



The impact of 100% tax on production and consumer prices in Kosovo

Comparing periods: January - October 2018 and January - October 2019



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and consumer prices in Kosovo**
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March 2020

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This analysis was originally written in Albanian

Executive summary

The current government, namely Prime Minister Kurti, in February 2020 presented his proposal to abolish the 100% tariff on raw materials imported from Serbia and Bosnia and Herzegovina, starting on March 15, 2020.¹ As a second step, complete abolishment of the tariff for all products from the two countries was proposed, as of April 1, 2020 for a period of 90 days. However, though the deadline has passed, the government is yet to take a decision to abolish the tariff on raw materials, and the tariff is still in force. Specifically, as of November 21, 2018, Kosovo applies a 100% tariff on products imported from Serbia and Bosnia and Herzegovina (BiH).² This tariff was preceded by an earlier measure applying a 10% tariff on products imported from these two countries. The decision to apply the 100% tariff was of a political nature, and came one day after Kosovo failed to gain membership in Interpol. Until then, Serbia was the main exporter in Kosovo, but at the same time it was the country applying most trade barriers to Kosovar businesses exporting there.³ The introduction of the tariff has also presented challenges for a number of producers in Kosovo, due to their dependence on raw material coming from Serbia and for importers of final products. In addition to the need to replace products imported from Serbia, businesses have also faced increased transport costs. However, for others - local businesses and importers in Kosovo importing from other countries - the tariff presented an opportunity to increase their market presence.

This report strives to assess the impact of the 100% tariff on production and prices in Kosovo. Using direct and indirect indicators related to the processing industry's activity, we estimated the production growth in Kosovo. Whereas, based on consumer and import price indices for Kosovo and European Union countries, we made efforts to isolate the factors that contributed to the rapid rise in consumer prices in Kosovo after the introduction of the 100% tariff. This report is a follow-up of GAP Institute's first report on the effects of the 100% tariff on domestic production and prices in Kosovo, only now covering a longer comparative period.⁴

Findings indicate that imports from Serbia and Bosnia and Herzegovina have declined sharply since the introduction of the 100% tariff. From importing around 450 million Euro per year from Serbia before the tariff, in 2019 the total value of imports in Kosovo from Serbia dropped to about 5.8 million Euro. In the case of BiH, the value of imports has fallen from around 81 million Euro per year in the past to just 2.2 million Euro in 2019. Greece, North Macedonia, Bulgaria, were among the countries that have had the most significant increases in their share of Kosovo's total imports. While Kosovo's exports to Serbia and BiH, although declining, have not been as emphatic as in the case of imports from these two countries. The value of products exported to Serbia from Kosovo in 2019 was about 17% lower, from 27 million Euro in 2018 to 22.8 million Euro in 2019.

The value of products exported to BiH from Kosovo in 2019 was about 28% lower than in 2018, from 6.7 million Euro to 4.8 million Euro in 2019.

¹ Office of the Prime Minister. Prime Minister Kurti: The tariff on raw materials imported from Serbia and Bosnia and Herzegovina to be removed from 15 March 2020 Source: <https://bit.ly/2vfF2XA>

² Government of Kosovo. Decision 1/76, 21.11.2018. Source: <https://bit.ly/2TRoDQc>

³ Ministry of Trade and Industry, "Trade Barriers, Trade Facilitation as a Tool to Eliminate Them", April 2018, Source: <http://bit.ly/2VdDjM5>

⁴ You can find the full report here: <https://bit.ly/2wXyFsj>

Kosovo's total imports in 2019 amount to around 3.5 billion Euro, or 4% higher than in 2018, which represents a slower growth of imports compared to 2018 and 2017. Whereas, total exports in 2019 amounted to 350 million Euro or about 6% higher than in 2018. The trade deficit remains virtually the same as in previous years where the rate of exports covering imports remains at around 10%.

Regarding the impact of the 100% tariff on domestic production in Kosovo, the report finds that there is an increase in activity in the manufacturing sector (processing industry). However, it is not significant and has lower trends than in the period prior to the introduction of the tariff. Specifically, during the period January - September 2019 this sector grew by 10%, while in the same period in 2018 the processing industry grew by 16%. In real terms, the processing industry recorded an average growth of 6.5% in 2019 compared to 2018.⁵ In addition, electricity consumption from this sector has increased by about 9.8% compared to 2018.⁶ Moreover, the average employment trend during the months of 2019 followed the trends of previous years, with no deviation from the downward and upward cycles in the number of employees. Specifically, during 2019, the number of employees in the processing industry increased on average by 7%, while in 2018 this increase was 10%.⁷

However, a more significant impact of the 100% tariff is observed on product prices during 2019. Most significant increases were in food and beverage prices, which increased by about 6.1% in January - September 2019 compared to the same period in 2018, which was the highest increase from 2017. The rise in prices was immediate and more dominant in the first half of the year, after the tariff was introduced. In the second half of 2019, there was a downward trend in prices compared to the same period in 2018, though prices were again higher by about 3.3%.

Imports from Serbia and Bosnia and Herzegovina to Kosovo before and after the 100% tariff




















During the year, Kosovo imported from Serbia high value products such as fuel, beverages, cereals, oils, etc., with the dependency on imports for such products from Serbia reaching up to 85%. Table 1 shows that in 2019, in a comparative period similar to 2018, namely January - October, Kosovo has increased its imports value by replacing them with products from other countries. Of the 83 million Euro of fuel imported from Serbia in 2018, in 2019 around 90 million Euro were imported from Greece and Slovenia. Similarly, while in January-October 2018 over 26 million Euro of cereals were imported from Serbia, in 2019 over 20 million Euro of cereals originated in Croatia and Bulgaria. In general, six main product groups imported from Serbia now mainly originate from North Macedonia, Bulgaria, Greece and Croatia.

5 Ministry of Trade and Industry. Report - Impact Assessment of the "Enterprise Development Program".
Source: <https://bit.ly/38RW0oX>

6 Kosovo Statistical Agency. Energy Balance in Kosovo. 2017-2019.

7 Kosovo Customs data for the period January-October 2018 and January-October 2019.

Table 1. Serbia's share in Kosovo's imports in several sectors

| TARIK ⁸ | Imports from Serbia January-October 2018 (euro) | Total imports of Kosovo, January - October 2018 (euro) | Serbia's share in total imports | Total imports of Kosovo, January - October 2019 (euro) | Increasing the share of Kosovo's total imports of some countries in 2019: |
|--------------------|---|--|--|--|---|
| 27. Fuel | 83,664,574 | 369,545,247 | 23%  | 378,423,911 |  Greece +105% (+57 mil.),  Slovenia +257% (+33 mil.) |
| 22. Beverages | 32,867,622 | 63,297,751 | 52%  | 65,151,129 |  North Macedonia +294% (+11 mil.),  Bulgaria +9709% (+14 mil.) |
| 10. Cereal | 26,123,910 | 30,893,797 | 85%  | 33,420,158 |  Croatia +2736% (+13.4 mil.),  Bulgaria +4798% (+6.8 mil.) |
| 15. Oils | 12,861,448 | 23,810,846 | 54%  | 24,701,246 |  Bulgaria +304% (+5.3 mil.),  North Macedonia +443% (+5.7 mil.) |
| 17. Sugars | 12,785,439 | 23,614,312 | 54%  | 24,955,757 |  France +23687% (+6.4 mil.),  Poland +115% (+2.8 mil.) |
| 23. Animal feed | 11,357,751 | 17,047,701 | 67%  | 13,228,832 |  Croatia +272% (+2 mil.),  Greece +118% (+ 900 thousand),  Bulgaria +345% (+112 thousand) |










Source: GAP Institute using Kosovo Customs data

The introduction of the 100% tariff on goods from Serbia and BiH has increased the presence of imports from other countries at a very high rate. In 2019, Bulgaria exported about 58 million Euro, or 87% more to Kosovo than in the previous year. Greece over 72 million Euro or 58% more, Croatia around 42 million Euro or 43% more and North Macedonia over 68 million Euro, or 40% more. For the majority of sectors in which Serbia covered the largest share of imports in Kosovo, there is a higher value of imports in 2019, which indicates that businesses in Kosovo have managed to find other sources for import, as noted in the earlier GAP Institute report.

Products that were imported the most from Bosnia and Herzegovina prior to the 100% tariff were mainly iron and steel, as well as meat and fish foods and dairy products. In 2019, Kosovo's total imports of these products declined, and most of the imports previously covered by BiH now come from Turkey, which has an increase of over 15 million Euro, or 731%, and Greece by 6 million or 98%. Whereas, meat and dairy products previously imported from Bosnia and Herzegovina, are now covered mainly by Slovenia and North Macedonia.

⁸ Kosovo Integrated Tariff (TARIK) is based on the harmonized system and combined nomenclature for classification of goods.

Table 2. BiH's share in Kosovo's imports in several sectors

| TARIK | Imports from Bosnia, January - October 2018 (euro) | Total imports of Kosovo, January - October 2018 (euro) | Bosnia's share in total imports | Total imports of Kosovo, January - October 2019 (euro) | Increasing the share of Kosovo's total imports of some countries in 2019: |
|--|--|--|--|--|--|
| 72. Iron and steel | 27,146,494 | 183,885,699 | 15%  | 171,993,390 |  Turkey +731% (+ 15 mil. euro),  Greece +98% (+6 mil.) |
| 16. Foods prepared from meat, fish, etc. | 6,588,334 | 22,773,034 | 29%  | 25,038,223 |  Slovenia +130% (+5.5 mil.),  North Macedonia +30% (+500 thou.) |
| 4. Dairy products | 4,963,134 | 39,749,246 | 12%  | 41,232,340 |  North Macedonia +64% (+ 2.1 mil.),  Slovenia +18% (1.7 mil.) |

Source: GAP Institute using Kosovo Customs data

Imports of main products from Serbia and BiH in 2019

After the introduction of the 100% tariff, the main products that continue to be imported from Serbia, as Table 3 shows, are pharmaceuticals, electricity and fuel and machinery. Whereas, meat, vegetables and fruits are the products that continue to be imported from Bosnia and Herzegovina. Elements that may affect the import of these products may be the difficulty of replacing them with other markets, or the need to import these products more quickly.

Table 3. Imports from Serbia and Bosnia and Herzegovina to Kosovo in 2019

| Main imports from Serbia in 2019 | Value (€) | Main imports from BiH in 2019 | Value (€) |
|---|------------------|--|------------------|
| 30. Pharmaceutical products | 935,534 | 16. Foods prepared from meat and fish | 1,318,852 |
| 27. Mineral Fuels (Electricity and Fuels) | 501,762 | 20. Preparation from vegetables, fruits or other parts of plants | 397,531 |
| 28. Inorganic chemicals (oxygen) | 482,772 | 25. Salts, lime and cement | 123,968 |
| 85. Machinery and Electrical Equipment (for TV) | 417,343 | 19. Preparations from cereals, pastry products or dough | 71,949 |
| 84. Machinery and boilers | 391,507 | 73. Iron and steel | 42,128 |
| 7. Iron and steel | 342,919 | 44. Wood, and wood products | 33,755 |
| 10. Cereal | 300,277 | 30. Pharmaceutical products | 33,416 |
| Total imports in 2019 | 5,792,645 | Total imports in 2019 | 2,148,743 |

Source: GAP Institute using Kosovo Customs data

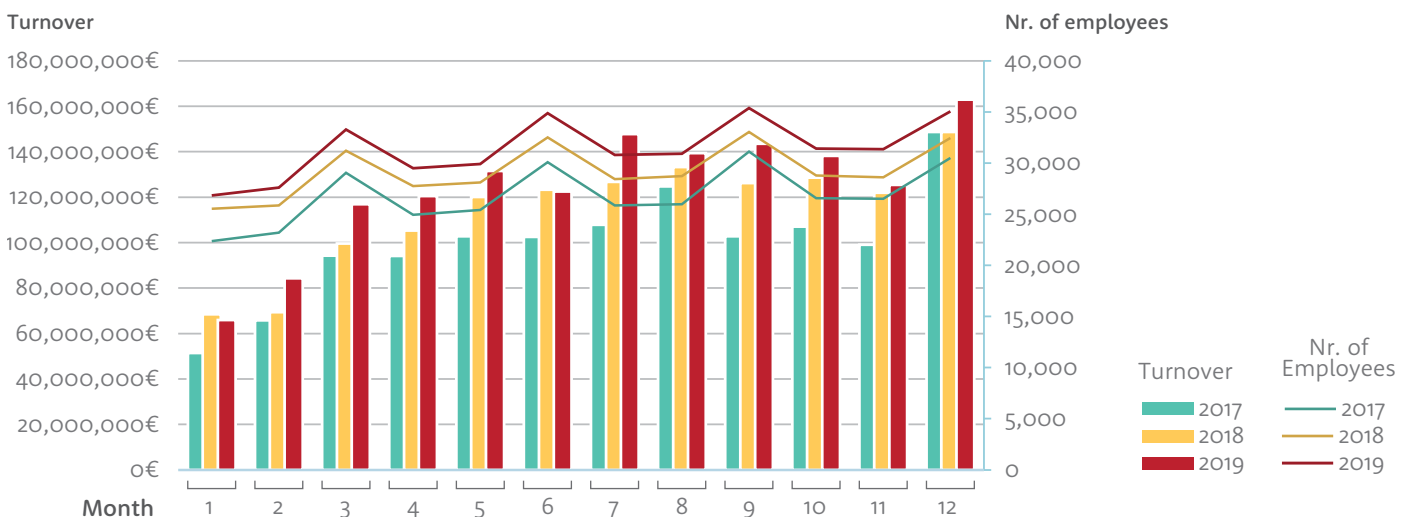
Impact of the tax on Kosovo's domestic production

To analyze the impact of the tax on domestic production in Kosovo, we have analyzed various indicators that respond directly to the increase of activity in the production sector. Specifically, indicators were used regarding the turnover of businesses from this sector, consumption of electricity and number of employees.

Turnover of businesses in the processing industry

In 2019, specifically in the period January - October 2019, according to the Tax Administration of Kosovo (TAK), the declared turnover of businesses from the processing industry has increased by 10%.⁹ Growth in this period is lower than in 2018, when, compared to 2017, growth was about 16%. Throughout 2019, the entire processing industry consisting of about 5,000 businesses¹⁰, had a higher turnover of around 130 million Euro, while in 2018 had a higher turnover of over 170 million Euro. A more significant increase of production activities in Kosovo, which had a higher advantage with the introduction of the 100% tariff, was supposed to be expressed in a higher growth of this sector particularly in the last months of 2019, since the effects may not be noticed in the first months due to the time producers take to either increase production capacity - though most declared to operate under the installed capacity - finding workers, or other factors.¹¹ Similarly, the increase in the number of employees in the sector is within the normal annual growth. Specifically, during January - October 2019, the number of employees in the processing industry increased by 7%, while in January - October 2018 this increase was 10%. Moreover, the average employment trend during the months of 2019 followed the trends of previous years, with no deviation from the downward and upward cycles in the number of employees.

Figure 1. Turnover and average number of employees in Kosovo's production industry, 2017-2019



Source: GAP Institute using TAK data

⁹ The data were received through the request.

¹⁰ Kosovo Agency of Statistics. Structural Business Survey.

¹¹ Ministry of Trade and Industry. Report - Impact Assessment of the "Enterprise Development Program".

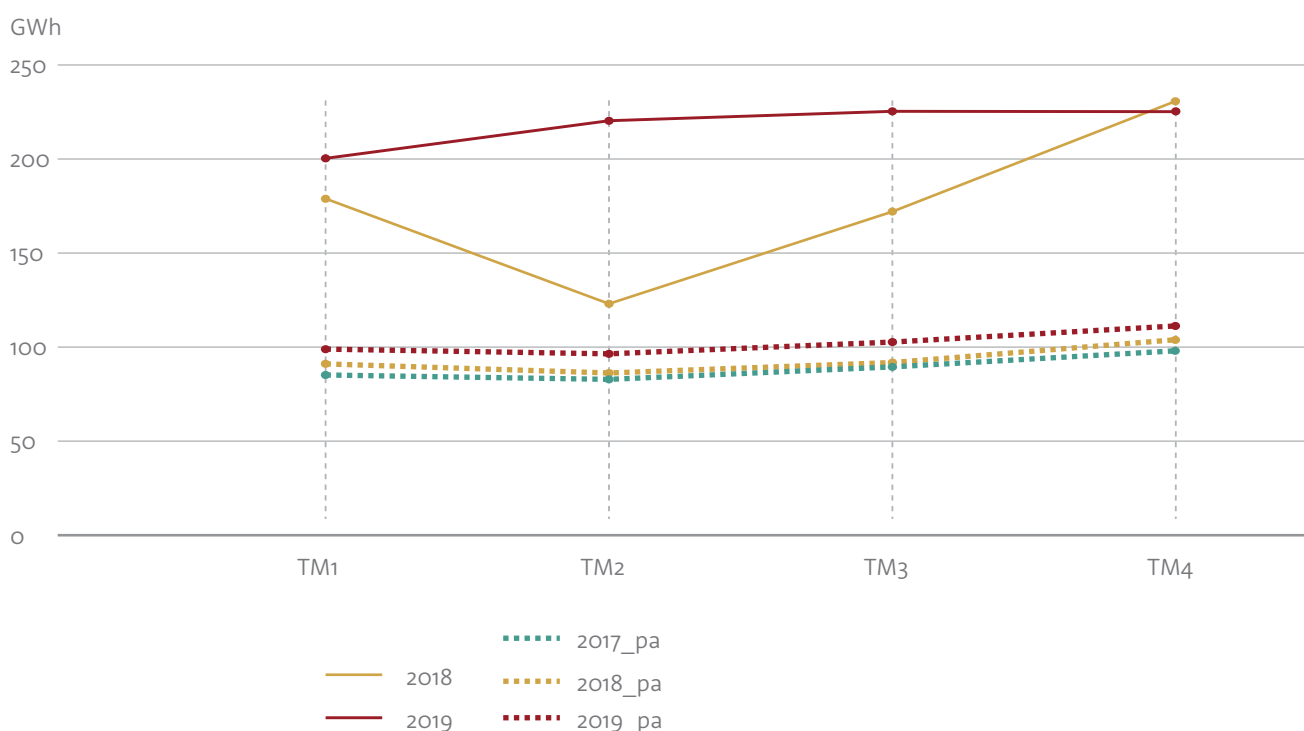
Source: <https://bit.ly/38RW0oX>

In real terms, according to the Kosovo Agency of Statistics (KAS), the processing industry recorded an average growth over the period January - September 2019 of 6.5%, compared to 2018. While the average real growth of the sector in the period January - September 2018, compared to 2017, was about 3.7%. Specifically, in 2019, the processing sector initially had a smaller activity in the first quarter, with only 2% growth compared to 2018, while in the second and third quarters there was a more emphatic real growth of the sector of 10.6% and 6.86%, respectively.¹²

Electricity consumption

Electricity consumption in 2019 by large consumers such as Ferronikeli, Trepca and Sharrcem, along with the industry sector, is notably higher than in 2018, by about 24%. However, as Figure 2 indicates, in the period 2017-2019 there are significant fluctuations between consumption in quarters over different years. This can also be greatly affected by the operation of large customers such as Ferronikeli which, in the past and including 2019, has completely stopped production in occasions during the year.¹³ Therefore, if we separate the industry sector, we notice a similar cycle of energy consumption by this sector over the quarters, with an upward trend. Specifically, in 2019, the consumption of electricity by the industry sector increased by about 9.8% compared to 2018, while in 2018 growth was about 5% or 4.8 percentage points lower.

Figure 2. Electricity consumption by all producers, and industry alone, 2017-2019



Source: GAP Institute using TAK data

Note: 2017 - 2019 without including large customers such as Ferronikeli

¹² Kosovo Agency of Statistics. Gross Domestic Production (GDP) with Expenditure and Production Approach, Q3 2019. Source: <https://bit.ly/33bhJLf>

¹³ Zëri. "Ferronikeli" is out of production for over two months. Source: <https://bit.ly/38IVFZA>

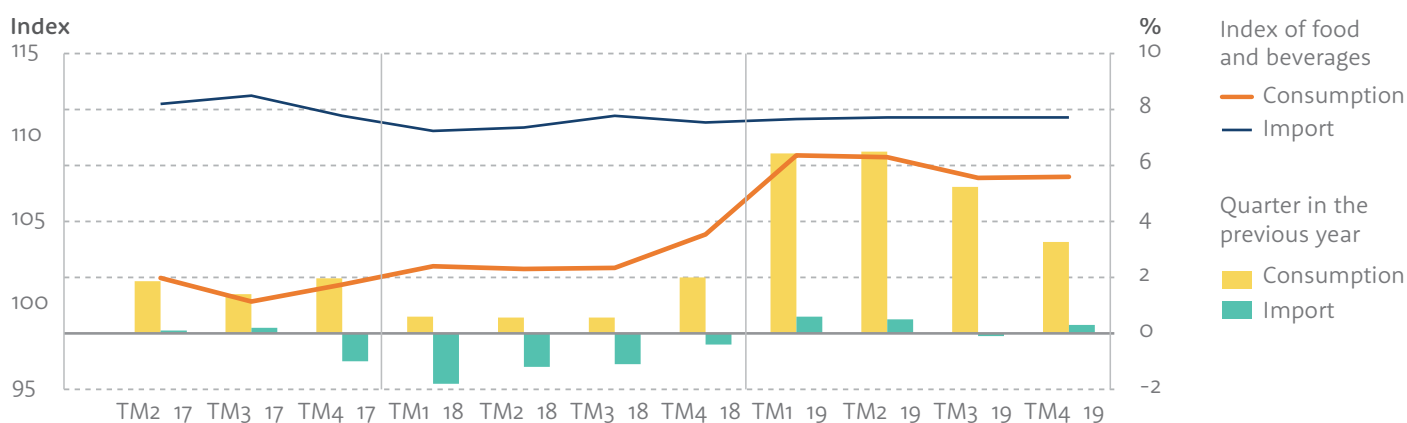
Impact on food prices

The introduction of the tariff has also presented challenges for a number of producers in Kosovo, due to their dependence on raw material from Serbia, and for importers of final products. Until the tariff, Serbia was Kosovo's main trading partner. In addition to the need to replace products imported from Serbia, businesses have also faced transport cost increases, as countries such as Bulgaria, Slovenia and Turkey, which have largely replaced Serbian products in Kosovo, are further away from Kosovo. For other parties, local businesses that do not depend on raw materials produced in Serbia, as well as importers who import from other countries, the tariff has presented opportunities to increase their market presence. Also, in addition to the increased transport costs, if the market demand had remained the same after tax, as reflected in the increased value of imports, and supply was limited, this led to an increase in product prices in Kosovo from producers and retailers.

In 2019, based on the harmonized index of consumer prices, there was an average price increase of 2.7% in Kosovo. The most significant increase was seen in food and beverage prices with about 5.4%. Since in the past Kosovo depended largely on imports from Serbia, especially for food products as indicated in Table 1, and since food products have a higher weight on the consumer basket in Kosovo, we have analyzed the impact of the 100% tariff 100 % in food prices.

As Figure 3 shows, food and beverage prices in Kosovo, expressed through the Consumer Price Index, after the introduction of the 100% tariff, increased by about 6.1% in January-September period 2019 compared to the same period in 2018, which was also the highest growth from 2017. The rise in prices was immediate and more dominant in the first half of the year, after the tariff was introduced. In the second part of 2019 there is a declining trend of prices compared to the same period in 2018, though prices were again higher by about 3.3%. In term of import prices, as indicated in the import price index of food and beverages in Figure 3, on average they were stable since the end of 2017, without any sharp decline or increase. In the period January - September 2019 they have only increased by 0.33% compared to 2018. Figure 3 illustrates a marked difference between average import prices and market prices for food products.

Figure 3. Differences in food and beverage prices compared to the previous year, import and consumption price index, Q2 2017-Q4 2019



Source: GAP Institute using KAS data

Due to the composition of many import index products for food and beverages, it is necessary to perform a more detailed analysis of some products. Some of the products that have had the highest price increases during January - October 2019 compared to the same period of the previous year are vegetables, cereals, coffee and meat. In the case of vegetables, cereals and meat, the increase in consumer prices was followed by the increase in import prices, while for coffee it was observed that despite a decrease in the import prices during January - October 2019, compared to 2018, consumption has gone up. Similarly, for tobacco and sugar products there was no change in import prices, but there has been an increase in consumer prices. The above products have a significant share in total imports and the consumer basket. However, there are cases when consumer prices have increased less than import prices, or have decreased such as in fruits and milk. However, these products, as Figure 4 indicates, have been shown to have large price movements over the years.

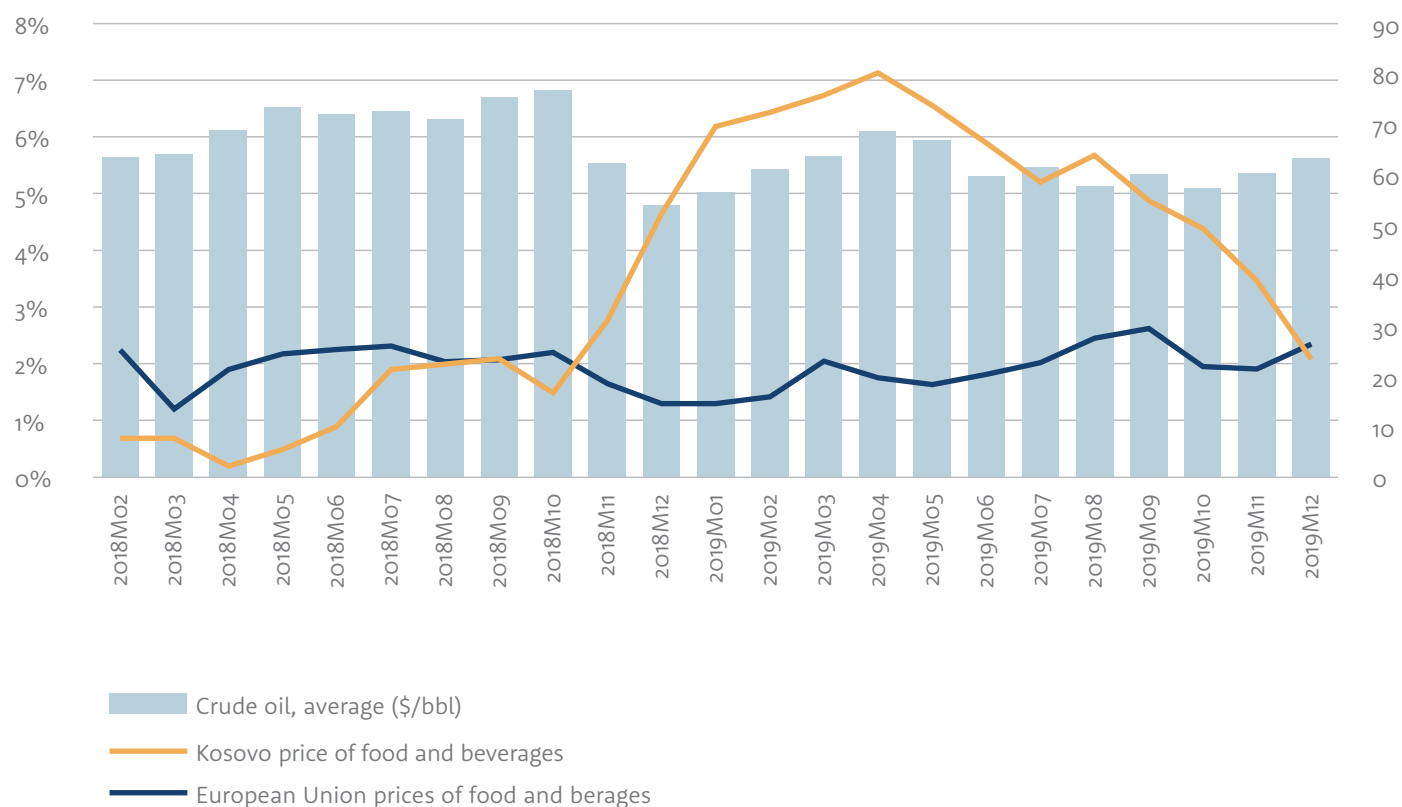
Figure 4. Differences in consumer and import prices for some products, 2016-2019



Source: GAP Institute using KAS and Kosovo Customs data

In addition, data on average food and beverage prices in the European Union (EU), where from some of Kosovo's main trading partners come, such as Germany, Slovenia, Greece, indicate that monthly changes in prices in the EU compared to the previous year were small, and there were no sharp increases in 2019, as it was the case in Kosovo. Also, as Figure 5 shows, the global average oil price in 2019 has decreased compared to 2018. This is an advantage for importers from Kosovo, as they have not had an increase in shipping costs affected by the price of oil. The increase may have only been reflected by the farther distance of the countries from which they import, after the introduction of the 100% tariff from Kosovo, if the origin of products imported was previously in Serbia. However, to a significant extent, the cost of shipping may be stabilized by the fall in oil prices. The data above also show that the source of price increases for some products must be from suppliers and producers within Kosovo, who after 100% tariff face less competition and greater demand, and thus increased the profit margin.

Figure 5. Food and beverage price change compared to previous year and oil price, February 2018 - December 2019



Source: GAP Institute using Eurostat, World Bank and KAS data

Removal of the tax on raw material

The current government, namely Prime Minister Kurti, in February 2020 presented his proposal to abolish the 100% tariff on raw materials imported from Serbia and Bosnia and Herzegovina, starting on March 15, 2020.¹⁴ As a second step, complete abolishment of the tariff for all products from the two countries was proposed, as of April 1, 2020 for a period of 90 days. However, though the deadline has passed, the government is yet to take a decision to abolish the tariff on raw materials, and the tariff is still in force. If the tariff on raw materials is removed, in economic terms it represents a positive step because raw materials are used to create an added value, namely in the production of final products. For Kosovo producers, lowering the cost of raw materials greatly benefits to enhance competitiveness. According to Kosovo Customs data¹⁵, Kosovo imported raw materials from Serbia in the amount of 28 million Euro in 2018. The group of main products imported as raw materials, as Table 4 indicates, includes wheat, sheet metal, iron and steel, paper, etc. A similar raw material value is expected to be imported from Serbia in 2020, thus increasing imports compared to 2019. Imports could rise at a much higher rate if the government pursues its plan to completely abolish tariffs in 2020.

Table 4. Main products imported as raw material from Serbia during 2018

| | Imported value | | Imported value |
|-------------------------|----------------|--|----------------|
| Wheat (not durum) | 11,087,340 € | Bitumen oil | 542,964 € |
| Durum wheat | 2,635,407 € | Copper | 491,622 € |
| Iron and steel | 2,508,920 € | Corn | 420,217 € |
| Aluminum barrels, bins | 2,254,338 € | Cartons, boxes and suitcases, paper or cardboard | 231,345 € |
| Non-alloy steel sheet | 1,846,792 € | Corn and other solid waste | 151,656 € |
| Paper and cardboard | 798,367 € | Testliner (recycled table viewer) | 163,906 € |
| Edible oil, unprocessed | 659,179 € | Crepe and textile paper from cellulosic fibers | 156,580 € |

Source: GAP Institute using Kosovo Customs data

¹⁴ Office of the Prime Minister. Prime Minister Kurti: The tariff on raw materials imported from Serbia and Bosnia and Herzegovina to be removed from 15 March 2020 Source: <https://bit.ly/2vfF2XA>

¹⁵ The data were received upon request.

Conclusion

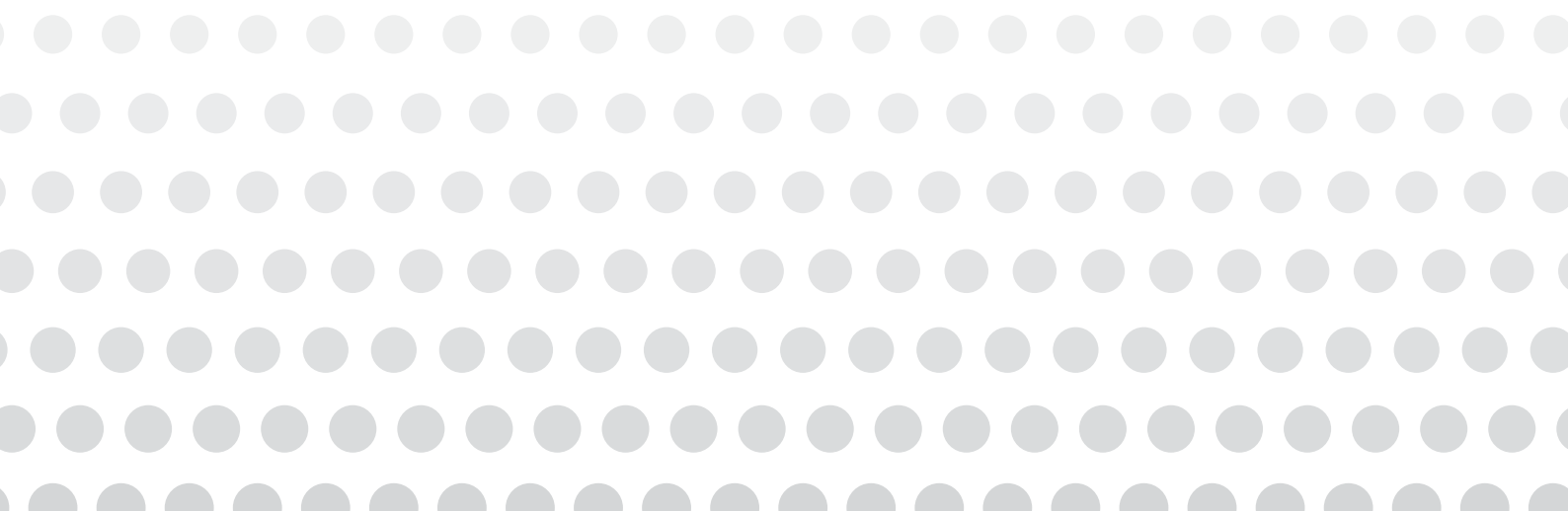
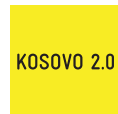
The current government has proposed an initiative to remove the 100% tariff, initially on raw materials, then for all products. Since November 21, 2018, Kosovo applies a 100% tariff on products imported from Serbia and Bosnia and Herzegovina (BiH). This tariff was preceded by an earlier measure applying a 10% tariff on products imported from these two countries. The decision to introduce the 100% tariff was largely of a political nature. This report assesses the impact of the 100% tariff on production and prices in Kosovo.

The findings of the report show that imports of products from Serbia and Bosnia and Herzegovina have fallen sharply since the introduction of the 100% tariff, while Kosovo's exports to these countries have declined slightly. It is also noted that there is an increase in manufacturing sector activities, though not a significant one. In the period January – October 2019, this sector grew by 10%, while in the same period in 2018 the processing industry grew by 16%. However, a more significant impact of the 100% tariff is observed on product prices in Kosovo during 2019. Most significant increases were in food and beverage prices, which increased by about 6.1% in January – 2019 compared to 2018, which was the highest increase from 2017. Sources of increased prices for some products were found to be increased prices from producers and importing businesses as a result of lower competition and higher demand, or increased shipping costs.



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KOSOVO 2.0

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