruptions and geopolitical tensions. Significant decline in prices were observed across key commodities in 2023, and further downward trends are anticipated for 2024, especially in fertilizers, energy and food. However, geopolitical uncertainties and climate-related disruptions remain potential risks. Gradual stabilization is expected in 2025-2026 with smaller price fluctuations.

Table 1. Change of price indices over the years for several items

y-o-y percentage change	2019	2020	2021	2022	2023	2024(pro.)	2025(pro.)	2026(pro.)
Energy	-12.4%	-32.7%	81.0%	60.0%	-29.9%	-5.8%	-6.2%	-2.1%
Food	-3.8%	7.1%	29.9%	14.2%	-9.2%	-8.5%	-4.0%	-0.4%
Fertilizers	-1.4%	-8.3%	104.1%	54.8%	-34.9%	-23.0%	-1.4%	1.6%
Base Metals	-9.9%	-1.8%	46.8%	4.0%	-11.0%	6.1%	0.8%	-2.6%
Natural Gas	-25.5%	-25.6%	187.2%	115.5%	-63.5%	-17.6	6.5%	-8.7%

[3] European Economic Forecast, Autumn 2024: https://ec.europa.eu/commission/presscorner/detail/en/ip_24_5787
[4] The calculations shown in this table were conducted using data of World Bank for Commodity Markets

3.2. Recent Economic Developments in Kosovo and Outlook for 2025

3.2.1 Real Sector

After a stable growth in 2023, the Kosovo economy continued its positive trajectory, achieving a real annual growth rate of 4.6% during the first three quarters of 2024. The real annual growth in the first quarter was 5.6% followed by a slower growth rate of 4.3% in the following quarter (Q2) and 4.0% in third one.

Figure 2. GDP real growth(%) and key contributors(p.p)

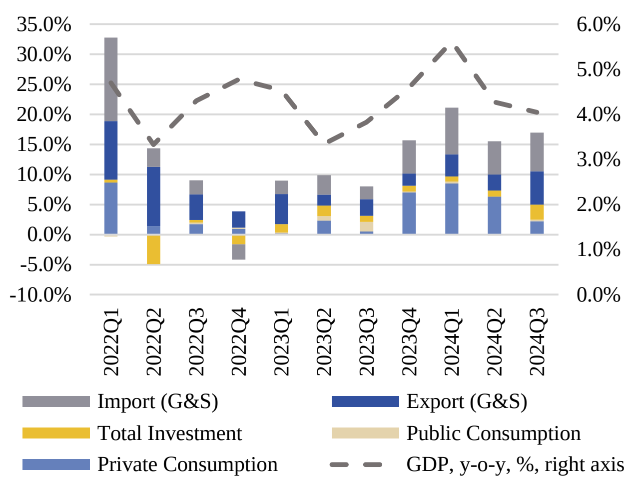
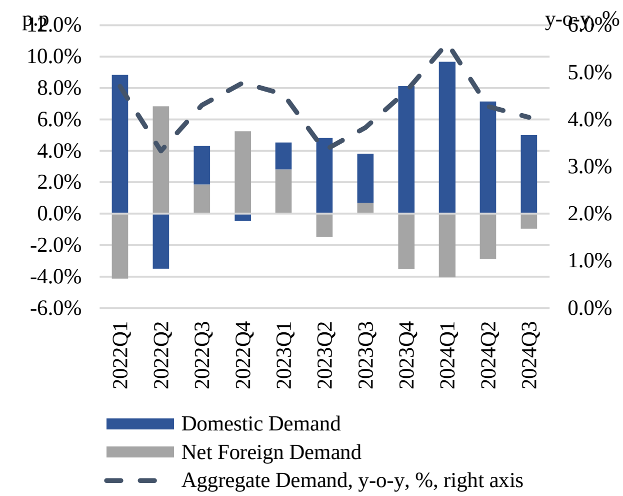


Figure 3. Domestic and Foreign Demand contribution on Aggregate Demand



In terms of aggregate demand, economic growth reflected the expansion of private consumption and investment, while net exports had a negative effect.

Based on KAS preliminary data on national accounts, during the period January-September of 2024 **total consumption** increased by 5.8% in real terms. Private consumption increased by 6.5%, while public consumption had a growth rate of 1.0%. The increase of private consumption was supported by a robust performance of compensation of employees (24.5%, *y-o-y*); and bank lending (new consumption loans 35.5%, *y-o-y*). The positive contribution of private consumption to GDP growth was higher in the first and second quarter of 2024 compared to the third quarter, due to improved consumer purchasing power. **Total investment** (private and public) for the first three quarters of 2024 increased by 4.7% in real terms. This increase resulted mostly because of the rebound in public investments. As a result of developments in consumption and investment, **domestic demand** had a significant positive contribution on GDP growth for the first three quarters of 2024. The **trade deficit (foreign demand)** worsened by approximately 9.0% during the reported period. The foreign demand contribution to GDP growth rate was negative, starting from a high rate of 4.1% in first quarter to a considerably lower rate of 1.0% in third quarter.

In sectorial terms, economic growth during the first three quarters of 2024 reflected the increase in all sectors, with the significant growth coming from the sector ‘electricity, gas, steam and air conditioning supply' at around 12.1% followed by hotels and restaurant recorded with an annual growth by 4.4%, other activities recorded growth around 4.1% and manufacturing with annual growth 3.7%.

Table 2. Leading and Coincidence Indicators for Aggregate Demand Components

Indicator*	***Proxy Variable***	***Indicator Type***	**2020 (Avg.)**	**2021 (Avg.)**	**2022 (Avg.)**	**2023 (Avg.)**	**2024* (Avg.)**
Energy Consumption	*Total Consumption*	*Coincidence*	2.7%	12.6%	-3.6%	4.2%	1.1%
Imports of Services	-	*Coincidence*	-19.5%	44.4%	29.9%	18.2%	19.0%
Exports of Services	-	*Coincidence*	-40.6%	91.6%	31.4%	18.4%	13.1%
Foreign Direct Investment	*Private Investment*	*Coincidence*	35.8%	21.7%	74.0%	14.8%	5.9%
Turnover (TAK)	*Private Consumption and Investment*	*Coincidence*	-7.5%	56.2%	21.8%	8.0%	7.6%
Remittance Inflows	*Private Consumption*	*Leading*	15.1%	17.7%	6.0%	9.2%	1.3%
VAT Collection	*Total Consumption*	*Leading*	-8.9%	34.8%	17.5%	11.9%	8.9%
Government Consumption	*Total Consumption*	*Coincidence*	5.3%	3.8%	1.7%	17.4%	10.0%
Government Investment	*Investment*	*Coincidence*	-28.5%	10.6%	-0.1%	32.2%	18.8%
Total Import of goods (CBK & Customs)		*Coincidence*	-5.7%	41.7%	20.8%	4.8%	7.8%
Total Export of goods (CBK & Customs)		*Coincidence*	20.8%	58.4%	23.8%	-6.5%	8.4%
New consumer loans	*Private Consumption*	*Leading*	-4.0%	40.3%	-6.3%	23.2%	35.5%
New investment loans	*Private Investment*	*Leading*	14.4%	-6.4%	8.9%	3.1%	18.9%

Note: *For 2024:
Data for energy consumption, import and export of services, Foreign Direct Investment, Turnover (TAK), total import and export of goods cover the period January-October;
Data on remittances, fiscal indicators (VAT collection and government consumption and investment) and new loans covers the period January-November.

According to the MFLT estimates, the GDP growth rate for 2024 is expected to be 4.5% in real terms. Such estimation presents an upward revision from the previous round of forecasts, resulting from the upward revision of the total consumption contribution, mostly due to a higher private disposable income also and from acceleration of the execution of capital spending compared to initial expectations.

Consumer price inflation showed consistency in 2024, reaching an average of 1.6%, starting from a rate of 1.8% in January down to 1.1% in December. This reflects the trends in 'food' and 'transport' prices, which are highly determined by the global fluctuations of food, energy, and oil prices. The contribution of the 'food' category to headline inflation was 0.7 p.p., while the contribution of 'transport' was negative, at around -0.4 p.p**.**

Inflation rates continue to be shaped by global developments, including factors such as the stabilization of energy prices and the monetary policies implemented by developed countries to counteract inflationary pressures. Meanwhile, the prolonged war in Ukraine and geopolitical tensions in Middle East still can impact on global supply chains which exert underlying inflationary pressures, particularly in tradable goods and commodities.

It is important to note that both headline and core inflation showed declines in 2024. The core inflation in 2024, measured excluding the categories "food and non-alcoholic beverages" and "transport", marked an average annual rate of 2.5% during 2024. This persistence in core inflation shows the second round such as elevated production costs and wage growth that has not kept pace with broader inflationary pressures. This indicates that inflationary pressures are influenced by both domestic and foreign factors. Likewise, the contribution of tradable inflation to total inflation is significant at around 0.9 p.p., whereas the contribution of non-tradable inflation is 0.7 p.p.

Figure 4. Contribution of tradable and non-tradable inflation

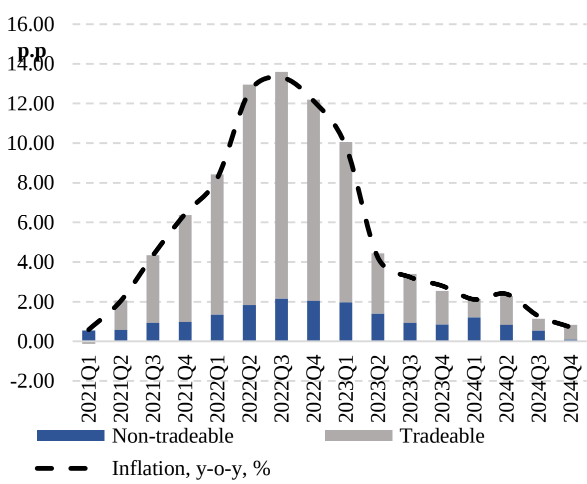
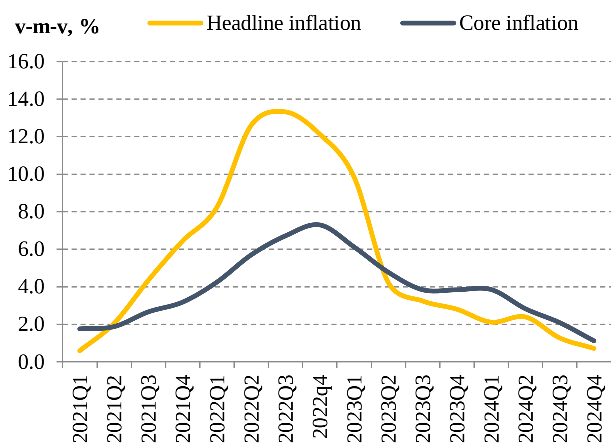


Figure 5. Headline Inflation vs. Core Inflation



3.2.2 Main labour market indicators

Labor market data from KAS are available only up to fourth quarter of 2023. In 2023, the participation rate was 40.7 %. The participation rate remains very low for women where 75.8% of women of working age are registered as inactive in labor force. The unemployment rate was 10.9%, which was also more emphasized among women (18.3%). Nevertheless, the unemployment rate is lower compared to the previous year by 1.7 percentage points.

The sectors with highest employment are trade with 20.0% of total employment, followed by construction with 11.8%, education with 9.9% and manufacturing with 9.2%. Male employment was higher in the sectors of trade, construction, and manufacturing, while female employment was higher in trade, education and healthcare sectors.

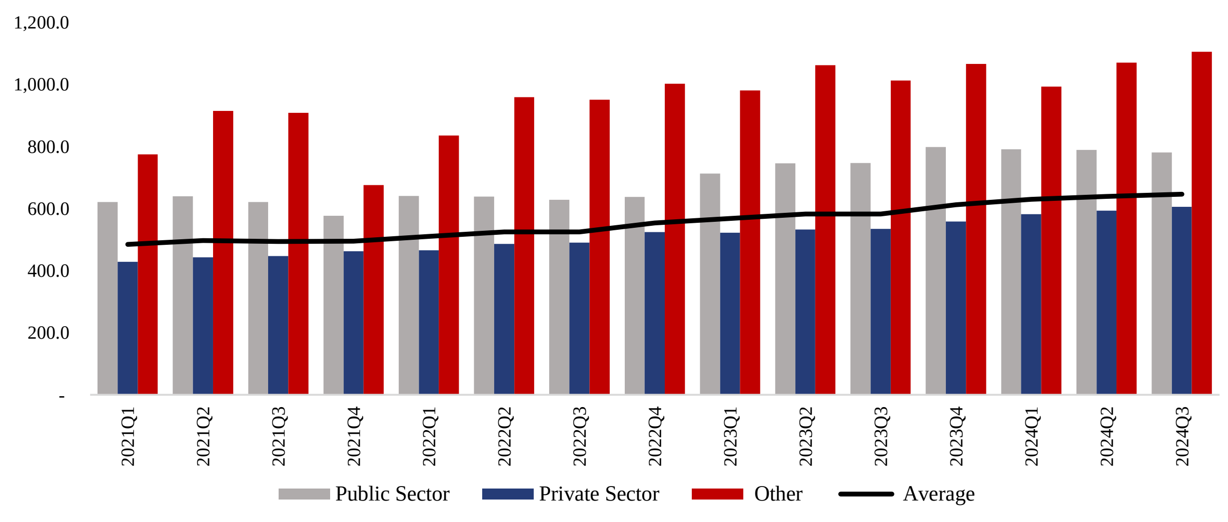
Table 3. Main labour market indicators

Indicator	2019	2020	2021	2022	2023
Total population	**1,796,376**	**1,795,666**	**1,798,187**	**1,773,971**	**1,762,220**
Female	*892,946*	*894,972*	*893,059*	*884,970*	*886,436*
Male	*903,430*	*900,694*	*905,.128*	*889,001*	*875,784*
Working age population	**1,206,806**	**1,222,104**	**1,231,695**	**1,195,426**	**1,171,763**
Female	*600,929*	*613,219*	*618,077*	*601,901*	*595,474*
Male	*605,877*	*608,885*	*613,618*	*593,525*	*576,289*
Labour force	**488,485**	**468,451**	**483,465**	**461,894**	**477,350**
Female	*126,971*	*127,686*	*135,860*	*132,425*	*144,331*
Male	*361,514*	*340,764*	*347,605*	*329,469*	*333,019*
Employed	**363,180**	**347,072**	**383,304**	**403,813**	**425,499**
Female	*83,242*	*86,480*	*101,853*	*110,528*	*117,990*
Male	*279,938*	*260,591*	*281,451*	*293,285*	*307,509*
Labour Force Participation Rate (LFPR)	**40.50%**	**38.30%**	**39.30%**	**38.60%**	**40.74%**
Female	*21.10%*	*20.80%*	*22.00%*	*22.00%*	*24.24%*
Male	*59.70%*	*56.00%*	*56.60%*	*55.50%*	*57.79%*
Employment Rate	**30.10%**	**28.40%**	**31.10%**	**33.80%**	**36.31%**
Female	*13.90%*	*14.10%*	*16.50%*	*18.40%*	*19.81%*
Male	*46.20%*	*42.80%*	*45.90%*	*49.40%*	*53.36%*
Unemployment Rate	**25.70%**	**25.90%**	**20.70%**	**12.60%**	**10.86%**
Female	*34.40%*	*32.30%*	*25.00%*	*16.50%*	*18.25%*
Male	*22.60%*	*23.50%*	*19.00%*	*11.00%*	*7.66%*

Source: KAS Labour Force Survey annual and quarterly publications

To offer further perspective on changes in the job market and present a summary of labor market trends up to the third quarter of 2024, we rely on administrative data from the Tax Administration of Kosovo (TAK). The TAK data indicates a growth of 3.3% in formal employment, aligning with developments observed in economic activity.

Figure 6. Gross average wages TAK, in Euro



The average gross monthly wage experienced an 10.5% rise in the first three quarters of 2024 when compared to the corresponding period of the preceding year. Specifically, private sector wages experienced a growth of 12.0%, while the average wage in the public sector surged by 7.1%.

This notable increase in public sector wages is attributed to the increase in value of wage coefficient according to the Budget Law for 2024. It is worth noting that the available data on wages obtained from TAK do not allow for a deeper analysis which considers changes in skill sets, offsetting private sector performance or potential under-reporting of earnings in the private sector.

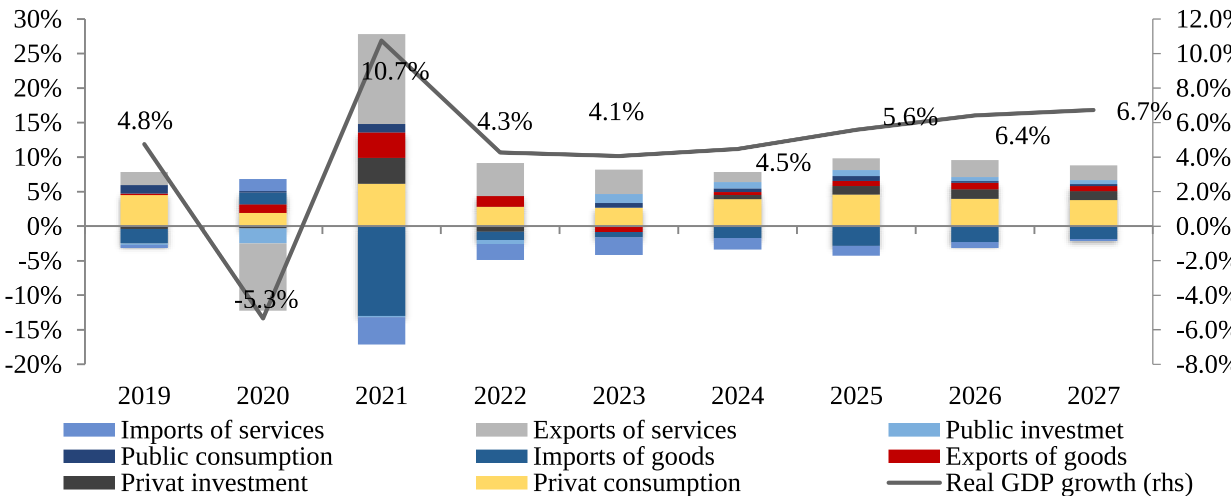
3.3 Medium-term macroeconomic scenario

3.3.1 Real sector projections

Based on current trend of macroeconomic indicators for 2024 as the base year for medium-term projections, and based on recent external economic developments and expectations, the economy of Kosovo in 2025 is expected to grow at a faster pace than in the current year, estimated at around 5.6% in real terms and 7.4% in nominal terms.

Total consumption is projected to increase by 5.4% in real terms in 2025 with contribution of 5.3pp in growth, continuing with an average real growth of 4.3% over 2026 and 2027, and providing an average contribution of 4.1% to real growth over the medium term. **Private consumption** is projected to grow by 5.5%, driven by the continued increasing trend in credit growth and increase in private disposable income as a result of stronger remittance growth, increase in minimum wage and children allowances. In addition, higher pension transfers in 2025, as a result of the decision of the Government to increase all the pensions by 20%, is expected to provide further positive stimulus to private consumption. **Public consumption** is expected to increase by 5.1% and contribute to economic growth by 0.7 pp., due to the increase in coefficient of wages in the public sector foreseen in Budget Law for year 2025 as well as the increase in expenditure for government goods and services due to the elections. The medium term projections include an ambitious investment plan, with an average growth of 5.7% over the medium-term.

Figure 7. Contribution to real GDP growth



Total Investment in 2025 is expected to increase by 6.1% in real terms and have a contribution of 2.1 p.p in economic growth. **Private investment** is projected to increase by 4.4% with a contribution of 1.2pp. in real growth. This growth will be supported by increase in capital of

Kosovo Credit Guarantee Fund(KCGF), which provides guarantees for loans to medium and small enterprises. In addition, the increase of capital of the Kosovo Credit Guarantee Fund is expected to further improve access to finance and enable investment credit expansion.

Public investment in 2025 is projected to increase by 13.4% in real terms and contribute by 0.9pp to economic growth. The quicker pace of execution is due to continuation of existing projects-implementation of which is expected to accelerate.

The medium term projections include an ambitious investment plan, with an average growth of 5.7% over the medium-term. **Total investment** is projected to provide an average contribution of over 1.9% to medium-term growth (private investment 1.3%, public investment 0.6%).

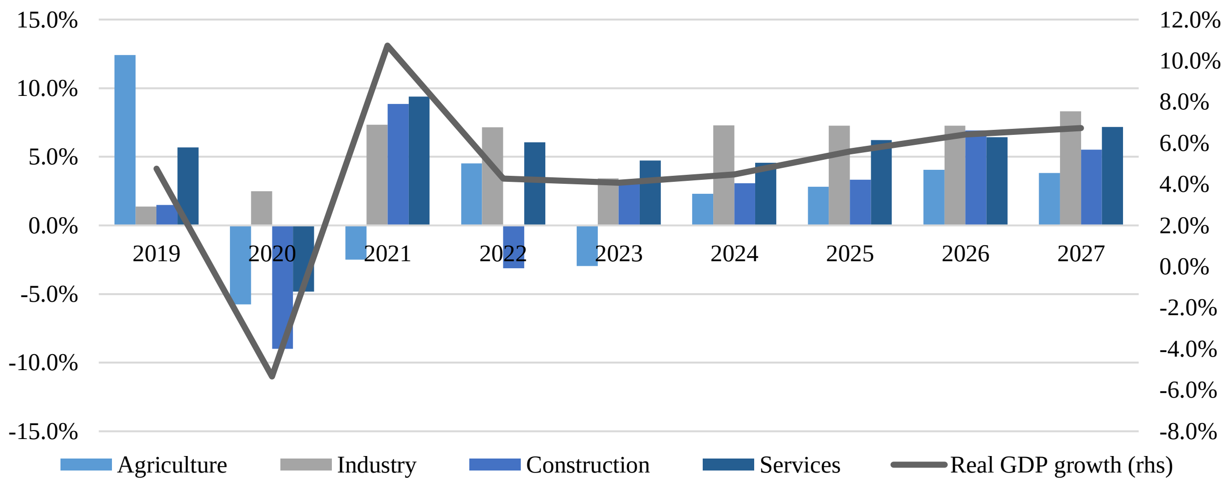
The net export in 2025 is expected to increase by 5.7%, and to have a negative contribution of 1.8pp, in real growth. **The export of goods and services** is expected to register a real growth of 6.1% with a positive contribution of 2.4 pp. **Export of goods** are expected to increase by 8.3% with a positive contribution to real growth of 0.8 pp. The expected increase is mainly due to the stabilization of commodities prices in international markets. **Export of services** is expected to follow its historical trend with an increase by 5.5% and contribution to real growth of 1.7p.p., mainly supported by travel and IT services. **The import of goods and services** is expected to grow by 5.9% in real terms and have a negative contribution to real growth of 4.2 pp. The import of goods is projected to increase by 5% with negative contribution to real growth of 2.8 p.p. This increase is in line with the expected dynamics of investment and consumption. On the other hand, import of services is expected to increase by 9.2% and have a negative contribution to real growth of 1.4pp. **Net exports** are projected to increase by an average of 1.7% during the 2026-2027. The exports of goods and services are expected to increase by 7.8%, while import of goods and services by 3.7%.

In 2025, based on the expectations of commodity prices in international markets, **inflation** in Kosovo is expected to fluctuate at around 1.8% in 2025 and in the medium term to increase at 1.6%, on average.

Over the next two consecutive years (both in 2026 and 2027), real economic growth is expected to be 6.4% and 6.7% respectively.

On the **production side**, the services sector is projected to remain the largest contributor to economic growth. Similar to its historical trends, construction sector is projected to continue growth with an increasing trend, marking a 4.7% average real growth over the projection period. Considering the demand for exports of travel services, the level of primary and secondary income flowing to the country, and measures to improve Kosovo's touristic products, service growth is an immediate result of the current growth model. In addition, value added from the industry sector is projected to increase by an average of more than 7.5% over the medium-term. While, agriculture is expected to have a moderate growth of 3.2% throughout the medium-term.

Figure 8. Sectorial real growth



However, the baseline projection for both, inflation and economic growth, is surrounded by increased risks related to elevated geopolitical tensions in global level. In addition, the continuation of the labor market tightening in Kosovo might generate additional upward pressures on inflation.

Information Box 1. Differences between actuals and projections, 2024

For 2024, the forecasted real GDP growth rate is revised downwards to 4.5%, which is 0.1 p.p lower than the rate projected in the previous ERP submission. As the growth remain almost the same as presented in a previous ERP, components of growth have been revised.

Public consumption is expected to increase by 3.8%, which is different from the value in the previous ERP, which foresaw a growth of 6.2%. Total investment is revised downwards at 4.6%, from 11.2% due to base effect of public consumption. Exports of goods is revised downwards, as a result of a significantly lower performance shown during January -October 20234. However, exports of services is expected to increase given that diaspora visits this year were considerably high. Import of goods and services, on the other hand, are expected to slightly decrease by 4.8% while in the previous ERP, they were projected to increase by 6.7%.

Inflation in 2024 (on average 1.6%) is lower than the inflation forecasted in the previous round of projections (on average 2.7%).

Table 1. Main differences between previous and actual round of projections for year 2024

Macroeconomic Indicators, *annual growth rates in real terms in %, unless otherwise stated*	2024 previous ERP projections	2024 current ERP projections
Real GDP	4.6	4.5
Nominal GDP	7.8	6.6
Consumer Price Index	2.7	2.0
Private Consumption	2.6	4.7
Public Consumption	6.2	3.8
Total Investment	11.2	4.6
Total Exports	6.5	4.8
Export of Goods	16.8	4.8
Export of Services	2.9	4.8
Total Imports	6.7	4.8
Import of Goods	7.0	3.0
Import of Services	5.6	12.2

3.3.2 Monetary and exchange rate policy and inflation

In 1999, Kosovo unilaterally adopted the Deutsche Mark and later (in early 2002) the Euro currency as its official currency. Consequently, the country is restricted in the availability of traditional monetary policy instruments to control inflation developments in its economy or to signal changes in current consumption behaviour towards future consumption. However, this does not mean that the Central Bank of Kosovo (CBK) has no means of influencing the economy.

Firstly, sound implementation of macro-prudential policies can mitigate systemic financial risks and avoid excessive credit accumulation during expansionary periods or excessive credit contracting during recessionary periods, which would help in moderating inflation or real exchange rate fluctuations.

Secondly, the Central Bank strives to promote and maintain a sustainable and efficient financial sector in Kosovo through licensing, regulation and supervision of banks, insurance companies and micro-credit organizations.

Thirdly, the CBK can influence the growth of commercial banks' credit by determining the level of demand for reserves or through other regulations on banking operations. On April 25, 2019 the Board of the Central Bank of the Republic of Kosovo approved the Regulation on the Repurchase of Securities with the Central Bank of the Republic of Kosovo, which authorizes the CBK to carry out credit operations with commercial banks in the country performing the role of securities-backed lender as collateral. This regulation will provide the banks with an alternative to manage liquidity and short-term financing.

Despite monetary policy constraints, over time inflation in Kosovo has been relatively stable, with the exception of year 2022, which is mostly attributed to external developments. In terms of exchange rate developments, Kosovo is not much exposed to exchange rate fluctuations. This is due to the fact that the majority of trading partners are from the Eurozone countries and a significant portion of other sources of financing are in Euro currency (e.g. bank lending or remittances). During 2024 (January- November), the euro was valued at around 1.1% compared to the currency basket of the leading international trading partners (NEER). This appreciation is mainly due to the appreciation of the Euro against the Turkish Lira (about 40.7%), meanwhile it marked a depreciation against the British Pound (about 2.6%), Albanian Lek (about 7.7%), and Swiss Franc (about 2.0%). Lastly, the real effective exchange rate appreciated by 1.1% compared to January- November of last year.

3.3.3 The external sector and its medium-term sustainability

3.3.3.1 Current Account

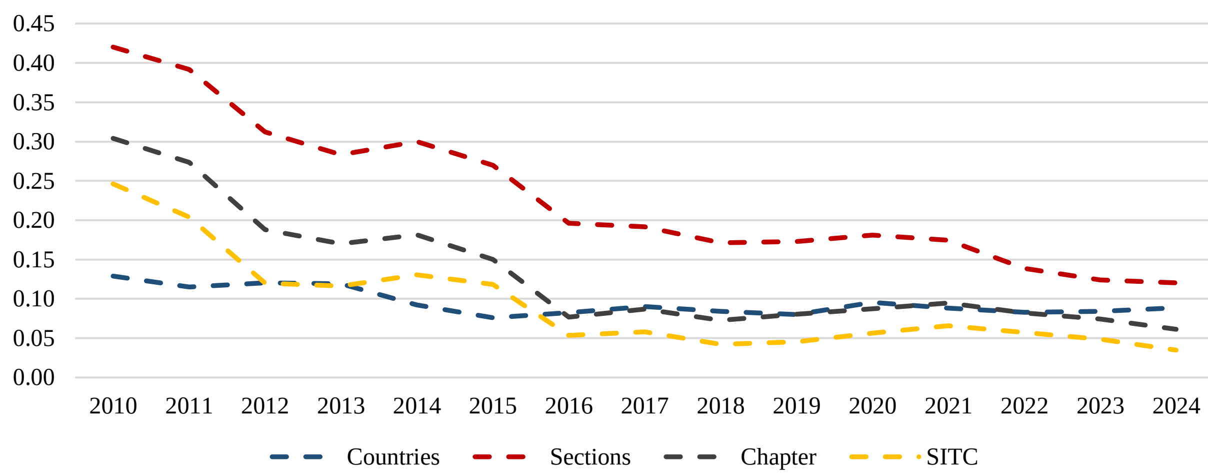
The current account balance during the period January-October 2024 amounted to a deficit of -591.8million euros, which compared to last year represents a significant expand by 26.3%. This is mainly attributed to the deficit of the goods trade and to the lower increase of the secondary income balance.

Export of goods in 2024 for the period January-October increased by 8.4% compared to the same period of last year. Export of “base metals and articles of base metals” continues to be the biggest category with a share of 24.4% in total exports. Similarly, the category of “plastic and rubber” and the category of “miscellaneous manufactured articles” continue to be the second and third biggest categories in the exports’ structure with a share of 13.1% and 11.2%, respectively. Categories that follow are the “prepared food, beverages and tobacco” with a share of 10.8% and “mineral products category” with a share of 8.6% of total exports.

Diversification is a positive development for an economy such as Kosovo because changes in the primary export mix help build buffers in the economy, and Kosovo should aim to further diversify its export of goods. These buffers will reduce the negative effect stemming from the volatility of world commodity prices and lessen the vulnerability of the economy to adverse external shocks. In addition, diversification can also lead to economic development by progressing towards the export of more sophisticated products.

The **Herfindahl-Hirschman Index**[5] has been used to measure export diversification. According to this index, although at a slow pace, in the past few years Kosovo has continued to diversify its exports. In 2024, as expected, the HHI shows an increasing trend of the exports diversification, especially in terms of SITC and chapters, which can also be attributed to recent policy measures targeted to incentivizing domestic producers and exporters, the diversification of exports in terms of sections remain the same as previous year while the diversification of exports in terms of countries show a decrease.

Figure 9. Herfindahl-Hirschman Index



Export of services for the period January-October 2024 increased by 13.1% in annual terms. This increase is attributed mainly to the export of travel services with a contribution of 7.3 p.p and an annual increase of 9.5%, followed by the "other business services" with an annual increase of 33.6% and a contribution of 2.1 p.p and a "telecommunications, computer, and information services" with an annual increase of 23.4% contribution of 2.0 p.p. Export of services for 2024 is expected to reach 3,172.0 mln Euro, thereby marking an annual increase of 6.9%.

For the period January-October 2024, **import of goods** increased by 7.8% in annual terms. This increase is mainly attributed to the import of "transport of means" with a contribution of 2.7 p.p an increase of 11.6%, followed by the category of "Machinery, appliances, electrical, etc. " with a contribution of 1.5 p.p. and annual increase of 12.0% and the category " Products of the chemical industries or allied industry" with a contribution of 1.2 p.p (annual increase of 7.6%). Kosovo

[5] The Herfindahl Hirschman Index is calculated as the sum of squared shares of each product in total export. A country with a perfectly diversified export portfolio will have an index close to zero, whereas a country with a concentrated portfolio will have a value of 1 (least diversified).

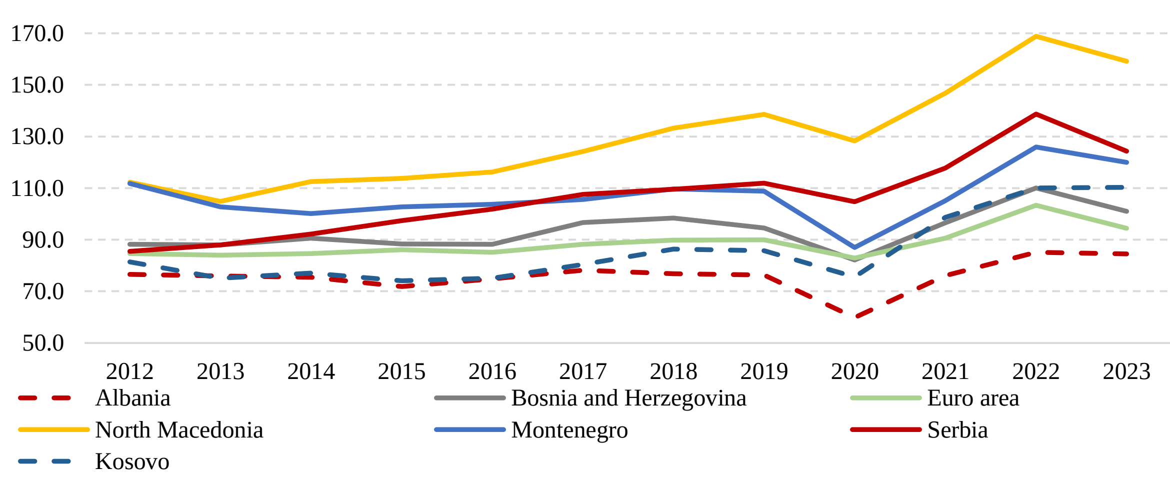
continues to import from relatively the same countries and group of countries as in recent years mainly due to the SAA and CEFTA. In 2024, Turkey was the leading country for Kosovo's imports (14.6% of total imports) followed by Germany and China with 14.1% and 11.9% of total imports, respectively. In 2024, import of goods is expected to increase by 6.2% compared to 2023.

Import of services for the period of January-October 2024 registered an annual increase of 19.0%. The import of "travel services" had the highest contribution at around 9.7 p.p and an annual increase of 20.2%; followed by "transport" with contribution of 4.8p.p. an increase of 23.9%, and the category of "other business services" with a contribution of 2.0p.p and an annual increase of 15.5%. Import of services in 2024 is expected to register an increase of 16.5% compared to 2023.

As per the above, for the period January-October 2024 the deficit of goods trade widened by 7.7%, while of the surplus of services trade increased by 8.7%.

Overall, despite being a small open economy with a liberal trade regime, Kosovo is characterized by lower **trade openness**[6] mainly due to the low export base, which represents one of the main structural challenges of the country's economy. As shown in the graph below, the COVID-19 pandemic in 2020 halted the increasing trend of the trade openness level in the country. However, the trend gained momentum in 2021, spiking up to well above pre-pandemic levels. This upturn was mainly as a result of the ease of travel restrictions as well as measures undertaken by the government to stimulate exporters and help producers with their investment loans.

Figure 10. Trade Openness Index



In the medium term, imports are expected to continue increasing in line with domestic demand projections. Exports are expected to continue their positive contribution, mainly due to the base effect but also due to the stabilization of the prices of basic goods in international markets.

[6] The Openness Index is an economic metric calculated as the ratio of country's total trade, the sum of exports plus imports, to the country's gross domestic product. = (Exports + Imports)/(Gross Domestic Product). "The higher the index, the more influence trade has in that country's domestic activity."

However, the continuation of the war in Ukraine and other geopolitical tensions have produced an uncertain environment for these medium term projections (2025-2027).

Table 4. Export and Import of goods and services

% change, unless stated otherwise	2021 Actuals	2022 Actuals	2023 Estimation	2024 Projections	2025 Projections	2026 Projections	2027 Projections
Exports *(nominal, in million €)*	2,658.7	3,436.0	3,837.2	4,121.1	4,468.0	4,946.3	5,399.5
Exports	81.0	29.2	11.7	7.4	8.4	10.7	9.2
-Goods	58.4	23.8	-6.5	9.0	12.0	13.6	10.9
-Services	91.7	31.4	18.4	6.9	7.3	9.8	8.6
Imports *(nominal, in million €)*	5,190.9	6,350.3	6,806.2	7,364.7	7,978.2	8,514.1	8,943.5
Imports	42.2	22.3	7.2	8.2	8.3	6.7	5.0
-Goods	41.7	20.8	4.8	6.2	7.2	6.1	5.3
-Services	44.6	29.9	18.2	16.5	12.4	8.8	4.3

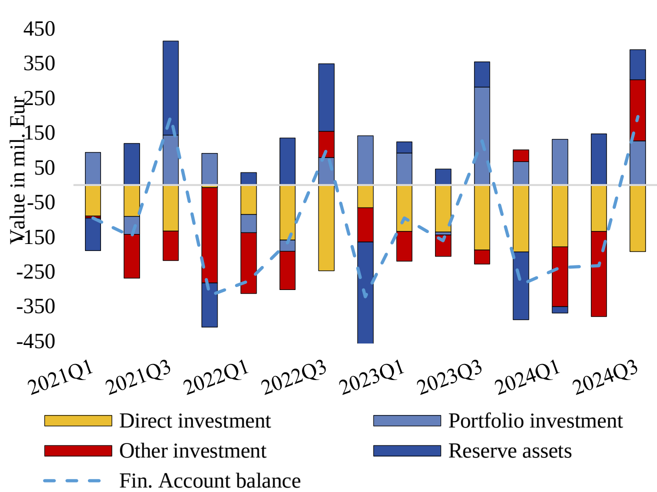
The **primary income** balance marked an increase of 14.2% in annual terms for the period of January-October 2024 with the main contribution attributed to the category of "compensation of employee". For the whole of 2024 primary income balance is expected to register an annual 34.4% due to the base effect, while for the medium term is expected to increase on average by 11.1%.

The **secondary income** balance increased by 1.0% in annual terms, the low increase on secondary income is mainly attributed to the category "Financial corporations, nonfinancial corporations, household and NPISHs", which during this period registered decrease by 0.2%, while the category of general government has increase by 8.6%. As a result, for 2024 the secondary income balance is expected to increase by 4.3% in annual terms and by 7.3% in the medium-term.

3.3.3.2 Financial Account

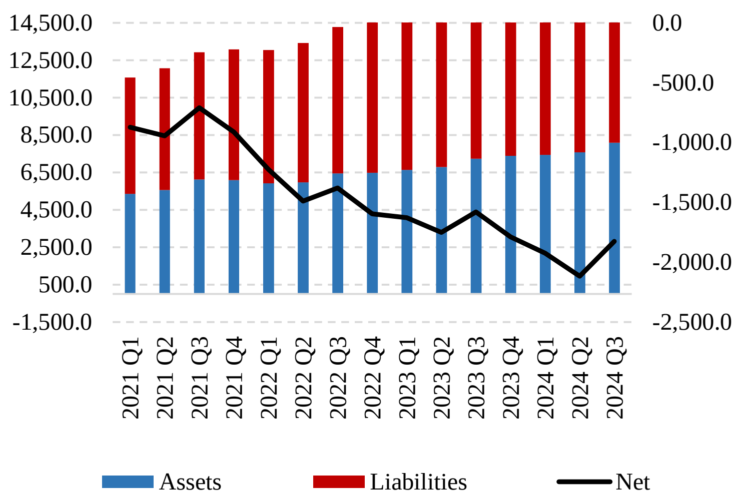
For the period January-October 2024, direct investments abroad decreased by around EUR 6.8 million. Portfolio investments in foreign assets contracted by EUR 154.1 million, while other investments decreased by EUR 503.7 million. With regard to liabilities, direct investments inflows increase by 41.0 million of euros, while other investments experienced a decline of EUR 79.7 million.

Figure 11. Financial account components, mln Eur



It is worth noting that Foreign Direct Investment continue to represent the biggest share in financial account liabilities at around 85.1%. As such, FDI is seen as a sustainable financing source since it has better risk sharing capabilities and it is more amenable to macro stability. During January-October 2024, FDI was mostly directed toward "real estate activities", accounting for 71.6% of total FDI. This is followed by "financial and insurance activities" placing them as the second largest absorber of FDI, accounting for 15.9% of total FDI. This capital inflow into the non-tradable sector (such as real estate and financial and insurance activities) is more prone to creating financial fragility through the balance of payments' mismatches since such sectors are difficult to generate revenue.

Figure 12. Net International Investment Position, mln Eur



The International Investment Position (IIP) reached -1,825.5 million Euro in the third quarter of 2024. During this period of 2024, assets were dominated by the category of "portfolio investments", which amounts to around 39.8% of total assets; followed by the category of "other investments" composing 29.1% of total assets; "reserve assets" and "direct investment" accounting for 17.4% and 13.7% respectively. Regarding liabilities, "direct investments" continues to be the largest category in the composition of liabilities. By the end of third quarter of 2024, "direct investments" account for around 69.6% of total liabilities whereas, "other investments" comprises 30.3% for the rest of the countries liabilities.

3.4 Financial sector

3.4.1 Overview of the financial sector

Kosovo's financial system has continued its sustainable growth, maintaining a double-digit increase for the fourth year in a row. As of September 2024, the total assets of the financial system amounted to 12.01 billion euros, representing a 13.4% annual growth, slightly higher than the 12.2% increase recorded in the same period last year. This growth was primarily driven by the banking sector, followed by pension funds. The banking sector remains the largest component, comprising 66.3% of the total market, with pension funds contributing 25.6%. Microfinance institutions, insurance companies, and financial auxiliaries account for smaller market shares, at 5.1%, 2.8%, and 0.1%, respectively. Financial intermediation has seen steady expansion, with a ratio of 117.0% in September 2024, up from 109.5% the previous year, reflecting a faster growth in financial assets compared to the overall economy. Foreign banks continue to dominate the banking sector, representing 83.3% of total banking assets. Market concentration as measured by the CR3 index has decreased slightly to 51.7% from 52.4% in the previous year, and significantly lower than the 67.3% recorded in September 2014. Whereas the CR5 index increased slightly to

79.2% from 78.7% in 2023 and the Herfindahl-Hirschman Index rose to 1,407 points, a 12-point increase compared to September 2023.

As of September 2024, banking sector assets in Kosovo reached 7.97 billion euros, representing around 77.6% of the country's GDP[7]. Lending portfolio continued its steady double-digit expansion, accounting for 53.7% of GDP at end September 2024, up from 49.5% in the previous year. By September 2024, total loans reached 5.51 billion euros, a 15.1% annual increase, compared to 13.3% in the previous year The household sector contributed the most to the overall growth rate, therefor the non-financial sector continues to hold the largest market share in total loans, accounting for 58.7% as of September 2024. However, its share is on a declining trend. Lending to households has been growing at an accelerated pace, increasing by 20.8% as of September 2024, compared to 17.3% in the previous year. This growth was primarily driven by a significant 32.0% annual increase in new loans to households. Within this category, consumer loans surged by 35.5%, reaching 607.1 million euros, while mortgage loans grew by 27.3%, amounting to 182.1 million euros. This represents a recovery in mortgage lending, following a 9.2% decline in the previous year. According to the latest Bank Lending Survey[8], the growth in lending to households was mainly demand-driven, with increased demand for both consumption and house purchases. On the supply side, credit standards remained largely unchanged during the period. Analyzing the total stock of household loans by maturity, loans with a maturity of 5–10 years continue to dominate. However, loans with maturities exceeding 10 years are growing rapidly and have made the largest contribution to the overall growth of household loans. This trend highlights the increasing demand for house purchase loans, which are typically associated with longer maturities. Lending to non-financial corporations grew by 11.2%, a 0.3 percentage point increase compared to the growth rate during the same period of the previous year. This growth was primarily driven by the wholesale trade sector, which recorded an annual increase of 12.9% and accounted for 42.3% of the total loan stock to non-financial corporations. The construction and agriculture sectors also experienced notable annual growth rates of 11.2% and 15.4%, respectively. In contrast, the manufacturing sector saw a modest increase of just 0.2%, a sharp decline from the 11.2% growth observed in 2023. New loans to non-financial corporations recorded slower annual growth of 5.5%, down from 8.5% in the same period of the previous year. This slowdown was mainly attributed to a 12.5% decline in new loans for non-investment purposes, compared to a 14.0% increase the year prior. Conversely, new investment loans showed robust growth of 19.3%, significantly higher than the 8.4% increase in the previous year. According to the latest Bank Lending Survey, the growth in lending to non-financial corporations was primarily demand-driven, particularly by small and medium-sized enterprises (SMEs). On the supply side, credit standards applied by banks to both SMEs and large enterprises remained largely unchanged. In terms of loan maturity, the structure of total loans to non-financial corporations has remained stable, unlike

[7] Value of GDP for 2024 used in the calculations is based on CBK forecast data.
[8] Survey was conducted for Q3 2024 and expectations for Q4 2024.

household loans. Loans with maturities of 2–5 years dominate this segment, comprising 37.8% of the total, followed by loans with maturities of 5–10 years, which hold a 33.1% share.

Deposits, which remain a reliable and stable source of funding for banking activities, continued to grow at a similar pace. As of September 2024, deposits increased by 11.2%, maintaining a level comparable to the 11.3% growth recorded in September 2023, reaching a total of 6.51 billion euros (5.85 billion euros in September 2023). Household deposits, the largest component of total deposits, grew by 8.0%, slightly below the 9.0% growth recorded in 2023 and the 11.5% growth in 2022. Similarly, deposits from non-financial corporations grew by 14.4%, maintaining a similar level to the 14.9% growth in 2023 and slightly below the 16.2% growth in 2022. In contrast, deposits from other financial corporations, primarily from the pension sector, grew at a much lower rate of 17.4%, following a substantial increase of 37.4% in 2023 and more moderate growth of 7.4% in 2022.

The easing of the ECB's monetary policy, specifically reductions in key interest rates, has impacted interest rate dynamics in the domestic banking sector. This has led to a decrease in loan interest rates, impacting households and nonfinancial corporations as well. As of September 2024, interest rates of loans decreased to 6.1% (6.5% in September 2023 and 6.4% in January 2024). Interest rates were to some extent more favorable for the household segment, standing at 5.8%, compared to those for enterprises standing at 6.3%. Meanwhile, interest rates for non-financial corporations decreased to 6.3% in September 2024, down from 6.7% in September 2023. On the contrary, due to domestic financing pressures, interest rate on deposits have increased, reaching 2.9% in September 2024, from 2.4% in September 2023 and 2.7% in January 2024. Consequently, the spread between interest rates on loans and deposits narrowed to 3.2 percentage points in September 2024, from 4.1 percentage points in the same period of the previous year.

The banking sector has a low level of non-performing loans. As of September 2024, the NPL ratio stood at 2.1% (2.0% in September 2023), and its coverage with provisions stood at 123.8% (143.5% as of September 2023). By economic sector, energy and agriculture sectors have the highest rate of NPL of 10.5% and 7.6%, respectively. Nevertheless, the lending to these sectors accounts for a very low share to total gross loans (0.8% energy and 1.2% agriculture), with a respective NPL value share of 4.2% and 4.3%, respectively. Trade sector, with the largest share in total loans of 25.4% has a 1.5% NPL ratio. The household segment remains the segment with one of the lowest levels of NPL ratio, 1.5% as of September 2024, an annual increase by 0.1 percentage points.

As of September 2024, the banking sector reported a net profit of 138.6 million euros, reflecting a 12.1% year-on-year increase. Revenues amounted to 373.2 million euros, a rise of 17.7% compared to the previous year. Of these revenues, 75.5% were derived from interest income, primarily from loans, and the remaining income from placements with banks and interest received from investments in securities. Non-interest income reached 78.6 million euros, largely driven by fees and commissions. Expenditures rose by 21.3%, totaling 234.6 million euros, with interest expenses on deposits and personnel costs being the major contributors. As of September 2024, the

Return on Assets (ROA) remained unchanged at 2.6%, consistent with the previous year, while the Return on Equity (ROE) decreased to 19.2%, down from 20.9% in the same period of the previous year.

The capital position, measured by the regulatory capital ratio to risk-weighted assets, increased to 15.6% in September 2024, up from 15.3% in September 2023. This 0.3 percentage point rise was primarily driven by stronger growth in regulatory capital compared to risk-weighted assets. By the end of the third quarter, regulatory capital grew by 14.5% year-on-year, up from 11.4% in the previous year, reflecting improved capital accumulation. In contrast, risk-weighted assets experienced a slower growth rate of 12.0% year-on-year, compared to 15.2% in September 2023.

The sector's Liquidity Coverage Ratio (LCR) remained well above the regulatory requirement of 100%, despite a decrease from 260.5% in September 2023 to 211.4% in September 2024. Despite this decline, banks continue to maintain a robust buffer of liquid assets to cover potential short-term outflows. Similarly, the Net Stable Funding Ratio (NSFR) deteriorated, declining from 142.6% to 137.3%, indicating a slight decrease in the bank's ability to maintain stable long-term funding. Furthermore, the liquidity ratio, which measures the proportion of liquid assets to short-term liabilities, saw a decrease of 1.4 percentage points, dropping to 31.1%. This decline is attributed to the higher growth rate of short-term liabilities (12.4%) compared to liquid assets (7.4 %). As well, the loan-to-deposit ratio increased by 2.9 percentage points, reaching 84.7%, mainly due to a more rapid expansion in lending relative to deposits.

The pension funds' assets amounted to 3.1 billion euros as of September 2024, reflecting an annual increase of 17.7% (12.8% the previous year). Kosovo Pension Savings Fund (KPST) accounts for 99.7% of the total pension funds' assets, while 0.3% are assets of the Slovenian-Kosovar Pension Fund (SKPF). The accelerated asset growth reflects mainly the effects of good financial performance amidst the favorable interest rate environment in foreign markets, and to a lesser extend the growth in pension contributions. Gross return on investments amounted 203.5 million euros in September 2024. The investment portfolio of KPST reached a gross return of 202.6 million euros (47.6 million euros in previous year), representing the strongest increase of the post-pandemic period (2021 and onwards). Whereas contributions amounted to 227.0 million euros, reflecting a moderated annual growth rate of 6.9%, down from 19.9% growth in the previous year. This deceleration in growth indicates that the market has absorbed the immediate effects of the implementation of the Law on Public Officials and the Law on the Minimum Wage in 2023, both of which initially contributed to a significant increase in the value of contributions. On the other hand, SKPF also achieved a high growth in investment returns totaling 0.90 million euros, while the collected contributions fell slightly to 0.49 million euros.

The micro financial sector (MFIs), similar to banking sector, is dominated by foreign-owned institutions, representing 73.6% of the sector's assets, while the three largest institutions exceed half of the total sector's assets (51.8% in September 2024, down from 53.5% in the previous year). The microfinance sector further accelerated its annual assets growth to 28.4% from 25.1% growth last year, amounting at 615.0 million euros. This increase was largely financed through external sector borrowings, the value of which constitutes about 60.3% of the total sector liabilities of MFIs, while 26.0% of total liabilities is financed by own capital. Total loans amounted to 420.1 million euros in September 2024, reflecting a slightly slower growth rate of 23.7% compared to 25.0 % at end September 2023. The household segment remains the primary contributor to total credit growth, with loans to households accounting for 59.6% of total loans, amounting to 250.5 million euros in September 2024. However, this represents a slightly slower growth rate of 18.2% compared to 20.5% in the same period of 2023. Similarly, loans to non-financial corporations, comprising 40.4% of total loans, reached 169.6 million euros in September 2024, reflecting a high growth rate of 32.8%, albeit slightly slower compared to 33.3% in September 2023. Leasing activity, representing 16.5% of total assets, stood at 101.3 million euros at end September 2024, marking a significant y-o-y growth slowdown to 9.1% from 29.6% in September 2023. Leasing to non-financial corporations held the largest share, accounting for 70.7% of total leasing. This segment grew from 63.8 million euros 71.6 million euros in September 2024, yet its year-on-year growth rate declined sharply, from 45.9% to 12.2%. The share of households leasing to total leasing continued its downward sloping trend. By September 2024, household leasing accounted for 29.3% of total leasing, with a slowed growth rate of 2.2% compared to 4.1% in the previous year, amounting to 29.7 million euros.

Net profit of the MFI sector reached 15.2 million euros, reflecting an annual increase of 18.8%. The growth in financial performance was driven by strong revenue growth, which outweighed the rise in expenses. Total income amounted to 66.0 million euros, reflecting a significant increase of 33.6%, compared to 19 % in the previous year. Of this total, 55.3 million euros were generated from interest on loans - a category that grew by 23.9% y-o-y. On the other hand, total expenses increased by 39 %, up from 30 % in the prior year, primarily driven by a sharp rise of 77% in interest expenses, compared to 56 % in the previous year. Meanwhile, the growth in personnel costs slowed to 16 % from 19 %.

Loans issued by the MFI sector carry higher interest rates compared to banks, as their financing is mainly done through external borrowing which is a more expensive funding source compared to retail deposits. In September 2024, the average interest rate on MFI loans stood at 19.2%, marking a y-o-y increase of 0.3 percentage points. Non-financial corporations had more favorable rates, averaging 15.9%, slightly up from 15.7% in September 2023. In contrast, households faced higher rates, at 21.9%, marking a 0.1 percentage point drop from a year ago. Despite the higher interest rates, microfinance institutions maintained strong credit portfolio performance, with non-performing loans accounting for only 2.0% of total loans (slightly up from 1.9% in September 2023). Furthermore, the coverage ratio of non-performing loans with provisions with provisions was robust at 139.8%, albeit slightly lower than the 145.1% recorded in the previous year.

The insurance sector in Kosovo is less concentrated in foreign ownership compared to the banking and MFI sectors, with foreign insurance companies representing 53.1% of the assets. Its concentration in terms of the three largest participants is also lower, with the three largest insurance companies accounting for 37.7% percent of the total sector assets, slightly up from 36.5% in

September 2023. Total insurance sector assets amounted to 338.1 million euros, a decelerated y-o-y growth rate of 12.5% from 16.1% in 2023. The value of written premiums reached 127.0 million euros (110.1 million euros last year), where 5.6 million euros are premiums for 'life' insurance and 121.3.0 million euros are premiums for 'non-life' insurance. Claims paid by the insurance sector reached 53.5 million euros (53.1 million euros last year), where 48.1 million euros are damages paid by insurance companies and 5.5 million euros are damages paid by Kosovo Insurance Bureau. Net profit of the insurance sector reached 10.6 million euros, up from 9.5 million euros in the previous year. Additionally, the claims to premiums ratio declined to 42.2% compared to 48.2% last year, potentially reflecting an improvement in the sector's claims management.

Despite these improvements, the evolving risk landscape—shaped by both domestic financial sector deepening and global uncertainties, including technological advancements and geopolitical tensions—emphasizes the importance of proactive measures to sustain resilience. Household resilience, underpinned by stable incomes and remittances, mitigates some risks, though rising living costs remain a concern, even in the context of subdued inflationary pressures.

To address these challenges and ensure long-term stability, the Central Bank of Kosovo (CBK) has announced the activation of specific macroprudential measures, effective June 2025. These measures, namely the Positive Neutral Capital Buffer and Systemically Important Institutions Buffer, aim to build macroprudential capital buffers by leveraging the sector's current high profitability. By enhancing resilience in a climate of narrowing margins and intensified competition, these policies are expected to fortify the sector against future shocks, ensuring its sustained contribution to economic growth.

3.4.2 Financial System Risks

The Kosovo financial sector has remained robust, successfully navigating challenges of the past years. Despite the economic slowdown in the previous year and perceived credit risks linked to rising inflation and migration, the sector performed well, capitalizing on higher interest rates, further boosting profits and improving capital ratios. By September 2024, risks to financial stability are considered to have subsided due to better macroeconomic performance and more positive growth prospects.

Credit and Liquidity Risks

The banking sector has sustained its financial robustness throughout 2024, also as a result of proactively prudent lending practices and effective risk management. However, the dynamics of increased competition for deposits, coupled with a high rate of credit growth, have introduced new challenges in the context of falling interest rates. The persistent double-digit lending growth reflects robust financial deepening, with heightened demand for financing exerting upward pressure on deposit interest rates. Concurrently, loan rates have begun to slightly decline in response to the ECB's easing monetary policy.

The assessment of credit risk remains moderate. Asset quality indicators at the portfolio level are favorable and stable, with the non-performing loan (NPL) ratio slightly increasing to 2.1% in September 2024, up from 2.0% last year. The low level of NPL ratio is attributed to a higher credit growth of around 15.1%, as there has been a significant rise in the value of non-performing exposures, which increased by 22.5%, compared to an 8.4% increase last September. The rising value of non-performing exposures (up 22.5% by September 2024), even though to a large extent concentrated at a handful of large exposures, underscores the need for continued vigilance, even as Stage 2 loans showed signs of stabilization. The decline in the growth rate of Stage 2 loans to 12.9% in September 2024, from 27.3% over the previous year, indicates improved reclassification practices amidst a more favorable environment.

Liquidity risks remain contained, supported by steady deposit growth, which rose by 11.2% year-on-year in September 2024. The Liquidity Coverage Ratio (LCR), however, declined to 202.3% from 260.5% a year earlier, driven by rising net cash outflows. Although liquidity indicators remain comfortably above regulatory thresholds, disparities across banks highlight varying capacities to attract and retain deposits at competitive costs, posing potential funding risks for certain institutions.

Profitability and Structural Shifts

Bank profitability remained robust, primarily driven by higher net interest income and credit growth. Larger banks have benefited from diversifying their earnings through investments in foreign markets, though this trend decelerated in late 2024 due to declining global interest rates. However, the competitive pressures on deposits and narrowing interest margins could create challenges for smaller banks, particularly as administrative and deposit interest expenses continue to rise.

The structural composition of the banking system has undergone notable shifts, with a doubling share of variable rate loans over a couple of years as interest rates started to increase. This trend has nevertheless eased in 2024, with the share of variable-rate loans dropping to (30.6% in September 2024 from 32.6% in September 2023). While this measure helped the sector shield itself from interest rate risks, this will contribute further to the pressure to retain current high profitability position with interest rates trending downward. Another structural shift being observed is the shifting of the household sector portfolio toward longer-term loans, particularly household loans with maturities exceeding 10 years. While this development reflects the natural process of financial deepening as the sector converges towards its regional peers (Financial intermediation of households rose to 21.7% of GDP from 19.1% in the previous year), it is also a result of increasing preference for consumption and mortgage loans on the back of better income expectations and more favorable borrowing conditions (larger unsecured loan amounts), but also by the higher overall prices (renovations, car purchases and house investments have become costlier relative to previously).

The faster growth in loans to households relative to the enterprise sector has resulted in a gradual increase of the relative share of household loans to total lending portfolio to 40.5% from 38.6% in

September 2023. The Kosovo banking sector household intermediation rate now aligns with the regional average which stood around 20% in September 2024, whereas the intermediation for enterprises has exceeded the regional average since 2017.

Resilience and Capital Strength

The sector's solvency has strengthened, as profits have been prudently allocated to reserves, further increasing the capital ratios. The quality of capital is also high, with 87.7% of capital comprising of CET1 capital.

3.5 Alternative Scenarios and Risks

The baseline macroeconomic scenario that underpins the medium term budget projections and the outlook presented on this update of the ERP results from a careful consideration of both downside risks and potential developments, associated with economic developments expected in the medium term. Compared to the ERP 2024, the external environment has become less favorable over the medium term, which translates into higher probability of realization of shocks to foreign sources of financing for the Kosovo economy (remittances, foreign direct investment, and exports).

It is important to note that the baseline scenario presented in the current ERP (2025-2027) does not account for the potential impact of implementation of Reform Agenda outlined in this year's ERP.

Internal energy crisis, fiscal risks from public enterprises, risk from contingent liabilities arising from on-lending are some of domestic risks that are reflected on this updated ERP, whereas measures to address core inflation in the Eurozone, and upward pressures on prices due to climate change and geopolitical tensions are some of external risks.

Domestic risks

Challenges in the energy sector, fiscal vulnerabilities from public enterprises and contingent liabilities from on-lending represent notable risks to the baseline scenario.

Internal energy crisis-The rise in energy prices due to the geopolitical tensions combined with high winter consumption demand and the fragile capacities for domestic power generation, could lead to a substantial increase in the need for energy imports. This would likely have a negative impact on production and will have affect in consumer prices. In other side shortages in energy will affect economic activity and consequently on the collected budget revenue.

Fiscal risks from Public Enterprises- Overall, publicly-owned enterprises continued to generate profits in 2023, leading to an improvement in their liquidity positions. As a result, these enterprises are now better equipped to meet their financial obligations. In spite of this improvements in operational performance among individual public enterprises compared to the previous year, overall the performance of POEs experienced a deterioration because of one company with substantial net loss, which adversely impacted the overall net profits of POEs.

Risk from contingent liabilities, on-lending and Guarantees-A potential source of this risk are guaranteed public sector loans and international loans sub-borrowed to the companies providing essential public services. Financial and economic risk analyses have raised concerns about the poor performance of public companies. To limit the impact of risk from contingent liabilities, a number of measures will continue to be implemented, such as: (a) monitoring the financial position of beneficiaries (b) initial assessment of the possibility of materialization of existing contingent liabilities. Depending on the assessments for the alleged losses, the applicable guarantee fees according to the Law on Public Debt will be determined. As a measure for the management of these risks also serves the inclusion of guarantees in the amount of total debt, in the calculation of the debt limit to GDP.

External risks

Geopolitical tensions - The conflicts in Ukraine and the Middle East could introduce further disruptions to supply chains, significantly impacting global trade and energy markets. Such developments may lead to unexpected surges in the prices of food, energy, and oil. While the conflict in the Middle East has had a limited effect on oil prices to date, any further escalation could profoundly influence financial conditions, energy costs, global economic output, and overall inflation.

Remittances - Another channel through which international developments could impact economic activity in Kosovo is through remittances from the diaspora, primarily residing in major European countries. A potential rise in prices abroad would diminish the real incomes of Kosovar emigrants, leading to reduced remittances, a decline in travel-related services, and/or lower foreign direct investment. These reductions in inflows would directly affect private disposable incomes, curbing consumption and private-sector investment, ultimately resulting in lower GDP and, consequently, decreased budget revenues compared to projections. Additionally, tighter financial conditions could further elevate financing costs, constrain bank lending, and suppress demand for goods and services within Kosovo’s economy.

Monetary Policy– Given the significant interconnectedness of Kosovo's economy with international markets, heightened vigilance is necessary regarding the effects of monetary policy tightening by Kosovo's key trading partners. Rising interest rates abroad could increase the cost of imported goods, contributing to higher imported inflation in Kosovo.

Climate Change – Climate change poses additional risks to domestic inflation, particularly by disrupting global food supply chains. A decline in cereal production across various countries could lead to rising food prices. Moreover, efforts to reduce fossil fuel-based electricity generation for environmental protection, coupled with inadequate compensation from renewable energy sources, could result in production shortfalls, further driving up energy prices and contributing to broader inflationary pressures.

Summary of shocks and risks

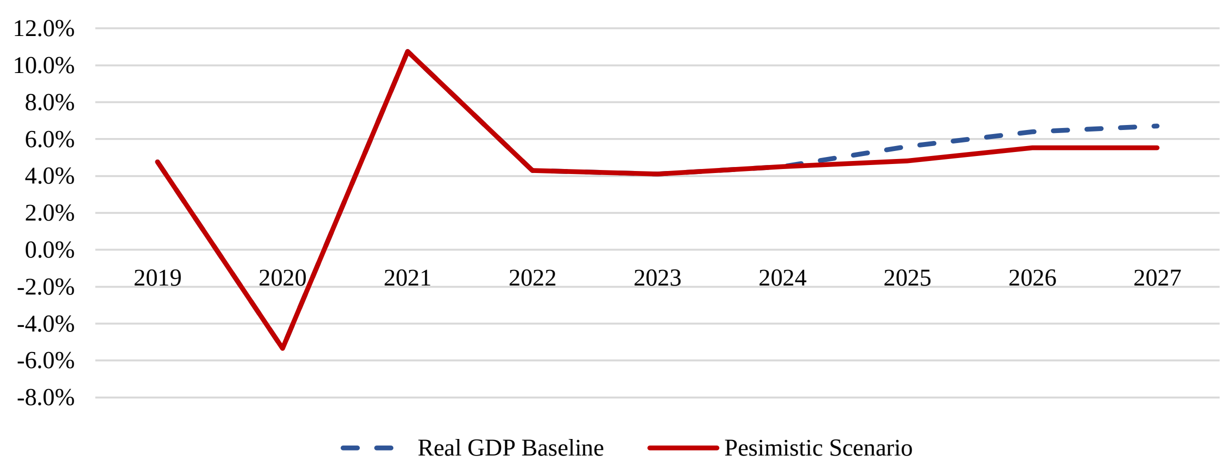
Table 5. Sensitivity analysis of the budget to fluctuations of macroeconomic variables for 2025- 2027

Variable	Magnitude of Shock compared to baseline	Revenues		Budget Balance
		% of projected revenues annual average	impact in million Eur	impact in million Eur
Under execution of Public Investment	-10.00%	-0.57%	-60.3	-60.3
Remittances	-6.30%	-0.79%	-84.2	-84.2
Exports (G&S)	-7.50%	-0.64%	-69.0	-69.0
Combination of three shocks		-2.00%	-213.5	-213.5

Note: Numbers shown in this table represent the sum of effects of various shocks for three years.

In the low scenario, total government revenue underperformed by an average of 2.0% compared to the baseline projections for the period 2025-2027. This under-performance will be more pronounced in the category of indirect tax revenues. In addition, in the low scenario a lower level of implementation for capital expenditures is assumed, which in average will be around 10% lower than the capital expenditure projected during 2025-2027 in the baseline scenario. Lower remittances and lower exports of goods and services are related to uncertainties in external environment mostly in the countries where Kosovan diaspora residing. When aggregating all downside risks, real GDP growth is estimated to fluctuate around 5.3% on average over the period 2025- 2027, which is around 2.9 percentage points lower than the real growth in the baseline scenario.

Figure 13. Real GDP growth: Baseline vs. Pessimistic Scenario



3.6 Alternative Scenario using the implementation of selected measures from the Reform Agenda

The impact assessment for the Reform Agenda (RA) is conducted to evaluate the economic effects of key policy measures and investments proposed within the framework. This process ensures that the reforms are grounded in evidence and their potential contributions to economic growth, employment, and infrastructure improvement are clearly understood.

The reforms selected for impact assessment were identified based on their expected contribution to GDP growth, particularly those that generate significant investment, employment opportunities, or enhance the business environment. Additionally, the selection focused on reforms with sufficient data and information availability, ensuring that the calculations and projections are based on reliable inputs and methodologies. It is important to note that the estimates provided through the impact assessment were not included in the baseline scenario or fiscal framework.

I. Impact assessment for each reform

2.5.1. Development of transparent and competitive procedures for deployment of renewable energy

This reform is expected to generate significant investment and employment opportunities. In terms of employment, the deployment of renewable energy sources will directly create jobs in construction, operations, and maintenance of renewable energy projects. The assessment focused on increasing renewable energy capacity and prosumer incentives. Targets included installing 0.9 GW of solar and wind capacity by 2027. The economic impact was modeled through investment requirements and projected outputs, linking energy reforms to long-term economic and environmental goals.[9] To reach the target of 0.6 GW through IRENA published 2023 cost of deploying 1kw of RES and the Kosovo NECP, investments of around 605 million euros are needed to reach the target for installing 0.6 GW. These investments would also generate potential full-time jobs of around 4800 new jobs.

The investment is assumed to be spread out equally in the medium-term period and the results from the additional investment in the Macro Model suggest additional real GDP growth of 2.5%. This is also supported by the alternative methodology using the study[10], which suggests economic multipliers of 1.12(lower bound) and 1.73 (upper bound) for investments in renewables.

2.6.1 Implementation of the Energy Efficiency Directive and the Energy Performance in Buildings Directive

The reform targeted a 3% additional annual renovation of public buildings, supported by new energy efficiency laws and market-based ESCO mechanisms. In addition, the measure foresees a

[9] Nicoletta Batini, Mario Di Serio, Matteo Fragetta, Giovanni Melina, Anthony Waldron, Building back better: How big are green spending multipliers?, Ecological Economics,Volume 193, 2022

[10] Nicoletta Batini, Mario Di Serio, Matteo Fragetta, Giovanni Melina, Anthony Waldron, Building back better: How big are green spending multipliers?, Ecological Economics,Volume 193, 2022

target of renovating 0.5 million m2 of residential buildings. Using the baseline indicators in the RA, the public buildings renovated include additional 0.06 million m2 and 0.5 million m2 of residential buildings.

The assessment estimated investment costs based on Slovenian NRRP benchmarks and modeled impacts on job creation, reduced energy costs, and GDP growth, aligning with NECP and EU energy directives. The estimates suggest renovations of public and municipal buildings that require partial investment in the range of (263-391 Euros per m2) and for multi-apartment buildings that require investment in the range of (211.5 Euros per m2).

Based on the number of buildings planned to be renovated and the square meters they cover, the estimates suggest an investment of 120.2 million Euros for these efficiency measures for the medium term. This measure is also expected to create additional employment using the multipliers of 7.75 jobs per 1 million USD investment in energy efficiency which is around 930 new jobs created. **Using the investment estimates in the Macro Model as an exogenous shock, the results suggest an additional real GDP increase of 0.7% in the medium term, cumulatively.**

2.2.1 Financial Support for Startups and MSMEs

This reform aims to foster the creation and scaling up of start-ups and micro, small, and medium enterprises (MSMEs) in the ICT and green and circular economy sectors. It seeks to address fragmentation within the innovation ecosystem by providing integrated support mechanisms through the establishment of the Innovation Fund and business incubators. The reform also emphasizes modernizing start-up financing methods, such as venture capital and crowdfunding, which are currently underutilized.

The specification is based on a study that estimated a panel of EU28 countries and found that a 1 percentage point increase of the GDP share of R&D expenditure increases the real GDP growth rate by 1.11 to 2.27 percentage points[11], depending on model specification. In addition, the investment estimates coming from this reform include 3 million investments each year in R&D (1.5 million Euros Innovation Fund and 1.5 million co-financing). **The results based on this study suggest that the envisaged investment in R&D coming from this reform (including the co-financing from private sector) leads to an additional of 0.2%~0.3% Real GDP growth in the medium term. The results are comparable with the estimates received from the Macro Model.**

Reform Measure	Impact on Real GDP Growth	Impact on Employment
	Cumulative 2025-2027	
2.5.1.	2.5%	4,800
2.6.1.	0.7%	930
2.2.1.	0.2%	N/A

[11] Guellec, D., & van Pottelsberghe de la Potterie, B. (2004). From R&D to Productivity Growth: Do the Institutional Settings and the Source of Funds of R&D Matter? Oxford Bulletin of Economics and Statistics, 66(3), 353–378.

4 FISCAL FRAMEWORK

4.1 Budget implementation in 2024 (Preliminary Data)

Based on preliminary data, public revenues and expenditures experienced growth during January-September 2024 compared to the previous year, and the Government fully adhered to applicable fiscal rules. The budget deficit, as per the legal deficit rule, is estimated at -1.1% of projected GDP in 2024, well below the 2% of GDP legal cap. Government cash balances at the end of the year are estimated at 2.1% of GDP.

Budget revenues for the period January-September 2024 have increased by 7.2% compared to the same period of previous year. In absolute terms, budget revenues reached the value of 2,256.3, achieving a realization rate of 99.5% compared to budget estimates.

The revenues from direct taxes marked an increase of about 3.9% for this period in 2024 reaching the value of 390.8 million Euros. Revenues from personal income tax increased by about 9.8% compared to the same period of the previous year, which can also be attributed to the increase in the number of private sector employees and the increase in value of coefficient of public wages in accordance with budget law. Revenue from corporate income tax followed an upward trend, as well, with an increase of 8.1%. As for the property tax, the income from this tax has decreased by -33.7% for this period.

Revenues from indirect taxes during the period January-September 2024 marked an annual increase of 10.8%, reaching the value of 1,669.1 million Euros, which represents a collection rate of 99.6% of the budget projections. While, revenues from customs duty increased during this period at the rate of 11.5%. An upward trend also is marked by excise duty growing at an annual rate of 12.4% and collection rate of 101.0%.

Non-tax revenues during this period reached the value of 256.5 million Euros, or an increase of 30.0% for this period. The highest growth among non-tax revenue categories was recorded by central level revenues, with an increase of 38.6%, followed by concessionary fee with an annual increase of 26.3%, mostly due to the increasing trend in the number of passengers at Pristina International Airport. Non-tax revenues at local government recorded an annual increase of 2.8%, while royalties increase by 1.2%.

Budget expenditures were higher than in 2023, while the execution rate was different among various categories. They marked an increase of 9.2% reaching the value of 1,986.8 EUR. The current expenditures increased by 7.0% compared to last year. The category of salaries and allowances recorded an annual increase of 13.0% compared to last year mostly due to the increase in the wage coefficient as is determined in Budget Law 2024, with an implementation rate of 106.6%. Expenditures for goods and services also recorded a significant increase (9.6%), reaching the value of 281.8 million Euros, and an execution rate of 86.5%. On the other hand, subsidies and transfers were not characterized by any significant movement compared to 2023, with a slight annual increase of 1.1%, and an execution rate of 95.8%. This is due to the high growth in the past year as a result of implementation of the measures of the economic revival package.

Capital expenditure in 2024 marked a significant increase of 23.1% compared to same period of 2023. The financing structure of capital expenditures in 2024 is dominated by the regular budget, which accounts for 92.6% of total capital expenses.

Interest expenses reached the value of 32.3 million euros, marking a decrease of -1.7% on 2024 compared with same period of previous year.

Table 6. General Government Operations, in million Euro

Description	2022	2023	2024
Total Revenue	**1,842.9**	**2,104.2**	**2,256.3**
Tax Revenue	**1,643.2**	**1,839.3**	**1,999.8**
Direct Taxes	**313.9**	**376.1**	**390.8**
Tax on Corporate Income	125.7	145.3	157.0
Tax on Personal Income	158.6	189.2	207.7
Tax on Immovable Property	26.7	39.2	26.0
Other	3.0	2.5	0.0
Indirect Taxes	**1,377.5**	**1,506.7**	**1,669.1**
Value Added Tax:	896.0	989.1	1,087.4
Customs Duty	95.4	110.4	123.2
Excise	385.8	407.1	458.5
Other indirect	0.3	0.1	0.0
Tax Refunds	**(48.2)**	**(43.5)**	**(60.0)**
Non-tax revenue	**189.4**	**197.4**	**256.5**
Fees, charges, and other - Central Level	113.0	109.5	151.8
Fees, charges, and other - Local Level	38.4	45.7	47.0
Concessionary fee	14.3	20.0	25.2
Royalties	1.5	1.9	1.7
Budget support and grants	**10.3**	**-**	-
DDG - Donor designated grants		**67.5**	
Total Expenditure	**1,579.75**	**1,820.02**	**1,986.79**
Recurrent Expenditure	**1,579.8**	**2,359.8**	**2,264.7**
Wages and Salaries	477.5	566.1	639.9
Goods and Services	218.4	257.2	281.8
Subsidies and Transfers	698.5	700.1	708.1
Capital Expenditure	**158.1**	**263.8**	**324.7**
Public Debt Interest	**27.2**	**32.9**	**32.3**
DDG - Donor designated grants	**5.3**	**6.3**	**13.4**
Overall budget balance,	**263.1**	**284.1**	**269.5**
Available bank balance	**678.2**	**638.8**	**625.4**

4.2 Budget Plans for 2025 and the mid-term period

In the upcoming medium term 2025-2027, budget revenues are expected to increase by 8.0% on average, reaching an average ratio of 29.6% of GDP. The projection of budget revenues over the period 2025 - 2027 takes into account all estimated effects of fiscal policies, such as the new excise calendar, Government decision to increase the minimum wage and also adjusted tax rates of PIT. Tax revenues are projected to be around 26.4% of GDP.

In 2025 revenues are projected to increase by 9.2% compared to the revenues projected in budget law for 2024. The increase in total revenues comes as a result of the contribution from indirect taxes, direct taxes and non-tax revenues with the participation of about 73.5%, 17.7% and 10.8%

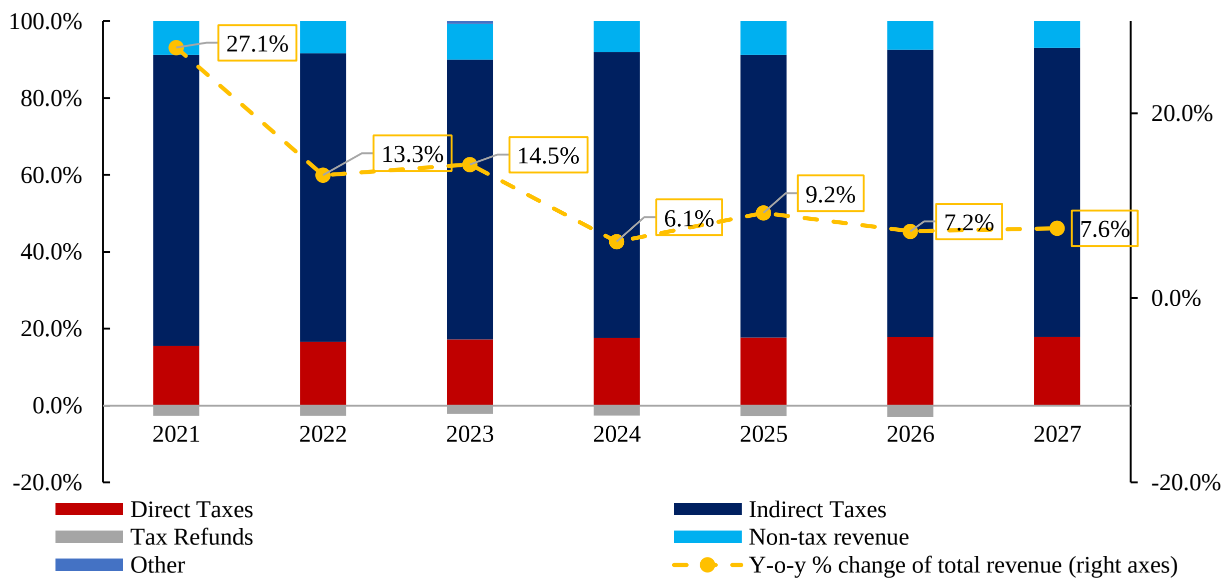
respectively. As a share of GDP, the structure of revenues is projected to be as follow: direct taxes 5.3% of GDP, indirect taxes 21.9% and nontax revenues 3.2% of GDP.

Indirect tax revenues for are expected to increase by around 8.1% in 2025 compared to 2024. The indirect tax revenues will continue to represent the highest share in total revenue in 2025. The key contribution to indirect tax revenue growth is attributed to VAT, with an annual growth of 7.8%. This increase is driven by a nominal growth of imports of about 7.2 %, a projected increase of 7.4% in private consumption, and an increase of over 3.3% in government purchases of goods and services. Exports of travel services, which represent typically non-refundable migrants' consumption during their stay in Kosovo is also expected to contribute to VAT growth. Excise tax revenues are projected to increase by 7.6% - such growth takes into account the calendar of excise in tobaccos and some other products. Intensified public and private investment is projected to increase demand for fuel which is likely to be another growth driver for customs duties, which are projected to increase annually by 7.6%.

Revenues from direct taxes during 2025 are expected to increase by about 9.7% compared to the 2024 and constitute 17.7% of total revenues. The CIT is projected to increase around 5.2%, supported by continued fighting of informality, among other factors. PIT is projected to increase by 16.9% mostly due to the formalization and increase of employment but also higher coefficient in public wages and changes in personal income tax rates. Property tax is projected to increase by 12.2%, mostly due to the low base year.

On the other hand, non-tax revenues during 2025 are expected to increase by 21.8% compared to 2024, reaching the amount of about 356.6 million Euros. In 2025, grants are expected to reach the value of 22.5 million Euros.

Figure 14. Revenue structure



In the following years 2026-2027, budget revenues are expected to increase by an average of 7.4% (7.2% in 2026 and 7.6% in 2027). While direct taxes in the period 2026-2027 are expected to increase by 7.7% on average; indirect taxes will increase by 8.6%. On the other hand, non-tax revenues are expected to have a slower trend with an average increase of 0.8% in the period 2026-2027.

4.3 Expenditures forecast for 2025 and the medium-term period

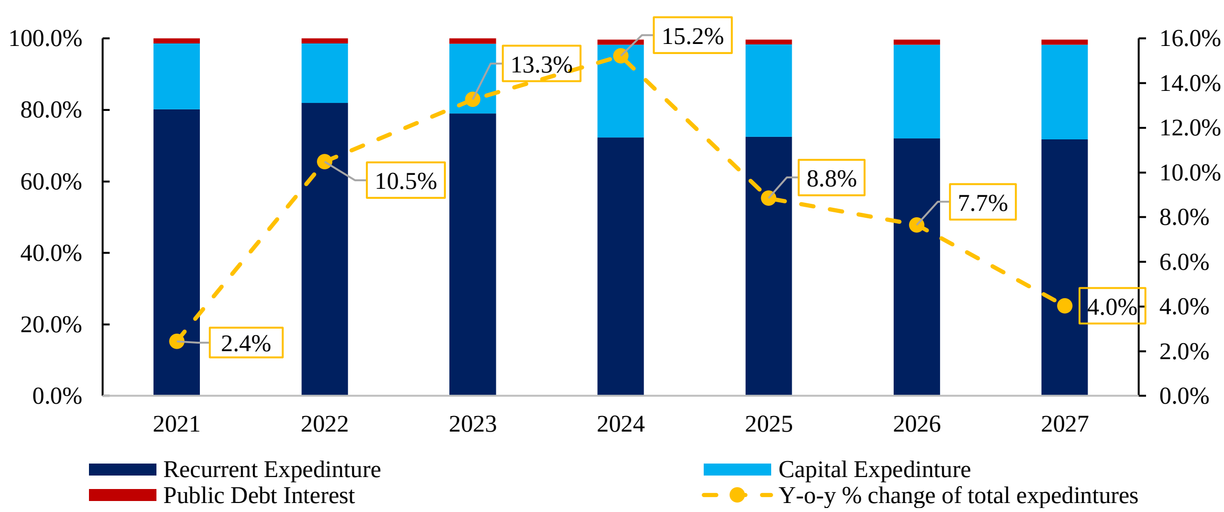
Total budget expenditures in 2025 are expected to increase by 8.8% compared to the 2024, reaching 32.5% of projected GDP. The increase in expenditure in 2025 is mainly attributed to increase in wage bill and increase in capital expenditure.

Current expenditures during 2025 are projected to increase by 9.1%. Expenditures for category wages and salaries are projected to reach the value of 916.5 million Euro in 2025, which represents an increase of around 13.8% compared to the projections in budget law for 2024. This increase is due to the increase in the coefficient on public wages. Expenditure for goods and services is projected to increase by 3.3%, this increase is as a result of elections (parliamentary and municipality) which will be held during 2025. Subsidies and transfers are expected to increase by 8.8% compared to 2024.

Interest expenditures are projected to 49.5 million of Euros. For the current reserve category, around 7.5 million Euros have been allocated for 2025.

Capital expenditures are expected to increase by 8.3% in 2025, reaching a share of 25.8% of total expenditures, and 8.4% of GDP. Most of the capital investments are expected to be financed from the regular budget, but also the projects from the Investment Clause which are carried over from previous years.

Figure 15.Expenditure's structure



4.4 Fiscal Structural Balance

Structural balance represents the fiscal balance of the government, adjusted for the effects or fluctuations of the business cycle, which are not directly controlled by the government. Often it is argued that the overall fiscal balance does not provide a comprehensive view of the fiscal position because it is significantly influenced by the business cycle. During periods when an economy experiences strong economic growth, tax revenues tend to increase; while in the conditions of economic slowdown, budget revenues, especially those from income and consumption, decrease, and at the same time government spending increases mainly due to higher expenditure on unemployment benefits and other government subsidies. These changes in fiscal indicators, which occur without any discretionary government intervention, help alleviate economic fluctuations and are therefore known as "automatic stabilizers". The structural fiscal balance (adjusted for business cycle) aims to measure the fiscal position “free” from these stabilizers, providing a better understanding of the scale and intensity of discretionary fiscal policy.

In order to obtain the structural balance, it is important to isolate the cyclical component of the fiscal balance, which depends on the size of the output gap and on the output elasticity of the budget. In the case when an economy is at its potential level (output gap is zero), this cyclical component of fiscal balance will be zero and consequently the current fiscal balance represents at the same time the structural balance. Assessment of the structural balance presented in this section, should be interpreted with considerable caution, due to the limited availability of the annual GDP data and uncertainties surrounding the estimation of potential output. In this updated version of ERP, structural balance is estimated using annual data covering the period 2008-2027 (in total 21 observations, out of which 3 are projections).

The variables used to estimate the fiscal structural balance are: real GDP, potential GDP (calculated using the HP filter), the output gap, budget revenues (more specifically tax revenues, non-tax revenues and grants), expenditure, and the output elasticity of tax revenues. In order to remove the cyclical component, or to 'adjust' the necessary variables for this calculation, the following specification was used:

$$Adjusted\ fiscal\ variable = Unadjusted\ fiscal\ variable * \left(\frac{GDP\ potential}{GDP\ actual}\right)^{Elasticity}$$

Tax revenues were adjusted using the output elasticity of tax revenues, estimated at around 1.9 for the period 2008- 2027. This elasticity implies that tax revenues disproportionately grow faster than GDP, which can be explained by several factors. One factor could be that tax revenue series are not adjusted for discretionary policy changes. Another reason can be attributed to distortions brought by the informal sector, which affect tax buoyancy and elasticity. As for the elasticity used to ‘adjust’ non-tax revenues, the value 1.00 was used. The rationale for the use of this value is based on the theoretical explanation that non-tax revenues usually move in line with GDP. Also, taking into account the fact that Kosovo does not have automatic stabilisers (such as unemployment benefits), implying that expenditures do not depend on the cyclical state of the economy, no adjustment was applied to any expenditure category. The same applies to grants.

After the above-mentioned variables were 'adjusted', the primary structural balance was calculated as in the following:

Primary Structural Balance =Adjusted Tax Revenues +Adjusted Non-tax Revenues + Grants – Expenditure

Figure 16. Unadjusted Primary Balance, Primary Structural Balance and the Output Gap (2007-2027)

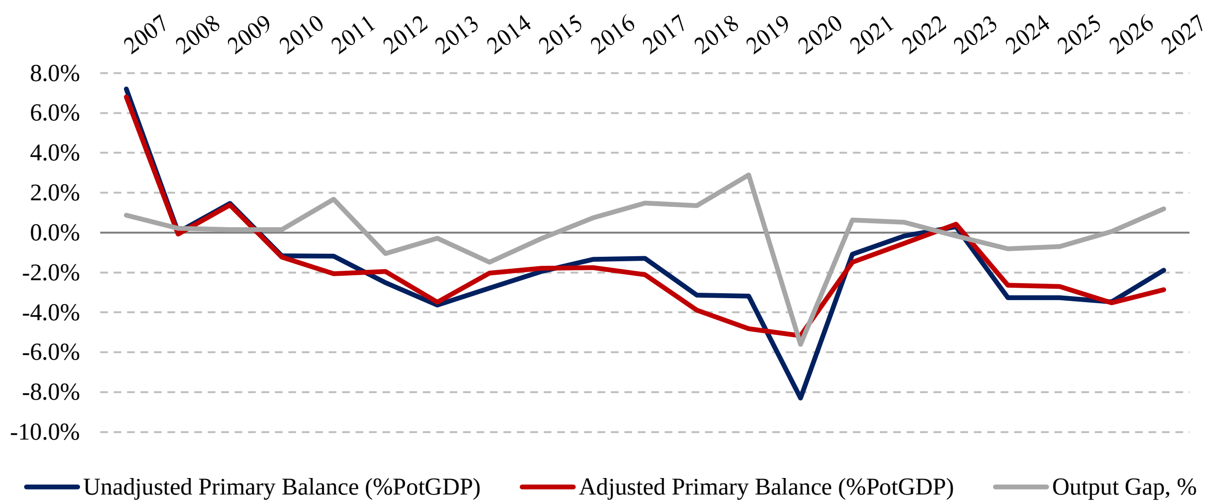
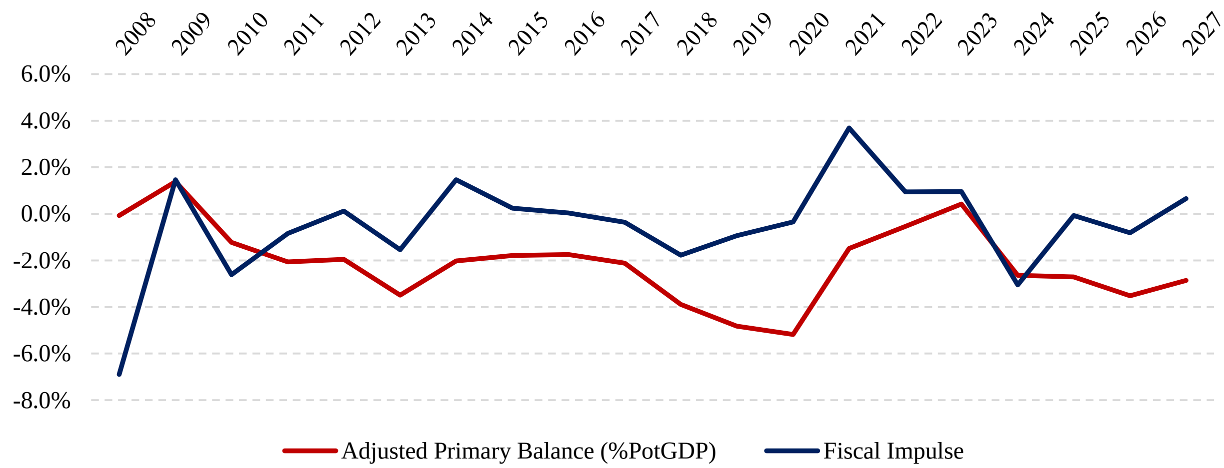


Figure 16 shows the relationship between the unadjusted primary balance, structural primary balance, and the output gap. The primary structural balance shows what the primary balance would be like if the current GDP were equal to the potential GDP (i.e., if the cyclical component is subtracted from the primary balance). It also shows that during periods when the economy operates below potential (or when output gap is negative), the structural primary balance is higher than the unadjusted primary balance, and the reverse occurs when the economy exceeds its potential.

Based on these results, the periods during which the economy was operating below its potential level are during the period 2012- 2015, in 2020 and in projected period 2024-2025. During the remaining periods, the economy generally operated slightly above its potential. The fiscal stance variable, measured by the structural primary fiscal balance, indicates whether the fiscal position of the government has been expansionary or contractionary over time. Based on the results shown in Figure 16, it can be seen that Kosovo from 2010 onwards (even in the projected years 2025-2027) has pursued and is expected to pursue an expansionary fiscal policy.

Lastly, the variable 'Fiscal Impulse', which is calculated as the first difference of the fiscal stance (the structural primary balance), measures the direction and magnitude of changes in fiscal policy, with negative values indicating an increase in fiscal momentum, while positive values indicating a withdrawal of fiscal momentum in aggregate demand. From the estimations shown in Figure 17, it can be noticed that the measures taken by the Government in 2021 in response to the pandemic have contributed to an increase in fiscal momentum. However, in 2022 and 2023, there was a withdrawal of the fiscal momentum, mostly due to the base effect in 2021, and satisfactory performance of budget revenues. In the medium term, the fiscal momentum is expected to rise again in 2024, followed by a gradual decline over the next two years.

Figure 17. Primary Structural Balance, Fiscal Stance and Fiscal Impulse (2007-2027)



4.5 Debt levels and developments, analysis of below-the-line operations and stock-flow adjustments

Kosovo has adopted a prudent legal framework to prevent unsustainable debt practices. Based on the new Law on State Debt and State Guarantees No. 08/L-099, the Ministry has the sole authority to negotiate and borrow state debt on behalf of the Republic of Kosovo, through the relevant Minister of Finance, as the only authorized person, without the right to delegate such authorization. Under the Constitution, every international agreement has to be ratified by a two-thirds majority in Parliament.

Unless otherwise regulated by the Law on Public Finance Management, as per current date, the Law on State Debt and State Guarantees includes several provisions that ensure fiscal stability, the total debt ceiling including state guarantees may not be higher than forty percent (40%) of the GDP, as well as certain limitations on municipal borrowing. Contingent liabilities are accounted as state debt and state guarantees, as per this indicator. The Law on State Debt and State Guarantees mandates regular reporting to the Assembly (Article 9) through the preparation of a State Debt Program, which includes a medium-term debt strategy, to be submitted to Government for approval and to the Assembly for information.

With regard to other restriction on state debt and state guarantees, an amendment was added to the Law on Public Finance Management and Accountability (LPFMA) which limits the annual budget deficit to no more than 2% of forecasted GDP. Another amendment to the LPFMA was added in 2015 which allows the government to contract debt in excess of the 2% rule, given that the financing is provided by international financial institutions and is dedicated for capital projects (investment clause).

The Ministry of Finance, Labour and Transfers has issued regulations on external debt and domestic debt, which contribute to an efficient state debt management. Based on the Regulation on Procedures for Issuance and Management of State Debt, State Guarantees and Municipal Debts, international agreements are negotiated by an official team consisting of members from different departments: Department of Financing, Legal Department, Budget Department and relevant Budget Organizations. The issuance of state debt through Government securities is authorized by the Law on State Debt and State Guarantees, and it is regulated by the Regulation for the Primary and Secondary Market of Government Securities of the Republic of Kosovo No. 01/2014. The current practices of state debt management are in full compliance with the requirements arising from the primary and secondary legislation.

The new Law on State Debt and State Guarantees is ratified in the end of 2022. In order to advance and align the legal infrastructure with European Union standards and international best practices, the primary and secondary legislation has undergone a review process. In the end of 2022, primary legislation has been approved while the secondary legislation is in process, it is expected to be completed and approved by 2025.

Table 7. Total Government Debt, in million euro (unless otherwise indicated)

Description	2021	2022	2023	2024	P.2025	P.2026	P.2027
External Debt	576.7	641.2	692.9	736.5	1,266.5	1,584.6	1,838.3
Domestic Debt	1,106.1	1,112.0	970.2	962.2	1,072.9	1,172.9	1,272.9
Total State Debt	1,682.8	1,753.2	1,663.1	1,698.7	2,339.4	2,757.5	3,111.2
State Guarantees	30.6	29.6	28.6	3.6	2.6	1.5	0.5
State Debt and Guarantees (% of GDP)	**21.5%**	**20.0%**	**17.5%**	**16.1%**	**21.1%**	**23.0%**	**24.0%**

Contingent Liabilities

By the end of 2024, the state guarantee portfolio consists of a single active state guarantee:

1. The Ministry of Finance issued a guarantee in 2016 for a loan provided by the EBRD to the local public enterprise, Urban Traffic, in the amount of EUR 10 million. The loan was fully disbursed, and its repayment began in 2018.

The state guarantee for the DIFK credit line, issued in 2017 for EUR 24 million, is no longer active, as the availability of the guarantee ended on 31 December 2023.

During 2024 the Government has not entered into new state guarantee agreements.

Table 8. State Guarantees

	2021	2022	2023	P.2024	P.2025	P.2026	P.2027
State Guarantees	30.6	29.6	28.6	3.6	2.6	1.5	0.5
Guarantee for Urban Traffic Pristina	6.6	5.6	4.6	3.6	2.6	1.5	0.5
Guarantee for Second Credit Line to DIFK	24.0	24.0	24.0	0.0	0.0	0.0	0.0
State Guarantee (% of GDP)	**0.4%**	**0.3%**	**0.3%**	**0.03%**	**0.02%**	**0.01%**	**0.004%**

4.6 Sensitivity analysis and comparison with the previous programme

4.6.1 Comparison with the previous programme

Compared to ERP 2024, ERP 2025 projects a higher revenue collection for year 2025 by 3.5%, which is due both to higher expected tax revenues and higher non- tax revenues. Also, in year 2026, higher revenues are projected to be collected compared to the previous programme (by 4.0%), as result of higher tax and non-tax revenues.

In addition expenditures are projected to be higher compared to projections presented in ERP 2024 by 3.0% and 6.6%, respectively. This is due to higher recurrent and capital spending in both years compared to the previous years.

Budget deficit is projected to remain within the 2% fiscal rule limit for years 2025 and 2026. The bank balance as percentage of GDP is expected to reach 3.1% in 2025 followed by 3.3% of GDP in 2026 (bank balance rule not applicable – no PAK finances will be used). In line with the expected performance in the budget deficit, the bank balance as percentage of GDP, in the current version of ERP, is higher than the balance projected when preparing the previous year's ERP.

Lastly, some policy changes and developments during 2025 which are included in the forecasting process of this year's ERP relate to: i) increase in all state-funded pension benefits; ii) increase in child allowances; and iii) the increase in minimum wage and changes in personal income tax rates.

A more complete comparison with the previous program is presented in annex.

4.7 Fiscal governance and budget frameworks

The Law on Amending and Supplementing the Laws that Determine the Amount of the Minimum Wage, Procedures on Setting of Minimum Wage and Tax Rates on Personal Income came into force during 2024. This Law does not set the minimum wage, it regulates the process of determining the minimum wage and other related benefits, such as social schemes which are related to minimum wage.

Based on this law the Government of Kosovo adjusted tax rates reducing the bracket of 4%, also the Government of Kosovo took a decision to increase the minimum wage to 350 euros.

In 2024 the government took a decision to increase by 20% all state-financed pension benefits, which reflects accumulated cost of living adjustments.

In the context of social inclusion, ongoing efforts are being made under the Reform of the Social Assistance System of Kosovo project, with the aim of implementing more efficient and inclusive social programs. In this context the project has begun the beneficiaries have been identified and new applications are being evaluated.

Draft of the Law on Public Financial Management and Accountability (LPFMA) which is aligned with the EU standards and best international practices of accountability, transparency and efficiency is finalized and soon will be published on the public consultation platform.

Recently The Assembly approves the Draft Law on compulsory health care insurance. Implementation of this Law will increase the scope of services provided by the public health system and improve its financial sustainability and will not put additional pressure on the budget.

Regarding the fiscal rules, they have been maintained as per law in place, and are planned to be maintained in the medium term framework.

4.8 Sustainability of Public Finances

4.8.1 Debt Sustainability

To ensure fiscal sustainability, Kosovo has maintained consistent fiscal rules, including a public debt ceiling of 40% of GDP, where any external borrowing is subject to ratification by parliament. Since 2015, Kosovo has respected fiscal rules, with the exception of 2020 due to the challenges created by the COVID-19 pandemic. Over time, the fiscal rules limiting public debt and deficit levels have proven to be an important anchor in maintaining long-term fiscal stability.

The public debt to GDP ratio has remained stable, with a slight upward trend until 2020, primarily driven by projects funded by International Financial Institutions. In 2020, the debt-to-GDP ratio increased more significantly (approximately 4.8 percentage points higher than in 2019) due to additional funding needed to address the economic crisis caused by COVID-19. In the following years (2021, 2022, and 2023), the satisfactory budget revenue performance boosted by the economic recovery and high inflation in 2022 allowed the government to build fiscal buffers and reduce new debt issuance, resulting in a decline in the debt to GDP level.

The Republic of Kosovo started issuing securities in January 2012, and the development of its market have been very successful in terms of investor interest and borrowing costs. To mitigate refinancing risks, Kosovo has been working to extend the maturity of its domestic debt. Starting in 2018, Kosovo started issuing 10-year bonds. In 2021, Kosovo introduced ‘diaspora bonds’, aiming to attract capital from abroad as well as from Kosovar residents.

International debt, on the other hand, is composed mainly of concessional loans from International Financial Institutions.

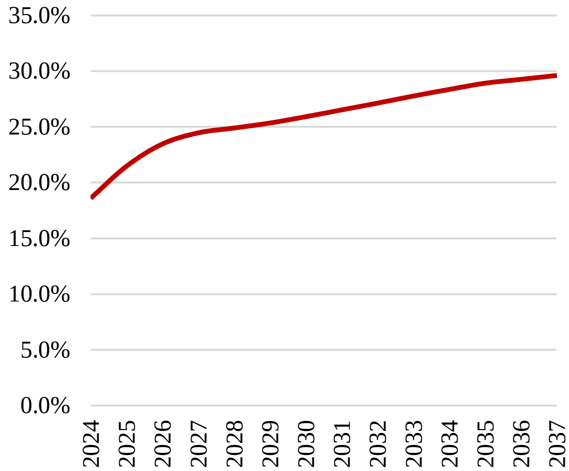
Key Assumptions of the Debt Sustainability Analysis

- Debt Sustainability Analysis (DSA) takes into account the macroeconomic forecasts for medium-term growth. Nominal growth is projected to average 8.0% from 2025-2027, and then stabilize around 4.0% from 2028 to 2037. The deficit, excluding projects financed by IFIs, is projected to remain within the fiscal rule limit after 2024 throughout the analysis period.
- Public debt in the analysis does not include the debt of POEs, but only government debt and guarantees.
- Short-term debt is projected to decrease during the analysis period, as the government increases the average amortization of securities. Since 2017, the Ministry of Finance, Labour, and Transfers focused on extending the average maturity time and issuing instruments with a maturity of 5, 7 and 10 years. International debt from IFIs will reflect the terms of existing debt agreements during the forecast period. Disbursements from the investment clause are projected to continue until 2026, while liquidation funds are not expected to continue.
- The assumption of maintaining a bank balance of 4.5% of GDP is not applicable in 2024 and beyond, as this level is not mandatory in years when liquidation funds are not used to finance capital expenditures.
- Debt structure includes a mix of commercial debt, concessional debt, and government securities. The shares of each type of debt are given based on some assumptions by the Debt Department of the Ministry of Finance, Labour and Transfers, with the share of commercial debt increasing over the years given that infrastructure projects and development needs will be gradually met by IFI-funded projects.
- The DS analysis covers the period up to 2037, as for this period there are more detailed data regarding the amortization of project loans and the performance of securities.

The baseline scenario shows that the public debt stock will remain stable. The debt to GDP ratio is expected to show a slight upward trend over the forecasting period and exceeds the level of 30% of GDP in 2038Interest expenditure as a share of the overall deficit remains low in the initial years, consistent with previous projections.

The financing need remains well below 10% of GDP, staying within the threshold for developing economies set by the DSA. Between 2025 and 2027, the financing need is projected to be 3.0% of GDP. The gradual reduction of the investment clause has led to the need for financing to gradually decrease.

Figure 18. Debt as % of GDP- Baseline Scenario **Figure 19. Financing need as % of GDP – Baseline Scenario**



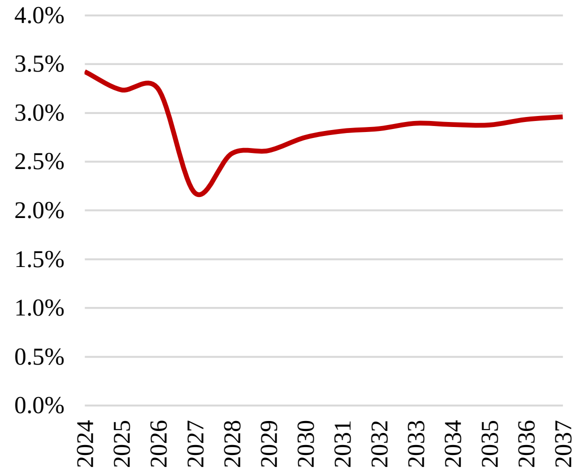
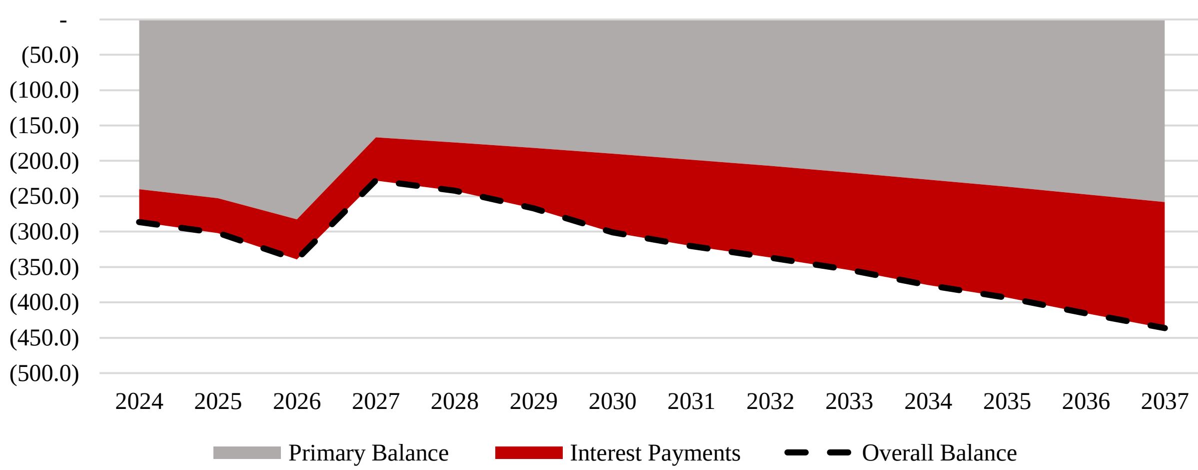


Figure 20. Overall Balance Structure – Baseline Scenario (mil Eur)



Alternative Scenarios

Shocks under different scenarios affect the debt level as a percentage of GDP, but the financing need is expected to remain stable. This is mainly due to the compliance with the fiscal rule for a deficit of 2.0% in all three of the alternative scenarios.

Scenario 1 – Shock to GDP Growth

A negative shock of 1 p.p to GDP growth between 2028-2037 brings the the debt-to-GDP ratio reaching 33.4% by the end of the forecasting period, or an increase of 3.8 p.p compared to the baseline scenario. However, it is assumed that the fiscal rule will remain adhered to in this scenario and this serves as a buffer to the debt level. As a result, regular expenditures are reduced so that the fiscal balance complies with the fiscal rule of 2% of GDP.

Scenario 2 – Shock to Budget Expenditures (Primary Balance Shock)

A shock to the primary balance by increasing spending by 1p.p of GDP over the period 2028-2037 would increase the debt-to-GDP ratio to 45.4% by the end of 2037. This scenario assumes that the fiscal deficit rule is adhered throughout this period. Consequently, the debt level would increase significantly, by approximately 15.8 percentage points, compared to the baseline scenario.

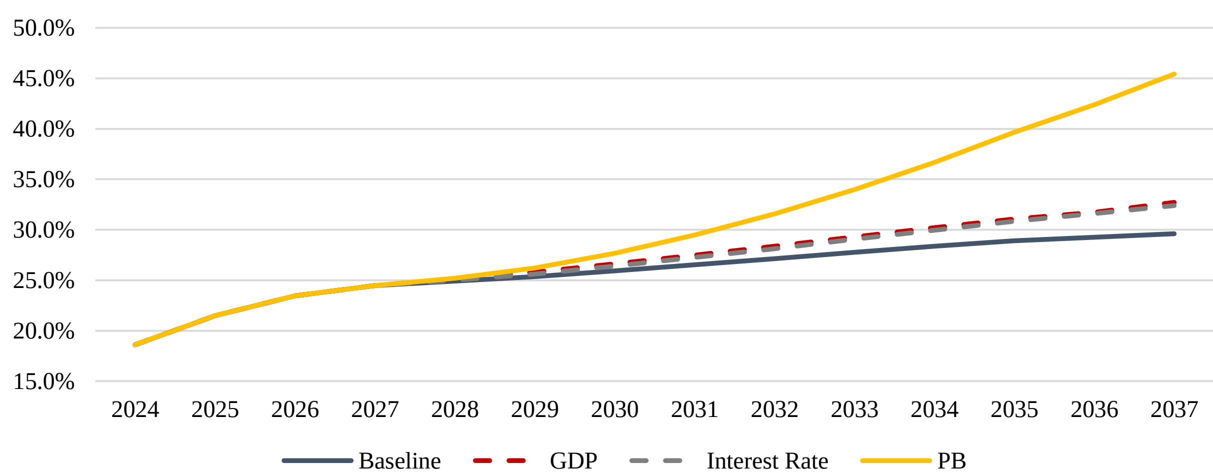
Scenario 3- Shock to interest rates

The third scenario presents an increase of 1 p.p. in interest rates on loans (both commercial and concessional) and domestic debt. However, the risks to debt levels arising from the public debt interest are within “acceptable limits” because they are regulated in the debt strategy and the fiscal deficit rule. However, assuming an interest shock of 1.0 p.p. in a scenario of not adhering the budget deficit rule, debt stock would rise significantly. Debt stock in this scenario at the end of 2037 is forecasted at 32.4% of GDP, or 2.8 percentage points higher than the level in the baseline scenario.

To sum up, Kosovo's public debt is expected to increase, but in both the baseline and alternative scenarios, it is expected to remain within acceptable levels. These results show that the current fiscal rules, especially the one that limits the deficit to 2% of GDP, act as a stabilizing factor for debt levels.

The following graph summarizes the results for the baseline and three alternative scenarios, regarding the long-term dynamics of public debt in Kosovo.

Figure 21. Debt Stock According Baseline and Alternative Scenarios



ANNEX

Table 1a: Macroeconomic prospects

Percentages unless otherwise indicated	ESA Code	Year 2023	Year 2023	Year 2024	Year 2025	Year 2026	Year 2027
		Level (bn EUR)	**Rate of change**				
1. Real GDP at market prices	B1*g	9.258	4.1	4.5	5.6	6.4	6.7
2. Current GDP at market prices	B1*g	9.680	8.8	6.6	7.4	8.1	8.5
Components of real GDP							
3. Private consumption expenditure	P3	8	3.1	4.7	5.5	4.8	4.6
4. Government consumption expenditure	P3	1	5.8	3.4	5.0	1.8	2.3
5. Gross fixed capital formation	P51	3	4.4	5.1	6.6	5.9	5.7
6. Changes in inventories and net acquisition of valuables (% of GDP)	P52+P53	0	1.7	1.6	1.5	1.4	1.3
7. Exports of goods and services	P6	4	7.2	4.8	6.1	8.5	7.0
8. Imports of goods and services	P7	7	4.7	4.8	5.9	4.4	3.0
Contribution to real GDP growth							
9. Final domestic demand		12.1	4.9	6.0	7.4	6.2	6.0
10. Change in inventories and net acquisition of valuables	P52+P53	0.2	-0.2	-0.1	0.0	0.0	0.0
11. External balance of goods/services	B11	-3	-0.6	-1.5	-1.8	0.3	0.8

Table 1b: Price developments

Percentage changes, annual averages	ESA Code	Year 2023	Year 2024	Year 2025	Year 2026	Year 2027
1. GDP deflator		4.6	2.0	1.8	1.5	1.6
2. Private consumption deflator		3.5	2.0	1.8	1.6	1.6
3. HICP		4.6	2.0	1.8	1.5	1.6
4. National CPI change		3.5	2.0	1.8	1.6	1.6
5. Public consumption deflator		9.5	5.1	2.3	2.3	2.1
6. Investment deflator		1.1	2.9	2.0	1.9	1.8
7. Export price deflator (goods & services)		4.1	2.5	2.2	2.0	2.0
8. Import price deflator (goods & services)		2.4	3.2	2.3	2.2	2.0

Table 1c: Labour markets developments

	ESA Code	Year 2023	Year 2023	Year 2024	Year 2025	Year 2026	Year 2027
		Level	Level/Rate of change				
1. Population (thousands)			1,762.2	:	:	:	:
2. Population (growth rate in %)			-90.1	-100.0	:	:	:
3. Working-age population (persons)[1]			1,172	:	:	:	:
4. Participation rate			40.7	:	:	:	:
5. Employment, persons [2]			425	:	:	:	:
6. Employment, hours worked[3]			41.3	:	:	:	:
7. Employment (growth rate in %)			5.4	:	:	:	:
8. Public sector employment (persons)			84.6	:	:	:	:
9. Public sector employment (growth in %)			-1.6	:	:	:	:
10. Unemployment rate [4]			10.9	:	:	:	:
11. Labour productivity, persons[5]		21.8	-1.2	:	:	:	:
12. Labour productivity, hours worked[6]			5.5	#REF!	:	:	:
13. Compensation of employees	D1	3.0	11.6	:	:	:	:

[1] Age group of 15-64 years
[2] Occupied population, domestic concept national accounts definition
[3] National accounts definition
[4] Harmonised definition, Eurostat; levels
[5] Real GDP per person employed
[6] Real GDP per hour worked

Table 1d: Sectoral balances

Percentages of GDP	ESA code	Year 2023	Year 2024	Year 2025	Year 2026	Year 2027
1. Net lending/borrowing vis-à-vis the rest of the world	B.9	-7.0	-8.5	-8.9	-7.7	-5.8
of which:						
- Balance of goods and services		-30.7	-31.4	-31.7	-29.8	-27.3
- Balance of primary incomes and transfers		23.0	22.5	22.4	21.7	21.2
- Capital account		0.6	0.5	0.4	0.4	0.3
2. Net lending/borrowing of the private sector	B.9/EDP B.9	-7.4	-6.2	-6.6	-5.3	-1.5
3. Net lending/borrowing of general government		-0.2	-2.8	-2.7	-2.8	-4.6
4. Statistical discrepancy		0.0	0.0	0.0	0.0	0.0

Table 1e: GDP, investment and gross value added

	ESA Code	Year 2023	Year 2024	Year 2025	Year 2026	Year 2027
GDP and investment						
GDP *level* at *current* market prices (in domestic currency)	B1g	9.7	10.3	11.1	12.0	13.0
Investment ratio (% of GDP)		32.2	32.7	33.1	33.0	32.8
Growth of Gross Value Added, percentage changes at constant prices						
1. Agriculture		-3.0	2.3	2.8	4.1	3.8
2. Industry (excluding construction)		3.4	7.3	7.3	7.3	8.3
3. Construction		3.2	3.1	3.3	6.9	5.5
4. Services		4.7	4.6	6.2	6.4	7.2

Table 1f: External sector developments

Billion Euro unless otherwise indicated		Year 2023	Year 2024	Year 2025	Year 2026	Year 2027
1. Current account balance (% of GDP)	% of GDP	-7.6	-8.1	-8.4	-7.3	-5.4
2. Export of goods	bn EUR	0.9	0.9	1.1	1.2	1.3
3. Import of goods	bn EUR	5.5	5.8	6.2	6.6	7.0
4. Trade balance	bn EUR	-4.6	-4.9	-5.2	-5.4	-5.6
5. Export of services	bn EUR	3.0	3.2	3.4	3.7	4.1
6. Import of services	bn EUR	1.3	1.6	1.8	1.9	2.0
7. Service balance	bn EUR	1.6	1.6	1.7	1.8	2.1
8. Net interest payments from abroad	bn EUR	:	:	:	:	:
9. Other net factor income from abroad	bn EUR	0.2	0.3	0.3	0.3	0.4
10. Current transfers	bn EUR	2.0	2.1	2.2	2.4	2.5
11. Of which from EU	bn EUR	:	:	:	:	:
12. Current account balance	bn EUR	-0.7	-0.8	-0.9	-0.9	-0.7
13. Capital and financial account	bn EUR	-0.3	-0.8	-0.7	-0.6	-0.6
14. Foreign direct investment	bn EUR	-0.7	-0.7	-0.7	-0.7	-0.7
15. Foreign reserves	bn EUR	0.0	0.2	:	:	:
16. Foreign debt	bn EUR	3.8	4.0	:	:	:
17. Of which: public	bn EUR	0.7	0.7	:	:	:
18. O/w: foreign currency denominated	bn EUR	:	:	:	:	:
19.O/w: repayments due	bn EUR	:	:	:	:	:
21. Exchange rate vis-à-vis EUR (annual average)	NCU/EUR	1.0	1.0	1.0	1.0	1.0
p.m. Exchange rate vis-à-vis EUR (annual average)	*%, year-on-year*	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*
20. Exchange rate vis-à-vis EUR (end-year)	NCU/EUR	1.0	1.0	1.0	1.0	1.0
p.m. Exchange rate vis-à-vis EUR (end-year)	*%, year-on-year*	*0.0*	*0.0*	*0.0*	*0.0*	*0.0*
22. Net foreign saving	% of GDP	2.4	2.5	2.7	3.1	3.6
23. Domestic private saving	% of GDP	1.4	1.6	1.7	1.9	2.2
24. Domestic private investment	% of GDP	2.6	2.7	2.9	3.1	3.3
25. Domestic public saving	% of GDP	1.0	1.0	1.0	1.1	1.4
26. Domestic public investment	% of GDP	0.6	0.7	0.8	0.9	0.9

Table 1g: Sustainability indicators

	Dimension	Year 2020	Year 2021	Year 2022	Year 2023	Year 2024
1. Current Account Balance	% of GDP	-7.0	-8.7	-10.3	-7.6	-8.1
2. Net International Investment Position	% of GDP	-12.0	-11.5	-17.9	-18.5	-20.5
3. Export market shares	%, yoy	:	:	:	:	:
4. Real Effective Exchange Rate [1]	%, yoy	0.2	2.3	5.4	1.5	1.1
5. Nominal Unit Labour Costs	%, yoy	5.6	-2.9	-13.3	14.0	:
6. Private sector credit flow	% of GDP	33.4	36.1	39.0	40.7	42.7
7. Private sector debt	% of GDP	25.3	25.3	28.5	32.9	30.0
8. General Government Debt	% of GDP	22.4	21.5	20.0	17.5	21.2

[1] Please explain the methodology used (deflators, trade weighing, etc)

Table 2a: General government budgetary prospects

	ESA code	Year 2023	Year 2023	Year 2024	Year 2025	Year 2026	Year 2027
		Level (bn NCU)	% of GDP				
Net lending (B9) by sub-sectors							
1. General government	S13	-0.02	-0.2	-2.8	-2.7	-2.8	-4.6
2. Central government	S1311	:	:	:	:	:	:
3. State government	S1312	:	:	:	:	:	:
4. Local government	S1313	:	:	:	:	:	:
5. Social security funds	S1314	:	:	:	:	:	:
General government (S13)							
6. Total revenue	TR	2.85	29.5	29.4	29.8	29.6	29.3
7. Total expenditure[1]	TE	2.88	29.7	32.1	32.5	32.4	33.9
8. Net borrowing/lending	EDP.B9	-0.02	-0.2	-2.8	-2.7	-2.8	-4.6
9. Interest expenditure	EDP.D41 incl. FISIM	0.04	0.4	0.4	0.4	0.5	0.5
10. Primary balance[2]		0.02	0.2	-2.3	-2.3	-2.4	-4.1
11. One-off and other temporary measures [3]		:	:	:	:	:	:
Components of revenues							
12. Total taxes (12 = 12a+12b+12c)		2.52	26.0	26.5	26.8	27.0	26.9
12a. Taxes on production and imports	D2	2.08	21.5	21.8	21.9	22.1	22.1
12b. Current taxes on income and wealth	D5	0.44	4.6	4.7	4.9	4.9	4.8
12c. Capital taxes	D91	:	:	:	:	:	:
13. Social contributions	D61	:	:	:	:	:	:
14. Property income	D4	0.05	0.5	0.5	0.4	0.4	0.4
15. Other (15 = 16-(12+13+14)) [4]		0.29	3.0	2.4	2.6	2.2	2.0
16 = 6. Total revenue	TR	2.85	29.5	29.4	29.8	29.6	29.3
p.m.: Tax burden (D2+D5+D61+D91-D995) [5]		2.52	26.0	26.5	26.8	27.0	26.9
Selected components of expenditures							
17. Collective consumption	P32	1.19	12.3	12.8	13.1	12.7	12.2
18. Total social transfers	D62 + D63	0.67	6.9	7.2	7.3	7.4	6.5
18a. Social transfers in kind	P31 = D63	0.67	6.9	7.2	7.3	7.4	6.5
18b. Social transfers other than in kind	D62	:	:	:	:	:	:
19 = 9. Interest expenditure (incl. FISIM)	EDP.D41 + FISIM	0.04	0.4	0.4	0.4	0.5	0.5
20. Subsidies	D3	0.40	4.1	2.9	2.9	3.1	3.4
21. Gross fixed capital formation	P51	0.56	5.8	8.3	8.4	8.5	8.2
22. Other (22 = 23-(17+18+19+20+21)) [6]		0.01	:	:	:	:	3.1
23. Total expenditures	TE [1]	2.88	29.7	32.1	32.5	32.4	33.9
p.m. compensation of employees	D1	0.77	7.9	7.8	8.3	8.1	7.8

[1] Adjusted for the next flow of swap-related flows, so the TR-TE = EDP.B9.
[2] The primary balance is calculated as (EDP B.9, item 8) plus (EDP D.41, item 9).
[3] A plus sign means deficit-reducing one-off measures
[4] P.11+P.12+P.131+D.39+D.7+D.9 (other than D.91).
[5] Including those collected by the EU and including an adjustment for uncollected taxes and social contributions (D995), if appropriate.
[6] D.29+D4 (other than D.41)+ D.5+D.7+D.9+P.52+P.53+K.2+D.8.

Table 2b: General government budgetary prospects

	ESA code	Year 2023	Year 2024	Year 2025	Year 2026	Year 2027
		bn NCU				
Net lending (B9) by sub-sectors						
1. General government	S13	-0.02	-0.29	-0.30	-0.34	-0.59
2. Central government	S1311	:	:	:	:	:
3. State government	S1312	:	:	:	:	:
4. Local government	S1313	:	:	:	:	:
5. Social security funds	S1314	:	:	:	:	:
General government (S13)						
6. Total revenue	TR	2.85	3.03	3.31	3.54	3.81
7. Total expenditure[1]	TE	2.88	3.31	3.61	3.88	4.40
8. Net borrowing/lending	EDP.B9	-0.02	-0.29	-0.30	-0.34	-0.59
9. Interest expenditure	EDP.D41 incl. FISIM	0.04	0.05	0.05	0.06	0.06
10. Primary balance[2]		0.02	-0.24	-0.25	-0.28	-0.53
11. One-off and other temporary measures		:	:	:	:	:
Components of revenues						
12. Total taxes (12 = 12a+12b+12c)		2.52	2.74	2.97	3.23	3.49
12a. Taxes on production and imports	D2	2.08	2.25	2.43	2.65	2.87
12b. Current taxes on income and wealth	D5	0.44	0.49	0.54	0.58	0.63
12c. Capital taxes	D91	:	:	:	:	:
13. Social contributions	D61	:	:	:	:	:
14. Property income	D4	0.05	0.05	0.05	0.05	0.06
15. Other (15 = 16-(12+13+14)) [4]		0.29	0.24	0.29	0.26	0.26
16 = 6. Total revenue	TR	2.85	3.03	3.31	3.54	3.81
p.m.: Tax burden (D2+D5+D61+D91-D995)		2.52	2.74	2.97	3.23	3.49
Selected components of expenditures						
17. Collective consumption	P32	1.19	1.32	1.45	1.52	1.58
18. Total social transfers	D62 + D63	0.67	0.74	0.81	0.88	0.84
18a. Social transfers in kind	P31 = D63	0.67	0.74	0.81	0.88	0.84
18b. Social transfers other than in kind	D62	:	:	:	:	:
19 = 9. Interest expenditure (incl. FISIM)	EDP.D41 + FISIM	0.04	0.05	0.05	0.06	0.06
20. Subsidies	D3	0.40	0.30	0.32	0.37	0.45
21. Gross fixed capital formation	P51	0.56	0.86	0.93	1.02	1.07
22. Other (22 = 23-(17+18+19+20+21)) [6]		0.01	0.04	0.04	0.04	0.40
23. Total expenditures	TE [1]	2.88	3.31	3.61	3.88	4.40
p.m. compensation of employees	D1	0.77	0.81	0.92	0.97	1.02

[1] Adjusted for the next flow of swap-related flows, so the TR-TE = EDP.B9.
[2] The primary balance is calculated as (EDP B.9, item 8) plus (EDP D.41, item 9).
[3] A plus sign means deficit-reducing one-off measures
[4] P.11+P.12+P.131+D.39+D.7+D.9 (other than D.91).
[5] Including those collected by the EU and including an adjustment for uncollected taxes and social contributions (D995), if appropriate.
[6] D.29+D4 (other than D.41)+ D.5+D.7+D.9+P.52+P.53+K.2+D.8.

Table 3: General government expenditure by function

% of GDP	COFOG Code	Year 2023	Year 2024	Year 2025	Year 2026	Year 2027
1. General public services	1	5.4	:	:	:	:
2. Defence	2	1.0	:	:	:	:
3. Public order and safety	3	2.8	:	:	:	:
4. Economic affairs	4	4.9	:	:	:	:
5. Environmental protection	5	0.1	:	:	:	:
6. Housing and community amenities	6	0.5	:	:	:	:
7. Health	7	3.1	:	:	:	:
8. Recreation, culture and religion	8	1.1	:	:	:	:
9. Education	9	4.1	:	:	:	:
10. Social protection	10	7.3	:	:	:	:
11. Total expenditure (item 7 = 23 in Table 2)	TE	29.7	32.1	32.5	32.4	33.9

Table 4: General government debt developments

% of GDP	ESA code	Year 2023	Year 2024	Year 2025	Year 2026	Year 2027
1. Gross debt [1]		17.5	16.5	21.1	23.0	24.0
2. Change in gross debt ratio		-2.6	-1.0	4.6	1.9	0.9
Contributions to change in gross debt						
3. Primary balance [2]		-0.2	2.3	2.3	2.4	4.1
4. Interest expenditure [3]	EDP D.41	0.4	0.4	0.4	0.5	0.5
5. Real growth effect		-0.7	-0.7	-1.1	-1.3	-1.4
6. Inflation effect		-0.8	-0.3	-0.3	-0.3	-0.3
7. Stock-flow adjustment		-1.2	2.0	-1.4	0.6	-1.9
of which:						
- Differences between cash and accruals		:	:	:	:	:
- Net accumulation of financial assets [5]		:	:	:	:	:
of which:						
- Privatisation proceeds		:	:	:	:	:
- Valuation effects and other [6]		:	:	:	:	:
p.m. implicit interest rate on debt [7]		2.4	2.7	2.3	2.4	2.2
Other relevant variables						
8. Liquid financial assets [8]		:	:	:	:	:
9. Net financial debt (9 = 1 - 8)		:	:	:	:	:

[1] As defined in Regulation 3605/93 (not an ESA concept).
[2] Cf. item 10 in Table 2.
[3] Cf. item 9 in Table 2.
[4] The differences concerning interest expenditure, other expenditure and revenue could be distinguished when relevant.
[5] Liquid assets, assets on third countries, government controlled enterprises and the difference between quoted and non-quoted assets could be distinguished when relevant.
[6] Changes du to exchange rage movement, and operation in secondary market could be distinguished when relevant.
[7] Proxied by interest expenditure divided by the debt level of the previous year.
[8] AF1, AF2, AF3 (consolidated at market value), AF5 (if quoted at stock exchange; including mutual fund shares).

Table 5: Cyclical developments

		2023	2024	2025	2026	2027
1. Real GDP growth (%, yoy)	B1g	4.1	4.5	5.6	6.4	6.7
2. Net lending of general government	EDP.B.9	-0.2	-2.8	-2.7	-2.8	-4.6
3. Interest expenditure	EDP.D.41	0.4	0.4	0.4	0.5	0.5
4. One-off and other temporary measures[1]		:	:	:	:	:
5. Potential GDP growth (%, yoy)		:	:	:	:	:
Contributions:						
- labour		:	:	:	:	:
- capital		:	:	:	:	:
- total factor productivity		:	:	:	:	:
6. Output gap		:	:	:	:	:
7. Cyclical budgetary component		:	:	:	:	:
8. Cyclically-adjusted balance (2-7)		:	:	:	:	:
9. Cyclically-adjusted primary balance		:	:	:	:	:
10. Structural balance (8-4)		:	:	:	:	:

[1] A plus sign means deficit-reducing one-off measures.

Table 6: Divergence from previous programme

	Year 2023	Year 2024	Year 2025	Year 2026	Year 2027
1. GDP growth (%, yoy)					
Previous programme	3.9	4.6	4.8	4.4	:
Latest update	4.1	4.5	5.6	6.4	6.7
Difference (percentage points)	0.2	-0.1	0.8	2.0	:
2. General government net lending (% of GDP)					
Previous programme	-0.3	-2.7	-2.7	-1.9	:
Latest update	-0.2	-2.8	-2.7	-2.8	-4.6
Difference	0.0	-0.1	0.0	-0.9	:
3. General government gross debt (% of GDP)					
Previous programme	19.4	20.7	22.3	23.2	:
Latest update	17.5	16.5	21.1	23.0	24.0
Difference	-1.9	-4.2	-1.1	-0.1	:

Table 8: Basic assumptions on the external economic environment [1]

	Dimension	Year 2023	Year 2024	Year 2025	Year 2026	Year 2027
Short-term interest rate	Annual average	3.4	3.5	2.1	2	:
Long-term interest rate	Annual average	2.4	2.3	2.3	2.4	:
USD/EUR exchange rate	Annual average	1.1	1.1	1.1	1.1	:
Nominal effective exchange rate	Annual average	7.02	3.22	0.17	0	:
Exchange rate vis-à-vis the EUR	Annual average	:	:	:	:	:
Global GDP growth, excluding EU	Annual average	3.7	3.5	3.6	3.6	:
EU GDP growth	Annual average	0.4	0.9	1.5	1.8	:
Growth of relevant foreign markets	Annual average	:	:	:	:	:
World import volumes, excluding EU	Annual average	1.3	3.2	3.3	3.3	:
Oil prices (Brent, USD/barrel)	Annual average	82.5	80.7	73.1	71.5	:

[1] If necessary, purely technical assumption.

Document	Description	2022	2023 Budget	2024	2025	2026	2027
ERP 2024	Total revenues	2,493.5	2,884.1	3,028.0	3,193.6	3,406.9	n/a
	Tax- Revenues	2,525.4	2,525.4	2,705.1	2,864.3	3,062.5	n/a
	Non-tax Revenues	261.2	261.2	292.9	306.8	321.9	n/a
	Total expenditures	2,539.6	3,238.6	3,314.3	3,502.2	3,642.7	n/a
	Recurrent spending	2,082.0	2,359.8	2,396.8	2,513.2	2,617.1	n/a
	Capital expenditure	422.6	819.9	859.2	921.2	951.2	n/a
	Overall budget balance	-46.1	-352.9	-284.6	-306.7	-233.8	n/a
	Budget balance (as per fiscal rule)	13.9	-219.4	-209.6	-227.5	-181.6	n/a
	GDP	8,936.2	9,842.9	10,552.3	11,344.2	12,121.2	n/a
	Overall deficit, as % of GDP	-0.5%	-3.4%	-2.7%	-2.7%	-1.9%	n/a
	Bank balance, as % of GDP	3.2%	2.8%	2.8%	2.6%	2.7%	n/a
	Capital Expenditure, as % of GDP	4.7%	8.3%	8.1%	8.1%	7.8%	n/a
	Recurrent expenditure, as % of GDP	23.3%	23.8%	22.7%	22.2%	21.6%	n/a
Document	**Description**	**2022**	**2023**	**2024 Budget**	**2025**	**2026**	**2027**
ERP 2025	Total revenues	2,493.5	2,854.1	3,028.0	3,305.4	3,544.3	3,812.4
	Tax Revenues	2,217.0	2,505.9	2,705.1	2,926.4	3,178.1	3,428.1
	Non-tax Revenues	204.9	210.6	222.4	356.6	343.7	361.8
	Total expenditures	2,539.6	2,876.6	3,314.3	3,607.5	3,883.6	4,040.2
	Recurrent spending	2,082.0	2,273.5	2,396.8	2,615.7	2,798.5	2,900.3
	Capital expenditures	422.6	560.9	859.2	930.3	1,016.3	1,067.1
	Overall budget balance	-46.1	-20.9	-284.6	-300.3	-336.7	-225.1
	Budget balance (as per fiscal rule)	13.9	54.5	-209.6	-222.3	-242.5	-225.1
	GDP	8,895.7	9,680.1	10,552.3	11,083.6	11,976.9	12,989.5
	Overall deficit as % e GDP	-0.5%	-0.2%	-2.7%	-2.7%	-2.8%	-1.7%
	Bank balance as % of GDP	3.2%	2.3%	2.8%	3.1%	3.3%	3.8%
	Capital Expenditure, as % of GDP	4.8%	5.8%	8.1%	8.4%	8.5%	8.2%
	Recurrent expenditure, as % of GDP	23.4%	23.5%	22.7%	23.6%	23.4%	22.3%
Difference between ERP 2025 and ERP 2024	Total revenues	0.0%	-1.0%	0.0%	3.5%	4.0%	n/a
	Tax Revenues	-12.2%	-0.8%	0.0%	2.2%	3.8%	n/a
	Non-tax Revenues	-21.6%	-19.4%	-24.1%	16.2%	6.8%	n/a
	Total expenditures	0.0%	-11.2%	0.0%	3.0%	6.6%	n/a
	Recurrent spending	0.0%	-3.7%	0.0%	4.1%	6.9%	n/a
	Capital expenditures	0.0%	-31.6%	0.0%	1.0%	6.8%	n/a
	Overall budget balance	0.0%	-94.1%	0.0%	-2.1%	44.0%	n/a
	Budget balance (as per fiscal rule)	0.0%	-124.8%	0.0%	-2.3%	33.5%	n/a
	GDP	-0.5%	-1.7%	0.0%	-2.3%	-1.2%	n/a
	Overall deficit as % e GDP	0.0p.p.	3.2p.p.	0.0p.p.	0.0p.p.	-0.9p.p.	n/a
	Bank balance as % of GDP	0.0p.p.	-0.6p.p.	0.0p.p.	0.5p.p.	0.6p.p.	n/a
	Capital Expenditures, as % of GDP	0.0p.p.	-2.5p.p.	0.0p.p.	0.3p.p.	0.6p.p.	n/a
	Recurrent expenditure, as % of GDP	0.1p.p.	-0.3p.p.	0.0p.p.	1.4p.p.	1.8p.p.	n/a